Australian tax plan: A "golden honeypot" for the wealthy

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Only two months after finalising plans to give the wealthy income tax cuts of up to $60 a week each, the Australian government has unveiled a new tax blueprint that will hand over billions of dollars per year to the corporate elite. It is another milestone in the complete restructuring of the taxation system to shift the burden from the rich to the working people.

When Treasurer Peter Costello released the package on Tuesday, the response in most big business circles was ecstatic. “High income-earners have just been given a second big bite of the tax-cut cherry,” observed Ross Gittins in the *Sydney Morning Herald*. “Business people are dancing in the streets.”

A spokesman for speculative investors, Andrew Green, the executive director of Australian Venture Capital Association Ltd, declared: “This is the golden honeypot that will enable us to live out the dream.” According to the front-page headline in Murdoch's the *Australian*: “Business hails tax revolution.”

It is not hard to explain the cause for these celebrations. The new tax system is substantially based on report compiled by leading businessman John Ralph. It features, first, a halving of the capital gains tax (CGT) and, second, the lowering of the company tax rate from 36 percent to a record low of 30 percent. Business and wealthy individuals stand to gain $3.5 billion a year from the company tax handout and $600 million from the cutting of the CGT.

Both measures have vast economic and social implications. By cutting the top capital gains tax rate to half the income tax rate, the government is enshrining the principle that cash obtained by buying and selling assets for speculative profit is taxed at a far lower rate than wages and salaries.

This windfall will go almost exclusively to the few in society who can afford to trade and speculate in such assets—everything ranging from companies to real estate, shares, works of art, antique clocks, vintage wine, rare stamps and racehorses. Those earning more than $60,000 a year will still pay the top marginal income tax rate of 48.5 percent but their capital gains tax rate will be slashed to 24.25 percent.

The package is so blatant that it makes a mockery of the government and media claim that ordinary "mums and dads" will gain. Trying to defend it in parliament, Prime Minister John Howard declared that it was an "extraordinary proposition" to say that the policy favoured the rich, because 77 percent of people who paid CGT earned less than $50,000.

The government's own statistics, however, show that most of those earning less than $50,000 (60 percent of the population) have only small CGT bills, if any at all. Taxation Office figures demonstrate that people earning more than $50,000 pay 80 percent of all CGT.

Moreover, the government is attempting to ensure that the plan will only benefit those who have sufficient finances and the know-how to make large and quick profits. It has scrapped the indexation of the CGT to adjust for inflation. As a result, small investors who typically hold property for longer periods—say a decade—will, in fact, pay more tax.

For that reason, the real estate industry has accused the government of "conning" small property investors. Real Institute of Australia chief executive Daryl Smeaton charged that people with long-term property holdings would be the big losers.

Some other industry sectors condemned the government for promoting "unproductive" speculative investment, which will undermine investment in manufacturing, construction, mining and other areas. The new arrangements have been designed to reward what is euphemistically called venture capital. On a global scale this primarily consists of funds that specialise in share market speculation. In particular, the government wants to attract the billions of dollars held by US pension funds.

Similar structural issues are raised by the pledge to cut the new company tax rate far below the top income tax rate. The government is not only providing the largest firms with tax handouts. The lower corporate rate will generate a whole new tax avoidance industry, as will the CGT cut. Business people will re-arrange their accounting to take full advantage of the new rates by disguising their income as capital gains or company profit, rather than personal income.

Far from discouraging such tax avoidance, the government will encourage it. Treasurer Costello announced a delay in promised clampdowns on tax minimisation, such as in the personal services industry and on tax "losses" incurred by the "hobby" businesses of the wealthy. These loopholes alone are worth an estimated $1 billion a year.

Finally, the government dropped the pretence that the outcome of the Ralph review would be "revenue neutral". Originally Howard and Costello claimed that by abolishing other business tax concessions, they would offset the corporate tax cuts. This provoked considerable conflict within ruling circles, with the finance sector demanding that the government go further by reducing social spending to finance the tax cuts.

In the end, after much haggling between different corporate interests, the government did offset part of the corporate tax cut by axing the accelerated depreciation allowance—an allowance that enables capital-intensive industries, such as mining and manufacturing, to claim massive tax write-offs for the cost of their equipment.

But the package retained huge tax breaks for mining companies on the cost of what is known as overburden removal. It also introduced a totally uncosted "case-by-case" investment allowance that the government will use as a sweetener to attract large projects.

The net result is what the *Financial Review* describes as a "gaping revenue hole". By the fifth year of the new plan, some economists say the gap could amount to $4 billion a year, despite the government's own rosy forecasts. This is on top of the yawning "black hole" created by July's income tax cuts—estimated at $11.5 billion by Steve Burrell of the *Sydney Morning Herald*. Inevitably the government will insist that spending on welfare, health, public housing and education must be reduced further to make up this shortfall.

The overall revenue gap will almost certainly be larger because the government's calculations are based on the highly dubious assumption that the business tax cuts will fuel economic growth and hence raise the tax intake. Costello claims that the cut in the CGT will exactly double the level of asset buying and selling and therefore neatly pay for itself. Even the generally enthusiastic media pundits described this assertion as "heroic". Ernst and Young tax partner Richard Snowden called it "pie in the sky stuff". In the 1980s the Reagan administration in the US made similar assertions and its program became known as "voodoo economics".

Just days before releasing the tax plan, Costello warned that the costs of the military operation in East Timor, and of boosting the defence budget in the long-term, would require belt-tightening. But there was no suggestion of halting the multi-billion dollar tax handouts to the rich.

The corporate media largely welcomed the achievement of an "internationally competitive tax regime". With a 30 percent corporate tax rate, Australia matches Singapore, Germany and Britain. It is lower than the 42 percent charged in Japan and the US. In Asia, only Hong Kong, with a 16 percent rate, offers a more lucrative deal.

Yet, many commentators and editorials immediately declared that the process of "reform" had only just begun. Costello's plan was "too little, too late" to entice overseas investors much, said Peter Carre of Wilshire Global Advisors. "Still not the last word on reform," stated the *Financial Review* editorial. "Where to next?" asked the *Sydney Morning Herald's* Steve Burrell.

Answering his own question, Burrell said global pressure would force further changes. He identified payroll tax and superannuation taxation as the next targets, as well as even lower income tax levels at the upper end. In fact, as he pointed out, the government's tax plan contains its own in-built pressure for a "flatter" income tax scale, precisely because high income earners will sharply lower their taxes anyway by turning themselves into companies.

In releasing the package, Costello claimed that it would generate "investment and jobs". The truth is that any investment will be largely speculative and parasitic, and it will accelerate the destruction of jobs. The Australian Stock Exchange chief executive Richard Humphrey said the package would "facilitate corporate restructuring that is vital for continuing Australia's productivity growth". The Ralph report itself predicts a 125 percent increase in takeover activity in the first year and 70 percent thereafter.

The two official opposition parties, the Labor Party and the Australian Democrats, initially backed the tax package and indicated that the government could expect a reasonably swift passage of the necessary legislation through both houses of parliament. Labor's shadow treasurer, former ACTU president Simon Crean, stressed his party's support for lowering the capital gains and company tax rates. Labor's Bob Carr and Michael Egan, the Premier and Treasurer of New South Wales respectively, enthused that the package would help make Sydney a global financial centre.

Later in the week, the Labor leaders sought to distance themselves slightly from the package, while still pleading with the government to strike a deal that would enable them to join hands in pushing the tax cuts through before the October 1 deadline for their implementation. Inside parliament, Costello made fun of Crean's efforts to criticise aspects of the CGT scheme while pledging to help pass the legislation as quickly as possible. Outside parliament, Labor leader Kim Beazley offered to work with the government to fix the revenue hole.

For electoral purposes, both Labor and the Democrats posed as opponents of the massive tax cuts delivered to high income earners two months ago in the first instalment of the tax plan, which featured the introduction of a highly regressive 10 percent Goods and Services Tax (GST). The Democrats ultimately struck an agreement with the government to introduce the GST, leaving the Labor leaders to caste a symbolic vote against.

This time, Labor's leaders are determined to be part of the tax "reform" alliance, seeking to reclaim the backing of the corporate world that they enjoyed during 13 years in office from 1983 to 1996. At the same time, they are courting the support of the "aspirational layers" who stand to gain from the tax “revolution”—the 20 percent of the population who take home nearly half the country's income.