

Review of Tax Impediments to Small Business
Board of Taxation Secretariat
C/- The Treasury
Langton Crescent
PARKES ACT 2600
By email to: taxboard@treasury.gov.au

4 June 2014

Dear Sir/Madam,

The Regional Australia Institute (RAI) provides this short submission to the Board of Taxation on the tax impediments to small business. While it would not be in the normal course of business for the RAI to put in a submission on an issues as specific as small business tax impediments, the RAI does have staff with considerable experience and expertise in small business taxation issues and felt it important to provide information on previous work undertaken in this area that could be useful for the Board's deliberations. While both scope and time constraints have resulted in this submission being very brief, the RAI would welcome the opportunity to discuss any of the issues raised.

Background

The RAI is an independent policy think tank and research organisation dedicated to regional issues. The majority of businesses operating in regional Australia are small businesses and as such, taxation has a significant impact on businesses in regional Australia. While corporate Australia has a major footprint across regional Australia, through enterprises such as the banks and Australia Post, they are primarily head officed in a major city and therefore the taxation impacts are less likely to be differentiated across the regions.

Compliance costs

The compliance burden of taxation represents a significant burden for small business and the cumulative burden of compliance is quite often the 'straw that breaks the camel's back'. A major piece of work was undertaken for the Office of Small Business, in the then Department of Industry, Tourism and Resources in 2005 that sought to identify the cumulative compliance burden on small business in four industry sectors – retail, hospitality and catering, primary production and building and construction. While the actual dollar value of the compliance burden identified in the report would be dated, the relative burden remains and would have increased significantly over time. There are also additional regulations that have been implemented since this time that add to the cumulative burden on small business.

The compliance requirements to starting a business are immense and a large impediment for small business. Taxation issues form a large part of this. While attempts have been made over the years to provide a 'one stop shop' for small business and start-ups, there is still a plethora of regulations and requirements that small business needs to navigate and lack of knowledge, particularly in the micro and home based business sector, is high. Work undertaken in conjunction with the compliance burden project mentioned above examined attitudinal responses to small business compliance and the consequences of particular remedies on small business behavioural response. The Review panel should be able to access both these reports from the small business division now located in The Treasury.

More recent work undertaken by Philip Lignier and Chris Evans, *The rise and rise of tax compliance costs for the small business sector in Australia*, also provides relevant data about the compliance burden of the tax system on small business.

Some specific taxation impediments to small business that relate to compliance costs include:

- CGT small business concessions – these are complex and require specialist advice – something that many small business in regional Australia may not have access to;
- FBT – small business seeks to stay out of the FBT system by ‘cashing out’ the value of the fringe benefit however this is a high compliance burden and once again requires specialised advice; and
- GST compliance – removal of exemptions from the GST system would simplify compliance for small business.

In addition, it is worth mentioning the Alienation of Personal Services Income and Non-commercial Loss regimes. The regulatory outcome of both these regimes is not questioned, however the design of the law and consequent drafting of the provisions have resulted in both these regimes being highly complex, resulting in a high compliance burden.

Regulatory impacts

While a robust regulatory impact analysis process was introduced in 2007, adherence to this by Australian Government departments and agencies and politicians has been poor. The requirement to include a Small Business Statement as part of the Regulation Impact Statement (RIS) is rarely done, and like the RIS itself, little importance is attached to need to undertake adequate impact assessment.

What is required is a genuine commitment to identifying and costing the compliance burden on small business. There are questions as to whether pursuing a small business statement, along with a regional impact statement in the RIS is effective unless and until there is a strong commitment by Ministers and heads of government agencies to reduce the red tape on small business. Without such a commitment the impact on small business of government regulations, including taxation will be largely ignored and government will continue to bear the brunt of complaints and require ongoing reviews.

Small business tax entity

The RAI has turned its mind to a possible solution, given that small business compliance costs and the burden of taxation are perennial issues.

Many of the complexities in the tax system relate to the legal structure that a business uses to operate their business. While many small and micro businesses operate as partnerships, there is a growing trend, driven primarily by accountants and advisors, to structure the business through a complexity of trusts, bucket companies and self-managed superannuation fund. This structure seeks to protect assets and enables the splitting of income, however brings with it significant compliance, accounting and legal cost that are not just one-off but are ongoing. Consideration could be given to the creation of a small business entity or structure for taxation purposes. Such an entity conceivably could be extended for other purposes, such as workplace relations.

From a taxation perspective, such an entity could provide access to the STS, CGT small business concessions, GST simplified reporting and relief from FBT. The flow through of income could be allowed and a differential entity tax rate could be considered.

In the mid 2000's research around a small business taxation entity was undertaken for the Office of Small Business and for the Minister for Small Business at the time, the Hon. Joe Hockey MP. This work examined the S corporation regime in the US and Limited Liability Partnerships used in the US and the UK. These regimes provide a simpler structure for small business that provides a shield against personal liability, while allowing income or losses to be passed through to individuals, similar to a partnership.

Conclusion

The compliance burden on any business is an impediment to competitiveness and productivity, however in the case of small businesses, particularly those operating in regional Australia, these impediments are magnified. Tax impediments constitute a major part of the overall compliance burden, and add to the cumulative compliance burden.

The RAI would be happy to discuss any of the points mentioned in this short submission, or discuss the tax impediments more broadly to small businesses operating in regional Australia at a time that is convenient to the Review panel.

Yours sincerely



Su McCluskey
Chief Executive Officer

su.mccluskey@regionalaustralia.org.au