10th May 2002

The Board of Taxation
C/- The Treasury
Langton Crescent
PARKES ACT 2600

SUBJECT – JOINT SUBMISSION ON THE TAX VALUE METHOD

This joint submission is made by the following organisations, all of whom were members of the TVM Working Group established by the Board of Taxation to provide business input into the legislative development of the TVM proposal. The organisations, in alphabetical order, are as follows:

- CPA Australia
- Law Council of Australia
- National Farmers Federation, and
- Taxation Institute of Australia

The submission is made in response to the invitation by the Board of Taxation for submissions on the current version of the Tax Value Method proposal (Prototype 4, released 6 March 2002).

We would like to acknowledge at the outset the open and inclusive consultative process that the Board has overseen. We appreciate the opportunity to participate in that process and to make this submission.

This submission is intentionally brief. Many of the technical issues surrounding the operation of the TVM proposal that might have been raised in a submission have already been raised by our representatives with the Board through the consultative forums and Working Group established by the Board. Although there is an argument that these concerns should be put on the public record as part of the process, we have chosen to not do so through this submission. Instead, this submission will focus on our key conclusion and the reasons for it.

We have carefully followed the development of the TVM proposal over the last 3 years from its exposure in embryonic form in the Overview to the Review of Business Taxation's paper, *A Platform for Consultation* (1999) to the current iteration of TVM in the Demonstration Legislation (Prototype 4), Explanatory Material and Information Paper. We have all also been actively involved in the work over the last two years on further developing the TVM proposal, and participated in detailed briefings on the TVM proposal. We believe the TVM proposal has now been developed to a stage where we can reach a considered view about its merits with confidence based on a robust understanding of the TVM mechanism. Our assessment of the TVM proposal is that it is structurally flawed, and also is unlikely to provide enough benefit to the community to justify the cost that it will entail.

The model is flawed

The key attribute of the TVM model is that it would provide a more principled approach to law development for the future. However this proposition does not hold true, as the theoretical underpinnings of the model are flawed and incorrect. TVM fails in this task as it requires special rules for some ordinary transactions rather than a straightforward application of the methodology. While government policy may result in circumstances that require an acceptable need to draft exception rules, in all other circumstances the transaction should be dealt with under the core rules and this is not the case with the TVM.

TVM involves real, substantial and certain costs expended pursuing uncertain, implausible and unquantifiable benefits

If the reform of the Australian income tax system were starting from scratch, the TVM proposal would obviously deserve serious consideration. But this is not reality and so a considered judgment must be made whether the costs of the TVM proposal would be sufficiently small or uncertain and the benefits sufficiently large to warrant the effort involved in the change.

It is abundantly clear that the costs of the TVM proposal, both transitional and ongoing, will be real, substantial and certain. Those costs have been outlined elsewhere - we note just a few here: purging at one stroke the confidence drawn from 70 years of tax case law and accepted administrative practice, eradicating all current tax private and public rulings, and requiring extensive rewrites, and imposing the substantial transitional costs associated with re-establishing current business tax systems and compliance programs. These costs are real, certain and will inevitably prove substantial.

On the other hand, the assurances that TVM will deliver real and substantial benefits are not convincing. In our view, many of the benefits claimed for TVM are uncertain or implausible. At present, all are unquantified. Some are probably unquantifiable, but others which might be rigorously tested have not yet been. In particular, we doubt the claims that TVM will reduce compliance costs and the current levels of complexity in the income tax system.

Moreover, while it is unfortunate, doubts about the benefits of the TVM proposal are only heightened when TVM is supported by claims which are either demonstrably false or else greatly exaggerated.

We acknowledge that benefits might be possible from TVM, but it is not certain they will be significant, and they have not been convincingly demonstrated or quantified. Instead, exaggerated claims have been made.

A new agenda for tax reform

Hence, we submit that the Board should terminate further work on the development of the TVM proposal and advise the Treasurer accordingly.

However it is vital that work on tax reform should continue under the Board's auspices because important and valuable lessons have been learned from the TVM consultative process. We would strongly encourage the Board to redirect the resources currently devoted to the TVM proposal to exploring other options for the reform of the income tax system. In particular, work should continue on ways to deal with compliance costs and complexity. This work should also include the unfinished business of establishing an integrated tax code and the subsuming of the now almost forgotten TLIP as proposed in the government's 1998 plan for a new tax system *Tax*

Reform: not a new tax a new tax system. We would be keen to support the Board in developing further short-term and long-term projects for achieving a more certain, stable and robust income tax system.

Sincerely

Mr Greg Larsen
CEO
CPA Australia

Mr Tony Abbott
President
Law Council of Australia

Mr Ian Donges
President
National Farmers' Federation

Mr Barry Low
President
Taxation Institute of Australia