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The White Paper Task Force
The Treasury
Langton Crescent
PARKES ACT 2600

To the White Paper Task Force,

BP welcomes the opportunity to participate in this initial discussion on the Australian Government's Tax discussion paper "Re:think". Tax reform is a considerable lever to actualise the economic and social changes required to maintain Australia's prosperity. The Intergenerational Report, Federation White Paper and Tax discussion paper present a trilogy of necessary reforms to stimulate economic growth and maintain Australia's high standard of living. We commend the government for initiating this discussion for indeed it is critical and necessary and will allow Australia to participate constructively and profitably in the future. Instigating reform requires substantial public support and trust, as well as strong and effective leadership. In this submission we have included a 10 point plan for the Task Force to consider. This is a plan that may take reform from paper to practice in a simple, efficient manner.

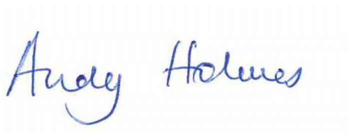
BP values the process of reform development and implementation as much as the policy settings themselves. We believe the actual process can have a positive impact on business and consumer confidence. A broad and comprehensive consultation process is conducive to a favourable outcome; this requires working openly and collaboratively with the state and territory governments and key representative bodies from society and business. Indeed, before leaping to the assumption that taxes should realign to match expenditures, we should consider whether expenditures are being undertaken at the right level. Hence tax reform must align with accountabilities agreed under the Federation White Paper. A more inclusive and collaborative process would build trust and assist political expediency and passage of future reform. It would also enable business to invest with more confidence that a better, fairer and more competitive tax system will be delivered over time. The options paper outcome should present all recommendations and include a five-year road map for reform so all Australians have the opportunity to engage and participate.

BP's *Energy Outlook 2035* projects that world energy demand will rise by 37 per cent, led largely by the Asia Pacific region with demand for all fossil fuels expands over this time led by gas (+99%), oil (+41%) and coal (+38%) and presents an exceptional opportunity for Australia to continue to capitalise on this transformational economic era. Competition for capital is intense as countries seek to meet their energy demand and Australia needs to be supported by a more competitive tax system to maintain and grow its position in the global market. The tax system should not be a barrier to investment but rather an incentive. Tax policy should be diverse, responding appropriately and fairly to drivers of current economic growth such as commodities as well as stimulating new, economic activity.

BP wants to see this reform succeed. As committed long-term investors in the Australian economy, a simple, competitive and fair system that encourages economic growth is a most favourable investment environment. We look forward to an ongoing discussion with Treasury that draws on our global tax expertise through this reform development process.

If you have any questions on this submission, please feel free to contact me or John Condon on 03 92683219.

Yours sincerely,



Andy Holmes

Executive summary

The federal budget papers reveal that the rate of spending growth to gross domestic product (GDP) is outstripping the rate of taxation revenue growth to GDP by some three per cent per annum. This is a significant issue that the Australian Government must respond to in order to safeguard the Australian economy and maintain the current standard of living.

As CPA noted in their February 2015 *Tax Reform in Australia – The Facts* report, Australia has one of the lowest goods and services tax (GST) rates and one of the highest dependencies on income taxes in the Organisation for Economic Co-operation and Development (OECD) (see a comparison of GST rates in Appendix 1). Given income taxes from large businesses can vary dramatically, often impacted by fluctuations in commodity prices and the Australian dollar, the ideal tax mix would mitigate these variances in taxation revenue and reflect a modern economy engaged with the world.

We believe Australia needs a tax system that is resilient to economic environmental pressures such as commodity market shocks, delivers lower, simpler and fairer taxes while still balancing the budget and supporting high levels of economic growth.

BP is encouraged by the federal government's appeal to Australians to "have a go" and developing policy settings that will drive economic growth through greater participation, innovation, and productivity. In response BP suggests the following complementary 10 point plan for consideration.

Our **10 point plan** is:

1. Build investor confidence that the federal, state and territory governments can work together to bring revenue and expenditure growth back into balance over time.
2. Fall in line with most of the developed world by shifting the burden of taxation more towards consumption and less towards personal and corporate tax to encourage growth. In the short term commit to GST reform and signal the rate is too low and the base is too narrow and is undermining the ability to maintain living standards. In the longer term, commit to returning bracket creep in a fair and transparent way that encourages greater participation and older people staying in the workforce longer.
3. Address vertical fiscal imbalance (VFI) in the first instance by seeking efficiencies in which the states and territories deliver their routine services through national collaborative agencies rather than the current costly duplication of transactional agencies.
4. Reach agreement with the states to harmonise one or two efficient state taxes (e.g. payroll tax and land tax) across the nation before the options paper is released to help build momentum and confidence.
5. Abolish "nuisance" state taxes to create a consistent investment culture in Australia.
6. Address issues of inequality in the tax system so that the community feels the government is responding to restrict excessive benefits, i.e. those not necessary to maintain living standards in retirement.
7. Pursue simplification of the downstream fuel excise regime to reduce unnecessary complexity and costs for Australian Taxation Office (ATO), Customs and industry.
8. Confirm a commitment to continue to improve deductibility of exploration expenditure for the resources and oil and gas sector so that it is aligned to competitor jurisdictions.
9. Commit to retain a competitive corporate tax rate in light of actions by other countries and or a multilateral agreement on the OECD base erosion profit shifting (BEPS) action items; and,
10. Simplify and make certain petroleum resource rent tax (PRRT) with amendments that confirms deductibility of feasibility costs, including costs incurred in unsuccessful designs and allow automatic project combinations for "common operating developments".

As a priority all levels of government should work together to improve the efficiency of taxes to promote economic growth and allow all governments more predictable revenue. As such BP supports the work being pursued through the Federation White Paper and recommends that the two discussions happen in tandem. This includes harmonising the more efficient state taxes (i.e. payroll tax and land tax) and actively exploring increasing the rate and base of the GST.

The real opportunity to address revenue needs of the states and improve the efficiency of the tax system overall is to recognise what many other countries have already done by increasing the rate of GST. Even if the rate was increased to 15 per cent it would still be well below the average OECD rate of 18 per cent. If the base of the GST was broadened and the rate increased, we believe inefficient state taxes including insurance taxes and motor vehicle taxes (stamp duty and motor vehicle registration) and the state reliance on stamp duty on residential and commercial property (thereby improving housing affordability and labour mobility) can be addressed.

BP suggests state and federal governments should align on the optimal tax mix and harmonise efficient state taxes across the nation. This harmonising reform of the more efficient state taxes together with increasing the rate and base of the GST (one of the most efficient taxes), would go a long way to addressing the fiscal challenge facing the nation.

BP's *Energy Outlook 2035* projects that world energy demand will rise by 37 per cent, led largely by the Asia Pacific region with demand for all fossil fuels to expand over this time led by gas (+99%), oil (+41%) and coal (+38%) and presents an exceptional opportunity for Australia to continue to capitalise on this transformational economic era. Competition for capital is intense as countries seek to meet their energy demand and Australia needs to be supported by a more competitive tax system to maintain and grow its position in the global market. We believe it is important for Australia, as a relatively small and open economy, to respond in the medium term to the changing competitive tax landscape. We recognise adjustment to corporate tax is a sensitive issue for the government given the over reliance on corporate tax revenue from existing investment. However a lower corporate income tax rate over time will give meaning to Australia "playing to its strengths" and capturing a disproportionate share of demand for resources from Asia.

Australia has a relatively high corporate tax rate and existing thin capitalisation provisions for the infrastructure intensive industries partly offsets this rate while imputation creates a competitive system for domestically focussed companies. However, if Australia implemented further changes to thin capitalisation rules, e.g. following the OECD BEPS work, this will add pressure to reduce the comparatively high corporate tax rate if it is to remain competitive in the infrastructure led industries (e.g. mining and oil and gas).

Joining the National Conversation on Tax Reform

BP agrees with the opportunities available in undertaking the White Paper review. Our initial comments are provided below.

1. The time for a national conversation on tax reform is now

BP agrees that now is the time for a national conversation on tax reform, given the decline in income growth and that bracket creep is becoming acute, to allow for a proper debate on options and trade-offs to improve upon the existing system.[i] Of immediate concern to Australia is the precarious state of federal and state government budgets.[ii] Current spending is outstripping revenue and interventions are required on some spending and tax areas to bring confidence that Australians are living within their means. As outlined in the Henry Tax Review, the tax and transfer architecture is overburdened and beginning to fail in dealing efficiently and effectively with multiplying policy goals and demands. Without acting now Australia risks a future budget crisis that could jeopardise living standards of present and future generations. Designing and implementing tax policies to improve upon the existing system and encourage higher productivity and growth will underpin future living standards and investor confidence.

The global economy is rapidly changing particularly in the energy sector and BP agrees this requires a national conversation on how Australia responds. The changes are not just cyclical, but rooted in a deep structural change created by the urbanisation and industrialisation of Asia, and changes in the energy mix and balance of demand shifts.[iii] As a relatively small and open economy, Australia cannot ignore actions by other countries on corporate tax, particularly as free trade agreements are being negotiated. A more competitive and stable tax system should encourage further foreign investment but doing nothing raises investor concerns about future tax surprises.

2. We need to keep the economy growing to safeguard our way of life

Australians today generally enjoy a unique and high standard of living. In 2014, four of Australia's cities were ranked in the top ten most liveable cities in the world.[iv] Australia is also in its 23rd year of consecutive economic growth. We recognise this quality of life has been hard-won but has also been assisted by increased demand for Australia's resources from Asia.

Examples of collaborative engagement of governments and business working together that have helped shape this way of life include tariff and subsidies reform, major infrastructure developments (national roads, snowy mountain hydro scheme), improved industrial relations and competition policies, introduction of the GST and steps towards *Closing the Gap* in Indigenous Australian communities.

BP agrees Australia needs to safeguard its way of life and develop good policies to support sustained long-term economic growth. Threats to continued high living standards include but are not limited to an ageing population, lower commodity prices, competition from other countries capital investment, unsustainable health and education costs, increasing levels of household debt, and complacency.

Growth in the economy will support governments, business, civil societies and the wider community to respond to these threats by creating greater resources, skills and financial capacity to respond. Growth can come from a number of sources such as higher participation and a more mobile labour force, increased productivity, a more efficient tax mix, trade and foreign investment. Getting the tax mix right and making improvements in our existing system to improve competitiveness and encourage more people into work and to stay in the workforce for longer are critical to success and building confidence.

BP observes recent analysis by the Grattan Institute that suggests improving the tax mix is one of three things that has a significant positive impact on economic growth well beyond other measures.

3. Our tax system needs to support the modern economy

BP recognises the need for governments to have a predictable and sustainable revenue stream to support the delivery of essential services and for the tax system not to unnecessarily distort economic activity. This balance needs to reflect the modern economy. Where the tax mix overly relies on profits based taxes, governments will be unable to comfortably predict reliable revenue streams where profits are subject to volatility e.g. commodity prices and exchange rates. Where the tax mix under-utilises consumption based taxes, governments miss an opportunity to gain a more reliable and predictable revenue stream without materially jeopardising economic activity.

4. The Government's review of roles and responsibilities across the Federation provides a once-in-a generation opportunity to examine the whole of the tax system

Any tax reform discussions should be considered alongside the Federation White Paper to ensure a holistic approach is undertaken given inextricably linked federal and state government taxes and services. We also believe the consideration of the federation and tax at the same time is a unique opportunity to address VFI and horizontal fiscal equalisation (HFE).

As a priority, removing duplication in government services will reduce the cost of government. Nevertheless, BP does recognise there will be examples where duplication is necessary in terms of providing states with the power to take actions. The transformative effect of modern information technology in diminishing the impact of geographical distance needs to be fully taken into account. Information technology – in particular the ability to rapidly process large amounts of data – enables both greater complexity in decision making as well as greater centralisation of service delivery and implementation. For example, Australia has eight different state and territory vehicle licensing agencies. Their work is entirely non-contentious, except for the decision of state governments on what vehicle registration fee to charge. Information technology would allow each state and territory to make its own decision on motor vehicle registration fees if these had to stay post reform, with a single national agency implementing their decisions, collecting fees and distributing licences on a postcode basis. There are a host of routine administrative government actions that could be centralised in this way without eroding state decision making autonomy, and in the process VFI will be reduced and net efficiencies captured.

This means that an innovative rethink between centralised federalism and decentralised state autonomy is emerging (e.g. Infrastructure Australia) – one in which national (not necessarily federal) agencies are accountable for delivering government tax and spend activities from an *a la carte* menu available to the states, who continue to make policy decisions within boundaries. BP believes this creates three choices to debate to achieve government funding from tax collections. These are:

1. Centralise revenue collection and policy decision making over tax bases and tax rates and distribute an agreed percentage of the total revenue to the states to spend as they wish;
2. Centralise policy decision making over tax bases and rates and policy expenditure, but decentralize decision making to allow the states to continue to define rates and policy service levels from an *a la carte* menu;
3. Decentralise decision making and collection by reversing the post-war trend of centralisation to the federal level.

BP recommends as an interim step, and in order to build reform momentum and trust, that the federal government collaborates with the states on the second option and choose one or two existing state taxes, e.g. payroll tax and land tax, to nationalise under one law for each. Harmonisation of policy measures like this, if successful, would create an opportunity to extend the approach to other state taxes that are considered efficient and part of the mix of taxes to retain (e.g. resource production royalties).

As importantly, since consumption taxes need to shoulder a greater share of the burden of revenue raising in Australia, governments should consider increasing the rate and broadening the GST while still keeping it at a competitive level within OECD nations. Reforms such as these would need to be part of a *quid pro quo* for the abolition or reduction of inefficient state taxes: e.g. commercial transfer duty, residential transfer duty, fire insurance levy, motor vehicle stamp duty, insurance duty and motor vehicle registration fees. We refer the Task Force to KPMG's 2011 publication *Economic analysis of the impacts of using GST to reform taxes* (appendix 3).

Once policy over tax bases is harmonised, future reforms to broaden and or lower rates can be more easily achieved. BP sees merit in local governments continuing to be able to set and collect municipal taxes to fund their services.

5. The tax systems raises the revenue required to fund public services

BP recognise the requirement to have efficient, reliable and predictable revenue streams to support funding of essential public services. Please refer to our responses in two and three above.

6. There is evidence that the economic costs of revenue-raising in Australia are higher than they need to be

BP recognise that all taxes cause an economic burden reducing economic growth. Empirical evidence suggests that some taxes are worse than others. It is referred to as the relative economic burden of a tax. Income taxes tend to have a greater relative economic burden than consumption and land taxes. BP agrees that in order to raise revenue in an economically efficient way the mix of taxes should have the lowest impact on economic growth over time and raise sufficient revenue for governments despite commodity price and foreign exchange rate fluctuations.

For example, a road map to reform over the next five years could see a commitment to broaden the base and increase the rate of GST (gradually over time); harmonise the more efficient state taxes nationally (including uniform exemption thresholds for payroll tax); reduce and abolish inefficient state taxes; adjustments to deal with bracket creep on Pay As You Go (PAYG) staged over time; and a commitment to reduce the corporate tax rate to remain competitive internationally.

Gradual change will help the community manage transition and also the government to make any adjustments along the way as circumstances change. Smaller amendments across a number of tax bases over time reduces the negative impacts of more significant changes to one or two taxes alone. It would also improve investor confidence that surprise material ad hoc changes will not occur. A plan to control government spending over the same time is equally important with the private sector shouldering more of the burden for economic growth.

7. There are opportunities to simplify the tax system

There are areas of tax law that could be simplified. BP supports the federal government's announcements for small business allowing immediate deductibility for costs of up to $20,000. The closer the income tax system can be to cash flow taxation the more economically efficient the system will be (i.e. tax will not distort decision making).

As highlighted in the BCA's *The Future of Tax: Australia's current tax system* publication (2014), 10 taxes raise approximately 90 per cent of Australia's tax revenue, while around 115 taxes raise the remaining revenue. There is great complexity associated with managing and administering all of these taxes and where a tax generates little or no revenue it should be abolished, e.g. onshore condensate and oil excise.

Amendments to PRRT to simplify the system and reduce disputes and uncertainties are clearly needed. The progress on the ATO's updated income tax ruling dealing with exploration expenditure highlights a gap with the interpretation of exploration for PRRT purposes. If alignment is not possible, a new category of PRRT expenditure is probably required to recognise feasibility costs or the definition of general project expenditure should be expanded to include feasibility costs incurred prior to a production licence being granted. BP believes that as feasibility is incurred without knowledge that the development will proceed, the costs should be transferable and so would prefer a separate new cost category. The augmentation rate could align to general project expenditure.

Another PRRT simplification would be to take the new concept of a "common operating development" being introduced for income tax tenement re-alignment rollovers and use this to determine the definition of a PRRT "project" without having to go for the Federal Minister's project combination approval. This is important to ensure feasibility studies that go into design concepts that are subsequently rejected do not fall into a "black hole" but ultimately still form part of a project that goes ahead under a different design concept. Also, it allows for full recoverability of costs in all parts of the project before a PRRT liability arises and simplifies compliance.

Another opportunity for simplification is in downstream fuel excise. There is a very strong case for reform. Dual administration, weekly settlement of duty, licencing of storage warehouses and the under-bond system reflect an outdated system that does not take advantage of modern business practices and technology. We believe the government should work with industry to significantly simplify compliance by moving the taxing point to ex refinery or import of product and payment aligned with filing of the monthly GST business activity statement (BAS). Transition terms should be determined in consultation with industry to reduce any negative impacts of change for either the industry or government.

8. There are opportunities to improve the fairness of the tax system

BP believes that Australia's tax system today is relatively fair for individuals. Progressive marginal tax rates, high tax free threshold, low income rebate, and targeted social security all contribute to a relatively fair system. We note these elements in addition to relatively high minimum and high average wages makes investment in Australian more costly than many other countries. Despite the relatively favourable and fair system today for individuals, there are, however, increasing concerns about the fairness of superannuation tax benefits and the relatively higher tax burden the younger generation shoulders compared to the older generation because of super concessions. As discussed in PWC's 2014 publication *Protecting our prosperity series*: *How do we fix a tax system,* 'Failure to find sustainable ways to fund important social policies, or to address intergenerational inequities in current tax and transfer arrangements, may increase the economic burden on our children and our children's children (appendix 4).'

BP encourages the government not to look at super concessions in isolation but to consider what a mature superannuation system should look like in 25 years' time, how much reliance is placed on it compared to other savings options and the pension. Any reforms in this area should be evaluated with other savings incentives like negative gearing, the capital gains tax (CGT) discount and principal residence exemption. We note New Zealand is taxing gains on the sale of principal residences when sold within two years. As a general principle BP believes where existing incentives are targeting wealth creation to maintain independent living standards in retirement, these should be retained. But excessive benefits should be restricted particularly if this increases scope to be more competitive on corporate tax to partly offset higher Australian wage costs for investors.

We also recognise there are community concerns around fairness of the system with a perception that large multinational companies may not be paying their fair share of tax and so contributing to contraction of public services. In order to address this concern BP supports the government's involvement and leadership in the OECD's BEPS action plan and further disclosures by companies to explain their tax profile. The more companies can do to demonstrate their commitment to compliance the more confidence and voluntary compliance there will be from everyone.

BP is supportive of a multilateral, uniform tax agreement that addresses BEPS concerns. It is not in Australia's interest to address this issue unilaterally as such measures encourage other countries to also act unilaterally and so increase the risk of double taxation. We do however support the Australian Government's strong measures in the budget as a leadership position for OECD to consider particularly the caveat on deemed permanent establishments that this only applies if income is otherwise assessable in a low tax country.

9. The tax treatment of savings is very complex and distorts savings choices

This is a complex and sensitive area. We encourage the government to engage in consultations with a broad spectrum of the community and look at policy settings that take a longer term view. If Australia's superannuation system is still relatively immature, then tinkering with policy may encourage individuals to take more risk outside the system. Any revision of savings policies should have regard to changes in circumstances to when the policy was originally enacted. This would help explain the rationale for discussion about reforms that may be needed. Any reform should consider the impact on economic activity and not unfairly disadvantage one sector over another.

10. Transitional arrangements are important

As above, an inclusive and open consultative process followed by incremental reform over time will reduce any negative impacts of change. Transitional arrangements may be necessary in some areas to ensure investor confidence in decision making and the path forward on tax reform.

Conclusion

BP is pleased to offer these initial responses to the Government's "Re:think" discussion paper. We would be pleased to make more specific comments on options for reform as the government's consultation process continues and work with government and industry on any specific proposals that could impact the oil and gas industry. We are committed to Australia and wish the government and all stakeholders well on endeavours to make Australia an even better place to live, invest and grow.

Appendix 1

VAT/GST rates in OECD 1 January 2015			
Country	**Rate**	**Country**	**Rate**
Canada	5	Netherlands	21
Japan	8	Spain	21
Switzerland	8	Italy	22
Australia	10	Slovenia	22
Korea	10	Greece	23
Luxembourg	17	Ireland	23
New Zealand	15	Poland	23
Mexico	16	Portugal	23
Israel	18	Finland	24
Turkey	18	Denmark	25
Chile	19	Norway	25
Germany	19	Sweden	25
Austria	20	Iceland	24
Estonia	20	Hungary	27
France	20	Malaysia	6
Slovak Republic	20	Singapore	7
United Kingdom	20	Indonesia	10
Belgium	21	China	17
Czech Republic	21	**OECD average**	**18.19**

Appendix 2

KPMG
Getting the message across – Taxation contribution of the oil and gas industry in Australia, May 2015
APPEA Conference and Exhibition 2015
http://www.kpmg.com/AU/en/topics/Tax-Reform/Pages/Default.aspx

Appendix 3

KPMG
Economic analysis of the impacts of using GST to reform taxes
September 2011
http://www.cpaaustralia.com.au/~/media/corporate/allfiles/document/professional-resources/taxation/kpmg-econtech-final.pdf

Appendix 4

PwC
Protecting our prosperity series: How do we fix a tax system?
April 2014
http://www.pwc.com.au/tax/taxtalk/assets/monthly/pdf/Protecting-prosperity-Apr14.pdf

Annexure 1

About BP

BP is one of the world's leading integrated oil and gas companies. Our strategy is to be a focused oil and gas company that delivers value over volume by setting clear priorities, actively managing a quality portfolio and employing our distinctive capabilities. We play to our strengths and focus on projects and operations that generate the most value. Australia forms part of this highly valued portfolio as demonstrated by our extensive operations that cover upstream and downstream businesses, from exploration and production to refining and marketing.

We have been a participant in the North West Shelf Joint Venture since it began production in the 1980s, and it represents an investment of more than $A33.5 billion and accounts for more than one-third of Australia's oil and gas production. In South Australia, BP has four exploration permits covering 24,000km^2 in the Great Australian Bight and as the operator in our joint venture with Statoil, we plan to drill our first well in 2016. Other upstream operations include being a participant in the Browse Joint Venture gas project, and holding interests in the Greater Gorgon area.

BP's oil refinery in Kwinana has a 138,000 barrels per day crude distillation nameplate capacity and has been in operation since 1955, with this year marking its 60th anniversary. Fuels produced at the refinery are used in road, rail, air and marine transport as well as off-grid power generation and other diesel plants.

The recent changes announced in our fuel supply chain management reflect BP's response to a rapidly changing downstream landscape and the challenging external environment. We are repositioning our business to focus our investment towards our customers. These changes go beyond restoring our competitive edge. We are reinventing our business to be more responsive to our customers and become the most preferred fuel brand in Australia and New Zealand. We are the last remaining fully integrated global oil company, and there are some 1,400 BP branded service stations across Australia and we continue to expand our presence in this market.

Given our extensive Australian operations, BP is a significant tax payer. The effective tax rate paid by BP has consistently been at or above the 30 per cent statutory tax rate.

BP is a member of the following industry associations and is supportive of their comprehensive tax review submissions that capture a myriad of recommendations relevant to its members: APPEA, Business Council of Australia (BCA), Corporate Tax Association (CTA) and the Australian Institute of Petroleum (AIP). We also contribute in an advisory capacity to the Board of Taxation.

[i] Daley, J & McGannon, C 2014, *Budget pressures on Australian governments 2014,* Grattan Institute, May 2014

[ii] Business Council of Australia 2014, *The Future of Tax: Australia's current tax system,* September 2014

[iii] BP 2009, *In the jaws of prosperity: Challenge for Australian energy policy in a new economic era: Recommendations from BP Australia to the 2009 Energy White Paper process; and*
BP 2015, *Energy Outlook 2035,*

[iv] The Economist Intelligence Unit 2014, *A Summary of Liveability Ranking and Overview,* August 2014