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Dear Sir/Madam

Pre-Budget Submissions 2020-21: Opportunities to support growth for Mid-Sized Businesses

We refer to the Media Release dated 30 September 2019 by the Australian Federal Assistant Treasurer, the Honourable Mr Michael Sukkar MP, seeking submissions from individuals, businesses and community groups on their views for priorities for the 2020-21 Budget due by 20 December 2019.

We set out below our pre-Budget submissions and, as a supporting document, our report dated May 2019 entitled: "The overlooked opportunity in Australia's mid-sized business".

In summary, we submit that Government policy in the coming Federal Budget 2020-21 and indeed future Budgets can take advantage of a so far overlooked economic opportunity to encourage Australia's Mid-Sized Businesses (MSBs) with the right incentives and tax policies to grow in size, scale and reach to employ more (including more diverse) people and better contribute to the Australian economy.

For the purposes of our submissions, MSBs are businesses with a revenue of $50m-$500m.

Our submissions have focused particularly on MSBs because they are often overlooked in public discourse. MSBs are burdened by being in the middle. Too big to qualify for the advantages afforded to small business, yet too small to enjoy the scale advantages of the truly "big businesses". It should be noted that MSBs are often subject to much the same bureaucracy as "big business".

Our submissions have drawn extensively on the collective experience of our MSB clients and our firm of circa 160 partners and 1,100 staff nationwide. Our clients are nimble, entrepreneurial, innovative, growing, exciting and influential. They are inventing new medicines and products to improve the quality of life of people around the world. They are reimagining the way we bank. They are taking quality Australian produce around the world. These are companies that represent the best of what Australia has to offer, at the right size to take advantage of market trends without cumbersome legacy issues that come with being a large business. MSBs should be recognised for their contribution to the economy and be given incentives to thrive.

Our attached Report sets out more details supporting our submissions including comments provided by an Economist, Professor Neville Norman from the University of Melbourne and the Cambridge University, focusing on the potential payoff to the Australian economy from encouraging growth in MSBs. In particular, Professor Norman indicates that a 10% increase in revenue would articulate itself in one and five years in terms of profit and tax revenue, particularly in lieu of the proposed, but not ultimately enacted, general corporate tax cuts. The modelling indicates that a 10% boost in revenue for a $100m business would produce a 35% increase in cash flow over five years and a 25% increase in tax payable based on the 28.5% corporate tax rate.

Our submissions in respect of reducing company and personal income tax acknowledge the 5 December 2019 release of the Organisation for Economic Co-operation and Development's (OECD) 2019 Annual Revenue Statistics which reveal that Australia has a historically high reliance, compared to OECD averages, on taxation of income and gains of corporates (representing 18% of tax revenues v OECD average of 9%) and individuals (40% v OECD average of 24%). Therefore, we submit that there is a case to reduce Australia's reliance on corporate and personal income tax to more closely align with OECD averages to support a more competitive environment for all businesses, in particular MSBs, and to encourage retail spending.

Submissions

Submission 1 – Extending the lower BRE tax rate to more MSBs

The aggregated turnover threshold for the lower Base Rate Entity (BRE) tax rate (27.5% in 2020 to 25% in 2022) should be extended from $50m to $500m. This submission is based on lived global experience indicating that the current 30% Australian company tax rate is high by reference to OECD averages and the company tax rates of many of our major trading partners and major sources of foreign capital such as the USA and UK. Capital is highly mobile and opportunities to deploy capital are plentiful. A lower company tax rate would allow our MSBs to better compete for capital and to grow their business using after tax profits. Page 4 of the attached Report outlines these issues in further detail. We acknowledge the political challenges that have come from past efforts to reduce the company tax rate but it is our submission that, post the May 2019 Federal Election and with positive 2020 fiscal outcomes expected, another concerted attempt at this reform should be made.

Submission 2 – Providing more certainty for R&D tax Incentives

The R&D Incentives play an important part in the continuing innovation strategies of MSBs which cuts across a number of different industries including Agriculture, Manufacturing, Life Sciences and Technology. Right now, as reported by the Australian Small Business and Family Enterprise Ombudsman in its Review of the R&D Tax Incentive of December 2019, many companies are finding that their R&D Incentive claims are challenged and denied long after the claim has been made and the refund has been received (and reinvested in the business). This delayed denial creates financial and business stress. We call for improving the timeliness of administration of taxpayers' R&D claims by providing more funding to AusIndustry and the ATO. This will allow more assessors to spend more time with companies to provide guidance and information on how they administer this program and also allow the assessors to properly understand the business and the nature of the R&D being claimed. Part of this will be achieved through the changes announced in Treasury Laws Amendment (Research and Development Tax Incentive) Bill 2019, however more is needed. Given the proposed amendments have been reintroduced, we argue that the turnover threshold of $20 million for the refundable tax offset be raised to at least $50 million. To achieve the current non-refundable tax offset of 8.5% would require a company to have an R&D intensity of 13% and this practically will be hard to achieve. R&D is one of the levers companies can access to help in their growth and the amendments as they stand will disadvantage in particular MSBs.

Submission 3 – Supporting Australian manufacturers

The Manufacturing industry, which in Australia includes a large number of MSBs, has faced numerous headwinds in recent years, including the exiting of the Australian automotive industry and significant increases in energy costs. The industry is resilient and evolving, and remains a major employer and critical to our overall economy. Manufacturing is ideal for regional areas for a number of reasons, not least in easing the congestion pressures our largest cities are experiencing. One way the Federal government can further support a move by manufacturers to regional areas is to work with, and compensate, State governments for the removal of payroll tax altogether for businesses that offer employment in regional towns, together with relief from stamp duty on land acquired for manufacturing plants in regional towns. Governments should not be afraid to contemplate fundamental changes to such taxes.

Submission 4 – Easing the burden on housing affordability

In Australia, the proportion of tax revenue from property as a percentage of GDP was 10% compared to the OECD average of 6% (2019 OECD data). Australia's proportionately higher reliance on tax on property makes housing less affordable. We propose that, as part of a broader reform of our tax system, the Federal Government (in tandem with State and Territory Governments) reduce the tax on property through rebalancing taxes towards consumption taxes and removing inefficient transaction taxes. This can assist housing affordability while broadening the Australian tax base to capture a fairer proportion of tax from other goods and services, and bring our tax system more in line with the OECD averages.

Submission 5 – Additional investment in childcare and early years' education

Universal access to early childhood education is currently funded for four year olds, but there is emerging interest in extending this to three year olds. This would be a welcome initiative which would assist to bring our expenditure on early childhood education more in line with many other developed countries. Contemporary research demonstrates that investment in early years' education delivers outsized returns in terms of the future success of our citizens.

In addition, Australian women are under-represented in our workforce. Our workforce participation rate for those of working age is 74% for women and 83% for men. At the same time, women are over-represented in the ranks of our part-time workforce (40% of women work part-time, compared to 5% of men).

While there may be different approaches to quantifying the economic benefits of increased access to quality early childhood education, a Grattan Institute report from 2014 suggests that an additional 6% of women in the workforce would contribute an additional $25b to Australia's GDP. Remove the barrier to early childhood education and there will be a positive impact on Australia's bottom line, and importantly helps to increase workforce participation and diversity.

Submission 6 – Professional services – planning for growth offshore under the RCEP

Professional services firms constitute a significant segment of the MSB market and many welcome the opportunities for expansion, especially into China, that should flow from Australia's commitment to participate in the Regional Comprehensive Economic Partnership (RCEP) in 2020. However, outside the large international accounting and legal firms, many Australian MSB firms lack the international trade experience to do so. We therefore propose that the Federal Government allocate financial resources to specifically help Australian professional services understand and navigate the intricacies of the RCEP up to and post implementation, and to promote professional services into the RCEP participant nations, similar to the resources currently available to many of Australia's higher profile export markets such as tourism, education and food and beverage.

Submission 7 – Relieving pressures in Aged Care

The Aged Care sector faces a number of pressures including potential adverse findings from the Royal Commission into Aged Care Quality and Safety and the Federal Government response, tightening margins, and lengthening waitlists for home care and restorative care packages. These pressures increase the risk of more providers failing and more aged people suffering from a lack of needs based services. We welcome the Prime Minister's announcement on 24 November 2019, in response to the Royal Commission's interim report, to provide $537m for more than 10,000 new aged care packages, reduce the use of chemical restrains and reduce the number of younger people with disabilities living in aged care facilities. The Prime Minister has acknowledged that this is an initial response and more will be done. We submit that, in considering what more can be done, the Federal Government should take into account measures to further relieve these pressures such as:

- Providing appropriate levels of funding for more home care and restorative care packages. For example, the Department of Health submitted to the Royal Commission that an additional $2b-$2.5b each year would be needed to provide appropriate access to people currently on the waiting list (which Leading Aged Services Australia estimates to currently be circa 120,000 people). This funding will help ensure appropriate delivery to people requiring needs based services, prevent the failures identified by the Royal Commission, and ensure that older Australians needing care are not put at risk.
- Utilising the information and recommendations provided by the sector in the "Perspectives on the Future of Ageing and Age Services in Australia" report and the work of peak bodies such as Leading Aged Services Australia's "Working While We Wait" campaign to provide clear directions to the sector in advance of the final report by the Royal Commission in October 2020.
- Investing in appropriate technologies to improve the quality of information available to older Australians and their families, on the services that are available to them and how to access them.

Submission 8 – reviewing and better resourcing Primary Health Networks (PHNs) to improve Healthcare

Primary Health Networks ("PHNs") were established by the Federal Government in July 2015 as independent primary healthcare organisations that commission rather than provide services. The two primary objectives of PHNs are to improve the efficiency and effectiveness of medical services provided to patients and secondly to improve the coordination of care to ensure patients receive the right care in the right place at the right time. In our experience, some PHNs have been more successful than others and key learnings from one PHN are not necessarily shared across other PHNs. We are calling on the Federal Government in this Budget to set aside resources to review the work of PHNs to determine the key factors of success of the better performing networks, to ensure that key learnings are appropriately shared and to resource PHNs to adopt these learnings appropriately.

Submission 9 – Investing in a reliable and sustainable energy network

Australia is transitioning to a reliable and sustainable energy network and the pipeline of renewable energy projects in Australia is at unprecedented levels. However, aging infrastructure, difficulty in accessing finance and credit worthy off-takers of electricity are some barriers to this transition. To overcome these barriers, we propose that incentives such as Federal Government funding should be made available to investors ready to build and invest in energy projects of the future including solar and wind energy generation, and battery storage.

Also, Australia must ensure that the infrastructure connecting these energy sources together and to our communities can cope with new intermittent energy loads, as well as increasing energy demand from a growing population. We therefore further propose that Federal Government funding must also be made available for projects to modernise ageing infrastructure (including funds to help maintain the approximately 877,500kms of transmission and distribution lines across Australia), or create new infrastructure, including incentives for smarter Public-Private and/or Public-Public Partnerships to fund and own this infrastructure. 2019 Federal Budget initiatives such as the $2b Climate Solutions Fund, the $1.38b Equity investment into the Snowy 2.0 expansion and the $56m Marinus Link high-voltage interconnector between Tasmania and Victoria are prior examples of the types of funding required in this area.

Submission 10 – Supporting Australia's food basket

Australia has a reputation for quality produce and products, so much so that our neighbours in Asia will pay a premium for the "Made in Australia" label. MSBs in this sector are major contributors, especially as Australian and international consumers demand more artisan and niche products. We must provide opportunities for the sector to continue to invest in themselves. In the calendar year 2018, 24% of Australian agricultural assets sold were purchased by international acquirers, mainly from Asia Pacific, United States and Canada. To ensure that the "Made in Australia" label maintains its integrity, we recommend that the Federal Government investigate ways to support local owners survive and thrive, for example:

- Food producers cannot afford to turn the lights or refrigeration off during peak periods, but can barely afford to keep them on as required. Therefore, we support putting downward pressure on energy costs particularly for users in the supply chain from farm gate to table by the continued and additional investment in energy infrastructure (consistent with the proposals we put forward for the energy sector elsewhere in this submission).
- Inland Rail will be a crucial piece of infrastructure to move produce quickly along the eastern states of Australia and we propose that the time between commitment to infrastructure and breaking ground be shortened to provide more certainty and value to the sector.
- There is also no escaping how sensitive the sector is to climactic events with ever more severe and frequent occurrences of droughts, floods and fires. We acknowledge there is no one – or easy – solution to addressing the impacts of environmental events. We welcome measures such as the November 2019 Federal Government announcement of a $500m drought stimulus package and the overhauling of the Regional Investment Corporation's (RIC) funding rules to offer reconfigured and more favourable low interest government loans. We would simply add our proposal for further similar and larger packages as needed to support local food producers. We would also support processes that allowed water to be made available more freely to those mid-sized agricultural producers in need.

Submission 11 – Low consumer confidence impacting the retail sector

The retail sector employs more than one million Australians and is an important barometer for the economy. Retail consumers will spend when they feel optimistic and cut back when times are tough. Throughout the past few months we have seen a continued drop in retail sales, particularly in discretionary categories. The Australian Bureau of Statistics figures released for October show further cause for concern. Despite consensus economic forecasts for a moderate increase of 0.3%, headline retail spending was flat. The two largest states of NSW and Victoria declined by 0.4% and 0.2% respectively, whilst the key non-food categories of clothing, footwear and household goods all exhibited negative growth at the national level.

The Reserve Bank of Australia (RBA) has already reduced interest rates to record lows, but this has not led to an upturn in retail spending. The government's relatively modest tax cuts have also had negligible impact, with households preferring to pay down debt than increase spending.

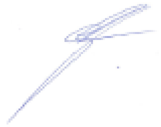
With the official cash rate at a record low 0.75%, the RBA has very few bullets left to fire. A further reduction in early 2020 to 0.5% would likely yield little impact on retail spending. We propose that the Federal Government consider measures to further boost consumer confidence and the retail sector. For example:

- Recent efforts to lower tax rates for individuals have been welcome and we would recommend seeing through of the cuts already proposed and potentially, as Budget conditions allow, further raise the tax-free threshold to boost lower to middle income earners' net of tax pay.
- The largest expense for retailers is the cost of labour, particularly in stores. Complexity around awards and wage compliance has given rise to an increased regulatory burden for retailers. We call for a simplification of the system to lift the burden currently borne by retailers and other businesses. When large retailers are inadvertently failing to adhere to the intricacies of the award system, it is clear that smaller businesses are drowning in complexity and desperately need help to simplify the regulatory environment.

In conclusion, initiatives and incentives aimed at supporting MSB will have a positive flow-on effect on the economy. Many of the recommendations we have highlighted are not only good for MSBs, but for the broader economy. With the right incentives, we can encourage more Australian MSBs to thrive, hire more people, reinvest in themselves and in more quality products. MSBs have the greatest potential to do this because they have greater resources than small businesses and are more agile and innovative than big business. They deserve to be incentivized to allow them to continue on their upward trajectory, supporting their local communities and economy as they grow.

We welcome the opportunity to discuss the untapped potential in Australian MSBs and our submissions with Government. We believe the submissions above represent positive, constructive proposals for the long-term benefit of the economy which are congruent with the Government's policy agenda,

Yours sincerely
Grant Thornton Australia Limited



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