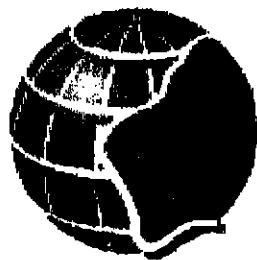


**REVIEW OF INTERNATIONAL TAXATION
ARRANGEMENTS**

Western Australian Government Response

October 2002



**Government of
Western
Australia**

General Comments

Western Australia welcomes the review of international taxation arrangements, as the State relies heavily on international markets and foreign investment in achieving its strong economic performance. Some Western Australian business leaders have indicated to the State Government that Commonwealth taxation is the most important factor affecting the international competitiveness of business across a wide range of industry sectors.

The four principal areas of review identified by the Treasurer are of significant interest to business in Western Australia, but other issues are just as important.

The State will increasingly rely on the competitiveness of our taxation system in the future as locally domiciled companies grow and become more connected with the global market. The State also relies on offshore investors to bring in much needed capital, market networks and expertise necessary for continued growth.

Western Australia is seeking to encourage domestically domiciled companies to be internationally focussed but there are many aspects of the taxation system that discourage this and that might even lead to companies currently based here to move offshore as they grow and become confident in the global market.

The State has been very fortunate to be endowed with so many natural resources and this has, until now, provided some insulation against the competitive international investment market. However, there is a real concern that the continued strong growth of the Western Australian economy is at risk unless the Commonwealth takes a more sophisticated approach to the increasingly seamless global market.

Support for Options Being Considered

Western Australia welcomes consideration of the options being put forward in the discussion paper prepared by the Department of the Treasury. In particular it welcomes the proposal to lessen the impact of provisions that discriminate against domestically domiciled companies investing offshore.

For many Western Australian companies, the notion that offshore investment should be treated any differently to domestic investment is anachronistic because they see markets in places like Southeast Asia as being inextricably linked to the Australian economy but choose Western Australia as a base for (among other things) lifestyle and security reasons. The spill-over benefits for Western Australia, through income generated in servicing these companies and the spending power of the employees is a significant contributor to Western Australia's continued growth.

Similarly, the impact of taxation provisions constraining offshore companies investing in Western Australia should be lessened. The hidden cost of discriminatory provisions in the taxation laws against foreign investors, is that the cost of project investment is likely to be higher. In many cases, Australian investors cannot meet the demands for capital for large capital intensive projects. Discriminatory provisions, such as those that relate to dividend imputation arrangements for foreign investors, are likely to be a significant barrier to competition on projects that rely on offshore investment.

Additional Factors Requiring Consideration

Chapter 1 of the discussion paper puts the case for an internationally competitive taxation system in Australia. However, the four principal areas for the review identified by the Treasurer address only a limited range of the factors affecting that competitiveness and a broader approach is necessary to make any substantial impact.

There is some concern that taxation competitiveness could negatively affect the growth prospects of the Western Australian economy.

For example, taxation rules may have contributed to the recent decline in the rate of mineral exploration in Western Australia and made it harder for businesses to attract investment capital.

Taxation treatment of Asset Depreciation

The State reflects the concerns of its key industries that companies cannot utilise accelerated depreciation provisions as they did in the past. There appears to be a widely held belief in business, that recent reforms that offset reductions in the corporate taxation rate against the removal of accelerated depreciation provisions were good for the established "service sector", but were detrimental to sectors requiring considerable new capital intensive investment. Western Australia's economy is very dependent on the latter type of investment for the growth of its capital-intensive resource based industries.

There is also a concern that the removal of accelerated depreciation provisions has had a greater impact on medium sized companies than larger companies because, among other things, their attractiveness to investors is dependent on them being able to demonstrate that they can provide investors with liquidity within a time frame that is often shorter than the effective life of the asset. On the other hand, larger companies have a greater capacity to address the liquidity needs of individual investors.

Western Australia seeks to promote the business environment for small and medium sized companies as these are often the companies that are Australian based and most likely to attempt to expand into new areas of resource utilisation or innovation. They are also a significant source of job creation.

The concern of business, about not having access to accelerated depreciation, is magnified because these provisions are in place in countries that compete with Australia for investment capital.

Discrimination between projects and types of projects

The State raises the issue of the arbitrary nature of concessions given to the treatment of depreciation of some assets and not others. There is a concern that the current process of granting concessions for the treatment of depreciation of assets is not transparent and that this may have a negative impact on investment in general.

Also, while support for resource based projects in Western Australia through direct Commonwealth grants is welcomed, there is concern that this form of support is probably made more necessary because the general taxation environment is not as conducive to investment as it should be.

Taxation treatment of investment in resource exploration

The nature of Western Australia's economy means that it relies heavily on new exploration to bring on line new resource development.

Recently the Commonwealth announced reforms to the taxation rules applying to venture capitalists aimed at promoting new investment (eg from venture capital funds which enjoyed tax free status in their source country). The reasoning for some of the reform is that the Commonwealth loses nothing by allowing offshore investors to enjoy tax concessions, similar to those that they are entitled to in their home countries, when they invest in Australia. If such concessions are not recognised by Australia, these companies simply don't invest in Australia.

A similar argument could be put for the taxation treatment of exploration. The State would support any moves by the Commonwealth to allow for more concessions to be applied to exploration including the allowance of tax write-offs to be applied to those projects where exploration was unsuccessful.

Conclusions

Western Australia supports the options outlined in the review discussion paper. As a principle Western Australia supports reform that moves toward treating all investors and investment on an equitable basis regardless of the country of origin or destination.

Western Australia believes that the issue of international taxation competitiveness is fundamental to its future success as a major contributor to the Australian economy. It urges the Board to give consideration to these broader issues when advising the Government on reform of international taxation arrangements.