



# Board of Taxation

Review into Small Business Tax Impediments

MAY 2014



Restaurant  
& Catering

## RESTAURANT & CATERING AUSTRALIA

Restaurant & Catering Australia (R&CA) is the national industry association representing the interests of 35,000 restaurants, cafes and catering businesses across Australia. R&CA delivers tangible outcomes to small businesses within the hospitality industry by influencing the policy decisions and regulations that impact the sector's operating environment.

R&CA is committed to ensuring the industry is recognised as one of excellence, professionalism, profitability and sustainability. This includes advocating the broader social and economic contribution of the sector to industry and government stakeholders, as well as highlighting the value of the restaurant experience to the public.



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## EXECUTIVE SUMMARY

Restaurants, cafes and hospitality providers are an important part of Australia's economic and social fabric. The food and beverage services sector is the single largest employer across all tourism-related sectors of the visitor economy. In June 2012, there are 280,088 tourism and hospitality businesses in Australia, of which 90 per cent were characterised as small businesses. The largest contributor was the café, restaurant and takeaway food services sector; with approximately 36,000 businesses employing 1 to 19 employees.

These small businesses generate significant tax revenue for the Australian government. In 2012-13, the visitor economy generated \$10.6 billion in taxes. Research indicates that each Australian household would have paid an additional \$1,207 in taxes without the tax revenue raised by the tourism and hospitality industry.

Yet service businesses such as these bear a disproportionate tax burden due to their labour intensity and customer service focus. Payroll tax, PAYG, superannuation, and income tax obligations represent a greater proportion of hospitality business revenues compared to small businesses operating in other sectors.

In addition, restaurants, cafes and caterers face considerable complexity in determining and claiming GST credits, as GST only applies to a proportion of their inputs. Add to this the complexities around Fringe Benefits Tax, and the cost of tax compliance becomes overwhelming and time consuming for small business operators.

Recognising the labour intensity of the sector and the predominance of small businesses operating in the hospitality industry, R&CA has summarised key reforms to sections of the taxation system which would provide the greatest benefit to these operators. This includes changes to the eligibility criteria of the Simplified Tax System, exempting small business from Fringe Benefit Tax, removing the requirement to pay superannuation to Working Holiday Makers, and raising the Superannuation Guarantee Threshold to \$600 per month.

These reforms will cut administrative red tape, improving the productivity of small businesses and allow them to focus on growing their business.

## RECOMMENDATIONS

### **SIMPLIFIED TAX SYSTEM**

- Amend the eligibility criteria of the Simplified Tax System to allow businesses with an annual turnover of less than \$2 million to use this system, bringing the criteria in line with the Australian Tax Office's definition of a micro business.

### **FRINGE BENEFIT TAX**

- In line with the recommendation to increase the eligibility criteria of the Simplified Tax System to \$2 million, small businesses with an annual turnover less than \$2 million should be exempt from FBT entirely.

### **GOODS AND SERVICES TAX**

- R&CA supports the broadening of the GST to include fresh food and produce.

### **SUPERANNUATION**

- Remove the requirement to pay superannuation to overseas workers including Working Holiday Makers.
- Raise the Superannuation Guarantee Threshold to \$600 per month (\$1800 per quarter) and index to CPI.

## THE TAX SYSTEM & THE HOSPITALITY SECTOR

### Tax contributions of the tourism and hospitality sector

The restaurant, café and catering sector forms a critical component of the visitor economy. The visitor economy is defined as the direct and indirect value generated from the provision of tourism-related goods and services<sup>1</sup>. Consumption across the visitor economy (including the broader hospitality sector) totalled \$128 billion in 2012-13<sup>2</sup>. Cafés, restaurants and catering services contributed \$19.1 billion in earnings to the national economy, \$16.8 billion of which was directly attributed to the visitor economy<sup>3</sup>. In 2012-13, the visitor economy generated \$10.6 billion in taxes for Australia. Research indicates that each Australian household would have paid an additional \$1,207 in taxes without the tax revenue raised by the tourism industry<sup>4</sup>.

### Small business is big business

In June 2012, there were 280,088 tourism businesses in Australia, of which 90 per cent were characterised as small businesses. The largest contributor was the café, restaurant and takeaway food services sector, representing approximately 60,000 businesses (or 22 per cent of all tourism businesses). Sixty one per cent (approximately 36,000) of these businesses employ 1 to 19 employees<sup>5</sup>.

Tourism Satellite Account data published in Tourism Research Australia's *Tourism Businesses in Australia* report indicates that tourism is a labour-intensive industry, driven by higher labour costs. The report demonstrates that as an industry, with a high share of micro and small businesses, the Gross Value Added (GVA) per employee is low. The average GVA for an employee in a tourism business in 2011-12 was approximately \$65,000, much lower than the average of \$119,000 for all industries<sup>6</sup>.

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<sup>1</sup> The Travel & Tourism Competitiveness Report 2009 World Economic Forum

<sup>2</sup> Tourism Research Australia (TRA), *Tourism Satellite Account 2011-12*, p.vi; ABS (2013) *8501.0 Retail Trade Australia*

<sup>3</sup> Tourism Research Australia (TRA), *Tourism Satellite Account 2011-12*; p.41

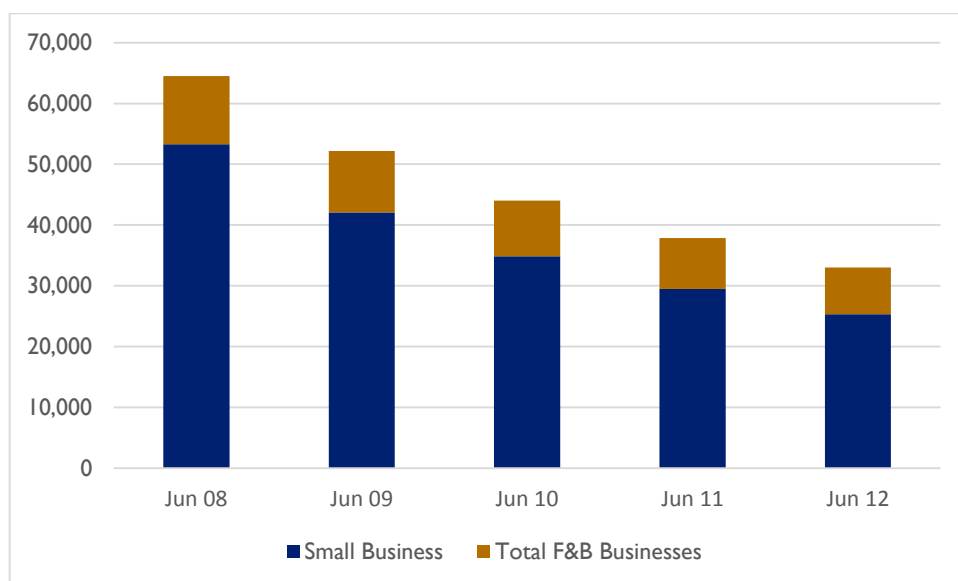
<sup>4</sup> Tourism & Transport Forum (2014) *Tourism and the Australian Economy: State & Territory Visitor Economy Impacts, 2012-13 Edition*

<sup>5</sup> Tourism Research Australia (2013) *Tourism Businesses in Australia, June 2010 to June 2012*

<sup>6</sup> Tourism Research Australia (2013) *Tourism Businesses in Australia, June 2010 to June 2012*, p1

In addition, the sector has seen significant declines in the number of food and beverage businesses in operation since 2008 (see Figure 1), with data revealing the accommodation and food services sector has the third highest rate of corporate insolvencies of around 8 per cent<sup>7</sup>.

**Figure 1: Survival of Food & Beverage businesses in Australia**



## Labour intensity

The food and beverage services sector - which includes restaurants, cafes and caterers - is a labour intensive sector. It is the single largest employer across all tourism-related sectors of the visitor economy. While the Tourism Satellite Account indicates the visitor economy directly and indirectly employs over a million people, a closer examination of employment data reveals the extent to which the food and beverage services sector provides employment opportunities across the Australian economy.

While cafes, restaurants and takeaway food services directly contribute 148,500 jobs to the visitor economy, the food and beverage service sector alone is responsible for employing 666,300 across Australia (See Table 1). As a result, payroll tax and superannuation obligations place a higher compliance cost burden on smaller businesses operating in this sector due to the sector's labour intensity.

<sup>7</sup> Dissolve (2013) *Corporate Insolvencies by Industry*, <http://www.dissolve.com.au/information-centre/statistics/corporate-insolvencies-by-industry/>

**Table 1: Employment by tourism-related industry sectors**

EMPLOYMENT BY INDUSTRIES (000s)	Nov 2012	Nov 2013	YoY Change	YoY Change
<b>Tourism Characteristic Industries</b>	<b>1,736.0</b>	<b>1,736.2</b>	<b>-19.8%</b>	<b>-1.1%</b>
Accommodation	106.3	105.7	-0.6%	-0.6%
Food & Beverage Services	678.5	666.3	-12.2%	-1.8%
Road Transport	244.9	234.1	-10.9%	-4.4 %
Rail Transport	43.2	47.1	3.9%	9.2%
Air and space transport	53.6	51.7	-1.9%	-3.5%
Water Transport	8.4	12.8	4.4%	52.7%
Other Transport	7.1	11.6	4.5%	63.1%
Sport and recreation activities	108.3	101.5	-6.7%	-6.2%
Creative and performing arts activities	40.4	38.6	-1.9%	-4.6%
Heritage activities	26.0	31.1	5.1%	19.6%
Gambling activities	31.3	29.6	-1.7%	-5.5%
Administrative services	190.9	190.3	-0.6%	-0.3%
Property operators and real estate services	147.8	152.2	4.3%	2.9%
Rental and hiring services	49.3	43.8	-5.5%	-11.2%
<b>Tourism Connected Industries</b>	<b>2,023.1</b>	<b>2,066.6</b>	<b>43.5%</b>	<b>2.2%</b>
Food retailing	375.7	394.3	18.6%	5.0%
Fuel retailing	35.9	36.5	0.7%	1.8%
Motor Vehicle and parts retailing	28.9	28.0	-0.8%	-2.8%
Other store-based retailing	665.4	678.9	13.6%	2.0%
Non-store and commission-based retailing	19.3	24.4	5.2%	26.8%
Primary and secondary educations	533.4	528.3	-5.0%	-0.9%
Tertiary education	239.2	229.1	-10.1%	-4.2%
Adult, community and other education	125.5	146.9	21.4%	17.0%
<b>All Tourism Related Industries</b>	<b>3,759.1</b>	<b>3,782.8</b>	<b>23.7%</b>	<b>0.6%</b>
All Australian Industries	11,548.9	11,635.2	86.3%	0.7%

Recognising the characteristics of the sector outlined above, R&CA has summarised key reforms to sections of the taxation system which would provide the greatest benefit to the sector. These reforms will cut administrative red tape, improving the productivity of small businesses which in turn allows them to focus on growing their business.

# TAXATION & COMPLIANCE REFORM

## Simplified Tax System

R&CA recognises the Simplified Tax System (STS) was established to provide small business taxpayers with a mechanism to simplify some aspects of their income tax affairs. R&CA supports the continuation of existing STS benefits, including:

- Cash accounting rather than accruals accounting;
- A simplified depreciation system (capital allowances); and
- A simplified treatment of trading stock.

However, in R&CA's experience, the STS is infrequently used by operators in the sector. This is due to the labour intensive (as opposed to capital intensive) nature of the industry.

To be eligible for the STS in an income year a business must satisfy the following three tests:

- Be carrying on a business in that year;
- Have an STS average turnover for that year of less than \$1 million; and
- The total of the adjustable values of the depreciating assets held by that individual and its grouped entities at the end of that year must be less than \$3 million.

While the sector is dominated by small business owners, the \$1 million average turnover threshold does not accurately reflect the operating capacity of even the smallest business operating in the sector. R&CA proposes that the STS criteria should be brought into line with the Australian Tax Office's own definition of a small business, which is a business with a turnover of less than \$2 million turnover per annum. R&CA further suggests that this be the only criteria for the use of the Simplified Tax System.

## Recommendation

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- Amend the eligibility criteria of the Simplified Tax System to allow businesses with an annual turnover of less than \$2 million to use this system, bringing the criteria in line with the Australian Tax Office's definition of a micro business.



## Fringe Benefit Tax

R&CA has long argued for changes to the Fringe Benefits Tax (FBT) treatment of business meals, recognising the compliance cost to small business is proportionately higher than for large corporations. This argument has centred on the inequity that exists in the ability of small businesses to employ strategies to avoid FBT compared to big business (i.e. big business is able to use strategies to avoid FBT, such as boardroom catering).

In a report prepared by Access Economics, it was found that FBT on business meals is overly complex and distorts market decisions. FBT on business meals over taxes 87% of the Australian population, with 23% of revenue collected being expended on compliance<sup>8</sup>.

In its submissions to the Henry Tax Review as well as the 2007 study of tax compliance costs by Treasury, R&CA highlighted that there is 39 different ways to classify a business meal for taxation purposes. This does not include classifications that exist for FBT on parking and other expenses that may also be applicable to the operation of a small business. In addition, a 2007 report on compliance costs for small business found that *'while very few small businesses pay fringe benefits tax, some small businesses undertake considerable compliance activities in order to avoid being included in the FBT system'*<sup>9</sup>. The following table, taken from the same report demonstrates the minimal FBT revenue collected from small business:

**Table 2: Micro-businesses: Taxpaying profile, 2004-05**

Taxpayers and \$ tax liability						
	Income Tax		Goods & Services Tax		Fringe Benefit Tax	
	No. of entities	\$ million	No. of entities	\$ million	No. of entities	\$ million
Individuals	1,532,079	16,034	924,524	1,071	214	1
Partnerships	368,200	0	320,708	14,525	452	2
Trusts	215,431	0	188,550	1,755	3,565	22
Companies	689,915	6,227	573,228	3,607	18,036	122
Total	2,805,625	22,261	2,007,010	7,958	22,267	147

Source: ATO. Based on tax returns processed to 18 May 2007 for entities that have lodged their 2004-05 income tax return. Data is rounded to nearest \$ million. The GST turnover threshold was \$50,000 in 2004-05.

<sup>8</sup> R&CA (2001) *The Case for, and Economic effects of, Part-recognition of business entertainment as legitimate business inputs or expenses for taxation purposes* prepared by Access Economics.

<sup>9</sup> Commonwealth Government of Australia (2007) *Scoping study of small business tax compliance costs - A report to the Treasurer*, Dec 2007

On the basis of the compliance cost and lack of access to strategies to minimise the burden of FBT, R&CA argues that the STS should include an exemption for small businesses from FBT entirely. That is, businesses classified as small businesses under the STS should be exempt from paying FBT altogether.

### **Recommendation**

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- In line with the recommendation to increase the eligibility criteria of the Simplified Tax System to \$2 million, small businesses with an annual turnover less than \$2 million should be exempt from FBT entirely.

## **Goods and Services Tax**

Since the delivery of the 2014-15 Federal budget, discussions have arisen over the broadening of the Goods and Services Tax (GST) to include fresh food and produce. Restaurants, cafes and caterers face considerable complexity in determining and claiming GST credits, as GST only applies to a proportion of their inputs. This is particularly true in relation to determining GST paid on produce in a restaurant business. For example, there is no GST on raw chicken, however GST is applicable to value-add products such as smoked chicken, cooked chicken or diced chicken products. This means to determine their GST liability, restaurant owners are forced to work through invoice by invoice the GST paid, while small businesses in other sectors can simply assume that all their inputs attract GST.

For a restaurant or catering business, the process of claiming a credit for the GST component of the purchase price of the item is varied and complex. The broadening of the tax base to include fresh food and produce for this sector would represent savings to businesses by reducing red tape and the administrative burden associated with calculating GST paid for tax purposes.

While this has been addressed to some extent by the 'averaging' method made available by the ATO, greater simplification of the GST would remove the additional burden altogether.

### **Recommendation**

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- R&CA supports the broadening of the GST to include fresh food and produce.

## Superannuation Guarantee Scheme

Australia's superannuation system was intended to deliver retirement savings to the economy, reducing the pressure on Australia's welfare system. There are, however, instances of leakage from the current superannuation system, in particular, contributions made for Working Holiday Makers.

Given the transient nature of employment within the sector, as well as ongoing skills shortages, Working Holiday Makers make up a disproportionate segment of the tourism and hospitality labour force.

Despite promoting the collection of superannuation contributions to Working Holiday Makers, very few collections are made. This is either because the amount of the contribution is so small that it is not worth rolling into another fund (due to the cost of administration fees), or they are unable to collect the funds from outside Australia.

As a result, the employer bears the administrative burden of the making contributions with no net benefit delivered to the employee or the economy. R&CA suggests superannuation contributions made for overseas workers including Working Holiday Makers are contributed to an education and training fund.

In addition, the Superannuation Guarantee Levy (SGL) threshold under the Restaurant Industry Award 2010 was lowered to \$350 per month. The SGL threshold was established in 1996 at \$450 per month with the minimum wage at the time of \$9.19. Today the minimum wage is \$16.37 (a 78% increase on 1996), yet the threshold has remained the same. Based on the growth in the minimum wage, the SGL threshold should be approximately \$577 per month or \$1731 per quarter. R&CA recommend the SGL threshold be raised to \$1800 per quarter and that it be indexed to CPI.

### Recommendation

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- Remove the requirement to pay superannuation to overseas workers including Working Holiday Makers.
- Raise the Superannuation Guarantee Threshold to \$600 per month (\$1800 per quarter) and index to CPI.

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