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INSTITUTE OF PUBLIC ACCOUNTANTS

# Submission to the Senate Select Committee on COVID-19

May 2020

## Introduction

The Institute of Public Accountants (IPA) welcomes the opportunity to make our submission to the Senate Select Committee on the Australian Government's response to the COVID-19 pandemic and related matters.

The IPA is one of the three professional accounting bodies in Australia, representing over 38,000 accountants, business advisers, academics and students throughout Australia and in over 80 countries.

Approximately three-quarters of the IPA's members work in or are advisers to the small business and SME sectors. The IPA Group represents the largest accounting body in the world focused on these sectors.

In 2015 the IPA established the IPA Deakin SME Research Centre which undertakes academic research to inform and develop the IPA's policy, advocacy and thought leadership on a wide range of issues relevant to the Australian and global economies.

If you have any queries with respect to our submission please don't hesitate to contact Vicki Stylianou at vicki.stylianou@publicaccountants.org.au or on mob. 0419 942 733.

28 May 2020

Committee Secretary
Department of the Senate
PO Box 6100
Parliament House
Canberra ACT 2600

via email: covid.sen@aph.gov.au

Dear Sir/Madam

## Australian Government's response to COVID-19

The IPA welcomes the opportunity to provide this submission to the Senate Select Committee on the Australian Government's response to the COVID-19 pandemic and related matters. We note that the terms of reference are broad and therefore, we will make comments on a range of topics.

### Accessing the stimulus measures – bearing the burden

Approximately 40% of IPA members are in practice, predominantly small accounting practices servicing individual and small business tax clients. Therefore, many of them have been at the coal face of assisting these taxpayers to access the numerous benefits under the Government's three stimulus packages and various other measures. This has created an overwhelming amount of work for our members, who have had to carry a huge burden in trying to assist clients to navigate and access the stimulus measures. The IPA has received literally hundreds of queries from members seeking guidance on interpreting and applying the measures (especially JobKeeper). Many have also been under enormous pressure to discount or write-off fees due to the financial distress being experienced by clients. The mental and physical stress on our members has been immeasurable.

### Improving consultation on stimulus measures – lessons learnt

We cannot question the speed and scale of government intervention during the COVID-19 pandemic in terms of health, social and economic measures. In response to the crisis, the Australian, State and Territory Governments introduced unprecedented social distancing restrictions. National and state borders were closed, travel was forbidden, businesses were closed, and health procedures and routines were established, among other initiatives. Meanwhile, the public had to comply with heavily enforced and rapidly changing restrictions to their personal freedoms designed to reduce the infection rate.

In terms of the economic response, a large proportion of the stimulus measures involved using one key agency, namely, the Australian Taxation Office (ATO). Two measures in particular, cash flow boost and JobKeeper, accounted for a major part of the Government stimulus packages. The ATO has a well-established consultation link to practitioners and professional bodies. Both of these measures placed a significant additional workload onto tax practitioners. The ATO was also challenged with putting systems in place in such a short time frame to accommodate these stimulus measures. The ATO should be commended for working with the tax practitioner community in resolving many of the implementation issues which subsequently surfaced following the passing of the relevant legislation for the stimulus measures referred to above.

Given the reliance on the tax system to deliver a major part of the stimulus expenditure, there appeared to be a lack of consultation which could have mitigated a lot of implementation issues experienced by practitioners and advisers. We are mindful of the speed in which the Government had to respond to the looming crisis, notwithstanding this constraint, the Government could have utilised some of the existing consultation infrastructure for input into the legislative agenda. The time frames between announcement and legislation were incredibly short and challenged the tax practitioner community who had to understand eligibility criteria in a short time frame to help their clients navigate access to government support. Whilst consultation would not have mitigated all the implementation issues due to the short time available for consultation, nonetheless it would have assisted a smoother pathway for practitioners to navigate the short implementation window.

**Tax reform – the road to recovery and beyond**

While we were in a relatively good position fiscally as compared to many OECD countries, with relatively low government debt and a Commonwealth budget almost back in surplus, we have a tax system ill-equipped to manage a downturn given the reliance on personal and company tax at the Commonwealth level and property transactions in the States. Australia has a high reliance on income taxes, including company income tax. Around 60% of the Commonwealth's tax receipts come through personal and company income taxes, nearly twice the OECD average.

Australia's experience from the Global Financial Crisis suggests that it will take a long time for corporate taxes to recover from the COVID-19 downturn as company losses are carried forward. This puts additional pressure on personal income taxes to carry the load.

The increase in unemployment (even with JobKeeper subsiding wages), and even further expected weakness in wages growth, suggests that personal taxes will also not provide a stable or growing base for the Commonwealth for many years.

The base and rate of our GST will also hamper the Government's ability to make up for any lost revenue from direct taxes on personal and company taxes. The percentage of consumption on which GST is payable now stands at around 47% due to exemptions on food, education and health. GST exemptions now disproportionately benefit higher income households.

The COVID-19 slowdown has undermined the ability of governments to raise revenue given the disruption to business and personal incomes and changed consumption and saving behaviour. With additional government expenditures to support the economy, governments will be challenged to reinvent their tax systems without stifling economic growth, and which we contend cannot be achieved without comprehensive tax reform. The COVID-19 pandemic has now exposed an ill-equipped tax system to support the recovery process.

To enable governments to support the economy back to health requires rebuilding the tax base with efficient growth-supporting taxes. Much work has already been done on the best way forward and in this regard, we want to draw attention to the Henry Review (The Australian Future Tax System Review).  We remain hopeful that the pandemic will show the urgent need for robust and genuine tax reform, and that the political will is found to tackle Australia's precarious revenue base.

**Wage subsidy programs in response to COVID-19: a comparison**

The United Kingdom, New Zealand, Canada, the United States, Australia and Denmark, among others, have all introduced wage subsidy schemes. The policy rationale is the same for all countries – to put the economy into 'hibernation' or a 'medically induced coma' or to 'freeze' the labour market – the idea is to keep workers connected to workplaces, stop businesses from closing permanently and minimise any lasting disruption to the economy. The hope is that the economy will rebound swiftly once restrictions are lifted. A lot depends on the length of the hibernation or freeze. All schemes are intended to be temporary, though for differing periods of time.

**United Kingdom**: *Coronavirus Job Retention Scheme:* restricted to employees who have been stood down (ie furloughed); covers 80% of usual wages (up to 2,500 pounds per month); in place for 3 months (but may be extended); open to any business which cannot maintain its workforce because of the Coronavirus; open to public authorities.

**New Zealand**: *Wage subsidy scheme:* different rates for part-time and full-time but not more than an employee's usual wage; open to sole traders and self-employed; paid as a lump sum covering 12 weeks; employers must have had at least 30% decline in revenue compared to last year for any month between January and June 2020; employers must use their best endeavours to pay a minimum of 80% of income; employers must take active steps to mitigate the impact (eg engage with their bank).

In contrast to the United Kingdom, **Australia** and **New Zealand** cover employees who are still working in addition to those stood down; and have economic impact eligibility criteria. The Australian scheme does not cover public authorities; and it covers fewer businesses but more employees, whereas the United Kingdom scheme covers more businesses but fewer employees than JobKeeper.

**Canada**: *Emergency Wage Subsidy:* covers 75% of an employee's wages up to CAN$847 per week for employers of all sizes and across all sectors who have suffered a drop in gross revenues of at least 15% in March and 30% in April and May; in place for 12 weeks from 15 March to 06 June 2020.

**United States**: *Paycheck Protection Program:* authorises up to USD$349 billion in forgivable loans to small businesses to pay their employees during the COVID-19 crisis. All loan terms are the same for everyone. Loans are forgiven as long as they are used to cover payroll costs and most mortgage interest, rent and utility costs over the 8 week period of the loan; and employee and compensation levels must be maintained; payroll capped at $100,000 annualised for each employee; not more than 25% may be for non-payroll costs; loan payments deferred for 6 months; distributed through Small Business Administration lenders and other approved lenders; waiving Credit Elsewhere requirement; program open until 30 June 2020.

Overall, the Australian JobKeeper scheme pays a flat rate, whereas other countries have introduced a proportional payment. Apart from claims of being egalitarian we are not able to identify the policy objective and rationale behind having a flat payment as opposed to a proportional payment, as is the case in most other countries. Most but not all schemes have the need to meet certain economic or financial eligibility criteria. There is also a difference in coverage, with some schemes preferring to cover more businesses or more employees. All schemes are temporary though the Australian scheme seems to be among the longest. Many have a built-in review period.

**Impact of wage subsidy schemes**

Wage subsidies will make a difference to the unemployment rate, in that it will go up less and down faster. Peak unemployment could be down to 9% from 17% (Westpac Bank); or 8% from 12% (Deloitte); or 10% (Treasury). Prior to this crisis the unemployment rate was around 5.2%. Australia's position heading into this crisis was stronger than many, with both the International Monetary Fund (IMF) and the OECD forecasting that Australia would grow faster than comparable economies, including the United Kingdom, Canada, Japan, Germany and France. The IMF and OECD indicate that Australia is one of the advanced economies best placed to provide fiscal support without endangering debt sustainability. This should be taken into consideration as we plan for the recovery and for the years ahead.

**Debt – how much is too much?**

Whilst our new debt level may be 'sustainable', it still needs to be repaid. However, it does not necessarily mean increased taxes or some kind of austerity program. According to some economists, Australia could take its time in repaying the debt, which would still be relatively low at a forecast 26% of GDP, compared to the latest OECD figures of an average 110% of GDP for gross debt (these figures are not strictly comparable but make the point). If we overcome our national obsession with surpluses, we could afford the debt for a while longer whilst investing in renewed productive capacity, as we did after World War II where debt levels soared to 120% of GDP. We need a similar kind of boost or boom after we come out of this crisis and start reviving the economy from its hibernation. There will no doubt be many submissions making the point that we will fall off an economic cliff once the JobKeeper scheme is unwound and that more stimulus in needed to prevent this situation. The Government needs to carefully and clearly communicate its intentions with respect to JobKeeper to enable businesses to plan accordingly.

**Policy rationale – the knowns and unknowns**

The lesson from the Global Financial Crisis of 2008 was to 'go hard, go early and go households'. Accordingly, in the current crisis, the Government similarly went 'hard', 'early' and went business, individuals, households and small business. Some commentators have observed that given the relatively restrained health crisis, whether the economic pain endured is proportional, that is, have we gone too 'hard' with our economic response. However, it would be extremely difficult to make accurate forecasts about the health crisis and we would contend that taking a cautious approach to both the health and economic response might be more aligned to community expectations.

Australia's economic stimulus packages have similar measures to other countries, based on similar policy objectives, so there are collective lessons to be learnt. Policy responses have generally focused on two immediate goals: health protection measures and economic support on both the demand and supply sides.

Large-scale and integrated measures across all policy areas are necessary to make strong and sustained impacts. Without appropriate policy measures workers could fall into poverty and find it harder to regain livelihoods during recovery. The International Labour Organization (ILO) says that 2.7 billion workers (81%) globally have been impacted by COVID-19, with 1.25 billion workers (38%) globally facing a severe impact or displacement (unemployment). Even though Australia is classified as a 'rich country', it is still critical to get the policy settings right, both during and after the pandemic.

## Policy responses – a useful framework

In terms of the response to the crisis and even looking beyond to the 'road to recovery' the IPA recommends an integrated policy framework such as the one outlined below from the ILO. Whilst there is always more work to be done and measurement is problematic, we believe that the Australian Government has performed relatively adequately against this framework. The expansive response against many of the ILO pillars, including measures around insolvency, early access to superannuation, childcare support, training programs etc etc, have been, overall, well received, widely utilised and we believe effective.

The ILO refers to the four pillars of policy responses to COVID-19. These are:

1. Stimulating the economy and employment, through fiscal and monetary policy, lending financial support to specific sectors, including the health sector.
2. Supporting enterprises, jobs and incomes, including employment and retention measures (wage subsidies), financial and tax relief for businesses, extending social protections for all.
3. Protecting workers in the workplace, preventing discrimination, adapting work arrangements (eg enabling teleworking), providing health access, expanding paid leave.
4. Relying on social dialogue for solutions, including building trust and confidence, strengthening capacity and resilience of workers' and employers' organisations, strengthening the capacity of governments, strengthening labour relations and processes.

## Academic research – what does it tell us?

There have been numerous studies and reports over the years on the effectiveness of Active Labour Market Policies (including wage subsidies). Indicative, overall, of the findings is *What Works for Active Labor Market Policies?* by Eduardo Levy Yeyati, Martín Montané and Luca Sartorio, Center for International Development, Harvard University, July 2019. Findings included:

- programs are more likely to yield positive results when GDP growth is higher and unemployment lower;
- programs aimed at building human capital, such as vocational training, independent worker assistance and wage subsidies, show significant positive impact; and
- program length, monetary incentives, individualized follow up and activity targeting are all key features in determining the effectiveness of the interventions.

Other studies have found that generous and long-lasting hiring subsidies can have more substantial positive effects in the long-term. By contrast, short-term hiring programs and subsidies are only effective if they comprise a substantial training element.

These might be useful indicators, considerations and features when designing policies to aid our recovery from this crisis and post-COVID-19.

**Stimulus measures worth keeping – government guarantee scheme**

The IPA Deakin SME Research Centre has undertaken significant research and policy development on government guarantee schemes and has been a long-time advocate. Australia was one of 47 developed countries, which until the pandemic, didn't have such a scheme to assist small businesses in accessing affordable finance and capital. One of the stimulus measures introduced has been a guarantee of 50% for business loans for small and medium sized businesses through eligible lenders. The total lending capacity will be $40 billion (2% of GDP). We also note the support measures introduced by the banking sector, which have been very welcome for many small businesses.

We urge the Government to retain a guarantee scheme post-COVID-19 and to have a coordinated program (with the Australian Business Securitisation Fund and the Australian Business Growth Fund) to genuinely assist small businesses and SMEs to access affordable finance and capital on appropriate terms and security (eg not having to mortgage the family home to secure business loans). Despite a slow start in take up rates, we believe that the Government's response has been well received.

**G20 – protecting the global economy – what's Australia's role**

We refer to an excerpt from the Extraordinary G20 Leaders' Summit Statement on COVID-19 (held 26 March 2020):

The unprecedented COVID-19 pandemic is a powerful reminder of our interconnectedness. We commit to do whatever it takes and to use all available policy tools to minimize the economic and social damage from the pandemic, restore global growth, maintain market stability, and strengthen resilience. We are currently undertaking immediate and vigorous measures to support our economies; protect workers, businesses—especially micro-, small and medium-sized enterprises—and the sectors most affected; and shield the vulnerable through adequate social protection. We are injecting over $5 trillion into the global economy, as part of targeted fiscal policy, economic measures, and guarantee schemes to counteract the social, economic and financial impacts of the pandemic.

The IPA believes the excerpt above shows that the need for a coordinated and committed global response has never been greater. The G20 talks of using 'all available policy tools' – which must be effectively leveraged for the benefit of all nations. We would urge the Government to continue taking part in these coordinated global policy responses; and note that the Australian Government has already shown leadership as a 'middle power' with respect to the health crisis. However, appropriate trade policy and ensuring a vital and well-functioning international trade system for a trade-dependent country such as Australia, are critical.

**Supply chains – the need to diversify**

The new normal will also depend on the reaction to globalisation and integrated supply chains. For Australia, which has the most concentrated trade profile in the world, this crisis has glaringly exposed the vulnerabilities of our supply chains. There is now widespread speculation about re-industrialisation and becoming more self-sufficient in the crucial medical supplies that matter in a pandemic.

The IPA strongly believes that the Australian Government needs to reassess its industry and innovation policies, digitisation policy, trade and investment policies in light of the pandemic. Whilst the stimulus measures have assisted during the crisis, our concern is that we may miss the opportunity to ‘reset’ or ‘reboot’ our policies and programs in these critical areas. Again, political will is needed and a willingness for genuine and robust reform.

**The issues we all need to confront**

The pandemic has exposed the weaknesses and flaws in many systems, processes, policies, legislation and structures. The IPA Deakin SME Research Centre will be considering, from a thought leadership perspective, many of the following questions. We anticipate that the Australian Government will also be addressing these issues.

- How will these economic stimulus packages ultimately be funded? Australia has just got its budget into surplus and now because of the crisis is facing possibly decades of debt and deficit. Can we avoid increasing taxes?

- How and when will these ‘temporary’ measures be unwound? There is no rule book on unwinding and bringing the economy back to life.

- What will be the longer term structural and budgetary implications? Many in Australia who had lobbied for increases in unemployment benefits are now saying the Government should maintain these levels of payment post-COVID-19.

- What will it mean for labour and workplace laws into the future? Does this prove that we can embrace the digital age, for example, working from home, which impacts workplace laws, urban planning, transport, workplace health and safety. Are we ready for the transformation?

- What will it mean for the ‘universal basic wage’ argument? Does this prove that it is a viable alternative, is it sustainable in the longer term?

- What will it mean for international trade, supply chains and diversification? Will the slowdown in trade continue, will there be a rise in nationalism, will the need for diversification accelerate?

- What will it mean for social policy? Will more people be driven into poverty? How will the world respond to potentially millions being dragged into poverty, back into poverty or further into poverty? Will existing social safety nets be able to cope? What will Australia’s response be and how will this shape our foreign policy in the coming decades?

- What will it mean for international organisations such as World Health Organisation, United Nations, ILO, IMF, World Bank Group, G20, World Trade Organisation? Is the need for reform even greater? What about funding and relevance? Are we equipped to prevent more pandemics and global catastrophes? What will Australia’s position be across these various institutions?

- What will be the ‘new economic normal’ going forward? We don’t know what it will look like but the world won’t be the same. Are we ready, what do we need to do to ensure our ongoing prosperity?