

Impacts of Unintended Double Duties for Victorian New Car Dealers

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1. About VACC

The Victorian Automobile Chamber of Commerce (VACC) is Victoria's peak automotive industry association, representing the interests of more than 5,000 members in over 20 retail automotive sectors that employ over 50,000 Victorians.

VACC members range from new and used vehicle dealers (passenger, truck, commercial, motorcycles, recreational and farm machinery), repairers (mechanical, electrical, body and repair specialists, i.e. radiators and engines), vehicle servicing (service stations, vehicle washing, rental, windscreens), parts and component wholesale/retail and distribution and aftermarket manufacture (i.e. specialist vehicle, parts or component modification and/or manufacture), and automotive dismantlers and recyclers.

In addition to VACC, its sister organisations – the Motor Trade Associations, represent the automotive industry for their respective states.

VACC is charged with the responsibility to communicate to government where policy matters adversely affect operations within the industry. This paper provides representations on behalf of the industry relating to a recent State Revenue Office (SRO) change of interpretation that is likely to result in retrospective double taxation (stamp duty) of certain vehicles bought and sold by Licensed Motor Car Traders (LMCTs)

2. Introduction – summary of issues and suggested solutions

LMCTs in Victoria are entitled to claim exemptions of stamp duty for vehicles purchased for trading stock or demonstration (for sale) purposes.

Until recently, SRO Victoria's interpretation of legislation in this area has been consistent with other states and territories, so that there has been parity and equal trading conditions across the country.

The SRO adopted a new interpretation of exemptions in relation to a category of vehicle, being Service Demonstrator Vehicles (SDVs). This new interpretation was adopted without consultation with industry stakeholders and was communicated via SRO bulletin D01-18 issued on 28/2/18, outlining an opportunity for dealers to make a voluntary disclosure to pay additional duty. The bulletin is unclear and does not provide a balanced assessment of the exemption criteria and of dealers' rights.

This new interpretation, if allowed to be implemented, will likely result in retrospective double taxation on vehicles within this category.

The new interpretation does not allow for any ancillary use of these vehicles, which is now out of step with other states and territories and will create disadvantaged trading conditions in Victoria.

As a result of the above, VACC research suggests the following may occur:

- a. Closure of 183 businesses and loss of 4000 jobs;
- b. Cross border trading in demonstrator vehicles, resulting in loss of Stamp Duty Revenue to Victoria;
- c. Significant adverse publicity and public backlash of such an impact, following the recent impacts of the shutdown of manufacturing in Victoria;
- d. Hardest hit areas will be regional, particularly Greater Geelong, which is still recovering from the closure of the Ford manufacturing plant, as well as Victorian border regions.

In addition, the VACC submits that this new SRO interpretation, if allowed to be adopted, is out of step with Government Policy, which has shown significant support for the broader automotive industry post shutdown of manufacturing in Victoria, such as retraining of ex-employees and retooling of plant.

The VACC submits that the new SRO interpretation as outlined in the Voluntary Disclosure bulletin be immediately withdrawn.

The VACC further submits that the Victorian Government direct the SRO to adopt similar interpretations to other states and territories to ensure parity, so that there is no loss of business and stamp duty revenue to Victoria.

Finally, the VACC submits that the SRO interpretative rulings DA.034 and DA.035 are not in step with the current trading environment and that these rulings should be reviewed and updated to fall in line with Government policy and in parity with other states and territories, with such review to be done collaboratively with the VACC.

3. Background in relation to current (new) SRO interpretive issues

The Victorian Automobile Chamber of Commerce (VACC) is Victoria's peak automotive industry association, representing the interests of more than 5,300 members in over 20 retail automotive sectors that employ over 50,000 Victorians.

Amongst its industry roles, VACC is charged with a responsibility to communicate to government where policy or planning matters adversely affect operations within industry, and in particular amongst VACC member businesses.

New vehicle dealerships represent a significant proportion of VACC's membership base. The Victorian Automobile Dealers Association, a Division of VACC, comprises of approximately 330 new car dealers representing 68 vehicle brands, who operate from 640 individual franchise outlets.

VACC has recently received increased communication from its new vehicle dealer members of uncertainty concerning the application of motor vehicle duty to demonstrator vehicles and any ancillary use that may be permitted, in particular, relating to the potential retrospective double taxation of such vehicles where there is ancillary use. This issue has arisen by the release of State Revenue Office (SRO) Bulletin D01-18. In bulletin D01-18, issued 28/02/2018 (attached) the SRO announce *an opportunity for Dealers to voluntarily disclose where they may have incorrectly obtained duty exemptions for motor vehicles registered and/or used as service demonstrator or loan vehicles (ancillary use)*.

This interpretation is a significant shift from the interpretation adopted by the SRO since 2006, as per revenue rulings DA.034 and DA.035 (attached). The drafting of these rulings was done in collaboration with the VACC, representing its members, and the industry has been operating under these guidelines for the past 12 years. The recent change in interpretation if followed through will likely result in costly and unnecessary financial imposts for many businesses, with the real potential for business closures and significant employment losses - an outcome which is undesirable for all stakeholders.

The new Victorian SRO interpretation was communicated via the voluntary disclosure bulletin without consultation with industry stakeholders. The new interpretation is now out of step with all other states and territories and is likely to result in double taxation. This report will outline the key issues currently facing Victorian dealerships regarding the new imposition of motor vehicle duty to certain demonstrator vehicles, along with recommended policy actions for Government that can address these matters in a fair and equitable manner.

4. Current requirements of the Duties Act 2000, Victoria and impact of new SRO interpretations

Chapter 9 of the *Duties Act 2000* in Victoria imposes duty on an application for registration or transfer of registration of a motor vehicle, unless an exemption applies. Duty is calculated on the dutiable value of a motor vehicle.

Sections 231 (1) and 231 (2) (a) (ii) of the Duties Act provide exemptions from duty for Licensed Motor Car Traders (LMCTs) for vehicles that are used as demonstrator vehicles. Demonstrator vehicles are motor vehicles that are available and used for demonstration to prospective purchasers for sale of vehicles of the same or similar class. This exemption reflects the Victorian Government's position that motor vehicle dealers should not be disadvantaged in relation to the payment of duty compared to other businesses, simply because the essence of their business is the acquisition and sale of motor vehicles (consistent with other states and territories). The exemption definition in the Act is very broad and open to interpretation, hence it is primarily administered by the SRO through various revenue rulings introduced (consistent with other states and territories).

The current requirements of the *Duties Act 2000* are supported by SRO Revenue Rulings DA.034 and DA.035. These Revenue Rulings were issued in 2006 by the SRO in collaboration with VACC, both in response to and as a reflection of the state of the new vehicle market at that time. Both market conditions and industry business practices however, are now fundamentally different to 2006. The current amended SRO interpretations and the guidelines in the revenue rulings are not in step with current industry business and trading conditions. As a consequence of this, many Victorian new car dealers are now facing retrospective double taxation, which will have significant repercussions to the industry and Victorian economy.

Sections 5 and 6 of this report will provide an overview of the structural and operational evolution of the new vehicle retailing industry over the past 12 years, specifically highlighting the evolution of a secondary new car market. During this period the industry has had a decline in profits and absorbed the impact of the burden of increased taxes at a state and federal level, and the administration and collection of taxes and duties on behalf of various government bodies. The report will outline how the new SRO interpretation will likely result in retrospective double taxation (stamp duty) to retail dealers. In such a challenging market environment, should this new interpretation be allowed to be implemented, significant business closures and loss of employment is foreseen by the VACC. Finally, the report will outline a suggested solution whereby the SRO interpretive rulings, DA.034 and DA.035 are collaboratively reviewed and amended to reflect current industry practice and to be consistent with other states and territories.

5. Industry structural change 2006 - 2018

Since 2006, there have been significant developments within the vehicle retailing industry, including major changes to dealership business models, processes and operating procedures.

Over the past 12 years, the industry has contracted by 187 businesses or 14.3 per cent in Victoria. There have also been substantial increases in the number of vehicle brands, as well as in the annual volume of new vehicles sold (Table 1).

The data points towards increased consolidation and concentration within the industry over the period, and this is particularly evident in terms of the number of large businesses (200 or more employees) and small businesses (1 to 19 employees) operating which decreased by 54.2 per cent and 29.8 per cent respectively (Table 2).

Table 1: Vehicle dealerships– Victoria

Year	No. of businesses	No. of vehicle brands	No. of vehicle makes	Volume of new vehicle sold
2006	1,308	59	310	242,879
2017	1,121	68	418	339,343
Change 2006 -17	-187	+9	+108	+96,464

Source: ABS and VFACTs data.

Table 2: Vehicle Dealerships by employment size - Victoria

YEAR ending June	Sole proprietors (No.)	Businesses with (1-19 employees) (No.)	Businesses with 20-199 employees (No.)	Businesses with 200+ employees (No.)	Total
2006	504	588	195	21	1,308
2017	507	413	191	10	1,121
Change 2006-17	3	-175	-4	-11	-187
Per cent change	0.6	-29.8	-2.1	-52.4	-14.3

Source: ABS

Table 3: Economic Contribution of Victorian New Car Dealers

Measure	Contribution
Turnover/Sales	\$16.568 billion
Dealer Wages	\$1.537 billion
Tax Contribution	\$612.233 million
Total of wages and other expenses	\$2.556 billion
Dealer Other Expenses	\$1.019 billion
Duties Collection	\$594.200 million
Dealer Employees	17,492
Total Economic Contribution	\$4.015 billion
New Vehicle Registration	\$252.833 million

Source: AADA.

In terms of industry structure, dealerships range from family-owned small businesses to larger businesses including three public companies (AHG Ltd, AP Eagers Ltd and Autosports Group Ltd). However, and importantly, these listed entities account for around 12 per cent of total vehicle dealerships.

As 88 per cent of franchised dealerships continue to be owned and operated by individual or family groups, the industry is far from being dominated by large multinational operators. Furthermore, the industry is not characterised by duopoly or oligopoly market dynamics as witnessed within retail banking and groceries industries in Australia. Annually, new car franchise dealers also contribute over \$3 billion in industry value-added to the Victorian economy.

6. Industry operational change 2006 -2018 and the evolution of a secondary new car market

The past 12 years has also seen a fundamental change in industry business models and practices, resulting in increased business challenges and costs. These developments have included:

- Significant changes in the commercial relationship between vehicle franchisors and their franchisee dealers. Franchise agreements between franchisors and franchisee dealers are now far more complex, with much greater capital expenditure requirements for investment in premises and equipment, working capital, increased dealership floor sizes and vehicle stock holdings. The infrastructure requirements to support a new vehicle dealership in 2018 can be several millions of dollars higher than in 2006.
- The sales process for both franchisors and franchisee dealers is now more sophisticated and multifaceted as it includes volume trades and warranty support. The after sales process is now comprised of many layers and there is an increased requirement to hold parts stock, specialised technicians and the on-going skilling of these technicians to meet the growing pace of technological advancement in motor vehicles.
- The advent of the digital economy has resulted in all new car dealerships not capturing a defined Prime Marketing Area (PMA) which is a key element in the value of a franchise agreement. Dealerships now advertise their stock to a national audience via their own factory-controlled webpages or mediums such as *casales.com* and *gumtree.com*. This can have a great effect on traders in rural or regional areas who no longer have a captive marketplace defined by a PMA.
- Franchisors often hold dealers (franchisees) accountable to unrealistic volume guides, where failing to hit target can result in significant financial losses. By providing significant bonuses for the sale of demonstrator vehicles, franchisors have effectively created a secondary new car market in the sale of demonstrator vehicles which did not exist 12 years ago. This market promotes increased volume at discounted prices and is largely responsible for the increased new car sales over this period to the detriment of profitability. These programs require high turnover and fast movement of stockholdings, generally within 6 months, for dealers to receive bonuses. As a by-product, some programs have ancillary uses (e.g. service demonstrator programs). The take-up of this additional vehicle stock by dealers is incentivised in the form of up-front bonus payments or commissions. A significant portion of the volume target for dealers in today's market falls within demonstration and service demonstration programs.
- The concept of the demonstrator vehicle has evolved since 2006. Demonstrator fleets held by dealerships now have alternate incidental use such as being provided as courtesy or loan vehicles, and these are known as *Service Demonstrator Vehicles (SDVs)*. The main and dominant use of SDVs however, is for demonstration of the vehicle for the purpose of its ultimate sale. This is supported by the significant percentage and numbers of vehicles held in stock for short periods and sold through Service Demonstrator Programs. VACC research data shows a substantial portion of these vehicles are sold within 3 months of registration and over 90% sold within 6 months of registration, evidencing the fact that they have been purchased for sale or demonstration, with an ancillary use. This is a significant factor in the rise in new vehicle sales over the past 5 years, ultimately leading to higher tax revenues for the Commonwealth and State.
- The resulting consequences of these developments have been increased price competition across vehicle brands at all levels of the supply chain, that have reduced industry profit margins from average levels of 4.8 per cent in 2006 to 2.6 per cent in 2017.

7. Current taxation and red tape impost to the industry resulting in commercial inequity

Victorian new car motor vehicle dealers are currently required to comply with a multitude of taxes, fees and duties that place a considerable financial, regulatory and administrative burden on these businesses. There are at least five state based and up to three federally based prescribed duties or fees that apply to the sale of a new motor vehicle in Victoria. On a typical \$35,000 motor vehicle these charges include:

- Motor vehicle duty of \$1,470 (\$8.40 per \$200)
- Registration fees (\$295.10)
- TAC Fee (\$425.00)
- Insurance Duty (\$45.00)
- Transfer Fee (\$20.20)
- GST
- LMCT Fees
- PPSR search fees

Excluding GST, PPSR search fees and LMCT fees, these charges constitute a significant sum of \$2,252.80 or 6.4 per cent of the vehicle's dutiable value in Victoria. Motor vehicle dealers have long bemoaned the fact that these imposts create a difficult and unfair trading environment that penalises both individual businesses and consumers in Victoria. Victorian dealers not only have to comply with more administrative requirements and taxes than interstate car dealers but are in desperate need of relief in order to remain competitive. This competitiveness is stifled when faced with a potential double duty scenario.

Feedback received by VACC across its dealer membership base indicates that Victorian car dealers are at a comparative disadvantage within the new car retailing market and are actively losing vehicle sales to interstate purchases by Victorian consumers.

This situation has arisen as a result of a commercial imbalance in trading conditions through the application of more taxes on Victorian car dealers than that imposed by other jurisdictions, and which Victorian businesses cannot absorb any further. The new car market is a very competitive and transparent market, where even small price differentials between competing interstate businesses are taken advantage of by increasingly savvy consumers. The potential double taxation of service demonstrator vehicles will accentuate this imbalance already in existence.

Indications received by VACC are that over the medium term, there will be significant closures of Victorian car dealership businesses if this imbalance in trading conditions is not appropriately addressed by the Victorian Government.

8. Vehicle stamp duty comparisons across jurisdictions

Table 3 below highlights the disparity that will exist in the application of tax duties between Victoria and other states/territories if the current SRO interpretation remains in place. In particular, Victoria is the only state where there is a “separate usage criteria” that determines whether duties are applicable (This analysis is based on the new SRO interpretation as communicated in their voluntary disclosure bulletin). As a result, under the new SRO interpretation, Victoria dealers will be at a trading disadvantage compared to other states and territories.

Table 4:

State/Territory	Practical position in relation to service demonstrator vehicle
NSW	No separate usage criteria - Vehicles registered as demonstrator vehicles are exempt from duty.
QLD	No separate usage criteria - Vehicles registered as demonstrator vehicles are exempt from duty, if sold within 1 year from registration.
TAS	No separate usage criteria - Vehicles registered as demonstrator and courtesy vehicles are exempt from duty.
SA	No separate usage criteria - Demonstrator vehicles are exempt from duty with allowance for incidental use. Main criteria is being available for sale on dealership premises during business hours.
WA	No separate usage criteria - Demonstrator vehicles are exempt from duty with allowance for incidental use. Main criteria is being available for sale on dealership premises during business hours.
VIC	Separate usage criteria - Vehicles used as service demonstrator or service loan vehicles in any form are non-exempt from duty.

The exemption of Stamp Duty applies to vehicles in Victoria, on the basis of the primary purpose and use. Motor vehicles are exempt from Duty if their primary purpose is for trading stock or for demonstration (sale) purposes.

The Victorian conditions are similar and consistent with the other States, with the exception of the separate criteria relating to loan or courtesy vehicles, as per the new interpretation of the SRO.

The SRO considers that a motor vehicle is used solely or primarily as a demonstrator vehicle where:

- The motor vehicle is available and used for demonstration to prospective purchasers for sale of vehicles of the same class; and
- The motor vehicle is available for such use during the LMCT's normal trading hours at the LMCT's business premises.

Service Demonstrator Vehicles satisfy this criteria.

"Service Demonstrator Vehicles" are intended to demonstrate the features and benefits of the vehicle to the consumers whilst the consumer's vehicle is being serviced. The intent of the dealer is to entice the consumer to upgrade their vehicle, having experienced the upgraded features of the service demonstrator vehicle. In the absence of this intent, the dealer could have made an older, roadworthy vehicle available, to solely serve the purpose of convenience to the consumer.

The primary purpose of the service demonstrator vehicle is for it to be sold to the consumer, which is no different to the purpose of any other "demonstrator vehicle". The franchisor programs generally require dealers to have an appropriate mix of vehicle models so that they can allocate an appropriate vehicle to each customer with the intention of upselling. The franchisor programs for these types of vehicles generally require them to be sold within 6 months, so they can be replaced to generate further sales. Accordingly, these vehicles are turned over regularly, and substantially within a 3 to 6 month period, as evidenced by VACC research data (refer section 6).

VACC does not believe it would be the intention of Victorian Government Policy to apply additional duty on a vehicle held for sale and sold within a normal stockholding period, upon which sale the retail customer will pay further duty.

Loan vehicle programs, where there is no incentive to sell, are easily distinguishable from service demonstrator programs and such vehicles should be dutiable. Vehicles in this category are generally treated as fixed assets rather than trading stock by dealers which creates a clear distinction for the dealers self-assessment and payment of duty on these vehicles.

9. Current impasse, potential solution

In the absence of specific information supporting the primary use of demonstration, the SRO does not consider a motor vehicle as being used solely or primarily as a demonstrator vehicle where:

- The motor vehicle has travelled a distance of more than 7,500 km since its acquisition and initial registration in the name of the LMCT; or
- The motor vehicle has been held for longer than 12 months after it has been initially registered in the name of the LMCT as a demonstrator vehicle.

These are the guidelines as per SRO Revenue Rulings DA.034 and DA.035 and the guidelines adopted by the industry over the last 12 years.

The current range of demonstration and service demonstration programs were not in existence 12 years ago, hence they have not been contemplated in the drafting of the rulings.

The SRO have now taken a position that any vehicle that has an ancillary use as a courtesy or loan vehicle is not exempt from duty, which was also not contemplated in the drafting of the rulings. The voluntary disclosure offer is also on this premise, which is unjust, in that it seeks to retrospectively charge duty to dealers who claimed exemptions on the basis of the SRO's stated guidelines. The SRO has categorised all service demonstration vehicles as non-exempt, without consideration of the facts and circumstances around the usage of each particular vehicle in that category.

The SRO, in its voluntary disclosure bulletin is not providing a balanced outline of exemption criteria, which may result in dealers making an unnecessary voluntary disclosure and pay unnecessary duty. Dealers most likely to do this will be small operators without the resources to pay advisors to represent them.

The legislation, particularly Section 231 for the Duties Act, in its broad effect, requires an analysis of the facts and circumstances of each vehicle usage to determine exemption. It is unjust for the SRO to adopt a blanket interpretation of a category of vehicles and it is not the overriding premise of the legislation or Government Policy. VACC research indicates that for the 68 brands being sold in the Australian market, over 300 different incentive programs exist, most of which change from year to year. To properly determine whether a vehicle has exempt usage, each vehicle in each program for each separate dealer would need to be reviewed annually. This is basically an impossible task. The SRO nor the dealer network have the time or resources to undertake this task. Should the current interpretation remain, the industry will be forced to run a test case, which will drag the issue out for many years to come. Following that, the extensive analysis on a case by case basis would need to commence, and there would be no realistic timeframe for an ultimate resolution.

As is the case in other states and territories, the exemption can continue to be determined on a self-assessed basis, under the guidance of interpretive rulings. The VACC puts forward that the current revenue rulings are largely satisfactory, with some updates required to be relevant to current market and trading conditions. Following that, the VACC would support a voluntary disclosure offer on the basis of the redrafted rulings.

10. Potential Impact on the industry/businesses

The current landscape of the industry is vastly different from when these rulings were first introduced in 2006 by the SRO in collaboration with VACC.

The impost of double duty will in all likelihood not be totally absorbed by business and partially be passed on to the consumer, as profit margins attributed to car sales in the current environment have eroded significantly in the past decade. The costs and burden to small business will be further increased due to the administrative requirements associated with the collection of these duties. Feedback provided to VACC from its dealer members support these findings.

This increased duty will also further impact the profit margin on individual car sales as consumers force prices down by reference to lower competitive interstate pricing.

Feedback provided to VACC from its dealer members suggest that up to 30 per cent of dealerships will be impacted adversely through these measures and will likely result in the further closure of 183 businesses and the loss of up to 4,000 jobs within the industry and consequently the Victorian economy. This further exacerbates the economic losses already sustained through the closure of car manufacturing operations in Victoria.

Furthermore, the presence of large dealer groups which have significant buying power can take advantage of cross-border trading. Larger dealer groups have the capacity to absorb these costs than smaller family owned dealerships.

Cross-border trading may also occur amongst consumers as the availability and further transparency of the internet allows consumers to conduct research in a thorough and efficient manner. The impost of these duties may be reflected in the price, leading consumers to purchase vehicles from interstate rather than from Victorian businesses. This trend is evidenced by a growing use of vehicle comparison websites, for example carsales.com.au and feedback provided to VACC indicates that there has been a rise in the loss of business to Victorian dealers from interstate dealers.

The increased loss in sales in Victoria to interstate dealers is likely to impact the level of revenue collected from Victorian dealers. The loss of sales will result in reduced profits for dealers and less resources available to invest in capital expenditure and to employ additional staff. In addition, the lack of sufficient capital expenditure may lead to individual breaches of Franchise Agreements between franchisee dealers and franchisors, with the possibility of termination of the Franchise Agreement by the franchisor.

From a policy viewpoint, following the adverse publicity resulting from the closure of vehicle manufacturing in Victoria, and the subsequent strong support for retraining of workers and retooling of plant to compensate for loss of jobs and enhance employment opportunities within the sector, the likely impact of business closures and loss of further jobs in the sector from an unnecessary retrospective double taxation, would seem out of step with government policy intentions.

In all likelihood, the areas hardest hit would be regional areas, such as greater Geelong, which was significantly affected by the closure of the Ford factory, as well as Victorian border regions.

Discriminatory duty payable on aftermarket/ accessories fitted to new car

A further complication and burden to the business is that accessories added to the vehicle at the point of the sale attract duty as they become part of the dutiable value of the vehicle. These aftermarket accessories can include the fitment of sun roofs, bull bars, tinted windows etc. The impact of this impost results in the loss of revenue to the dealerships as consumers often bypass the dealerships in favour of independent aftermarket sellers that do not attract a duty on these

aftermarket products. In an environment of low margin, this profit centre at dealerships is heavily relied upon. The discriminatory imposition of duty on these fittings and favouritism provided to the aftermarket in this regard would never have been the intention of SRO Ruling DA.022.

The serious impact of these duties, and of concern to VACC, is the effect on regional dealers and consequently regional communities. Regional dealerships engage heavily with their local community through sponsorships of sporting clubs, charities and not for profit associations. The loss of revenue, due to the double tax impost will significantly affect their ability to support such activities within their local communities and subsequently the wellbeing of the community overall. The value of support provided by vehicle dealerships to regional communities, should not be overlooked or under estimated.

11. Conclusion and recommendations

1. Immediately suspend current Voluntary Disclosure as mandated in SRO Bulletin D01-18, pending a review of relevant revenue rulings
2. Revenue Rulings DA.022, DA.034 and DA.035 are to be reviewed in collaboration with VACC to bring them up to date with the current trading environment, and in parity with other states and territories.
3. The Victorian Government direct the SRO to adopt similar interpretation to other states, allowing ancillary usage and ensuring parity in reference to the imposition of vehicle stamp duty and therefore be aligned with other Australian jurisdictions.