What Can Australia Teach us about Tax Reform

JONATHAN B FORMAN, University of Oklahoma

Available at: https://works.bepress.com/jonathan_forman/168/
What Can Australia Teach Us about Tax Reform?

by Jon Forman
Alfred P. Murrah Professor of Law
University of Oklahoma
www.law.ou.edu/faculty/forman.shtml

Law and Society Association
San Francisco, California
June 4, 2011
Chart 10: Major categories of tax receipts as a proportion of gross domestic product

(a) Sales taxes include the GST, luxury car tax and the wine equalisation tax.
(b) Other taxes includes other indirect taxes and FBT.
Source: 2010-11 MYEFO.
Chart 9: Australian Government tax mix, 2010-11

- Individuals income taxation: $138,360 million
- Fringe benefits taxation: $3,660 million
- Superannuation taxation: $7,330 million
- Company and petroleum resource rent taxation: $65,150 million
- Sales taxes: $50,440 million
- Petroleum excise: $16,060 million
- Other excise: $9,240 million
- Other taxation: $2,749 million
- Customs duty: $6,430 million

A Strong Economy

Getting back in the black

Chart 3: Net debt for Australia and the G7 economies, 2010-2016

Australian Government, *Budget Overview, Budget Statement 1*, at 1-13 (2011),
Past Political Achievements

- A Universal Pension System
- Goods and Services Taxation

Australia's national floral emblem is the golden wattle.
A Universal Pension

• 1986—industrial agreements for 3 percent of payroll contributions

• 1992/1993—superannuation guarantee legislation, mandating 3 percent contributions to individual retirement accounts
  – Higher levels phased in, reaching 9 percent in 2002/2003
Goods and Services Tax

- Broad-based consumption tax that replaced all sales taxes
- 10% tax on most goods and services
- John Howard, Liberal party Prime Minister
- Passed in 1999
- Began operation 2000
Australia’s Future Tax System Review

- An Overview of the Australian Tax System
- Australia’s Future Tax System Review – a/k/a The Henry Review
- The Government Response

Emu
the unofficial national bird
Australia’s Future Tax System Review

• In 2008, the Australian Government established Australia’s Future Tax System Review panel to examine Australia’s tax and transfer system and make recommendations to position Australia to deal with its demographic, social, economic and environmental challenges.
  – The Review Panel prepared detailed background reports, received more than 1,500 formal submissions, and held a two-day conference in June 2009.
  – In December 2009, the Review Panel delivered its final report to the Australian Government.
  – In May 2010, the Government released the report, along with an initial response.

• Will Australia’s Parliament soon enact comprehensive tax reform?

Australia’s Future Tax System Review

- Almost accidental birth
  - Not on the agenda when the Labor Government was elected in 2008
  - At a 2008 summit on Australia’s future, business leaders nominated tax reform as a priority area

- Government appointed the Secretary of the Treasury Ken Henry + four advisors
  - The Henry Review
The Henry Review, cont.

• In December 2010, the panel delivered its final report to the Government.
• On Sunday, May 2, 2010, at 2:30 p.m.
  – The Government released the Henry Review
  – And the Government’s Initial Response

Sydney Opera House
Many Australian taxes

• Australians pay at least 125 different taxes each year. Of these, 99 are levied by the Australian government (including 67 agricultural levies), 25 by the States and 1 (council rates) by local government.

• In 2006-07, the Australian government collected $262.5 billion in tax.

Ranking of Australian taxes by revenue in 2006-07

105 other taxes includes fringe benefits tax, gambling taxes, insurance taxes, beer and spirits excise, customs duties, motor vehicle taxes, crude oil excise and agricultural levies.
The personal income tax base

- Applied against most receipts that have the character of income
- Generally distinguish between income from capital and income from labor, except:
  - unlike in most other countries, fringe benefits are taxed in the hands of the employer rather than in the hands of the employee;
  - the range of deductions that can be claimed against income for tax purposes is broad by international standards; and
  - income from some forms of savings, such as superannuation and capital gains, is treated differently to other income.
- The Medicare levy is a structural element of the personal income tax system
  - another 1.5 per cent of a taxpayer's income
### Personal Income Tax

<table>
<thead>
<tr>
<th>Taxable Income</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>$0–$6,000</td>
<td>Nil</td>
</tr>
<tr>
<td>$6,001–$37,000</td>
<td>15</td>
</tr>
<tr>
<td>$37,001–$80,000</td>
<td>30</td>
</tr>
<tr>
<td>$80,001–$180,000</td>
<td>37</td>
</tr>
<tr>
<td>&gt; $180,000</td>
<td>45</td>
</tr>
</tbody>
</table>

### Medicare Levy

<table>
<thead>
<tr>
<th>Taxable Income</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>$0–$18,488</td>
<td>Nil</td>
</tr>
<tr>
<td>$18,489-$21,750</td>
<td>10% of &gt; $18,488</td>
</tr>
<tr>
<td>&gt; $21,750</td>
<td>1.5</td>
</tr>
</tbody>
</table>

### Low Income Tax Offset

<table>
<thead>
<tr>
<th>Taxable Income</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>$0-$30,000</td>
<td>$1,500</td>
</tr>
<tr>
<td>$30,001-$67,500</td>
<td>less 4% of &gt; $30,000</td>
</tr>
<tr>
<td>&gt; $67,500</td>
<td>Nil</td>
</tr>
</tbody>
</table>
Personal tax rates and progressivity

• Australia has a progressive personal income tax system.

• The personal rate scale has 4 personal income tax rates, as well as a zero rate of tax below the tax-free threshold.

• In addition, other elements such as the low income tax offset (LITO) alter the effective rate of taxation.
Statutory corporate income tax rates of OECD countries (1985 to 2008)
Henry Review Recommendations

• **Recommendation 1:** Revenue raising should be concentrated on four robust and efficient broad-based taxes:
  – personal income, assessed on a more comprehensive basis;
  – business income, designed to support economic growth;
  – rents on natural resources and land; and
  – private consumption.

• Additional specific taxes should exist only where they improve social outcomes or market efficiency through better price signals.
Personal Taxation

- **Recommendation 2:** Progressivity in the tax and transfer system should be delivered through the personal income tax rates scale and transfer payments. A high tax-free threshold with a constant marginal rate for most people should be introduced to provide greater transparency and simplicity.

- **Recommendation 6:** To remove complexity and ensure government assistance is properly targeted, concessional offsets should be removed, rationalised, or replaced by outlays.
Company and other investment taxes

• **Recommendation 26:** The structure of the company income tax system should be retained in its present form, at least in the short to medium term.
  – A business level expenditure tax could suit Australia in the future and is worthy of further consideration and public debate. It is possible that other economies will move towards such systems over coming years and it could be in Australia’s interest to join this trend at an early stage.

• **Recommendation 27:** The company income tax rate should be reduced to 25 per cent over the short to medium term with the timing subject to economic and fiscal circumstances. Improved arrangements for charging for the use of non-renewable resources should be introduced at the same time.
Chart 1: Statutory corporate tax rates, OECD countries 2009

Source: OECD Tax Database.
Charging for Nonrenewable Resources

• **Recommendation 45:** The current resource charging arrangements imposed on non-renewable resources by the Australian and State governments should be replaced by a uniform resource rent tax imposed and administered by the Australian government that:
  - (a) is levied at a rate of 40 per cent, with that rate adjusted to offset any future change in the company income tax rate from 25 per cent, to achieve a combined statutory tax rate of 55 per cent;
  - (b) applies to non-renewable resource (oil, gas and minerals) projects;
  - (c) measures rents as net income less an allowance for corporate capital, with the allowance rate set at the long-term Australian government bond rate;
  - (d) requires a rent calculation for projects;
  - (e) allows losses to be carried forward with interest or transferred to other commonly owned projects, with the tax value of residual losses refunded when a project is closed; and
  - (f) is allowed as a deductible expense in the calculation of income tax, with loss refunds treated as assessable income.
Taxing consumption

• **Recommendation 55:** Over time, a broad-based cash flow tax — applied on a destination basis — could be used to finance the abolition of other taxes, including payroll tax and inefficient State consumption taxes, such as insurance taxes. Such a tax would also provide a sustainable revenue base to finance future spending needs.
Alcohol and tobacco taxation

• **Recommendation 71:** All alcoholic beverages should be taxed on a volumetric basis, which, over time, should converge to a single rate, with a low-alcohol threshold introduced for all products.

• **Recommendation 73:** The existing regime for tobacco taxation in Australia should be retained, with the rates of tax substantially increased, depending on further evidence on the costs of harm from tobacco smoking.
Income support payments

• **Recommendation 82:** There should be three categories of income support payments:
  – (a) A pension category
  – (b) A participation category
  – (c) A student assistance category

• **Recommendation 90:** Current family payments, including Family Tax Benefit Parts A and B, should be replaced by a single family payment. The new family payment should:
  – (a) cover the direct costs of children in a low-income family (that is, the costs associated with food, clothing, housing, education expenses); and
  – (b) assist parents nurturing young children to balance work and family responsibilities.
State tax reform

• **Recommendation 119**: Reforms to State taxes should be coordinated through intergovernmental agreements between the Australian government and the States to provide the States with revenue stability and to facilitate good policy outcomes.

• **Recommendation 121**: Over time, State land tax and local government rates should be more integrated. This could involve:
  - (a) moving to a joint billing arrangement so that taxpayers receive a single assessment, but are able to identify the separate State and local component; and
  - (b) using the same valuation method to calculate the base for local government rates and land tax (with this method being consistent across the State).
The Government Response

• Released on Sunday, May 2, 2010, at 2:30 p.m.
• This was a long term plan to apply a Resource Super Profits tax to the profits earned from resources that are owned by all Australians, and use it to:
  – generate more superannuation savings for working families;
  – lower tax for all companies, especially small businesses; and
  – invest in our future infrastructure needs, particularly for mining states.
A 28% Corporate Tax Rate

• A LOWER COMPANY TAX RATE
  – The Government will cut the company tax rate to 29 per cent from the 2013-14 income year and then to 28 per cent from the 2014-15 income year.
  – will move Australia towards achieving an internationally competitive tax rate.
  – Australia will become an even more attractive place to invest.
  – is expected to increase long run GDP by 0.4 per cent (excluding the gains from refunding royalties).

• A HEAD START FOR SMALL BUSINESS
  – This measure reduces the company tax rate to 28 per cent for eligible small business companies from the 2012-13 income year, one year earlier than the start of the general reduction in the company tax rate.
Infrastructure

• INCREASING INVESTMENT IN INFRASTRUCTURE
  – The introduction of the RSPT will enable the Government to make infrastructure spending a permanent structural feature of State and Commonwealth budgets for the first time.
  – The Government will establish a new infrastructure fund for the States worth $700 million in 2012-13, and that will grow over time.

• PROMOTING RESOURCE EXPLORATION
  – The Government will also deliver on its commitment to promote investment in exploration, through a new Resource Exploration Rebate.
  – Under the new rebate, companies will receive a refundable tax offset at the prevailing company tax rate for their exploration expenditure.
40% Resource Super Profits Tax (RSPT)

• “BETTER CHARGING FOR NATURAL RESOURCES”
  – The RSPT is a more economically efficient arrangement for charging for our resources.
  – Royalties are amongst the most inefficient taxes levied in Australia (see Chart 2). An inefficient tax results in lower GDP because it induces people to change their work, investment or saving decisions.
Chart 2: Marginal welfare loss from a small increase in selected taxes

- Royalties and crude oil excise
- Insurance taxes
- Payroll tax
- Corporate income tax
- Motor vehicle taxes
- Conveyancing stamp duties
- Labour income tax
- Fuel taxes
- Goods and services tax
- Land taxes
- Municipal rates
- Petroleum resource rent tax

Welfare loss (cents/dollar of additional revenue raised)

- Australian Government
- State governments
- Local government
The Government will increase the superannuation guarantee (SG) rate from 9 to 12 per cent over time.

<table>
<thead>
<tr>
<th>Year</th>
<th>Rate (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2013-14</td>
<td>9.25</td>
</tr>
<tr>
<td>2014-15</td>
<td>9.5</td>
</tr>
<tr>
<td>2015-16</td>
<td>10</td>
</tr>
<tr>
<td>2016-17</td>
<td>10.5</td>
</tr>
<tr>
<td>2017-18</td>
<td>11</td>
</tr>
<tr>
<td>2018-19</td>
<td>11.5</td>
</tr>
<tr>
<td>2019-20</td>
<td>12</td>
</tr>
</tbody>
</table>
Superannuation

• GOVERNMENT CONTRIBUTIONS FOR LOW INCOME EARNERS
  – A new superannuation contribution of up to $500 will be provided by the Government for workers with income up to $37,000.

• CATCH-UP CONTRIBUTIONS FOR OLDER WORKERS
  – The Government will allow individuals aged 50 and over with total superannuation balances below $500,000 to make up to $50,000 in concessional superannuation contributions.
Lessons We Can Learn

• *Tax Reform is Political Everywhere*
• *Federal Power to Reform State & Local Taxes*
• *A Tax System Can Produce Surpluses*
• *Tax Expenditures are not Essential*
• *Create a Board of Taxation*
• *Corporate Tax Reform*
• *Experiment with Pre-filled Tax Returns*
• *Improve Compliance Efforts - High Net Worth*
• *Expand Withholding*
• *Tax Fringe Benefits*
Conclusion

• “Experience suggests that tax reviews rarely lead to successful tax reform.” . . . But “Tax Reform in Australia is necessary and overdue.” Chris Evans and Richard Krevor (2009).
• Let’s see if the Australia experience can help us do better in the US.
About the Author

• **Jonathan Barry Forman (“Jon”)** is the Alfred P. Murrah Professor of Law at the University of Oklahoma College of Law, teaching tax and pension law and the author of *Making America Work* (Washington, DC: Urban Institute Press, 2006). He was the Professor in Residence at the Internal Revenue Service Office of Chief Counsel for the 2009-2010 academic year.

• Prior to entering academia, Professor Forman served in all three branches of the federal government. He has a law degree from the University of Michigan and master’s degrees in both economics and psychology.

• Jon can be reached at jforman@ou.edu; www.law.ou.edu/faculty/forman.shtml