Business Bearing the Burden 2009


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¹ Julie Novak is Research Fellow, Institute of Public Affairs. The information contained in this paper is indicative estimates presented for illustrative purposes only. The IPA does not accept liability for any decisions or transactions made or effected on the basis of information contained in this paper. Individuals and businesses seeking tax information relevant to their own circumstances should consult their tax advisor.
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Executive Summary

- The IPA State Business Tax Calculator calculates the level of state government taxes on business in each of the six Australian states.
- The IPA analysis reveals:
  - South Australia has the highest taxes on business, while Western Australia has the lowest for the second year in a row.
  - The level of tax imposed on a business differs significantly according to industry and business size.
  - Transport and construction businesses are the most heavily taxed by state governments, while services firms are the most lightly taxed (e.g. a transport company in NSW pays almost twice as much tax as does an IT consultancy firm based in Queensland).
  - There is also a wide discrepancy between the level of specific state taxes on business (e.g. a business in South Australia pays at least six times more land tax than an equivalent business in Western Australia).
- Small businesses are taxed proportionately more heavily by state governments than medium or large businesses.
- The key policy implications of the IPA findings are:
  - Transaction-based taxes and charges at the state level disproportionately affect small business, a main driver of economic activity and employment in Australia.
  - The structure of state government business taxes militate against federal government policies (e.g. infrastructure-related companies are more heavily taxed by states than service firms).
  - The reliance of the states on inefficient taxes – including on transactions undertaken by companies – inhibits market processes and economic growth, and does not take into account the financial circumstances of the taxed corporation.
- State business taxes are widely held to impede efficiency, constrain business growth and reduce export opportunities.
- If state governments use the findings from this study to cut tax burdens, Australia stands to improve upon its currently subdued recovery and realise its bright economic potential.
Introduction

A multiplicity of taxes is imposed by Australia’s state governments. A business operating in every state could potentially be subject to a maximum of 117 taxing points. These include taxes on payroll, property, financial and capital transactions, on goods, and the performance of activities.

According to the Australian Bureau of Statistics, taxes imposed by state governments (excluding the ACT and NT) totalled approximately $51.7 billion in 2007-08, representing about one-third of general government sector revenue.

A significant proportion of this state tax liability burden is directly borne by business community – the prime generator of investment, jobs, and exports in Australia.

In practice, the myriad of taxes levied by state governments can make it difficult for busy business owners and managers to understand their liabilities. This is especially the case when governments change tax rates and bases, or when businesses grow in size. It can also be difficult for smaller businesses to appreciate how seemingly minute variations in state tax structures could yield significant variations in liability.

Government may see it as being in their own interests to obscure the ‘visibility’ of their taxes. Business taxes can potentially create a ‘fiscal illusion’ effect whereby voters and taxpayers are uncertain about where the final incidence of a tax falls, and even how much revenue the tax raises. This could make the tax burden in some instances seem much smaller than it actually is, with real consequences for broader community support for wide-ranging state tax reform.

Individual state revenue offices provide information about the potential tax liabilities applicable to their own respective jurisdictions. However, there remains a lack of a single information source on the tax burdens placed on a business if it were to operate in any of the six states. The Institute of Public Affairs State Business Tax Calculator has been developed to help fill the gap.

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2 PricewaterhouseCoopers, 2009, What is your company’s Total Tax Contribution? 2008 survey results. NSW had the highest number of state business taxes (21), followed by Victoria and South Australia (both 21) and Queensland (20). Tasmania had the smallest number of business taxes (14).

3 Australian Bureau of Statistics (ABS), Government Finance Statistics, Australia, 2007-08, cat. no. 5512.0.
This paper aims to shed light on comparative business tax liabilities for the five mainland states and Tasmania.

The next section will investigate why an analysis of state taxation is an important pursuit in the Australian economic context. After a discussion of the main features of the Institute of Public Affairs (IPA) State Business Tax Calculator, the indicative tax liabilities of businesses in the states as at 31 December 2009 are calculated using a ‘reference business’ concept adapted from World Bank competitiveness methodology.

This paper illustrates that there are significant variations in indicative state tax liabilities imposed on businesses, presenting opportunities for competition between governments to institute tax structures more amenable to economic development.
Why do state business taxes matter?

In modern societies governments compulsorily acquire revenue from a number of sources in order to fund the production and provision of certain goods and services – such as justice and policing, education, health and transportation. As noted above, taxation instruments represent a key element in the revenue-taking armoury of the Australian states.

Business taxes are a lucrative revenue earner for the six state governments

The six states impose a variety of taxes that impact directly upon businesses including:

- Payroll tax – a tax levied on employers and based on wages paid or payable (including non-cash fringe benefits and employer superannuation contributions in most states) to employees.
- Land tax – a tax levied on the unimproved value of selected categories of land held as at a particular date.
- Land transfer duty – a tax levied on the transfer of non-residential commercial (and residential) property, paid by the purchaser and based on the sale price (or value, if higher) of the property.
- Insurance duty – a tax levied on a variety of insurance policies, generally based on the annual premium.
- Motor vehicle registration duty – a tax on the value of a vehicle payable on the application initially to register a motor vehicle or the application to change the name of the registered owner.
- Motor vehicle registration fees – a fee paid prior to a motor vehicle being permitted to drive on public roads.4

Figure 1 illustrates the amounts and shares of revenue acquired by these taxes.

Most states levy other taxes that affect businesses, including those in the gambling industries, as well as specific levies including workers’ compensation premiums (included in this study).

**Figure 1: Revenue acquired from selected state tax bases**

Excluding ACT and NT, and excluding workers’ compensation premium payments. Shaded areas signify taxes included within the scope of this study. Revenue acquired under selected taxes, such as stamp duties, motor vehicle taxes, land tax and insurance taxes, are imposed on businesses and individuals. ‘Other taxes’ include taxes on gambling activities, other taxes on property and financial and capital transactions, statutory corporation levies and miscellaneous taxes.

**Source:** Australian Bureau of Statistics (ABS), Taxation Revenue, Australia, 2007-08, cat. no. 5506.0.

**State business taxes impose heavy efficiency costs on our market-based economy**

It is generally understood that taxes can have significant implications for the functioning of markets and the overall vitality of the competitive environment facing individual businesses, irrespective of their revenue-raising capabilities.

Specifically, taxes can affect behaviour by encouraging business to shift from heavily taxed to lightly taxed, or taxed to untaxed, goods and services. This could in turn alter the economic incentives to save, invest or consume outputs that are otherwise of value to business. Furthermore, taxes also reduce the disposable incomes available to, and affect the cash flows of, a business.

Australian state taxes have long been the target of pointed criticism from businesses and other groups in terms of their relatively poor efficiency properties. The recent Henry Review of taxation provided individual companies and business representative organisations an opportunity to highlight the distortions generated by state business taxes (Box 1).
Box 1: Submissions from business groups to the Henry Review on state taxation

A range of stakeholders from the business community, including individual corporations and representative organisations, have raised concerns about the economic efficiency and cost implications of existing state taxes in the context of the Henry Review. The following extracts are drawn from selected submissions tendered to the Review:

**Business Coalition for Tax Reform**

‘State governments are critically over-reliant on inefficient business taxes which jeopardise business growth and hold back the economy. Inefficient state business taxes such as stamp duties and property taxes are: volatile and unpredictable revenue sources; difficult and costly to manage; deadweight taxes that impede business efficiency and drag on the economy; unequally and unfairly applied; and harmful to business competitiveness.’

**Insurance Council of Australia**

‘The imposition of … stamp duties on general insurance premiums significantly increases the premium paid by the insured. The overall increase is exacerbated by the layering of different levels of taxation’

‘The Insurance Council commissioned Woolcott Research in September 2008 to survey 1,000 small to medium sized enterprises on their respective general insurance coverage. The research indicated that some 26% of SME’s surveyed did not purchase general insurance for their business and of the 67% who indicated that they had purchased insurance for their business, some 5% of this population indicated that they believed their general insurance coverage was inadequate. … Premium cost was cited by almost 80% of SME’s that were inadequately insured as their reason for not purchasing adequate insurance.’

**Tourism Transport Forum**

‘As a labour intensive industry, tourism bears a disproportionate burden of state taxation through the payroll tax system. This burden essentially encourages investment away from tourism into alternate economic activities that are less labour intensive, and impedes growth and innovation in the industry.’

‘the tourism industry bears a disproportionate burden of state taxation from land tax … the primary impact of land tax on tourism is to discourage economic activity and investment away from tourism to goods and services whose values does not lie in property … Land tax systems further disadvantage tourism property investment through the provision of exemptions on permanent use. … such exemptions increase returns for the development of residential properties over tourism.’

‘The cost of maintaining and establishing new [caravan and camping] parks does not offer a potential operator any real incentive to invest in parks due to land tax … Caravan parks are in many cases located on prime real estate, especially in coastal areas. … One operator, who saw a 50% increase in their land tax bill, calculated that the park site would need to recover an extra $240 per site per year to cover the land tax burden.’

‘Stamp duty is a significant impediment to investment and innovation in the tourism industry. Conveyance duty rates and additional premiums on business transactions inhibit tourism product development and innovation and as such adversely impacts on the attractiveness of Australia as an investment market.’
Box 1 (cont’d): Submissions from business groups to the Henry Review on state taxation

Urban Development Institute of Australia

Land tax ‘reduces project profitability and impacts on hurdle rates and therefore on investment in large urban revitalisation projects and developments.’

Victorian Land Tax Coalition

‘The unpredictable and sharp increases in land tax charges have had a significant impact on cash flow, particularly for owners of non-income-producing properties and for small and medium-sized businesses.’

‘Many small businesses have been forced to close because of excessive land tax bills. Smaller businesses typically operate on slim profit margins and simply cannot accommodate spiralling annual charges like land tax.’

‘The problems associated with land tax have not been confined to property investment. Any industrial ventures that are property-intensive have also been affected. One high-profile example of this was a leading provider of storage facilities which chose to stop investing in Victoria because of land tax rates and instead diverted its investible funds elsewhere.’

Source: Submissions tendered to Henry Review on Australia’s Future Tax System.

A growing number of empirical studies over the past decade support the claims of significant inefficiency costs associated with selected state taxes.

A March 2009 study by the Centre for International Economics (CIE) models the economic impacts of three policy scenarios that involve the reduction or elimination of some of the most pernicious state taxes (Table 1).

The CIE research suggests that tax reform would increase gross domestic product (GDP) in the long run compared to a no-change scenario:

- Scenario 1 would increase long run GDP by 0.6 per cent.
- Scenario 2 would increase long run GDP by 0.4 per cent.
- Scenario 3 would increase long run GDP by 1.7 per cent.  

All three tax change scenarios would also raise private sector investment, in itself a key determinant of economic growth.

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5 All simulation results are for economic growth consequent to tax reform, compared to a no-change growth baseline.
Table 1: State tax reform simulations in CIE study

<table>
<thead>
<tr>
<th>Change scenario</th>
<th>Objective</th>
<th>Source of funds</th>
<th>Proposed tax changes (cost of reforms)</th>
</tr>
</thead>
</table>
| 1               | Raise growth | Australian Government ($10 billion). | ▪ Reduce stamp duties on residential and non-residential property ($7.5 billion).  
▪ Remove insurance duties ($2.5 billion).  
Total change: $10 billion. |
| 2               | Enhance international competitiveness | Australian Government ($10 billion). | ▪ Reduce stamp duties on commercial property ($4.0 billion).  
▪ Remove land tax ($4.4 billion).  
▪ Reduce payroll tax ($1.7 billion).  
Total change: $10 billion. |
| 3               | Maximise elimination of the worst State taxes | Australian Government ($8.6 billion).  
State contribution via a broad State tax ($8.6 billion). | ▪ Remove stamp duties on residential and non-residential property ($12.5 billion).  
▪ Remove insurance duties ($2.5 billion).  
▪ Reduce land tax ($2.2 billion).  
Total change: $17.3 billion. |


In April 2008, Access Economics also undertook modelling of the impact of state tax reform. Based on an empirical assessment of the impact on consumption from raising tax revenue by $100 million, it is possible to obtain implied estimates of the welfare effects of selected taxes (Figure 2).

According to Access Economics, state stamp duties on motor vehicles, insurance and non-residential property are among the least efficient taxes levied in Australia.
Figure 2: Detailed efficiency ranking of selected commonwealth and state taxes

Estimates expressed in terms of relative efficiency compared to commonwealth personal income tax. Taxes that are less efficient than income tax score an ‘efficiency index’ score greater than one, with more efficient taxes scoring less than one. Efficiency ranking for taxes based on the ratio of the percentage change in real consumption to the percentage change in tax revenue attributable to changing each tax instrument.


A staff research paper by the Productivity Commission assessed the efficiency costs of the payroll tax system, finding that the marginal excess burden of payroll tax raised was between three and 12 per cent.\(^6\) Murphy found that the replacement of the payroll tax with a goods and services tax would permanently add $580 million per annum to economic welfare.\(^7\) A 2004 study by Dixon, Picton and Rimmer found that payroll tax deadweight costs were about ten per cent of payroll tax collections in Victoria alone.\(^8\)

\(^{7}\) Chris Murphy, 1998, Payroll Tax: Is It as Good as a VAT or as Bad as Sales Tax?, Report for Australian Chamber of Commerce and Industry, June.  
State business taxes deter business expansion

A number of studies have also suggested that state taxes, in particular payroll tax, may discourage some firms from expanding their size.

The Dixon-Picton-Rimmer study cited above found that payroll tax thresholds make firms smaller than they otherwise would be, and concentrate firms at just below threshold employment. In the case of the Victorian payroll tax:

‘thresholds exert a downward bias on firm sizes. This is most marked for firms whose efficient level of employment is between 1 and 1.5 times the threshold level of employment. … we found that the downward bias of thresholds was likely to cause a concentration of firms at about the threshold level of employment.’\(^9\)

Murphy also suggested that the existence of payroll tax thresholds might encourage businesses to remain inefficiently small in size: ‘the SBE [small business exemption] is not a policy for small business, rather it is a policy for making businesses smaller.’\(^10\)

State business taxes impede Australia’s international competitiveness

With many businesses operating across international, as well as Australian state, borders, it is essential to recognise that state business taxes can critically affect the business structure, production costs and investment decisions and thus their international competitiveness.

As noted in the 2009 CIE study many state taxes are effectively ‘origin’ taxes levied at points along the production chain (as opposed to on the final product), for items produced for both domestic consumption and export, and are generally not incurred (or are incurred at a lesser extent) by international producers.\(^11\)

This implies that state origin taxes cascade through the production process thereby penalising Australian exports and reducing our capacity to compete in the global marketplace.\(^12\)

\(^10\) Chris Murphy, 1998, Payroll Tax: Is It as Good as a VAT or as Bad as Sales Tax?, p. 3.
\(^12\) As an example of the corroding effect of state business taxes on our international economic position, Murphy estimated that the elimination of the payroll tax on a revenue-neutral basis would improve Australia’s trade balance by up to 0.5 per cent of GDP. Murphy, Payroll Tax: Is It as Good as a VAT or as Bad as Sales Tax?, p. 3.
Institute of Public Affairs State Business Tax Calculator

Taxes are a major source of costs outside the direct control of business, and so it is essential to develop tools that help shed light on the expected liability that firms are likely to face due to these imposts.

About the State Business Tax Calculator

The IPA State Business Tax Calculator (SBTC) is a quantitative model that calculates the tax liabilities applied to any business in the Australian states (New South Wales, Victoria, Queensland, Western Australia, South Australia and Tasmania). Calculations are based on the following major taxes, fees and levies:

- Payroll tax
- Land tax
- Stamp duties on the sale and purchase of non-residential commercial property, motor vehicles and insurance premiums
- Motor vehicle registration fees, including compulsory third party insurance and other associated charges
- Workers’ compensation premiums paid by employers

Using information on selected financial and economic activities provided by a business, the SBTC can compare tax liabilities between the different states to see which jurisdiction imposes the lowest tax burden. Not only can the SBTC calculate overall state tax liability for a business, but can allow for analysis and comparison of specific taxes.

Further, the SBTC offers insight into the burden of state business taxes on firms of different size profiles.

Report methodology

To illustrate the features of the IPA SBTC, the tax liability and workers’ compensation premium are calculated for a ‘reference’ business of medium size. This is a hypothetical business entity with similar economic, financial and operational characteristics that is used to highlight tax liabilities across jurisdictions.

The model used in this paper to construct the reference business is drawn from the World Bank’s annual Doing Business project. This project contrasts the ease and costs of operating a business, including tax compliance burdens, across 181 countries. The World Bank’s ‘standard case study company’ is taken to be the
basis for the reference business, and it is then subjected to the SBTC simulations.

To construct their standard case study company the World Bank use a series of weights, called ‘multiplication factors’, to take into account relative incomes for each economy surveyed. In order to capture the impact of taxes on the company, assumptions are also made concerning the employment of labour and specific transactions undertaken. For example, the World Bank company has approximately 60 employees, and this is taken to be the employment size of the reference business used in the SBTC.

The 2008 edition of the IPA SBTC tax benchmarking report was criticised by some state political representatives on the basis that its results were not based on detailed financial data drawn from real-world business entities. In the absence of such information, a reference business model is an accepted alternative method of obtaining tax comparisons (Box 2).

**Box 2: Validity of a hypothetical 'reference business' model for tax benchmarking**

For the purpose of this study, a hypothetical business – labelled a ‘reference business’ – was developed to generate comparable tax liability estimates across states.

In the absence of detailed financial data obtained from real-world entities, the reference business model is used to ensure that calculated differences in state tax liabilities actually reflect differences in tax systems, rather than differences in business characteristics. In other words, a consistent 'like with like' business comparison is provided.

To be sure, the reference business is not necessarily representative of the business population from a statistical perspective. Nonetheless, it accounts for the structural and operational characteristics, and activities, of a business that are reasonably commonplace including the hiring of labour, and ownership and sale of assets.

Consistent with this, as the relative concentrations of businesses of certain size thresholds can vary across the states, the SBTC module can also adjust the scale of the reference business. This effectively allows for sensitivity testing of results.

The development of a hypothetical entity has long represented an acceptable practice in benchmarking studies. The Paying Taxes module of the annual World Bank *Doing Business* project has been in use for three consecutive years and, as an indication of the acceptability of the methodological approach adopted, is used by governments and other relevant stakeholders as a reference to discuss tax policies in an international context.
Box 2 (cont’d): Validity of a hypothetical ‘reference business’ model for tax benchmarking

State governments in the past have also used hypothetical business constructs to sell their tax advantages compared to other jurisdictions. In the 2000-01 Queensland state budget, a hypothetical firm called ‘ABC Enterprises’ was used to compare average tax liabilities across states and territories. The study found that this firm could have saved up to 65 per cent in tax liability if it established operations in Queensland.

The use of hypothetical entities to benchmark interjurisdictional performance is used in other policy contexts. For example, the Productivity Commission has developed a series of regulation benchmarking reports that have used hypothetical businesses on occasions. This regulation benchmarking series has been endorsed by the Council of Australian Governments comprising commonwealth, state and territory heads of government.


Further details on the assumptions and methodology adopted in this report are provided in Appendix A.
Results

The following section provides indicative information on the magnitude of state tax liabilities faced by the SBTC-modelled reference business as at 31 December 2009 if it were to operate in different jurisdictions.\(^{13}\)

State tax liability (excluding worker’s compensation premiums)

In 2010 the reference business will be expected to pay, on average, $236,121 in selected state business taxes and fees (Table 2).

This represents about 18 per cent of the amount of commonwealth corporate income tax (CIT) paid – in other words, in addition to the reference business paying company tax levied by the commonwealth government, the business pays the relevant state government tax imposed on it which equates to approximately 18 per cent of what is paid to the commonwealth.

Table 2: Total state business tax liability

<table>
<thead>
<tr>
<th>State</th>
<th>Total ($)</th>
<th>Percentage of CIT (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>New South Wales</td>
<td>244,457</td>
<td>18.8</td>
</tr>
<tr>
<td>Victoria</td>
<td>228,609</td>
<td>17.6</td>
</tr>
<tr>
<td>Queensland</td>
<td>230,221</td>
<td>17.7</td>
</tr>
<tr>
<td>Western Australia</td>
<td>223,842</td>
<td>17.2</td>
</tr>
<tr>
<td>South Australia</td>
<td>247,437</td>
<td>19.0</td>
</tr>
<tr>
<td>Tasmania</td>
<td>242,161</td>
<td>18.6</td>
</tr>
<tr>
<td>States’ average</td>
<td>236,121</td>
<td>18.1</td>
</tr>
</tbody>
</table>

As at 31 December 2009. Including payroll tax, land tax, land transfer duty, insurance duty, motor vehicle duty and motor vehicle registration fee. WA taxes include Metropolitan Regional Improvement Tax. Excluding workers’ compensation premiums.

Source: IPA State Business Tax Calculator.

The tax liability imposed on the reference business is lowest in Western Australia ($223,842). This amount of liability is 5.2 per cent below the states’ (unweighted) average, and 9.5 per cent below South Australia’s tax liability. WA was followed by Victoria ($228,609), Queensland ($230,221) and Tasmania ($242,161).

\(^{13}\) These results reflect tax changes introduced by the states in their 2009-10 Budgets applicable to 2009 calendar year. They exclude announcements relating to the 2009 tax calendar year.
South Australia levies the highest tax liability of all the states for 2009. The reference business is estimated to incur a $247,437 impost, which is 4.8 per cent above the states’ average.

There is also significant variation between states in terms of liability imposed by specific taxes (Table 3). Across the major tax bases (excluding motor vehicle registrations and workers’ compensation premiums), Western Australia registers the smallest liability levied on a reference business ($221,426). This is primarily due to a relatively low land tax impost.

Conversely, South Australia is the highest taxing jurisdiction in terms of major taxes ($244,110), followed by New South Wales ($242,367) and Tasmania ($239,355).

**Table 3: State business tax liability for selected taxes**

<table>
<thead>
<tr>
<th></th>
<th>Payroll tax</th>
<th>Land tax</th>
<th>Stamp duties</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Total ($)</td>
<td>Total ($)</td>
<td>Total ($)</td>
</tr>
<tr>
<td>New South Wales</td>
<td>174,890</td>
<td>20,573</td>
<td>46,904</td>
</tr>
<tr>
<td>Victoria</td>
<td>154,914</td>
<td>8,156</td>
<td>62,477</td>
</tr>
<tr>
<td>Queensland</td>
<td>159,100</td>
<td>23,509</td>
<td>43,483</td>
</tr>
<tr>
<td>Western Australia</td>
<td>161,127</td>
<td>5,560</td>
<td>54,739</td>
</tr>
<tr>
<td>South Australia</td>
<td>152,439</td>
<td>35,381</td>
<td>56,290</td>
</tr>
<tr>
<td>Tasmania</td>
<td>162,844</td>
<td>32,277</td>
<td>44,234</td>
</tr>
<tr>
<td>States’ average</td>
<td>160,886</td>
<td>20,909</td>
<td>51,355</td>
</tr>
</tbody>
</table>

As at 31 December 2009. Including payroll tax, land tax, land tax, land transfer duty, insurance duty, motor vehicle duty and motor vehicle registration fee. WA taxes include Metropolitan Regional Improvement Tax. Excluding workers’ compensation premiums.

**Source:** IPA State Business Tax Calculator.

**Industry tax liability (including worker’s compensation premiums)**

The IPA SBTC also calculates tax liabilities borne by selected industries, which allows for an estimation of workers’ compensation insurance payments to government.

Table 4 provides information on the tax liabilities plus workers’ compensation premiums of businesses within construction (residential housing), transport (road freight), retail services (clothing), financial services (investor services) and professional services (IT support and consulting).
Table 4: State business tax and workers’ compensation premium liabilities for selected industries

<table>
<thead>
<tr>
<th></th>
<th>Construction Total ($)</th>
<th>Transport Total ($)</th>
<th>Retail services Total ($)</th>
<th>Financial services Total ($)</th>
<th>Professional services Total ($)</th>
</tr>
</thead>
<tbody>
<tr>
<td>New South Wales</td>
<td>434,654</td>
<td>475,497</td>
<td>303,036</td>
<td>258,182</td>
<td>253,435</td>
</tr>
<tr>
<td>Victoria</td>
<td>294,363</td>
<td>386,132</td>
<td>261,504</td>
<td>240,016</td>
<td>240,016</td>
</tr>
<tr>
<td>Queensland</td>
<td>324,650</td>
<td>376,742</td>
<td>244,954</td>
<td>240,178</td>
<td>236,049</td>
</tr>
<tr>
<td>Western Australia</td>
<td>269,469</td>
<td>416,504</td>
<td>267,629</td>
<td>238,560</td>
<td>238,560</td>
</tr>
<tr>
<td>South Australia</td>
<td>368,863</td>
<td>523,405</td>
<td>302,631</td>
<td>269,514</td>
<td>262,155</td>
</tr>
<tr>
<td>Tasmania</td>
<td>379,777</td>
<td>412,893</td>
<td>273,805</td>
<td>258,719</td>
<td>257,247</td>
</tr>
<tr>
<td>States’ average</td>
<td>345,296</td>
<td>431,862</td>
<td>275,593</td>
<td>250,862</td>
<td>247,911</td>
</tr>
</tbody>
</table>

As at 31 December 2009. Including payroll tax, land tax, land transfer duty, insurance duty, motor vehicle duty and motor vehicle registration fee. WA taxes include Metropolitan Regional Improvement Tax. Queensland WorkCover premiums are subject to insurance duty of ten per cent, which are included in this table.

Source: IPA State Business Tax Calculator.

A reference business in South Australia – the highest taxing state – would pay the highest combined taxes and workers’ compensation premiums in transport, financial services and professional services.

At the other end of the scale, Western Australian reference businesses pay the lowest combined taxes and workers’ compensation charges in construction and financial services.

Caveats apply to the calculation of WorkCover liabilities used in Table 4. In particular, a number of states vary the effective premiums paid by applying industry-specific rates based on claims experience of employers in the relevant groups. For simplification, the base industry rate is applied to the reference business within the industries covered in this paper.

Other related charges, such as the NSW dust diseases levy, are excluded from this analysis.

**Impact of reference business scale on tax liabilities**

The IPA SBTC allows the calculation of tax liability according to the size of the business.

Table 5 illustrates the expected taxes to be paid by the reference business of different scale economies. The scales selected are 10 per cent, 50 per cent and 200 per cent of the size of the reference business.
Table 5: State business tax liability for selected reference business scales

<table>
<thead>
<tr>
<th></th>
<th>10 per cent</th>
<th></th>
<th>Reference business</th>
<th></th>
<th>200 per cent</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Total ($)</td>
<td>50 per cent</td>
<td>Total ($)</td>
<td>200 per cent</td>
<td></td>
</tr>
<tr>
<td>New South Wales</td>
<td>4,713</td>
<td>99,544</td>
<td>244,457</td>
<td>543,922</td>
<td></td>
</tr>
<tr>
<td>Victoria</td>
<td>6,079</td>
<td>97,708</td>
<td>228,609</td>
<td>497,408</td>
<td></td>
</tr>
<tr>
<td>Queensland</td>
<td>6,639</td>
<td>82,344</td>
<td>230,221</td>
<td>504,120</td>
<td></td>
</tr>
<tr>
<td>Western Australia</td>
<td>5,270</td>
<td>90,920</td>
<td>223,842</td>
<td>505,303</td>
<td></td>
</tr>
<tr>
<td>South Australia</td>
<td>7,146</td>
<td>97,019</td>
<td>247,437</td>
<td>552,985</td>
<td></td>
</tr>
<tr>
<td>Tasmania</td>
<td>6,688</td>
<td>85,652</td>
<td>242,161</td>
<td>554,482</td>
<td></td>
</tr>
<tr>
<td>States’ average</td>
<td>6,089</td>
<td>92,198</td>
<td>236,121</td>
<td>526,370</td>
<td></td>
</tr>
</tbody>
</table>

As at 31 December 2009. Including payroll tax, land tax, land transfer duty, insurance duty, motor vehicle duty and motor vehicle registration fee. WA taxes include Metropolitan Regional Improvement Tax. Excluding workers’ compensation premiums.

Source: IPA State Business Tax Calculator.

At the smallest reference business scale calculated (10 per cent of normal size), the tax liability imposed by NSW is in fact the lowest of all jurisdictions. This is followed by Western Australia ($5,270), Victoria ($6,079) and Queensland ($6,639). As the business increases in size the tax advantage of NSW dissipates and is, in effect, replaced by WA as the lowest taxing jurisdiction at the normal business reference scale.

Further insights on the effect of scale on tax liabilities can be gleaned by disaggregating on the basis of specific taxes (Table 6).

Table 6: State business tax liability for selected taxes and reference business scales

<table>
<thead>
<tr>
<th></th>
<th>10 per cent</th>
<th></th>
<th>50 per cent</th>
<th></th>
<th>200 per cent</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Total ($)</td>
<td>50 per cent</td>
<td>Total ($)</td>
<td>200 per cent</td>
<td></td>
</tr>
<tr>
<td>Payroll tax</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>New South Wales</td>
<td>0</td>
<td>2,623</td>
<td>69,103</td>
<td>174,890</td>
<td></td>
</tr>
<tr>
<td>Victoria</td>
<td>0</td>
<td>3,018</td>
<td>63,844</td>
<td>154,914</td>
<td></td>
</tr>
<tr>
<td>Queensland</td>
<td>0</td>
<td>2,510</td>
<td>49,862</td>
<td>159,100</td>
<td></td>
</tr>
<tr>
<td>Western Australia</td>
<td>0</td>
<td>2,854</td>
<td>59,938</td>
<td>161,127</td>
<td></td>
</tr>
<tr>
<td>South Australia</td>
<td>0</td>
<td>3,625</td>
<td>61,369</td>
<td>152,439</td>
<td></td>
</tr>
<tr>
<td>Tasmania</td>
<td>0</td>
<td>3,063</td>
<td>50,617</td>
<td>162,844</td>
<td></td>
</tr>
<tr>
<td>Average</td>
<td>0</td>
<td>2,949</td>
<td>59,122</td>
<td>160,886</td>
<td></td>
</tr>
</tbody>
</table>

As at 31 December 2009. Including payroll tax, land tax, land transfer duty, insurance duty and motor vehicle duty. Excluding motor vehicle registration fee and workers’ compensation premiums.

Source: IPA State Business Tax Calculator.
At the lowest reference business scale calculated, Queensland has the lowest liabilities whereas the imposition of $3,063 in stamp duties and $819 in land tax renders Tasmania the highest taxing jurisdiction at the 10 per cent scale level.

For a large reference business (scale at 200 per cent), Tasmania imposes the greatest tax burden ($551,676) followed by South Australia ($549,659) and NSW ($541,832).

The progressive rate structure for many state business taxes increase the effective liability faced by a reference business as it increases in size. For a reference business operating at a tenth of its basic size, the tax liabilities calculated are attributable to the transactions assumed to take place, such as the purchase and subsequent sale of motor vehicles.

Another way to examine these effects is to compare state business taxes across reference business scales, as a percentage of CIT levied by the commonwealth government. As noted by a 2007 BCA study, CIT accounted for two-thirds of total business taxes raised.14

As illustrated in Figure 3, the profile of state business taxes across the different scales reveals a 'L-shaped' curve. Specifically, state taxes impose a high burden on very small businesses up to five per cent of the scale of the reference business. The state business tax burden also tends to increase, albeit slightly, for businesses over 50 per cent of normal reference business size.

Figure 3: State business tax liability as a proportion of commonwealth corporate income tax

As at 31 December 2009. Including payroll tax, land tax, land transfer duty, insurance duty, motor vehicle duty and vehicle registration fee. WA taxes include Metropolitan Regional Improvement Tax. Including workers’ compensation premiums. Queensland WorkCover premiums are subject to insurance duty of ten per cent, which are included in this figure. South Australia and Western Australia highlighted in bold, signifying highest and lowest taxing jurisdictions respectively at the normal reference business scale (100 per cent).

Source: IPA State Business Tax Calculator.

Unlike corporate income taxes, transaction taxes at the state level tend to be insensitive to variations in profitability. Revenues from stamp duties are raised when a transaction is made, such as the purchase of land, a motor vehicle or insurance product. Since these transactions are assumed to be undertaken by the reference business, regardless of scale, it follows that state tax burdens will be disproportionately high on small firms with low profitability.

In terms of large businesses, the value of transactions tends to be relatively higher therefore state business tax liabilities tend to be large. The expanded reference business also bears higher payroll and land taxes, as they exceed tax-free thresholds. For these reference businesses, commonwealth corporate taxation tends to be higher compared to a small entity.

Very small reference businesses (at 0.5 per cent of normal scale) operating in Queensland pay the highest state business tax liabilities as a proportion of their commonwealth taxes. This is attributable to relatively high motor vehicle registration fees in that state, as well as a relatively low land transfer duty threshold.
By the ten per cent scale level, South Australia becomes the highest taxing jurisdiction as it claws back substantial duty revenue from non-residential property transfers. South Australia maintains this uncompetitive tax position at most reference business scale levels.

**Conclusion**

The publication of results generated by the IPA State Business Tax Calculator has a potentially more far-reaching objective than to provide a transparent, robust comparison of state business tax liabilities for a real or hypothetical business, as important as this may be.

It is hoped that the publication of these results will also help to foster greater yardstick competition between the states. As competitive pressures between states puts downward pressure on tax liabilities, businesses and citizens stand to benefit from the consequent cost savings and greater incentives to grow, save, invest and employ resources.

Attaining these potential benefits assumes even greater importance in an economic climate whereby wasteful fiscal stimulus programs pursued by federal and state governments alike will otherwise act as a drag on future productivity growth.

As this paper has shown, transaction-based business taxes at the state level with relatively low thresholds disproportionatley affect smaller businesses. This affects their capacity to acquire capital, labour and materials to expand.

At the other end of the scale, larger businesses are also adversely affected by state business taxation. In general terms, larger businesses tend to employ large numbers of people and invest significant amounts of capital in an attempt to exploit economies of scale and scope. State taxes can have often deleterious consequences, at least at the margin, for further expansion of existing firms.

Based on the analysis presented in this edition of the IPA state business tax benchmarking exercise, it is clear that state taxation should be reformed as a matter of priority to promote business development that, in turn, leads to sustainable investment, jobs and growth.
**Appendix A:**

**Methodology and assumptions**

*Introduction*

The Institute of Public Affairs State Business Tax Calculator (SBTC) is a quantitative spreadsheet model used to estimate financial liabilities imposed on real or hypothetical businesses attributable to state business taxes, including payroll tax, land tax, stamp duties, motor vehicle registration fees and workers’ compensation premiums.

*Reference business model and assumptions*

For the purpose of this study, a hypothetical business – labelled a ‘reference business’ – was developed to generate comparable business tax liability estimates across the six Australian states.

The underpinning financial and operational characteristics of the reference business are drawn from the ‘case study company’ used in the Paying Taxes module of the annual World Bank Doing Business competitiveness project. The uniform characteristics are selected to ensure that differences in state business tax liabilities reflect variations in tax structures, and not upon the underlying structure of the reference business construct.

Using information contained in the latest Paying Taxes report, a balance sheet (Table A.1) and profit-and-loss statement (Table A.2) is devised for the reference business.

**Table A.1: Balance sheet for reference business**

<table>
<thead>
<tr>
<th>Category</th>
<th>Multiplication factor</th>
<th>Value ($)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current assets</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Net cash</td>
<td>20</td>
<td>1,098,380</td>
</tr>
<tr>
<td>Inventory</td>
<td>35</td>
<td>1,922,165</td>
</tr>
<tr>
<td>Accounts receivable</td>
<td>50</td>
<td>2,745,960</td>
</tr>
<tr>
<td>Fixed assets (acquisition value)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Land</td>
<td>30</td>
<td>1,647,570</td>
</tr>
<tr>
<td>Buildings</td>
<td>40</td>
<td>2,196,760</td>
</tr>
<tr>
<td>Machinery</td>
<td>60</td>
<td>3,295,140</td>
</tr>
<tr>
<td>Motor vehicles</td>
<td>5</td>
<td>274,595</td>
</tr>
<tr>
<td>Computers</td>
<td>5</td>
<td>274,595</td>
</tr>
<tr>
<td>Office equipment</td>
<td>5</td>
<td>274,595</td>
</tr>
<tr>
<td>Total assets</td>
<td>250</td>
<td>13,729,750</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Category</th>
<th>Multiplication factor</th>
<th>Value ($)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current liabilities</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Short term debt</td>
<td>43</td>
<td>2,361,517</td>
</tr>
<tr>
<td>Accounts payable</td>
<td>50</td>
<td>2,745,950</td>
</tr>
<tr>
<td>Long term liabilities</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Long term debt</td>
<td>55</td>
<td>3,020,545</td>
</tr>
<tr>
<td>Equity</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Paid-in capital</td>
<td>102</td>
<td>5,601,738</td>
</tr>
<tr>
<td>Total liabilities and equity</td>
<td>250</td>
<td>13,729,750</td>
</tr>
</tbody>
</table>

As at 31 December 2009.  
**Source:** PricewaterhouseCoopers, 2009, Paying Taxes 2010: The global picture; IPA calculations.

Specific weights are then applied to each line item of the accounts – for example, turnover is assumed to be 1,050 times income per capita. For this study, these
weights are called ‘multiplication factors.’ We then apply Australia’s GDP per capita (estimated at $54,919 for 2009-10) to each multiplication factor to derive a value for each account line item.

Estimated tax results using this methodological approach can vary from year to year to the extent that the ‘flex mechanism’ of GDP per capita changes.

**Table A.2: Profit and loss statement for reference business**

<table>
<thead>
<tr>
<th>Category</th>
<th>Multiplication factor</th>
<th>Value ($)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales</td>
<td>1050</td>
<td>57,664,950</td>
</tr>
<tr>
<td>Cost of goods sold</td>
<td>875</td>
<td>48,054,125</td>
</tr>
<tr>
<td>Salaries for:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Managers</td>
<td>9</td>
<td>494,271</td>
</tr>
<tr>
<td>Assistants</td>
<td>10</td>
<td>549,190</td>
</tr>
<tr>
<td>Workers</td>
<td>48</td>
<td>2,636,112</td>
</tr>
<tr>
<td>Administrative expenses</td>
<td>10</td>
<td>549,190</td>
</tr>
<tr>
<td>Advertising expenses</td>
<td>10.5</td>
<td>576,650</td>
</tr>
<tr>
<td>Machinery repaid</td>
<td>3</td>
<td>164,757</td>
</tr>
<tr>
<td>Interest expense</td>
<td>5.5</td>
<td>302,054</td>
</tr>
<tr>
<td>Profit</td>
<td>79</td>
<td>4,338,601</td>
</tr>
</tbody>
</table>

As at 31 December 2009.


Of these line items, those which are subject to state business taxes are selected as inputs for the SBTC.

Additional assumptions are required to ensure comparability of liabilities upon the reference business across jurisdictions:

- The business will sell property at a price equivalent to 25 per cent of the total value of land held.
- The business will pay ten per cent of administrative expenses in insurance premiums, excluding workers’ compensation and motor vehicle insurance premiums.
- The business pays insurance premiums on motor vehicles owned at a rate of five per cent of the total value of vehicles owned.
- The business sells motor vehicles at a price equivalent to 25 per cent of the total market value of vehicles owned.
- The business owns five vehicles (cars), all of which are subject to vehicle registration fees and insurance.
- It is assumed that the business does not employ apprentices or trainees.
Table A.3: Values of selected transactions for reference business

<table>
<thead>
<tr>
<th>Category</th>
<th>Value ($)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total land value</td>
<td>1,647,570</td>
</tr>
<tr>
<td>Sale price of land</td>
<td>961,083</td>
</tr>
<tr>
<td>Total salaries</td>
<td>3,679,573</td>
</tr>
<tr>
<td>Business insurance</td>
<td>54,919</td>
</tr>
<tr>
<td>Total value of vehicles</td>
<td>274,595</td>
</tr>
<tr>
<td>Vehicle insurance</td>
<td>13,730</td>
</tr>
<tr>
<td>Purchase/sale of second-hand car</td>
<td>68,649</td>
</tr>
<tr>
<td>Profit</td>
<td>4,338,601</td>
</tr>
<tr>
<td>Corporate income tax liability</td>
<td>1,301,580</td>
</tr>
</tbody>
</table>

As at 31 December 2009.

Source: IPA calculations.

Reference business scale

The IPA SBTC includes a scaling factor to adjust the size of the reference business in an equi-proportional manner. For example, if the reference business size is scaled up by ten per cent then all financial aggregates and transactions are increased by that amount.

Quality checks

To ensure the accuracy and robustness of the estimates generated by the SBTC, the results are tested against tax calculators provided by state governments.