5 International comparison of Australia's tax-transfer system

Outline

This section provides an international comparison of some key aspects of Australia's tax-transfer system.

Key points

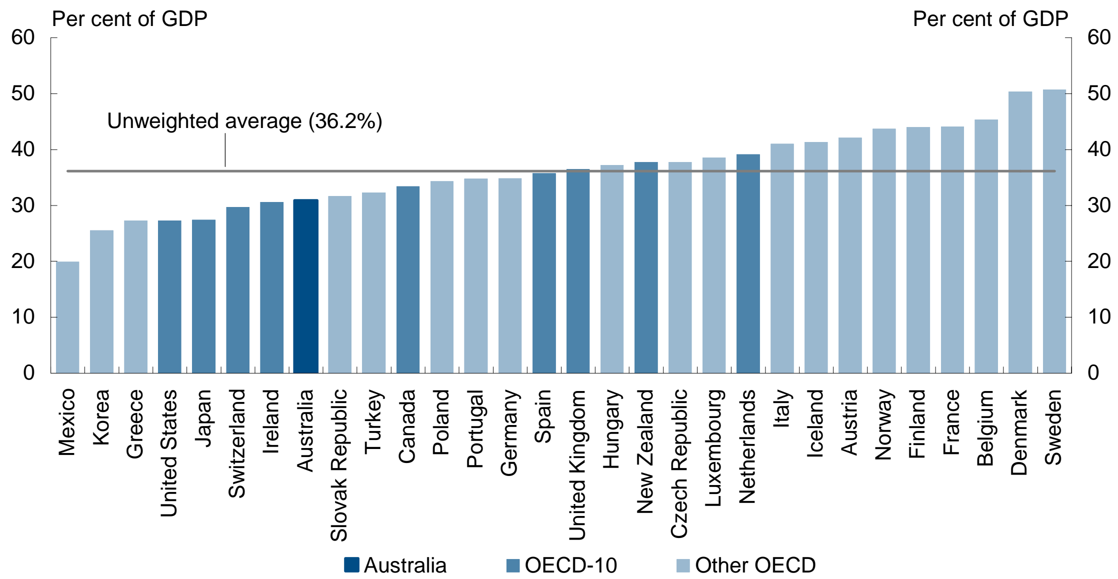
- Australia is a low tax country by OECD standards but our tax to GDP ratio is above that of our immediate neighbours, reflecting the greater role of government in our economy.
- While Australia's mix of direct and indirect taxation is broadly comparable to other OECD countries, its composition differs in several respects. Australia is one of two countries, with New Zealand, that do not levy a social security tax and which have a dividend imputation system. Our reliance on broad-based consumption taxes is below the OECD average, while our reliance on revenue from taxes on property is greater.
- Although Australia's top personal income tax rate is typical of the OECD, the absence of a social security tax means that Australia has a high tax burden on capital income relative to comparable OECD countries, taking into account differences in capital tax settings.
- Australia's corporate tax rate is the eighth highest in the OECD and above the OECD average. Corporate tax revenue as a percentage of GDP is the fourth highest in the OECD.
- Australia's taxes on fuel are low in comparison to other OECD countries.
- Australia's tax-transfer system is highly redistributive by OECD standards.

5.1 Australia's tax to GDP ratio by OECD standards

Australia's tax to GDP ratio is the eighth lowest in the OECD and substantially below the OECD average of 36.2 per cent (Chart 5.1). Government spending in Australia is the third lowest of all 30 OECD countries (Chart 5.2).

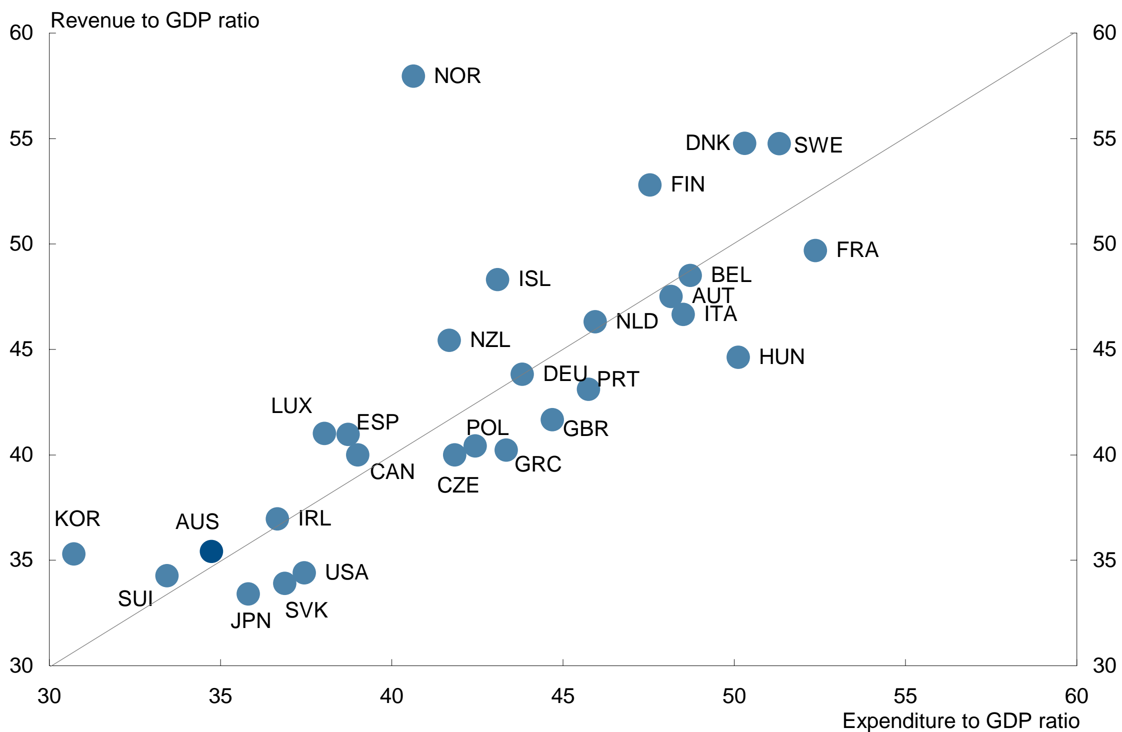
The gap between Australia's tax to GDP ratio and the OECD average has remained relatively constant at around 5.5 percentage points of GDP since 1965. Compared with the nine most comparable OECD countries (see Box 5.1), Australia's tax to GDP ratio is about average. However, two of the nine countries with lower tax to GDP ratios than Australia also run significant fiscal deficits (the United States and Japan).

Chart 5.1: Tax revenue as a percentage of GDP — OECD 2005



Source: OECD (2007a).

Chart 5.2: Size of government — OECD 2007(a)(b)



(a) Data for Mexico and Turkey not available.
(b) Revenue refers to receipts of tax and non-tax revenue.
Source: OECD (2008a).

Box 5.1: Comparator countries — the OECD-10

In the *International Comparison of Australia's Taxes* (Australian Government 2006) nine OECD countries were identified as being more suitable for drawing comparisons about specific tax settings. A key determinant of the countries selected was that they had broadly similar revenue to GDP and government spending to GDP ratios, as well as a similar role of government in their economies. One country, the Netherlands, was also included on the basis that it has strong investment and trade links with Australia and offered some interesting comparisons in terms of its capital tax settings. These nine countries — Canada, Ireland, Japan, the Netherlands, New Zealand, Spain, Switzerland, the United Kingdom and the United States — are also used in this paper to draw international comparisons of Australia's tax settings, in addition to the broader 30 OECD countries.

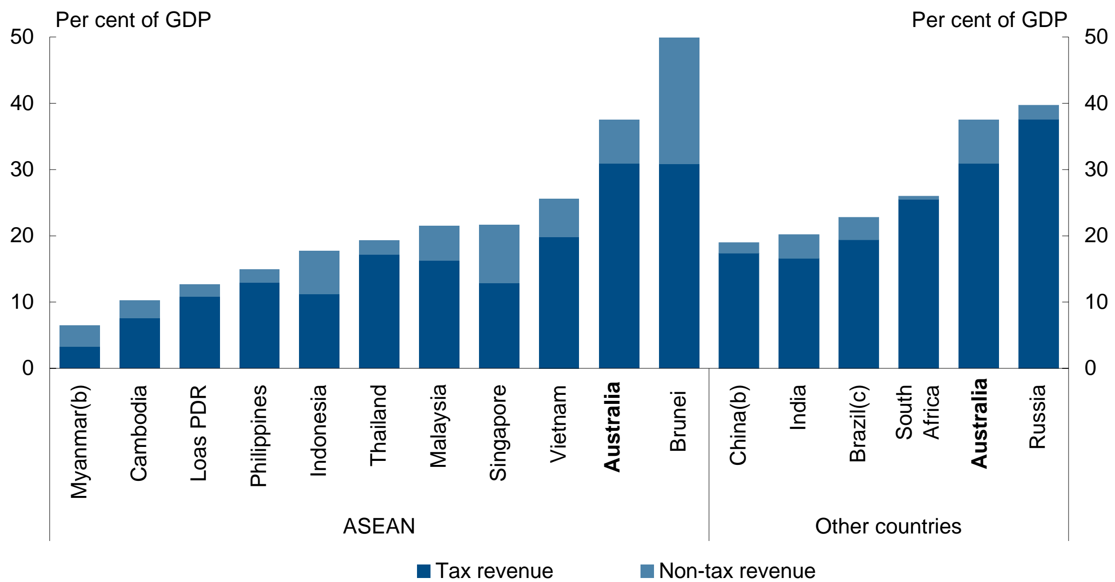
5.2 Tax to GDP ratios in other countries including our immediate neighbours

As a percentage of GDP, tax revenue in Australia is significantly higher than most ASEAN countries, as shown in Chart 5.3. While tax revenue in Brunei Darussalam is around the same as that of Australia as a percentage of GDP, 95 per cent of this comes from oil and gas companies. For many of these countries non-tax revenues, such as land sales and official development assistance, contribute a more significant proportion of overall government revenue. The role of government also tends to be more limited. When considering investment decisions, tax is only one of a range of factors, including: macroeconomic stability; a supportive legal and regulatory framework; skilled labour and labour market flexibility; and well-developed infrastructure. It is plausible that as these economies grow and the standards of living of our immediate neighbours rise, the role of government and the level of taxation in these countries will expand, as has been the case across most OECD countries over past decades.

The chart also shows a range of other countries, including Brazil, China, India, Russia and South Africa. Brazil, China, India and Russia represent around a quarter of world GDP and are increasingly integrating into the world economy. China and India are important trading partners and competitors for Australia. Brazil and Russia are significant commodity exporters, particularly in agricultural and resource commodities. South Africa is also an important commodity producer and exporter, particularly of minerals.

Relative to Brazil, China and India, Australia's tax to GDP ratio is high. It is more comparable with that of Russia and South Africa. In part, this reflects differences in the role of government expenditure. In Russia and South Africa, social expenditure as a proportion of total government expenditure is more comparable with Australia.

Chart 5.3: Tax and non-tax revenue as a percentage of GDP
Australia, ASEAN and selected other countries (2005)[a]

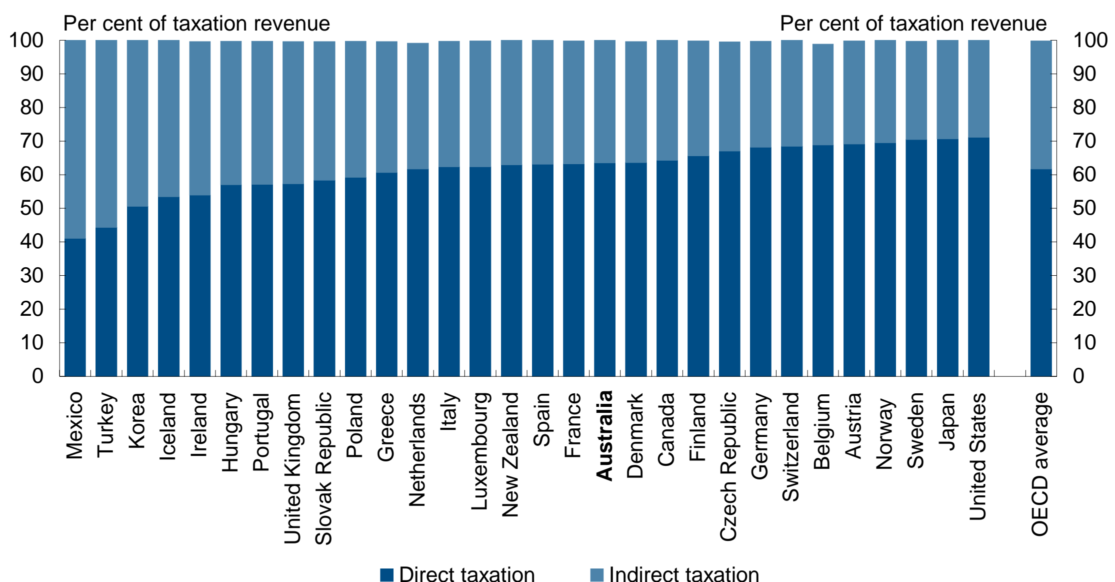


(a) Unless otherwise indicated, data reflect revenues at all levels of government.
(b) Data for 2004.
(c) Brazilian central government only.
Source: OECD (2007a); International Monetary Fund country reports; national governments; Australian Treasury estimates.

5.3 Australia's tax mix compared with other OECD countries

The Australian tax mix is broadly comparable with most OECD countries. Like most of these countries, Australia raises the majority of its tax revenue (64 per cent) from direct taxes on incomes. The OECD average is 62 per cent (Chart 5.4). The remaining 36 per cent of Australia's tax revenue is raised through indirect taxes including GST, excise and customs duties, and property taxes.

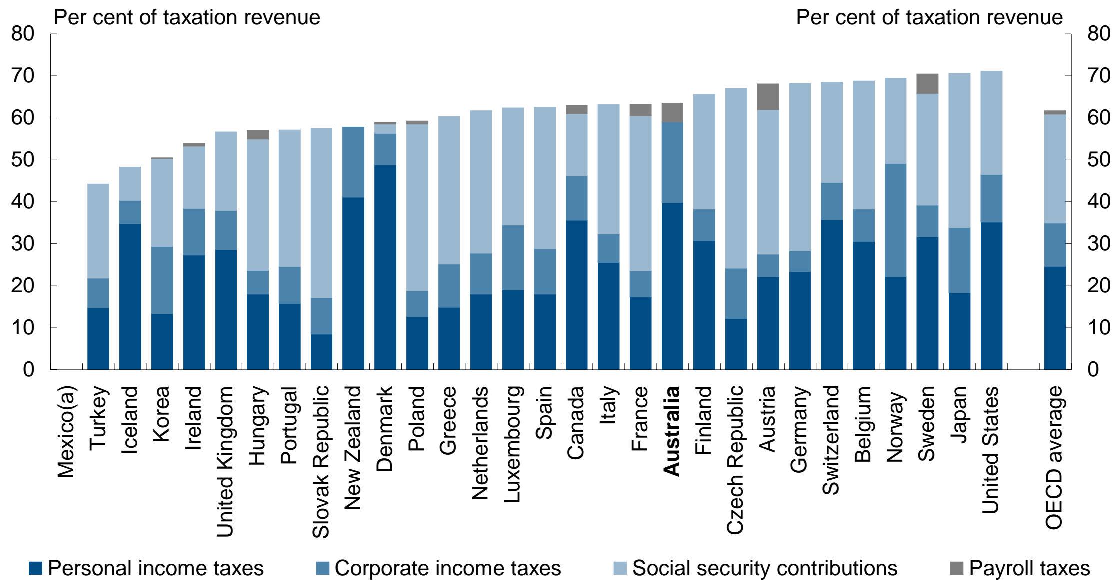
Chart 5.4: Direct and indirect taxes as a proportion of total tax revenue
OECD 2005



Source: OECD (2007a).

While the share of direct and indirect taxes in Australia is broadly comparable with the OECD average, there are some distinguishing features in terms of its composition. Australia is one of two OECD countries that do not raise tax revenue from social security contributions (Chart 5.5). The contribution of corporate income tax is higher for Australia than for most OECD countries.

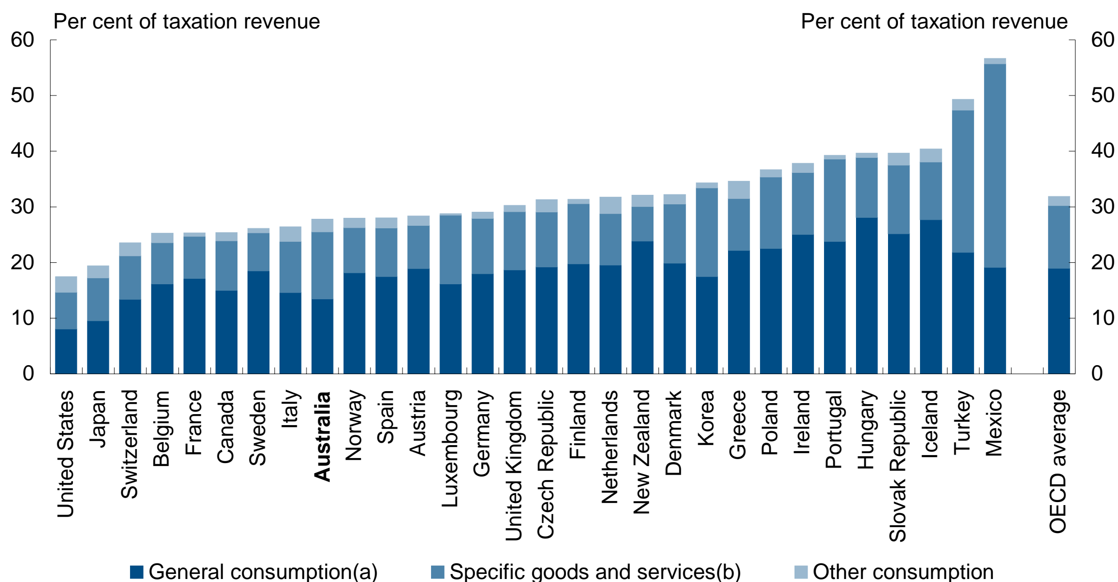
Chart 5.5: Components of direct taxation — OECD 2005



(a) Disaggregated income tax data for Mexico not available.
Source: OECD (2007a).

As with direct taxes, there are differences between the components of consumption tax in Australia and in other OECD countries. The most significant is the contribution to total tax revenue from general consumption taxes, which include value added taxes like the GST. In Australia, general consumption taxes (mainly the GST) contribute 13 per cent of tax revenue compared with an OECD average of 19 per cent (Chart 5.6).

Chart 5.6: Components of consumption taxation — OECD 2005

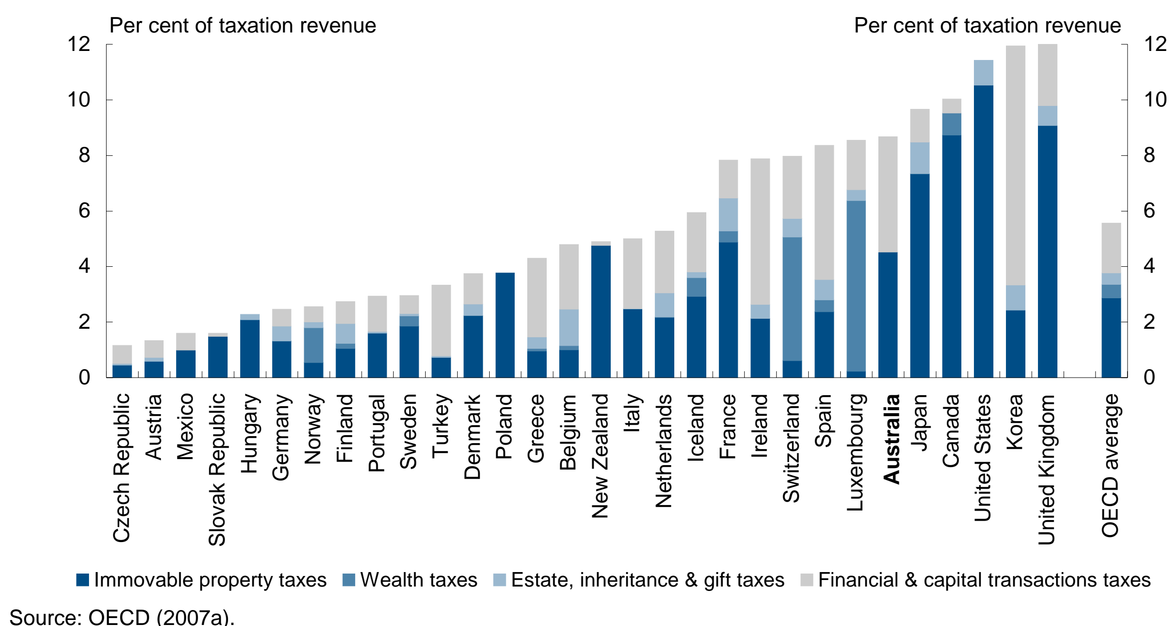


(a) Includes value added taxes.
(b) Includes excises.
Source: OECD (2007a).

Property taxes contribute just under 9 per cent of total Australian tax revenue compared with an OECD average of just under 6 per cent (Chart 5.7). Australia's property taxes come from two main sources. Taxes on immovable property contribute around 4.5 per cent to total tax revenue compared with an OECD average of around 3 per cent. Taxes on financial and capital transactions, which include conveyancing stamp duties, contribute around 4 per cent of tax revenue, compared with an OECD average of around 2 per cent.

Australia is one of 17 OECD countries that does not levy wealth taxes. This is an important source of revenue for only two countries — Switzerland (4.5 per cent of total tax revenue) and Luxembourg (6.2 per cent of total tax revenue). Australia is one of four OECD countries that does not levy estate, inheritance or gift taxes. However, in those countries that do, these taxes make a negligible contribution to total tax revenue, with an average across the OECD of around half of one per cent.

Chart 5.7: Components of property tax — OECD 2005



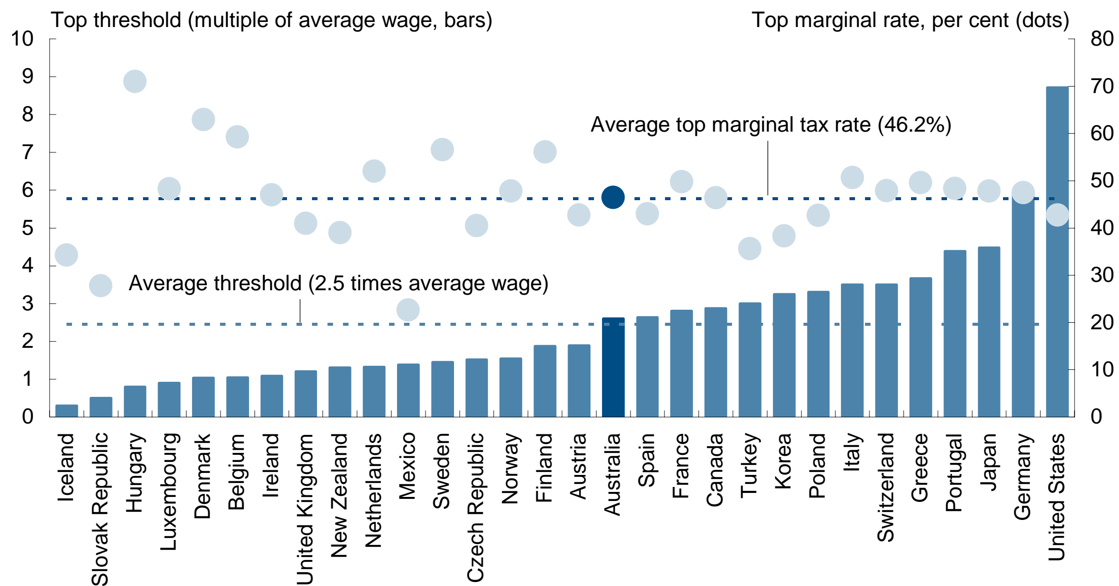
Source: OECD (2007a).

5.4 Australia's top personal tax rate

Chart 5.8 compares Australia's top marginal tax rate and threshold (as a multiple of the average wage) with other OECD countries in 2007. Australia's top marginal tax rate is average for the OECD.

Australia's top personal tax rate threshold was 2.6 times the OECD's measure of average wages — comparable with the OECD average of 2.5 times the average wage. The top threshold is within the same range as other OECD-10 countries. Increases in the top threshold over the past five years have improved Australia's relative position. This position may change again with the 1 July 2008 increase in this threshold. However, the relative position will depend on changes in other OECD countries.

Chart 5.8: Top marginal tax rates and thresholds for employees — OECD 2007
(unweighted averages)



Source: OECD Tax Database.

5.5 Approaches to taxing retirement savings

In Australia, retirement savings vehicles are subject to tax. Superannuation contributions and earnings are generally taxed at a flat rate of 15 per cent and benefits from a taxed fund are paid tax free from age 60 (see Section 2 for further detail).

Warburton and Hendy (Australian Government 2006) found that it was not possible to draw a conclusion about the relative ranking of the concessionality of the taxation arrangements applying to Australian retirement savings, owing to the lack of data and methodological issues with the various studies on the subject. However, their study found that Australian retirement savings are taxed concessionally compared to other savings. Section 8 compares the nominal effective marginal tax rate of superannuation with other assets and financing arrangements.

Australia's approach to taxing retirement savings follows a comprehensive income tax model, although generally at concessional rates of tax on contributions and earnings compared to the rates applied to income. In contrast, most retirement savings systems across the world follow variants of the expenditure tax model (Box 5.2).

Box 5.2: Definitions of alternative taxation regimes

In the academic literature, retirement savings tax regimes are generally classified by three letters which indicate the point(s) at which taxation is imposed. The presence of a 'T' reflects the imposition of tax, while an 'E' indicates an exemption from taxation. It does not reflect the overall burden of the tax imposed (for example, a system that imposes 1 per cent tax on contributions, 1 per cent tax on earnings, and 1 per cent tax on benefits would be described as 'TTT').

An expenditure tax model exempts contributions and earnings from tax, and taxes benefit payments ('EET'). In contrast, a comprehensive income tax model taxes contributions and earnings, and exempts benefit payments from tax ('TTE').

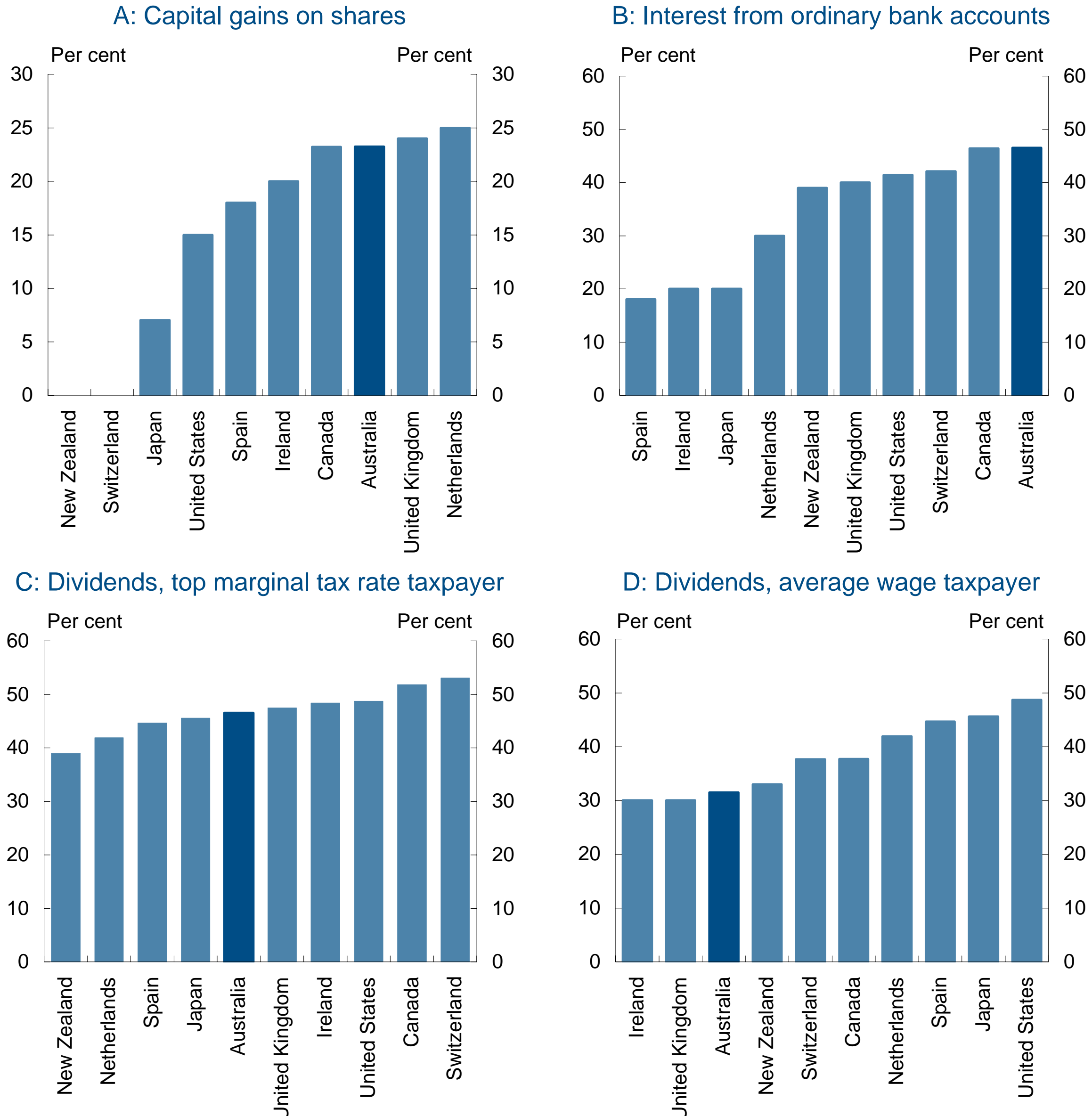
From a theoretical perspective, a TEE model produces an equivalent retirement income outcome to an EET model (for the same value of 'T'). Similarly, an ETT model produces an equivalent retirement income result to a TTE model.

5.6 Comparisons of the top personal tax rate on capital income

Chart 5.9 shows the top personal tax rate for the OECD-10 countries for three major classes of capital income, with Panel D showing tax on dividends at the marginal tax rate for the average worker.

Among the OECD-10 countries, Australia has one of the higher top personal tax rates on capital gains, notwithstanding the 50 per cent discount available for gains on assets held for at least 12 months. There is significant divergence between countries in the treatment of capital gains (Panel A). New Zealand does not impose capital gains tax (CGT) and of those that have a CGT regime, some have a flat rate, two have a stepped rate (as the holding period increases the tax rate decreases), and others (such as Australia and Canada) use a discount system for taxing capital gains (that is, only a proportion of the gain is taxable). For shares, Switzerland does not tax capital gains and the Netherlands only does so for gains on substantial holdings (greater than 5 per cent ownership).

Notwithstanding its comparable top personal income tax rate, Australia has a relatively high rate of tax on interest income compared with other OECD-10 countries. Many countries in the OECD-10 have a lower tax rate on interest income compared to the personal tax rate on wages and salaries. This generally arises because social security contributions apply to wage and salary income and not to capital income. For the Netherlands, a lower tax rate on capital income is a key feature of their schedular approach to tax. Half of the OECD-10 treat interest income as ordinary personal income for taxation purposes, namely: Australia; Canada; New Zealand; Switzerland; the United Kingdom; and the United States. Ireland, Japan and Spain impose final withholding taxes on interest at source while the Netherlands, which uses a schedular tax system, taxes an imputed return on deposits (Panel B).



Source: OECD Tax Database, unpublished OECD estimates, International Bureau of Fiscal Documentation, national tax administrations, Australian Treasury estimates.

Panels C and D illustrate tax rates on distributions of domestic source income to a resident individual shareholder, including corporate income tax, personal income tax and any type of integration or relief to reduce the effects of double taxation. The charts show that Australia's top overall tax rate on dividends sourced from domestic profits is in the middle of the range of other OECD-10 countries for high income earners, and relatively low for average income earners.

For Australia and New Zealand, the charts highlight the use of a full imputation system (where the credit depends on company tax paid). For the majority of the remaining countries, the top overall tax rate on dividends is greater than the top marginal personal tax rate, which primarily reflects their integration systems only providing partial relief of the double taxation of dividend income. The imputation system also has different equity implications as indicated by the change in Australia's ranking from fifth lowest for high income earners to second lowest for average income earners.

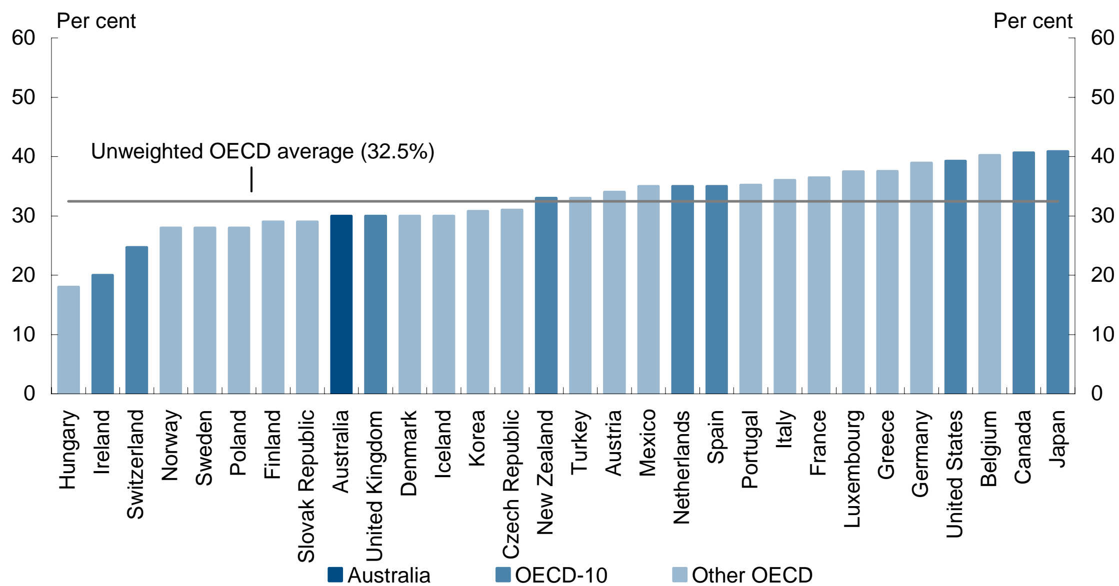
5.7 OECD comparison of Australia's corporate tax rate

Australia's corporate tax rate is above the OECD average. In 2001, following the reduction in the company tax rate from 36 per cent to 30 per cent, Australia's corporate tax rate was ranked 9th lowest in the OECD, equal to Demark, Iceland and the United Kingdom. The OECD average was 32.5 per cent (Panel A of Chart 5.10). In 2008, the corporate tax rate was 21st lowest, equal with New Zealand and Spain, and above the OECD average of 26.6 per cent (Panel B of Chart 5.10).

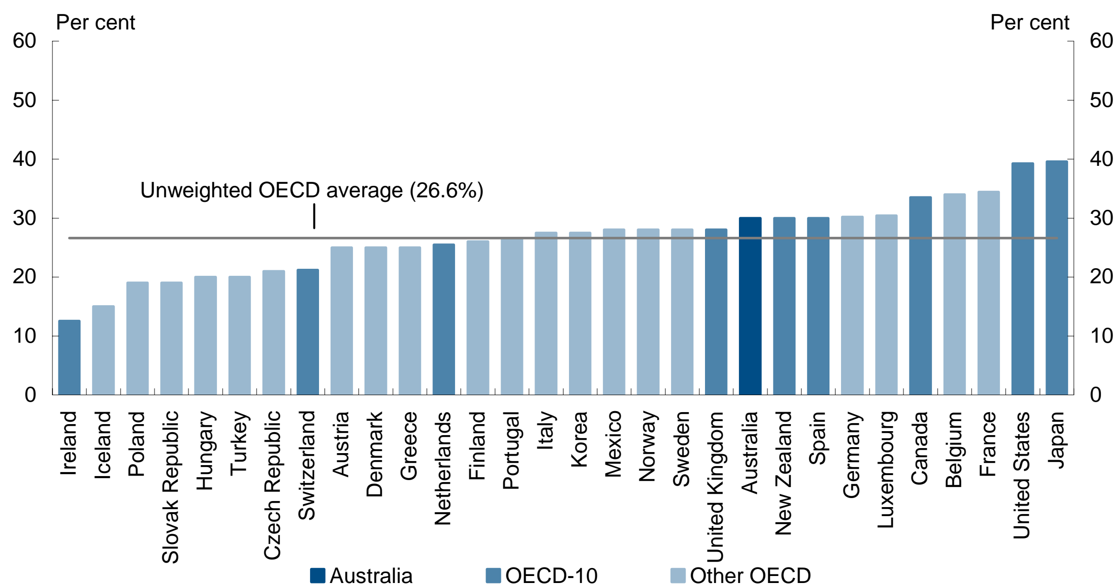
Since 2001 the unweighted average corporate tax rate for OECD countries has decreased by around 6 percentage points. This reflects the trend among OECD countries toward lower corporate tax rates driven, in part, by concerns about global capital mobility and economic efficiency.

Chart 5.10: Statutory corporate tax rate — OECD[(a)]

Panel A: 2001



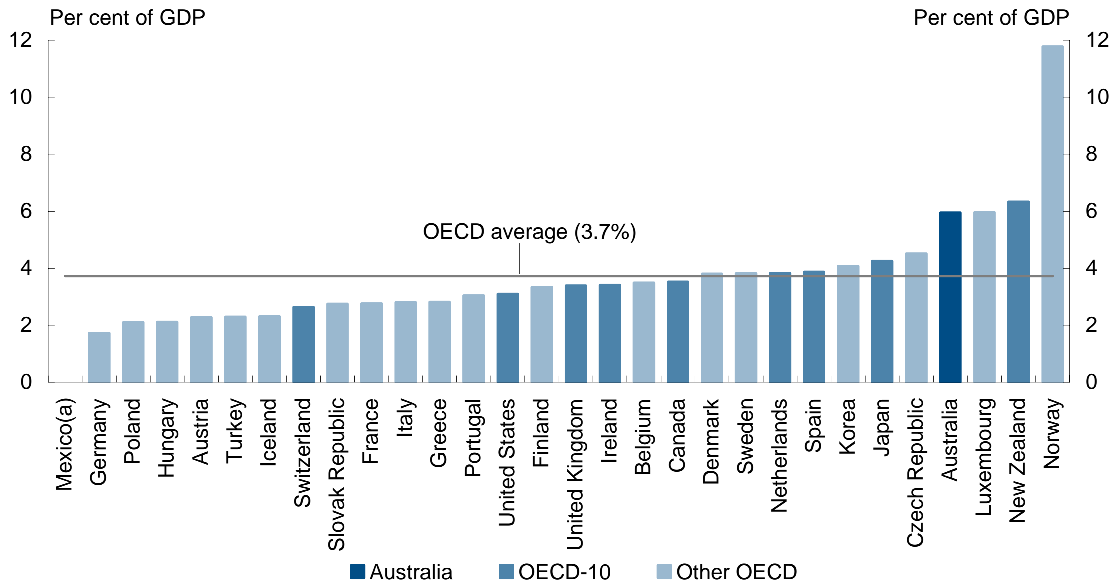
Panel B: 2008



(a) Rates are full (national, sub-national and surcharge) statutory corporate tax rates.
Source: OECD Tax Database.

Australia's corporate tax revenue as a proportion of GDP is the fourth highest in the OECD and significantly higher than the OECD average of 3.7 per cent (Chart 5.11). This largely reflects structural differences in the composition of the incorporated sector in Australia compared with other OECD countries, the imputation system, as well as the strong performance of the Australian corporate sector in recent years.

Chart 5.11: Corporate tax revenue as a proportion of GDP — OECD 2005

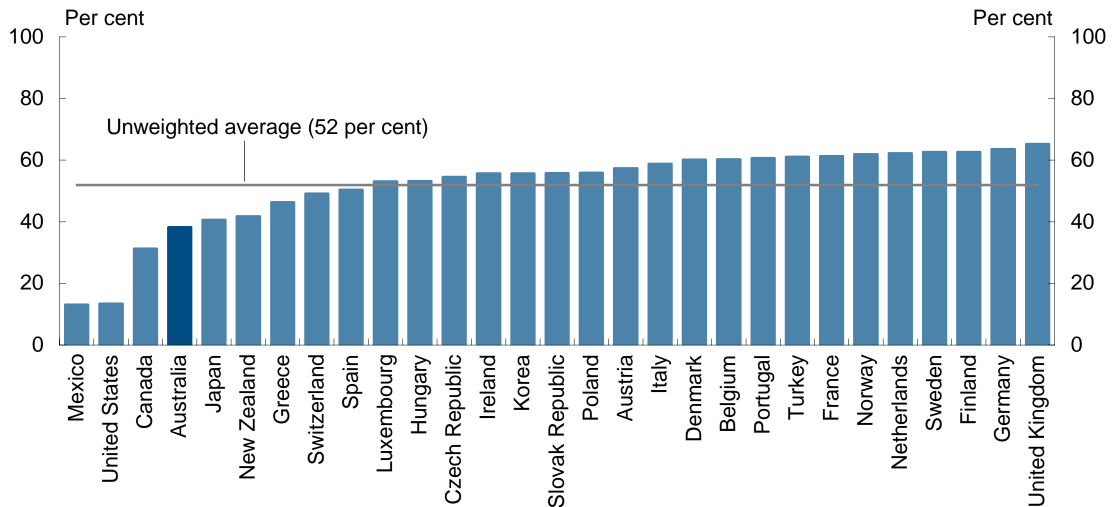


(a) Data for Mexico not available.
Source: OECD (2007a).

5.8 Taxes on fuel

All OECD countries impose taxes on petrol (Chart 5.12). The latest comparable data (first quarter 2008) show that Australia's petrol taxes are lower than the OECD average. The percentage of the total price attributable to taxes in Australia is the fourth lowest of the 28 OECD countries for which data are available.

Chart 5.12: Taxes as percentage of unleaded petrol price in 28 OECD countries
Includes excise/VAT-GST/sales taxes

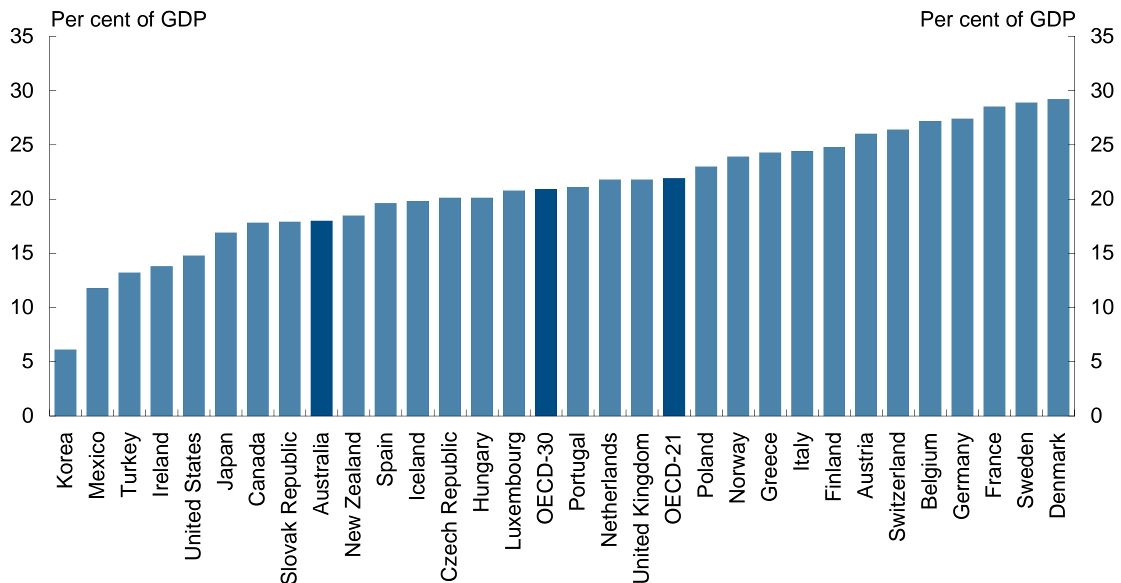


Source: International Energy Agency (2008).

5.9 OECD comparison of Australia's tax-transfer system

Compared with other OECD countries the Australian tax-transfer system is highly redistributive to those with least means. Australia's spending on social security is below the OECD average (Chart 5.13). This reflects a range of factors, including benefit levels that are unrelated to previous earnings, employer rather than public provision of sick leave and other important structural differences from most OECD countries.

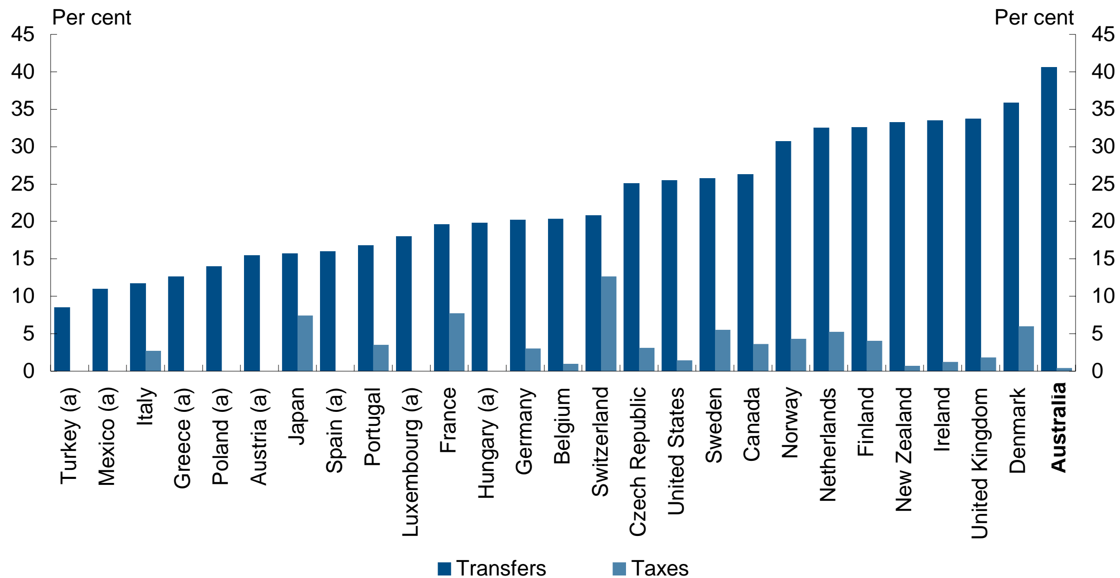
Chart 5.13: Social welfare spending as a percentage of GDP in 2001[(a)]



(a) 1999 data for Turkey for 2000 and 2001 OECD averages. OECD averages exclude countries where data are not available for related time series. OECD-21 exclude Austria, Czech Republic, Hungary, Iceland, Korea, Mexico, Norway, Poland and Slovak Republic.
Source: Whiteford (2007).

Despite Australia's relatively low level of aggregate spending, of the 27 OECD countries for which data are available, it has the highest proportion of public transfers flowing to the quintile of the population with the lowest private incomes (Chart 5.14). It also has the lowest rate of direct taxation on this quintile of the 19 countries that provide these data. This reflects the highly targeted nature of the Australian tax-transfer system.

Chart 5.14: Proportion of cash transfers received and direct taxes paid by households in the bottom quintile of the private income distribution — OECD 2005

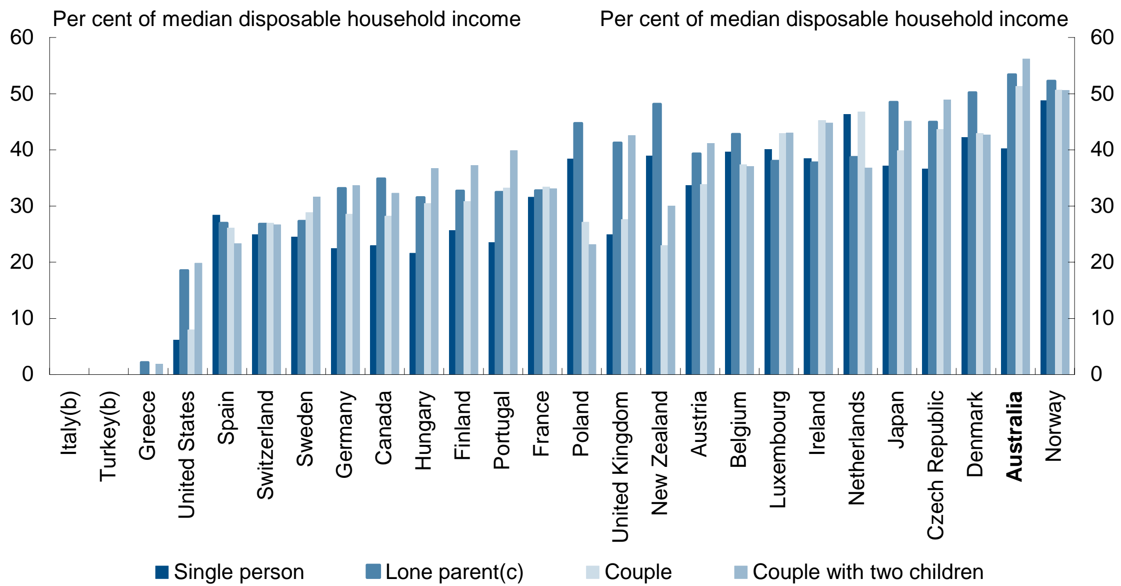


(a) Tax data not available.
Source: Whiteford (2005).

International comparisons of transfers can be complex because of the extent to which some countries often have short-term income related payments. However, the fundamental social assistance component of Australia's support to working aged families and individuals in periods of unemployment or other joblessness, provides a much higher replacement rate of income than most other OECD countries. Of the four family types for which the OECD publishes data, Australia has the highest replacement rate, relative to median disposable household income, for three family types, including both family types with children (Chart 5.15).

The highly targeted nature of the tax-transfer system has resulted in Australia having higher effective tax rates (ETRs) for certain household types than in other OECD countries. In three of the four household types with children, Australia has ETRs above the OECD average (OECD 2007b).

Chart 5.15: Net incomes of social assistance recipients relative to median household disposable income — OECD 2005[(a)]



(a) The OECD data for Australia is based on people receiving allowances. The replacement rates will be higher if the particular family type shown is receiving a pension.
(b) Data for Italy and Turkey not available.
(c) The lone parent family shown has two children aged four and six years.
Source: OECD (2007c), FaHCSIA estimates.