

Senate Standing Committee on Economics

ANSWERS TO QUESTIONS ON NOTICE

Treasury Portfolio

Budget Estimates

1 June – 3 June 2010

Question: BET 389

Topic: Treasury Paper - Disparities in Average Rates of Company Tax across Industries

Hansard Page: Written

Senator EGGLESTON asked:

1. A paper by three treasury officials titled “Disparities in average rates of company tax across industries” appeared on the Treasury website on 24 May. It concludes “The average tax rate is found to be relatively high in the finance & insurance industry and relatively low in the most capital-intensive industries, such as electricity, gas & water, and mining.” Also released that day to some journalists but not I believe publicly was a Treasury minute to the Treasurer recommending the release of the paper and providing some additional information not included in the article. This included estimates of average tax rates for the ten years to 2004-05 for mining (17%), transport & storage (27%) and finance & insurance (29%). These numbers were cited by the Treasurer and the finance minister.
 - a) Exactly when was the paper written?
 - b) Was it intended for publication/ If so, where?
 - c) Who decided that it should be released before publication?
 - d) Why was this done?
 - e) Is the data used in the paper publicly available?
 - f) If not, will Treasury make the data publicly available? (And if not, why not?)
 - g) Why does the paper use data to 2004-05? Was any later data available?
 - h) Has any work been done to update the data? If not, why not?
 - i) It quotes Markle and Shackelford (2009 not 2010) as “external validation”. Did the authors or any reviewers of the paper critically assess the validity of Markle and Shackelford (2009) or note that the 2010 update had removed the numbers relied upon for external validation?
 - j) The minute provides results for mining; electricity, gas & water (average tax rate of only 1%); construction (19%); transport & storage; communication (17%); finance & insurance. These sectors make up one third (34%) of gross domestic product. Average tax rates were calculated for some other sectors. These were agriculture; manufacturing; wholesale trade; retail trade; accommodation, cafes and restaurants; and property and business services. Why weren’t the results of these other sectors included?
 - k) Is it true that the minute notes large and inexplicable changes in the data for agriculture and manufacturing?
 - l) Is it true that the minute noted “significant measurement issues” for wholesale trade, retail trade and accommodation? Did it say the results for retail trade were “implausible”?
 - m) Were there also problems for property and business services data?
 - n) What were the results for these sectors that were not included?

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- o) If there were so many problems with the data for these sectors, how can we be sure that there are not problems with the data for the sectors reported in the minute?
- p) I ask again, will Treasury make the data behind the paper and minute publicly available so that independent researchers, the opposition and the public can assess the main claims in the paper and test their robustness?
- q) Is the Treasury paper the only analysis of effective or average tax rates by Treasury?

Answer:

1.

- a) The version of the paper released on 24 May 2010 was completed on 16 February 2010. There were some minor edits to the paper on the day of its release.
- b) The paper was intended for publication in Treasury's Economic Roundup series.
- c) The decision to release the paper on 24 May 2010 was made by the Treasurer in response to a Treasury minute.
- d) The paper was released then because it contained information of current public interest.
- e) Publicly available data was sourced from the ATO's *Taxation Statistics 1995-96* through to *Taxation Statistics 2004-05*; and ABS Catalogues 5204.0 and 5206.0. As the article notes, adjustments are made to the ABS data that replicates the measure of income derived by Clark, Pridmore and Stoney (2007), and that these adjustments are made based on judgements of the authors. As the purpose of the paper was to investigate whether the corporate tax system impacts differentially across industries rather than focusing on actual levels of average corporate tax rates, it was decided to present the results as differences from the industry-wide average tax rates. Other researchers are free to make their own judgements about the nature and amounts of adjustments appropriate to replicate the Clark, Pridmore and Stoney (2007) measure of income.
- f) The Treasury estimates used in the paper will not be made publicly available as the purpose of the paper was to investigate whether the corporate tax system impacts differentially across industries, rather than focusing on actual average tax rates.
- g) That paper used data to 2004-05 as this was the most fully enumerated data at the time the paper was prepared. More recent data was available from the

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ATO and ABS, however the more recent publications are more likely to be subsequently revised. To illustrate, the ATO's *Taxation Statistics 2007-08* publication notes that '[t]he statistics in these chapters are not necessarily complete and will continue to change as data from 2008 tax returns and schedules processed after 31 October 2009 is included'.

- h) The analysis was updated using data up until 2007-08. The results remain broadly similar and the updated version of the paper was published on 3 July 2010 in Treasury's Economic Roundup, Issue 2, 2010.
- i) The authors noted that the Markle and Shackelford (2009) paper reported that effective tax rates varied markedly across industries — supporting the authors' results. The authors did not note the 2010 update of the Markle and Shackelford paper as this was released on 22 March 2010, which was after the paper was completed on 16 February 2010.
- j) The results of other industries were not included in the paper as the authors judged that these estimates of average tax rates appeared to implausible. The authors judged that these spurious results were likely caused by industry classification issues; and measurement issues relating to some variables.
- k) Yes.
- l) Yes to both questions.
- m) Over the period examined, the property & business services industry suffered from continuous changes to the sub-industries included within its scope, making precise measurement difficult. In addition, the way in which the ATO measures rents (a significant income/expenditure source to this industry) causes some additional measurement issues.
- n) Agriculture (45%); Manufacturing (28%); Wholesale trade (49%); Retail trade (-89%); Accommodation, cafes & restaurants (40%); and Property & business services (20%).
- o) As the Roundup article notes, there is greater uncertainty about the accuracy in measurement of (specific) industry average tax rates, rather than of an (industry) aggregate average tax rate. Specifically, there is a reasonable level of certainty in relation to totals of variables for particular years. It is the distribution of these variables across industries that introduces the possibility of a misallocation. It is for this reason that the paper presents and interprets the results relative to the average tax rate for all industries. This is appropriate as the purpose of the paper was to investigate whether the corporate tax system impacts differentially across industries rather than focusing on actual levels of average corporate tax rates. In addition, the problems inherent in the industries omitted from the paper were specific to the industries and for the large part, readily explainable. Alongside external validation of the results (relating to the

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disparity in average tax rates), work was conducted to investigate the underlying data for each industry in an attempt to make sense of the results for all industries.

- p) No. See answers to questions e, f and o.
- q) This paper is the only work in Treasury to analyse average tax rates at the industry level. As the paper notes, similar results are obtained from analysing data from Bloomberg Professional service for listed companies for 2006-07, as well as using the ATO Taxation Statistics profit data.