Australia – the low tax country

OECD data shows Australia raises less tax revenue than almost all developed countries

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Introduction

Australia is a low-taxing country. While tax debate in Australia tends to focus on tax rates, with endless comparisons of different countries' rates of different taxes, these debates ignore the fact that Australia raises far less tax revenue than most developed countries.

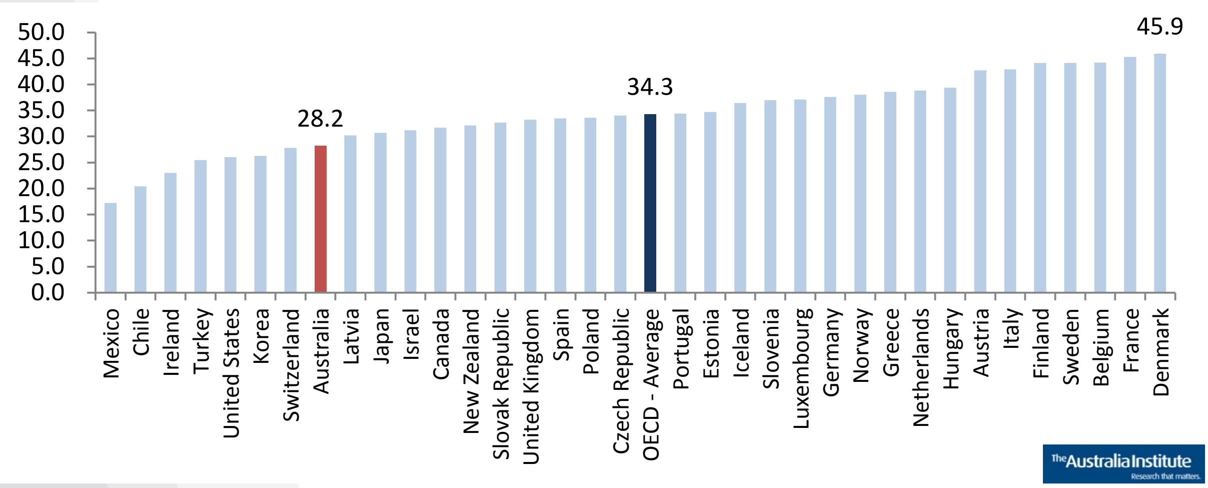
This is not a problem in itself. There is no right or wrong level of taxation. However, the level of tax revenue raised inevitably affects governments' ability to fund essential services such as health, education, social security, defence and infrastructure. Polling consistently shows that the Australian public would prefer higher levels of spending on public services than lower tax collection.[1]

Most of the data in this report is from the Organisation for Economic Cooperation and Development (OECD), an organisation of mostly high-income countries, that share data and analysis. The OECD publishes tax data from its members which consistently shows Australia collecting among the lowest amount of tax relative to Gross Domestic Product (GDP) of OECD members.

OECD tax comparison

The latest OECD data shows that Australia has a total tax to GDP ratio of 28.2,[2] making it the eighth-lowest taxing member of its 35 members, as shown in Figure 1 below:

Figure 1: Total tax revenue as percentage of GDP



Source: OECD Revenue Statistics, http://stats.oecd.org/

[1] See Australia Institute (2016) *New polling shows lack of support for income tax cuts*, http://www.tai.org.au/sites/defualt/files/MR%20Polling%20SA%20QLD%20Tax%20Reform.pdf; Australia Institute (2016) *Australians support a super profits tax on banks*, http://www.tai.org.au/content/australians-support-super-profits-tax-banks; Australia Institute (2017) *Voters oppose company tax cuts, dole cuts: Poll*, http://www.tai.org.au/content/voters-oppose-company-tax-cuts-dole-cuts-poll; Australia Institute (2017) *Polling – Cutting tax for large companies*, http://www.tai.org.au/sites/defualt/files/Polling%20Brief%20-%20Dec%202017%20-%20company%20tax.pdf; Australia Institute (2018) *68% of PM's electorate oppose company tax cuts*, http://www.tai.org.au/content/68-pm%E2%80%99s-electorate-oppose-company-tax-cuts

[2] Discussion of tax to GDP ratios in Australia often focuses on federal taxes. For example, the federal government's target ratio of 23.9% (See Coorey (2017) *Budget could contain tax increases, says Mathias Cormann*, http://www.afr.com/news/politics/budget-will-contain-tax-increases-says-mathias-cormann-20170402-gvc47a#ixzz5CEbS6aiE). This is lower than the OECD figures as it refers only to federal taxes, omitting state taxes such as payroll tax and stamp duty.

Figure 1 shows that Australia's tax to GDP ratio is substantially below the OECD average of 34.3.[3] To reach the OECD average, Australia would need to raise an extra 6.1% of GDP as tax revenue. 6.1% of Australia's AUD$1.8 trillion GDP in 2017 is approximately $110 billion.

Australian tax in context

It is worth putting in context what Australia could do if we raised tax revenue similar to the OECD average, or even to culturally similar countries such as New Zealand or the UK, as considered in Table 1 below:

Table 1: If Australia raised revenue like NZ, UK, OECD average and Denmark

	Tax:GDP difference	Dollar figure based on 2017 GDP (AUD millions)	With that money Australia could…
New Zealand	3.9%	$70,103	Almost triple assistance to people with disabilities - $38,538m
UK	5%	$89,875	Triple the aged pension - $45,391m
OECD average	6.1%	$109,648	Build two new NBNs every year - $49,000m
Denmark	17.7%	$318,158	Increase federal health AND education spending fourfold - Health - $75,277m, Education $33,800m

Sources: OECD Tax Statistics; ABS Australian National Accounts, table 1: Key national accounts aggregates; Australian Budget 2017–18, Budget Paper No. 1, statement 6; Parliamentary Budget Office (2016) *National Broadband Network: Impact on the Budget*

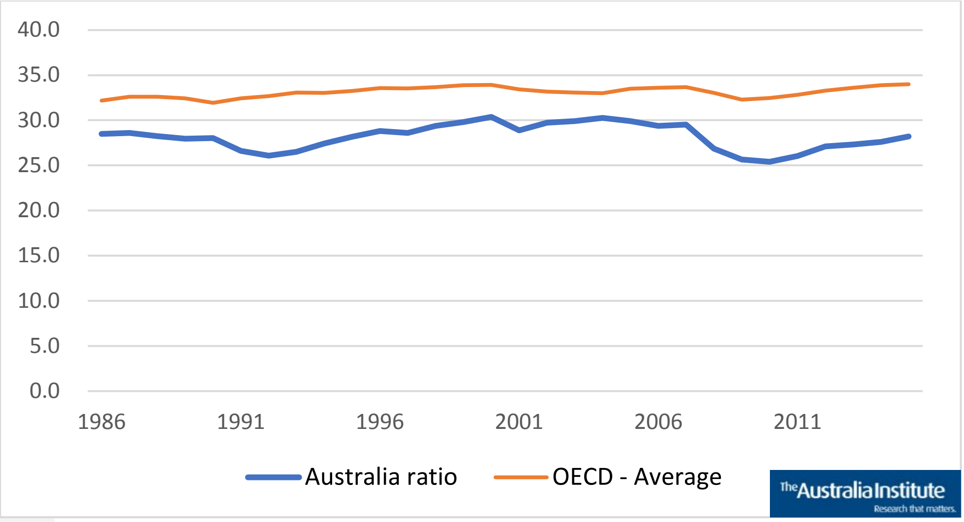
Table 1 puts into context Australia's tax choices. If we raised the level of tax of New Zealand we could triple spending on assistance to people with disabilities, including the NDIS. Raising revenue at UK levels would enable a tripling of spending on the aged pension. Raising the revenue at the level of Denmark would fundamentally transform Australia's education and health systems. The choices we make about how much tax to raise have major impacts on the services we fund and the society we want to have.

Australian tax over time

This latest data shown in Figure 1 is not an anomaly. Australia's tax to GDP ratio has been well below the OECD average for the last 30 years, as shown in Figure 2 below:

[3] Note that OECD reporting follows the calendar year, rather than the financial year as used by the Australian government. As such, OECD figures for Australia's tax to GDP ratio will differ slightly from official Australian figures. Consistent calendar year figures are used in this report.

Figure 2: Tax to GDP ratio over time, Australia and OECD average



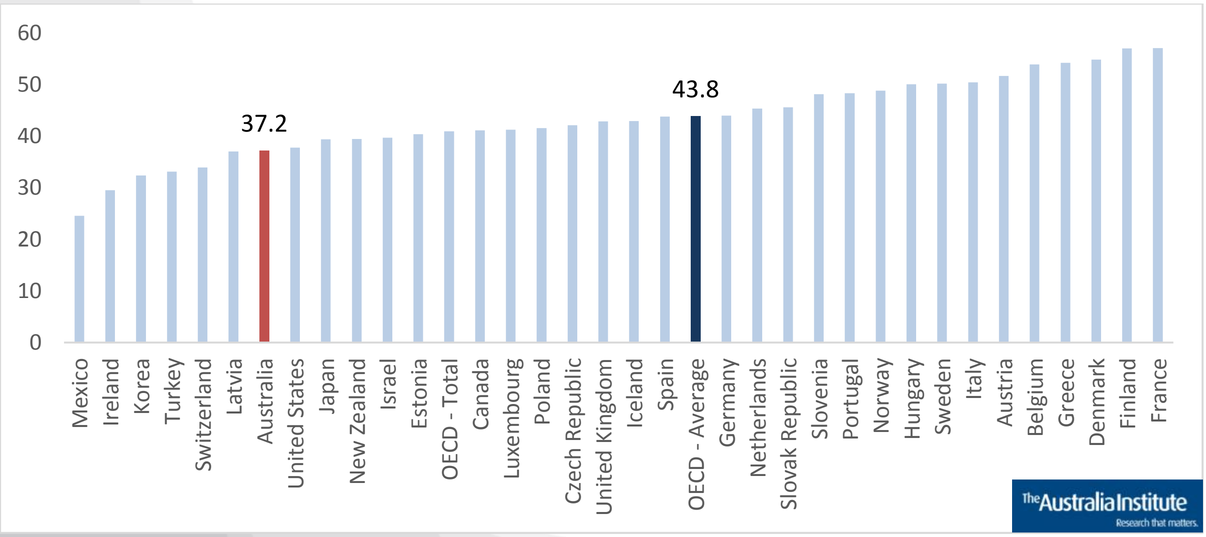
Source: OECD

Figure 2 shows that Australia's ratio has recently returned to 28.2%, the same level as in 1995. Our tax to GDP ratio was higher than at present from 1996 to 2007, the entire Howard era. Significant declines were seen following the Global Financial Crisis, which reduced tax revenues substantially, while Australia avoided a GDP-reducing recession.

OECD spending comparison

Countries with lower ratios of tax to GDP are also likely to have lower ratios of spending to GDP. This is the case in Australia, with only six countries having lower ratios, as shown in Figure 3 below:

Figure 3: Government spending to GDP, OECD countries

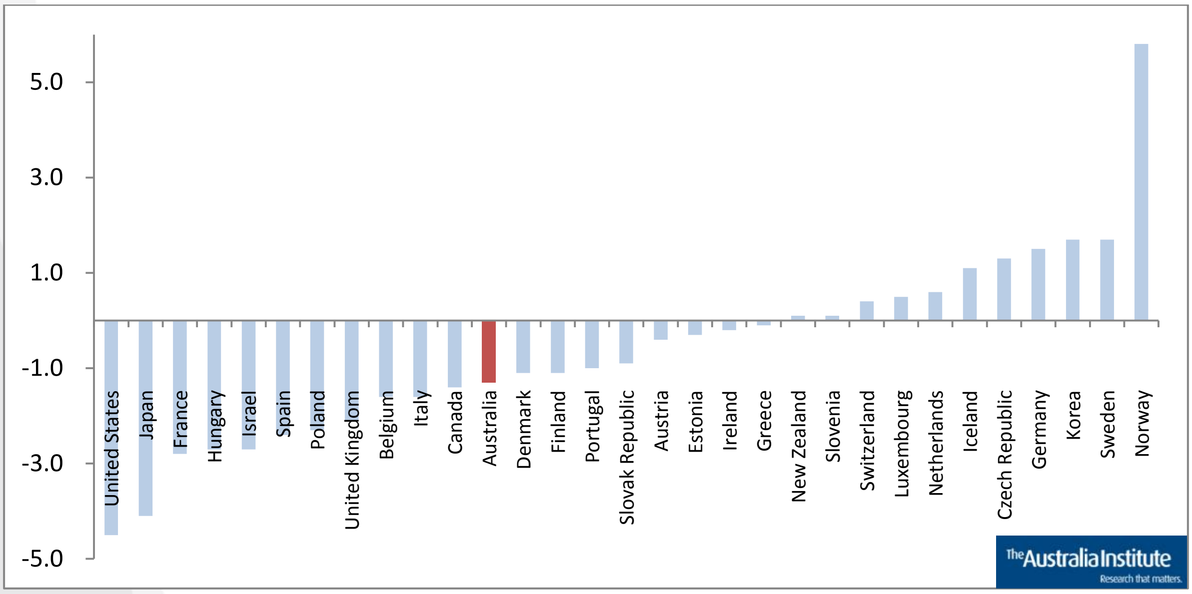


Source: OECD

Figure 3 shows that Australia's spending to GDP ratio is lower than even the United States, despite the 'small government' reputation commonly associated with the USA. Importantly, a huge amount of US spending is on defence: 3–4% of GDP. The USA is also financing the spending it has through large deficits, discussed below.

Note that the spending to GDP ratios shown in Figure 3 are generally higher than the tax ratios shown in Figure 1. This reflects two factors – other sources of government revenue and the fact that most OECD governments have budget deficits, including Australia. The OECD has stopped publishing data on non-tax revenue, but in its final 2007 dataset Australia's non-tax government revenue made up around 8% of GDP. A similar level can be inferred from Figure 4 below, as the OECD expects Australia to have a budget deficit of 1.3% of GDP in 2018:

Figure 4: Government budget balance to GDP, estimated 2018



Source: OECD

Figure 4 shows that Australia's budget balance is in the middle of the OECD field. There is no clear pattern between countries with high tax ratios and high budget surpluses. For example, Korea has a very low tax to GDP ratio, but is forecast to have a relatively high surplus. Both Korea and the United States are low-spending countries, but the USA is expected to run a large budget deficit. For all the criticism of Greece's economic management, the OECD expects its budget to almost balance in 2018. This reflects the multitude of factors that affect the budget of any country and, to some degree, how those factors are treated in OECD statistics.

Tax comparison and retirement income systems

One issue when comparing tax revenues internationally is that these total revenues come from many different compulsory payments – some of which are explicitly named as taxes, others of which are indisputably taxes despite having a different label (like the Medicare levy), and some of which are the subject of dispute like some fees and charges. The OECD classifications utilise clear and long-standing guidelines to decide which of these payments should be considered as taxes for international comparisons of public sector revenues. However, the inclusion or exclusion of some payments from the OECD's calculations has been challenged.

One such payment relevant to Australia is compulsory superannuation. Many countries in Australia's OECD peer group have publicly-run social security schemes that encompass earnings-related retirement income schemes that are in some ways similar to Australia's private superannuation system. These are typically publicly-run and funded by compulsory Social Security Contributions (SSCs). These SSCs are considered by the OECD as a tax because they are paid to a public entity and are not directly linked to the entitlement amounts any individual has from the social security benefits system. Compulsory contributions to Australia's superannuation system are not considered a tax by the OECD as they are paid to private entities, and the contributions of those paying into the system are directly linked to the benefits they will receive in the future.[4]

One argument for including compulsory superannuation contributions as part of a hypothetical 'international comparison tax base' is as follows.

> … through the introduction of compulsion into superannuation the government has been able to force households to save, making superannuation essentially a privatised public pension provision scheme.[5]

However, Australia has a public pension scheme funded from general taxation. Compulsory superannuation is just one part of Australia's total retirement system. Classifying compulsory superannuation payments as a tax for international comparisons would also suggest that comparisons of public spending should include retirement incomes from private superannuation balances as public expenses. This seems wrong.

Classifying SSCs as taxes seems right because these funds pay for services and welfare payments that Australia funds from general tax revenue, including unemployment benefits, disability pensions, and in some cases medical services. The crux of the matter is whether, because some OECD countries have pension benefits superficially like superannuation but run publicly, this similarity is sufficient to warrant inclusion of all compulsory superannuation contributions when comparing tax revenues.

To help clarify how Australia tax and social security system differs from others, Figure 5 below provides a rough sketch of the relationship between taxes, SSCs, and compulsory superannuation, to government spending and social security benefits.

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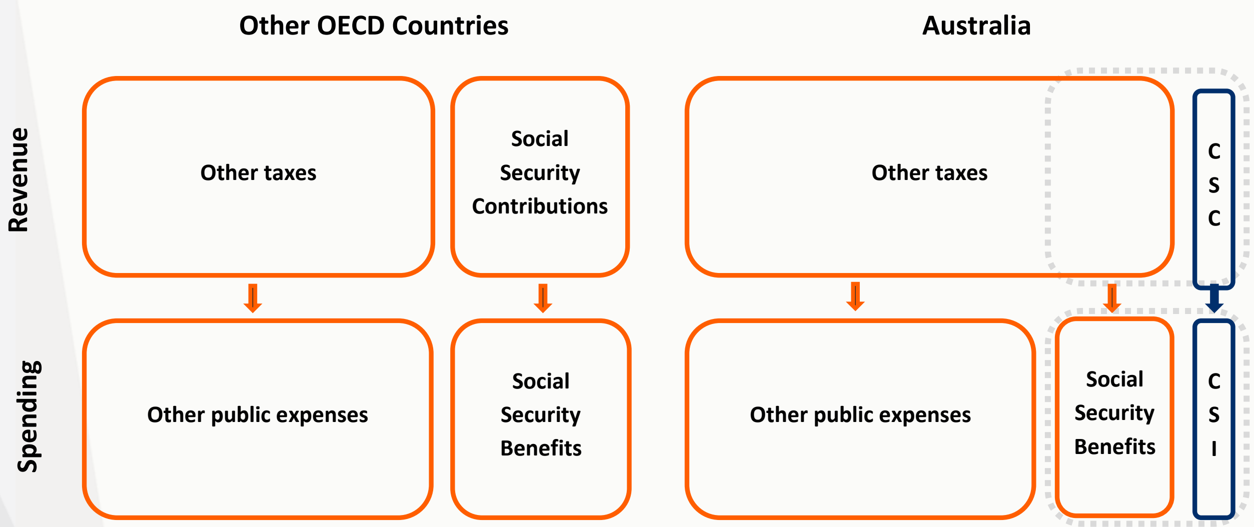
[4] OECD (2017) *Revenue Statistics. Interpretive Guide,* paragraph 37, http://www.oecd.org/tax/tax-policy/oecd-classification-taxes-interpretative-guide.pdf

[5] Warren (2004) *Tax: Facts, Fiction and Reform,* Australian Tax Research Foundation Study No 41, p 171

Figure 5: Representation of tax and social security systems



CSC = Compulsory Superannuation Contributions
CSI = Compulsory Superannuation Incomes
Blue boxes are payments to (and incomes from) private entities
Blue arrow is a direct link between contribution and benefit
Orange boxes are payments (and incomes from) publicly run entities
Orange arrows represent pooling of payments before spending is made

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The left panel of Figure 5 shows how some OECD countries have public agencies that pool SSCs to fund social security benefits — in principle detached from the rest of the tax system.

The right panel shows Australia's situation, with no SSCs, but where general tax revenue is pooled in government budgets to fund most social security benefits. However, the compulsory superannuation contributions (CSC) and the retirement incomes derived from CSCs would be comparable to just a small part of the social security system in other countries (as shown with the dotted box that represents the comparable social security schemes in other countries).

Disregarding which comparison is better, it is worth demonstrating how much of a difference including or excluding compulsory superannuation makes to tax comparisons. Using the OECD tax classification, excluding superannuation, Australian in 2015 had a total tax revenue of $463.1 billion for all levels of government, or 28.2% of GDP. This was 28th highest out of the 35 OECD countries.

In that year there were $53.3 billion of compulsory superannuation contributions.[6] Adding these makes an 'international comparison tax base' of $516.4 billion, or 31.4% of GDP, taking Australia to a ranking of 24th out of 35 OECD countries in terms of tax-to-GDP ratios.[7] Figure 6 shows this effect.

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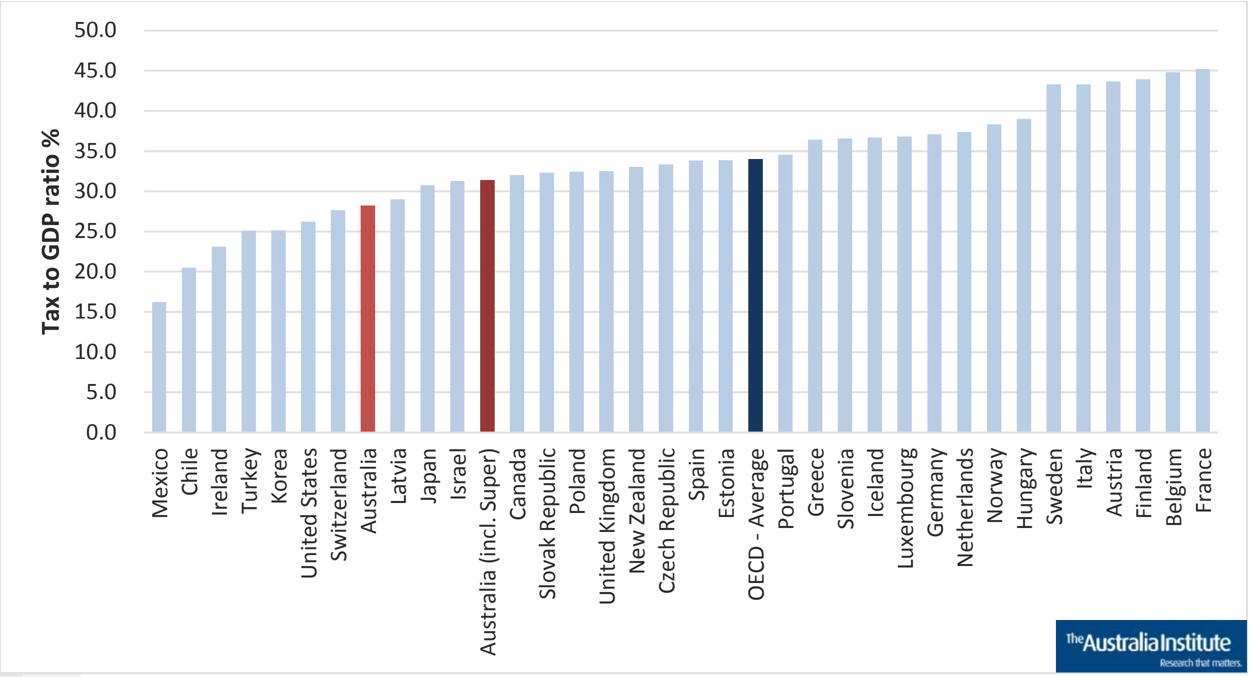
[6] APRA (2017) *Statistics: Quarterly Superannuation Performance*, p 9
http://www.apra.gov.au/Super/Publications/Documents/2016QSP201606.pdf
[7] OECD (2017) *Revenue Statistics Combined - Comparative tables,*
https://stats.oecd.org/Index.aspx?DataSetCode=REV

Figure 6: Tax to GDP ratios in OECD countries in 2015



Even when classifying compulsory superannuation as a tax Australia remains a low taxing country compared to peer nations, though there is no clear reason to prefer this comparison over a comparison using the OECD classification of compulsory superannuation as not being a tax.

Conclusion

As Australia debates our tax rates on corporate income, personal income and other revenue measures, it is important to realise that overall Australia is a low-taxing country. Few developed countries raise as little tax revenue as Australia does relative to the size of the economy. This is not new – Australia has taxed at below average OECD levels for decades.

Tax policy has a huge influence on what governments can spend and the sort of society we want to be and become. Increasing our tax to GDP ratio to levels comparable to New Zealand or the UK would raise revenue sufficient to have a major impact on our budget and funding of social services and infrastructure.