

CHAPTER 1: OVERVIEW

1.1 Introduction

The Tax Expenditures Statement (TES) provides details of concessions, benefits, incentives and charges provided through the tax system (tax expenditures) to taxpayers by the Australian Government. The publication of information on the Australian Government's tax expenditures is a requirement under the *Charter of Budget Honesty Act 1998*.

This statement lists 349 tax expenditures and, where possible, reports the estimated pecuniary value or order of magnitude of the benefit to taxpayers over an eight year period, from 2006-07 to 2013-14.

The tax expenditures in this statement reflect all announced policies applying up to the date of finalisation of the *Mid-Year Economic and Fiscal Outlook 2010-11*, with the exception of policy decisions relating to the minerals resource rent tax (MRRT) and the extended petroleum resource rent tax (PRRT) announced in July 2010. The Government is currently considering the recommendations of the Policy Transition Group in respect of the final design of these proposed reforms, which will then allow a natural resources benchmark to be developed that takes account of final Government policy. In the interim, this edition of the TES continues to apply the same natural resources benchmark as applied in the 2009 TES.

This statement incorporates a number of changes from previous years. These changes are reported in Appendix B and include the removal of tax expenditures recognised under the Carbon Pollution Reduction Scheme. This is consistent with the tax expenditure aggregates published in the 2010-11 Budget.

The remainder of this statement is divided into the following sections:

- Chapter 1 provides an overview of the Tax Expenditures Statement, trends and aggregates in the estimates and comparison with direct expenditures.
- Chapter 2 provides background on tax expenditures and the tax expenditure framework, including measuring tax expenditures, and the various approaches used to measure tax expenditures, including Treasury's approach.
- Chapter 3 outlines the benchmarks used to identify and measure tax expenditures, guidance on how to interpret tax expenditure estimates, and details of each tax expenditure, including an estimate (where possible) of the benefit taxpayers derive, a description of the tax expenditure, a legislative reference, and for more recent tax expenditures, the date the expenditure was introduced.

Tax Expenditures Statement

- Chapter 4 provides revenue gain estimates of several tax expenditures, guidance on how to interpret revenue gain estimates, and comparison to the estimates in Chapter 3.
- Appendix A provides an overview of the various modelling techniques used to estimate tax expenditures, detailed descriptions of the benchmarks used in Chapter 3, and technical notes on the estimates.
- Appendix B provides comprehensive information on the changes to the list of tax expenditures since the 2009 Tax Expenditures Statement – new tax expenditures, modified tax expenditures and tax expenditures no longer reported.
- Appendix C provides a discussion and comparison of alternative approaches to quantifying the owner-occupied housing tax expenditures, including estimates of the differing approaches.
- Appendix D provides aggregated information on tax expenditures related to funded superannuation.

1.2 Coverage of this statement

This statement covers the following Australian Government ‘taxes’:

- income tax (personal and business), including capital gains tax (CGT) and income tax paid on retirement income;
- fringe benefits tax (FBT);
- the goods and services tax (GST);
- excise duties;
- customs duty (including tariffs);
- wine equalisation tax;
- luxury car tax;
- petroleum resource rent tax;

- crude oil excise; and
- other indirect taxes.

1.3 Trends in tax expenditure estimates

The following tables provide summary and aggregate information on the tax expenditure estimates prepared for the 2010 TES. Comparisons across years are made on a consistent basis within this report for individual items and the aggregates.

The TES does not compare previous years' estimates with the current estimates except in very limited circumstances. Comparisons across different editions of the TES have always required great care due to the new data available each year and the identification of new tax expenditures, deletion of old tax expenditures and modifications arising from government policies. Further discussion of these issues is provided in the box *Interpretation of trends and aggregates*.

TRENDS IN MEASURED TAX EXPENDITURES

Total measured tax expenditures are reported in Table 1.1. Measured tax expenditures as a proportion of GDP peaked in 2007-08 at 10.6 per cent of GDP before falling to 8.7 per cent in 2008-09 and were 8.8 per cent in 2009-10. Growth in tax expenditures over the last two years has been somewhat softer than in preceding years. The current relatively muted growth appears, in the main, to result from the impact of the global financial crisis on superannuation returns.

In dollar terms, total measured tax expenditures in 2009-10 are estimated at around \$113 billion. Housing tax expenditures comprise around one-third of total measured tax expenditures, followed by superannuation tax expenditures which comprise around a quarter of total measured tax expenditures.

Interpretation of trends and aggregates

making comparisons across time and against direct expenditures. There are several major considerations that need to be taken into account when analysing tax expenditure aggregates.

- The cost of some tax expenditures are not reported owing to a lack of data or because of taxpayer confidentiality. Hence, tax expenditure aggregates underestimate the total benefit provided by tax expenditures.
- The trend in aggregates reflects changes in the extent to which individual tax expenditures are accessed, changes to the benchmarks, and changes in the number of tax expenditures being reported.
- Changes over time in methodology and data used to calculate the cost of tax expenditures can result in large revisions to the tax expenditure estimates. Estimates that were provided in previous editions of the Tax Expenditures Statement may not be directly comparable to estimates reported in this publication.
- Tax expenditure aggregates are net aggregates as they include the offsetting effects of negative tax expenditures.

Further details on how to interpret tax expenditure estimates are provided in Chapter 2.

Table 1.1: Total measured tax expenditures^{(a)(b)}

Year	Housing \$m	Superannuation(b) \$m	Other tax expenditures \$m	Total \$m	Tax expenditure as a proportion of GDP (%)
2006-07(est)	39,500	27,158	41,515	108,173	9.9
2007-08 (est)	41,000	38,965	45,875	125,840	10.6
2008-09(est)	29,500	31,945	47,614	109,059	8.7
2009-10(est)	39,000	26,972	46,932	112,904	8.8
2010-11(proj)	40,000	28,039	48,828	116,867	8.3
2011-12(proj)	42,500	30,863	49,440	122,803	8.3
2012-13(proj)	43,000	33,303	52,473	128,776	8.3
2013-14(proj)	43,000	37,983	58,635	139,618	8.5

(a) Total measured tax expenditures are derived by summing the individual tax expenditure estimates, excluding estimates that are rounded to zero (..) or unquantifiable (*).

(b) Includes the sum of tax expenditures C4 to C15 and C20.

Changes to benchmarks makes comparison of the aggregate estimates in the 2010 TES with the aggregate estimates provided in previous editions difficult. The 2010 TES excludes the value of tax concessions arising under the Carbon Pollution Reduction Scheme benchmark as a result of the Government's decision to defer this scheme.

Table 1.2 presents measured tax expenditures by the benchmark against which they are estimated for the period 2006-07 to 2013-14. The capital gains benchmark, containing the housing tax expenditures, is the largest benchmark classification. This is followed by the retirement savings and goods and services tax benchmark.

For all reported years, the total measured tax expenditures representing the commodity and other indirect taxes benchmark give rise to a negative estimate, largely reflecting customs duty (F20) and the higher rate of excise levied on cigarettes (F7).

Table 1.2: Measured tax expenditures by benchmark (\$m)^{(a) (b)}

Benchmark	2006-07 (est)	2007-08 (est)	2008-09 (est)	2009-10 (est)	2010-11 (proj)	2011-12 (proj)	2012-13 (proj)	2013-14 (proj)
Income tax								
Personal income	10,800	11,262	11,031	13,951	11,826	11,660	11,990	13,452
Business income	6,920	6,030	6,267	8,245	9,590	7,989	7,766	9,112
Retirement savings	29,068	40,930	34,605	29,082	30,039	32,848	35,253	39,968
Fringe benefits tax	3,836	3,531	3,635	3,985	4,048	4,399	4,716	4,945
Capital gains tax	46,535	52,050	41,060	43,812	46,331	50,086	52,117	53,947
Consumption								
Commodity and other indirect taxes	-3,781	-4,145	-4,219	-3,810	-3,868	-4,492	-4,825	-5,178
Natural resources taxes	790	980	580	600	580	580	580	590
Goods and services tax	14,005	15,202	16,100	17,039	18,321	19,733	21,179	22,782

(a) Measured tax expenditures by benchmark are derived by summing the individual tax expenditure estimates, excluding estimates that are rounded to zero (..) or unquantifiable (*).

(b) There are no tax expenditures against the Externalities benchmark.

LARGE TAX EXPENDITURES

Table 1.3 provides a list of the largest measured tax expenditures for 2010-11. The largest measured tax expenditures are the concessional capital gains taxation of owner-occupied housing (E4 and E5) which is estimated to provide a benefit to taxpayers of around \$40 billion in 2010-11. Together, these tax expenditures represent the exemption of owner-occupied housing from CGT.

After the owner-occupied housing exemption, the next largest tax expenditure is the concessional taxation of employer contributions to superannuation (C5) of around \$14.3 billion in 2010-11. This is followed by the concessional taxation of superannuation entity earnings (C6) and the GST-free status of food (H28). These tax expenditures are estimated to provide benefits to taxpayers in 2010-11 of around \$12.2 billion and \$5.9 billion respectively.

The largest negative tax expenditures in 2010-11 are customs duty (F20) and the higher rate of excise levied on cigarettes (F7). These tax expenditures are estimated to be around \$2.7 billion and \$1.5 billion respectively.

There are a number of tax expenditures for which an estimate is not available but which have been assigned an order of magnitude classification (for details refer to Chapter 3). The largest such tax expenditures are as follows:

- philanthropy – income tax exemption for charitable, religious, scientific, and community service entities (B72);
- income tax exemption for Commonwealth, State and Territory public authorities, and State and Territory entities (B3); and
- quarantining of capital losses (E31).

Table 1.3: Large measured tax expenditures in 2010-11

Tax expenditure	Estimate \$m
Large positive tax expenditures	
E5 Capital gains tax main residence exemption — discount component	22,500
E4 Capital gains tax main residence exemption	17,500
C5 Superannuation — concessional taxation of employer contributions	14,300
C6 Superannuation — concessional taxation of superannuation entity earnings	12,200
H28 GST — food — uncooked, not prepared, not for consumption on premises of sale and some beverages	5,900
E14 Capital gains tax discount for individuals and trusts	5,490
H19 GST — health; medical and health services	2,950
H16 GST — education	2,600
B110 Small business and general business tax break	2,350
H2 GST — financial supplies; input taxed treatment	2,200
B16 Exemption from interest withholding tax on certain securities	2,040
A45 Exemption of Family Tax Benefit, Parts A and B, including expense equivalent	1,950
C3 Concessional taxation of non-superannuation termination benefits	1,350
A24 Exemption of 30 per cent private health insurance refund, including expense equivalent	1,250
A23 Exemption from the Medicare levy for residents with a taxable income below a threshold	1,130
D18 Application of statutory formula to value car benefits	1,110
C8 Superannuation — deduction and concessional taxation of certain personal contributions	1,050
F3 Concessional rate of excise levied on aviation gasoline and aviation turbine fuel	1,000
H11 GST — imported services	1,000
H3 GST — financial supplies; reduced input tax credits	990
A33 Senior Australians' Tax Offset	960
D11 Philanthropy — exemption for public and not-for-profit hospitals and public ambulance services	920
D14 Philanthropy — exemption for public benevolent institutions (excluding public and not-for-profit hospitals)	920
B95 Statutory effective life caps	915
B4 Income tax exemption for local government bodies	820
A66 Philanthropy — deduction for gifts to deductible gift recipients	760
A49 Exemption of payments made under the First Home Owners Grant Scheme	760
H6 GST — water, sewerage and drainage	700
B106 Research and development — research and development tax concession	700
Large negative tax expenditures	
F20 Customs duty	-2,740
F7 Higher rate of excise levied on cigarettes not exceeding 0.8 grams of tobacco	-1,530

TRENDS IN TAX EXPENDITURES BY FUNCTION

Total measured tax expenditures by functional category are reported in Table 1.4 for the period 2007-08 to 2013-14. Significant changes underlying movements in functional categories are listed below.

- The decrease in the agriculture, forestry and fishing aggregate reflects an inability to quantify the farm management deposit scheme tax expenditure (B42) and the income tax averaging for primary producers tax expenditure (B43) from 2010-11 and 2009-10 respectively.
- The decrease in the fuel and energy aggregate is due to decreases in the tax expenditures for 'alternative fuels' (F6) and condensate (G4).
- The total for transport and communication is estimated to increase over the reported period owing to the statutory effective life caps (B95) tax expenditure.
- The increase in the recreation and culture aggregate over 2010-11 to 2012-13 is due to the rebate for broadcasting licence fees tax expenditure (B50).
- The growth in the education aggregate is due to the growth in the value of the GST exemption for education (H16) and the introduction of the Education Tax Refund (A19).
- The growth in the health aggregate is also significantly due to the growth in the value of the various GST exemptions related to health care.

Table 1.4: Aggregate tax expenditures by function^(a)

	Estimates (\$m)			Projections (\$m)			
	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14
General public services							
A. Legislative and executive affairs	2	2	2	3	3	3	3
B. Financial and fiscal affairs	2,760	2,760	2,970	3,190	3,420	3,700	3,990
C. Foreign affairs and economic aid	708	703	680	525	550	581	621
D. General research	0	0	0	0	0	0	0
E. General services	13	12	13	13	13	14	15
F. Government superannuation benefits	0	0	0	0	0	0	0
Defence	788	807	862	876	926	981	1,031
Public order and safety	0	0	0	0	0	0	0
Education	2,116	2,323	2,419	2,749	2,968	3,178	3,457
Health	4,835	4,930	5,740	6,160	6,555	6,905	7,425
Social security and welfare	47,951	41,254	36,026	36,555	39,629	42,489	47,739
Housing and community amenities	42,515	31,165	41,140	42,325	44,587	45,158	45,280
Recreation and culture	122	138	161	205	282	256	204
Fuel and energy	2,020	1,635	1,600	1,585	1,365	1,415	1,470
Agriculture, forestry and fishing	268	282	141	107	43	44	46
Mining, manufacturing and construction	-3,335	-3,250	-2,770	-2,553	-2,828	-3,098	-3,308
Transport and communication	494	625	748	830	914	949	963
Other economic affairs							
A. Tourism and area promotion	-6	0	0	0	0	0	0
B. Total labour and employment affairs	1,828	1,794	1,984	1,963	2,094	2,196	2,275
C. Immigration	0	0	0	0	0	0	0
D. Other economic affairs, nec(b)	22,050	23,171	20,420	21,508	21,399	23,054	27,407
Other purposes							
A. Public debt interest	0	0	0	0	0	0	0
B. Nominal superannuation interest	0	0	0	0	0	0	0
C. General purpose inter-governmental transactions	700	700	760	820	880	950	1,000
D. Natural disaster relief	11	8	8	6	3	1	0
E. Contingency reserve	0	0	0	0	0	0	0
Total(c)	125,840	109,059	112,904	116,867	122,803	128,776	139,618

(a) Total measured tax expenditures by functional category are derived by summing individual tax expenditure estimates, excluding estimates that are rounded to zero (..) or unquantifiable (*).

(b) 'nec' means not elsewhere classified.

(c) Totals may not sum due to rounding.

COMPARISON WITH DIRECT EXPENDITURE

The tax expenditure estimates for 2009-10 by functional category are presented alongside direct government expenditures in Table 1.5. The list of direct expenditures by function is reproduced from the *Final Budget Outcome 2009-10*.

Comparisons between tax expenditures and direct expenditures are informative in broad terms, although the costings are not strictly comparable. For example:

- Tax expenditure estimates measure the benefit of the tax concession to the recipient, whereas direct expenditure estimates measure the impact of the expenditure on the budget in pre-tax dollars.
- Direct expenditures are often taxable, whereas tax expenditures are not.
- The removal of a tax expenditure or a direct expenditure of the same magnitude may have different effects on the fiscal balance, owing to different behavioural responses.

The addition of tax expenditures and direct expenditures will also tend to overstate the impact on the fiscal balance. For example, the government's direct expenditure on certain income support benefits, pensions or allowances includes the full cost of the program to government but there is also an associated tax expenditure (A41) for the value of the income tax exemption of the benefits to the recipient.

Table 1.5: Aggregate tax expenditures and direct expenditures by function in 2009-10

	Tax expenditures (\$m)(a)	Direct expenditures (\$m)(b)
General public services		
A. Legislative and executive affairs	2	840
B. Financial and fiscal affairs	2,970	6,845
C. Foreign affairs and economic aid	680	4,869
D. General research	0	2,358
E. General services	13	818
F. Government superannuation benefits	0	3,472
Defence	862	20,150
Public order and safety	0	3,593
Education	2,419	34,889
Health	5,740	51,426
Social security and welfare	36,026	109,197
Housing and community amenities	41,140	9,029
Recreation and culture	161	3,280
Fuel and energy	1,600	8,473
Agriculture, forestry and fishing	141	2,816
Mining, manufacturing and construction	-2,770	1,630
Transport and communication	748	6,641
Other economic affairs		
A. Tourism and area promotion	0	162
B. Total labour and employment affairs	1,984	4,694
C. Immigration	0	1,571
D. Other economic affairs, nec(c)	20,420	2,200
Other purposes		
A. Public debt interest	0	6,303
B. Nominal superannuation interest	0	6,687
C. General purpose inter-governmental transactions	760	47,157
D. Natural disaster relief	8	136
E. Contingency reserve	0	0
Total(d)	112,904	339,239

(a) Total measured tax expenditures by functional category are derived by summing individual tax expenditure estimates, excluding estimates that are rounded to zero (..) or unquantifiable (*).

(b) Direct expenses by function, as reported in the *Final Budget Outcome 2009-10*.

(c) 'nec' means not elsewhere classified.

(d) Totals may not sum due to rounding.

1.4 Period covered by these estimates

The 2010 Tax Expenditures Statement generally uses the publication of the *Mid-Year Economic and Fiscal Outlook 2010-11* as the cut off for policy and information relevant to the estimation of tax expenditures. It does not take account of any policy decisions made after that date. As discussed in Chapter 1.1, it also does not take account of policy decisions relating to the minerals resource rent tax (MRRT) and the extended petroleum resource rent tax (PRRT) announced in July 2010.