CHAPTER 3: REVENUE GAIN ESTIMATES OF TAX EXPENDITURES

3.1 Introduction

The revenue gain approach is an alternative to the revenue forgone approach used to produce the tax expenditure estimates in Chapter 2. Revenue gain estimates for individual tax expenditure items are more akin to estimates of the revenue impact of budget measures.

Consistent with a recommendation of the Australian National Audit Office in its 2007-08 performance audit of the TES,[2] this Chapter reports revenue gain estimates for 10 large tax expenditures.[3]

- These tax expenditures have been chosen because they best illustrate the considerable differences between the revenue forgone and revenue gain approaches, and how those differences can vary between tax expenditure items.

Estimates for the revenue gain from the CGT concessions for housing and the CGT discount for individuals and trusts have not been quantified because those estimates are either very small and uncertain (housing) or because of the significant uncertainty regarding the magnitude of response effects to a change (CGT discount).

Revenue gain estimates should be treated with caution.

- They assume that a tax expenditure is abolished, which may be implausible in many cases.

- In practice, the revenue gain can be difficult to estimate as there is usually little, if any, information on how taxpayers might react to the removal of a tax expenditure. Assumptions about taxpayer behavioural responses therefore need to be made, and these assumptions can be difficult to meaningfully substantiate.

- Judgments also need to be made about likely policy settings – for example, whether it is realistic to assess the abolition of a single tax expenditure (for example, a particular GST exemption) while keeping other tax expenditures unchanged (for example, other GST exemptions).

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2 ANAO Audit Report No. 32, 2007-08, *Preparation of the Tax Expenditures Statement*, Recommendation 5.

3 Ranked according to their revenue forgone estimates.

3.2 Standard assumptions for the revenue gain estimates

The tax expenditures listed below have been estimated using both the revenue gain and revenue forgone approaches. The revenue gain estimates all assume that the tax expenditures:

- are removed with effect from 1 July 2014;
- apply prospectively to transactions entered into after that date; and
- include other specific assumptions concerning likely policy specifications for the removal of each concession as set out in the description.

The revenue gain estimates also incorporate the impact of direct behavioural responses from the change where these are expected to have a significant impact on the estimates. The revenue gain estimates do not include any allowance for second round effects (that is, those arising from the flow-on of a change, beyond those directly affected, into the wider economy) because of the considerable uncertainty regarding the magnitude and timing of such impacts.

3.3 Guide to revenue gain estimate descriptions

The descriptions of the revenue gain estimates in this chapter present the revenue forgone and revenue gain estimates for a four year period for comparison. A brief outline of the reasons for any difference in the estimates is then provided.

Reference code

A	Personal income
B	Business income
C	Retirement income
D	Fringe benefits tax
E	Capital gains tax
F	Commodity tax
G	Natural resource taxes
H	Goods and services tax

Tax expenditure title

Tax expenditure estimates
- nil
.. not zero, but rounded to zero
* estimate is not available

Estimates	Revenue forgone estimate ($m)				Revenue gain estimate ($m)			
	2014-15	2015-16	2016-17	2017-18	2014-15	2015-16	2016-17	2017-18

Reason for difference	Brief reasons including assumptions

3.4 Tax expenditures based on revenue gain approach

C3: Concessional taxation of employer superannuation contributions

Estimates	Revenue forgone estimate ($m)				Revenue gain estimate ($m)			
	2014-15	**2015-16**	**2016-17**	**2017-18**	**2014-15**	**2015-16**	**2016-17**	**2017-18**
	16,300	17,350	18,100	19,050	15,550	16,450	17,150	18,100

Reason for difference: Broadly, the revenue gain approach yields a lower estimate of the tax expenditure because it incorporates a likely behavioural response, with removal of the concessional taxation of superannuation leading to reduced superannuation contributions. It is assumed that the Superannuation Guarantee remains and therefore compulsory contributions continue. Voluntary contributions are assumed to be directed to alternative tax preferred investments.

C6: Concessional taxation of superannuation entity earnings

Estimates	Revenue forgone estimate ($m)				Revenue gain estimate ($m)			
	2014-15	**2015-16**	**2016-17**	**2017-18**	**2014-15**	**2015-16**	**2016-17**	**2017-18**
	13,400	16,150	21,600	26,800	11,750	13,700	18,250	22,450

Reason for difference: Broadly, the revenue gain approach yields a lower estimate of the tax expenditure because it incorporates a likely behavioural response, with removal of the concessional taxation of superannuation leading to reduced superannuation contributions (and lower balances). It is assumed current preservation rules remain. In the accumulation phase voluntary concessional contributions are assumed to cease (as in C3) and most non-concessional contributions are also not invested in superannuation after the start date. Over time this reduces the superannuation asset base and thus the revenue gain on withdrawing the earnings tax concession. Additionally, a significant proportion of funds in the retirement phase (not preserved) are withdrawn. Because of other tax concessions for older Australians (particularly the Senior Australians and Pensioner Tax Offset), the funds withdrawn attract minimal tax in the new investments chosen.

H28: GST — Food

Estimates	Revenue forgone estimate ($m)				Revenue gain estimate ($m)			
	2014-15	**2015-16**	**2016-17**	**2017-18**	**2014-15**	**2015-16**	**2016-17**	**2017-18**
	6,400	6,700	7,000	7,300	6,300	6,600	6,800	7,100

Reason for difference: Removing the GST exemption applicable to certain types of food would be expected to decrease demand for those items. However, the impact of this behavioural response is expected to be small as demand for GST-free food is likely to be relatively unresponsive to changes in price.

H16: GST — Education

Estimates	Revenue forgone estimate ($m)				Revenue gain estimate ($m)			
	2014-15	**2015-16**	**2016-17**	**2017-18**	**2014-15**	**2015-16**	**2016-17**	**2017-18**
	3,950	4,300	4,700	5,150	3,550	3,850	4,250	4,600

Reason for difference: Removing the GST exemption for education would be expected to decrease demand for education services. This is primarily due to an expected fall in demand for private education and ‘discretionary courses’.

H2: GST — Financial supplies - input taxed treatment								
Estimates	Revenue forgone estimate ($m)				Revenue gain estimate ($m)			
	2014-15	2015-16	2016-17	2017-18	2014-15	2015-16	2016-17	2017-18
	3,550	3,750	3,950	4,150	3,550	3,750	3,950	4,150
Reason for difference	Removing the input taxed treatment of financial services is not expected to materially impact the demand for these services. This is because of the relatively small increase in the price of financial services that would result from applying the normal GST rules and the lack of substitutable services that are available.							

H19: GST — Health - medical and health services								
Estimates	Revenue forgone estimate ($m)				Revenue gain estimate ($m)			
	2014-15	2015-16	2016-17	2017-18	2014-15	2015-16	2016-17	2017-18
	3,550	3,800	4,100	4,400	3,500	3,750	4,050	4,350
Reason for difference	Removing the GST exemption for medical and health services would be expected to decrease demand for those services. However, the impact of this behavioural response is expected to be small as demand for medical and health services is likely to be relatively unresponsive to changes in price.							

C5: Concessional taxation of non-superannuation termination benefits								
Estimates	Revenue forgone estimate ($m)				Revenue gain estimate ($m)			
	2014-15	2015-16	2016-17	2017-18	2014-15	2015-16	2016-17	2017-18
	2,700	1,950	1,900	1,900	2,700	1,950	1,900	1,900
Reason for difference	As this tax expenditure relates to termination of employment (including cases such as redundancy), it is expected that employees would have limited capacity to alter their employment status if the tax treatment changed. As a result there is expected to be no material difference between the revenue forgone and revenue gain estimates.							

F24: Customs duty								
Estimates	Revenue forgone estimate ($m)				Revenue gain estimate ($m)			
	2014-15	2015-16	2016-17	2017-18	2014-15	2015-16	2016-17	2017-18
	-2,550	-1,490	-1,250	-1,230	-2,550	-1,490	-1,250	-1,230
Reason for difference	Under the customs duty benchmark, goods imported into Australia are free from customs duty except to the extent that the duty is equivalent to taxes imposed on domestically produced goods. Bringing the customs duty tax expenditure in line with the benchmark would remove the revenue currently collected from tariffs on imports (which is reported as a negative tax expenditure). While the change may increase demand for imported goods, this would have no impact on customs duty revenue once the tax rate has been reduced to zero.							

A38: Exemption of Family Tax Benefit payments								
Estimates	Revenue forgone estimate ($m)				Revenue gain estimate ($m)			
	2014-15	2015-16	2016-17	2017-18	2014-15	2015-16	2016-17	2017-18
	2,220	2,170	2,110	2,040	2,220	2,170	2,110	2,040
Reason for difference	Removing the exemption of Family Tax Benefit, Parts A and B could be expected to result in a change in labour force participation; however, the size of the effect is uncertain and has not been quantified. As a result there is no difference between the revenue forgone and revenue gain estimates.							

B14: Exemption from interest withholding tax on certain securities								
Estimates	**Revenue forgone estimate ($m)**				**Revenue gain estimate ($m)**			
	2014-15	**2015-16**	**2016-17**	**2017-18**	**2014-15**	**2015-16**	**2016-17**	**2017-18**
	1,860	1,860	1,860	1,860	1,310	1,370	1,290	1,280
Reason for difference	Removing the exemption from interest withholding tax on certain securities would be expected to result in some borrowers switching to other forms of exempt borrowings, resulting in no revenue gain. In addition, some interest payments may be increased to cover the tax, leading to increased income tax deductions.							