

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 TES lists 363 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 2008-09 to 2015-16.

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 2012-13*.

This statement incorporates a number of changes from previous years. Changes to benchmarks are reflected in Appendix A. Changes to individual tax expenditures are reported in Appendix B.

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

- Chapter 1 provides an overview of the TES, trends and aggregates in the estimates and comparison with direct expenditures.
- Chapter 2 provides background on tax expenditures and the tax expenditure framework, as well as 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 the date the expenditure was introduced.
- 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.

Tax Expenditures Statement

- Appendix B provides comprehensive information on the changes to the list of tax expenditures since the 2011 TES – new tax expenditures, modified tax expenditures and tax expenditures no longer reported.

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;
- minerals resource rent tax;
- crude oil excise;
- other indirect taxes; and
- the carbon pricing mechanism.

1.3 Trends in tax expenditure estimates

The following tables provide summary and aggregate information on the tax expenditure estimates prepared for the 2012 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 editions’ 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 over 10 per cent of GDP before falling to 7.6 per cent in 2011-12. Growth in tax expenditures over the last two years of estimates has been softer than in preceding years. The current muted growth appears, in the main, to reflect the impact of the softer housing market on capital gains from housing.

In dollar terms, total measured tax expenditures in 2011-12 are estimated at around \$111 billion. Housing tax expenditures have fallen recently, with their share of total measured tax expenditures falling to around a quarter in 2011-12 from around a third in 2009-10. Superannuation tax expenditures comprise around a quarter of total measured tax expenditures.

Interpretation of trends and aggregates

Care must be taken when interpreting tax expenditure aggregates, particularly when 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 TES 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.
- Tax expenditure estimates are not strictly additive because the removal of one concession will affect the utilisation of other concessions for accounting and behavioural reasons, and tax expenditure estimates will tend to overstate the budgetary impact of removing concessions as the estimates do not take account of behavioural responses.

Chapter 2 provides further details on how to interpret tax expenditure estimates.

Table 1.1: Total measured tax expenditures^(a)

Year	Housing \$m	Superannuation(b) \$m	Other tax expenditures \$m	Total \$m	Tax expenditure as a proportion of GDP (%)
2007-08 (est)(c)	40,500	38,940	47,306	126,476	10.7
2008-09 (est)	28,500	28,787	50,943	108,230	8.6
2009-10 (est)	40,000	24,089	49,842	113,931	8.8
2010-11 (est)	35,500	27,450	52,032	114,982	8.2
2011-12 (est)	31,000	30,262	50,072	111,334	7.6
2012-13 (proj)	30,000	31,846	53,174	115,020	7.5
2013-14 (proj)	29,500	34,645	55,436	119,581	7.4
2014-15 (proj)	30,000	39,615	58,881	128,496	7.6
2015-16 (proj)	30,500	44,815	61,961	137,276	7.7

(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 C14 and C18.

(c) 2007-08 figures are taken from the 2011 TES.

Changes to benchmarks makes comparison of the aggregate estimates in the 2012 TES with the aggregate estimates provided in previous editions difficult. For example, 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, whereas the tax expenditures associated with the carbon pricing mechanism announced in the *Clean Energy Future* package are included in the 2011 and 2012 TES.

Table 1.2 presents measured tax expenditures by the benchmark against which they are estimated for the period 2008-09 to 2015-16. The capital gains benchmark is the largest benchmark classification, but is expected to be overtaken by the retirement savings benchmark from 2013-14 onwards. The goods and services tax benchmark remains the third largest 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 (F25).

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

Benchmark	2008-09 (est)	2009-10 (est)	2010-11 (est)	2011-12 (est)	2012-13 (proj)	2013-14 (proj)	2014-15 (proj)	2015-16 (proj)
Income Tax								
Personal income	11,254	13,591	11,956	10,167	11,248	10,520	10,956	11,271
Business income	7,078	8,924	10,134	9,035	8,013	8,846	8,609	8,601
Retirement savings	31,407	26,154	29,345	32,417	33,961	36,775	41,760	47,035
Fringe Benefits Tax	4,088	4,397	4,824	5,164	5,032	4,945	5,094	5,506
Capital Gains Tax	40,145	45,002	41,126	36,391	34,932	35,417	37,368	38,325
Indirect Taxes								
Commodity and other indirect taxes ^(b)	-2,360	-1,956	-1,443	-1,968	-2,490	-3,010	-3,174	-3,624
Natural resources taxes	580	600	590	520	0	0	0	0
Goods and Services Tax	16,038	17,219	18,450	19,608	20,994	22,578	24,183	25,942
Carbon Pricing Mechanism	0	0	0	0	3,330	3,510	3,700	4,220

(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) Tax expenditure estimates for excise levied on cigarettes (F12) are not reported in the 2012 TES because of taxpayer confidentiality.

LARGE TAX EXPENDITURES

Table 1.3 lists the largest measured tax expenditures for 2012-13. The largest measured tax expenditure is the concessional taxation of superannuation entity earnings (C6) of around \$17.1 billion in 2012-13.

The next largest tax expenditures are the two components of the concessional capital gains taxation of owner-occupied housing (E5 and E6) which are estimated to provide a benefit to taxpayers of around \$30 billion in 2012-13. 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 \$13.2 billion in 2012-13. This is followed by the GST-free status of food (H29), which is estimated to provide a benefit to taxpayers of around \$6.2 billion in 2012-13.

Tax expenditures for emissions exempted from the carbon pricing mechanism (CPM) are also significant. The exemptions of emissions from agricultural activities and from deforestation (I6 and I1) are estimated to provide benefits to taxpayers in 2012-13 of around \$2.0 billion and \$1.1 billion respectively.

The largest negative tax expenditures in 2012-13 are customs duty (F25) and excise levied on fuel oil, heating oil and kerosene (F10). These tax expenditures are estimated to be around \$3.0 billion and \$0.6 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:

- income tax exemption for Commonwealth, State and Territory public authorities, and State and Territory entities (B3);
- exemption for foreign branch profits from income tax (B13);
- off-market share buy-backs (B29);
- philanthropy – income tax exemption for charitable, religious, scientific, and community service entities (B69); and
- quarantining of capital losses (E32).

Table 1.3: Large measured tax expenditures in 2012-13

Tax expenditure		Estimate \$m
Large positive tax expenditures		
C6	Superannuation — concessional taxation of superannuation entity earnings	17,100
E6	Capital gains tax main residence exemption — discount component	16,500
E5	Capital gains tax main residence exemption	13,500
C5	Superannuation — concessional taxation of employer contributions	13,150
H29	GST — Food; uncooked, not prepared, not for consumption on premises of sale and some beverages	6,200
E17	Capital gains tax discount for individuals and trusts	4,180
H16	GST — Education	3,550
H19	GST — Health; medical and health services	3,000
H2	GST — Financial Supplies; input taxed treatment	2,850
A43	Exemption of Family Tax Benefit, Parts A and B	2,050
I6	CPM uncovered sectors — Agriculture	1,970
B16	Exemption from interest withholding tax on certain securities	1,730
A21	Exemption of 30 per cent private health insurance rebate, including expense equivalent	1,570
C3	Concessional taxation of non-superannuation termination benefits	1,500
D14	Philanthropy — Exemption for public benevolent institutions (excluding public and not-for-profit hospitals)	1,410
B91	Statutory effective life caps	1,335
A20	Exemption from the Medicare levy for residents with a taxable income below a threshold	1,300
A64	Philanthropy — Deduction for gifts to deductible gift recipients	1,120
D11	Philanthropy — Exemption for public and not-for-profit hospitals and public ambulance services	1,100
I1	CPM uncovered sectors — Deforestation	1,090
C8	Superannuation — deduction and concessional taxation of certain personal contributions	1,050
H21	GST — Health; residential care, community care and other care services	960
H3	GST — Financial Supplies; reduced input tax credits	940
D19	Application of statutory formula to value car benefits	930
F8	Concessional rate of excise levied on aviation gasoline and aviation turbine fuel	930
H6	GST — Water, sewerage and drainage	880
B93	Deduction for capital works expenditure	825
H5	GST — Child Care Services	820
B101	Research and development — Non-refundable tax offset	800
B4	Income tax exemption for local government bodies	720
H10	GST — Importation threshold	650
A32	Senior Australians' and Pensioners' Tax Offset	610
Large negative tax expenditures		
F25	Customs duty	-2,960
F10	Excise levied on fuel oil, heating oil and kerosene	-555

TRENDS IN TAX EXPENDITURES BY FUNCTION

Total measured tax expenditures by functional category are reported in Table 1.4 for the period 2009-10 to 2015-16. Significant changes underlying movements in functional categories are listed below.

- The increase in agriculture, forestry and fishing reflects the exclusion of agricultural emissions from the coverage of the carbon pricing mechanism (I6) which impacts on 2012-13 and later years.
- The decrease in the fuel and energy aggregate is due to the increase in excise on aviation fuel (F8) (which is part of the arrangements to make those fuels subject to an effective carbon price), the phased introduction of excise on certain alternative fuels (F9), and the change in the benchmark treatment of crude oil condensate (G7) when that fuel commences to be taxed under the PRRT from 1 July 2012.
- The total for transport and communication is estimated to increase over the reported period owing to the statutory effective life caps (B91) tax expenditure.
- The decrease in the recreation and culture aggregate is due to the expiration of the rebate for broadcasting licence fees tax expenditure (F4).
- The growth in the education aggregate is due to the growth in the value of the GST exemption for education (H16).
- The growth in the health aggregate is 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)		
	2009-10	2010-11	2011-12	2012-13	2013-14	2014-15	2015-16
General public services							
A. Legislative and executive affairs	2	2	1	1	1	1	1
B. Financial and fiscal affairs	3,200	3,450	3,530	3,790	4,050	4,320	4,590
C. Foreign affairs and economic aid	530	444	468	489	524	544	569
D. General research	0	0	0	0	0	0	0
E. General services	91	181	207	157	143	143	143
F. Government superannuation benefits	0	0	0	0	0	0	0
Defence	838	858	887	947	886	921	966
Public order and safety	0	0	0	0	0	0	0
Education	2,768	3,118	3,379	3,679	3,896	4,242	4,638
Health	7,520	8,110	8,595	9,440	9,295	9,780	10,300
Social security and welfare	33,008	36,472	38,150	40,412	43,286	48,701	54,276
Housing and community amenities	42,210	37,941	33,144	32,283	31,966	32,674	33,383
Recreation and culture	134	181	276	338	201	212	211
Fuel and energy	1,610	1,630	1,535	700	575	435	250
Agriculture, forestry and fishing	193	219	395	3,280	3,285	3,460	3,964
Mining, manufacturing and construction	-1,785	-1,553	-2,128	-2,358	-2,588	-2,708	-2,938
Transport and communication	819	956	1,104	1,311	1,428	1,447	1,379
Other economic affairs							
A. Tourism and area promotion	0	0	0	0	0	0	0
B. Total labour and employment affairs	2,237	2,480	2,518	2,096	1,714	1,554	1,686
C. Immigration	0	0	0	0	0	0	0
D. Other economic affairs, nec(b)	19,828	19,817	18,570	17,734	20,169	21,990	23,038
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	720	670	700	720	750	780	820
D. Natural disaster relief	8	6	3	1	0	0	0
E. Contingency reserve	0	0	0	0	0	0	0
Total(c)	113,931	114,982	111,334	115,020	119,581	128,496	137,276

(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 2011-12 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 2011-12*.

Comparisons between tax expenditures and direct expenditures are informative in broad terms, but the estimates are not 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, such as grants or Government program outlays, are usually taxable income in the hands of the recipient, 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 2011-12

	Tax expenditures (\$m)(a)	Direct expenditures (\$m)(b)
General public services		
A. Legislative and executive affairs	1	1,003
B. Financial and fiscal affairs	3,530	7,982
C. Foreign affairs and economic aid	468	5,878
D. General research	0	2,764
E. General services	207	1,432
F. Government superannuation benefits	0	4,094
Defence	887	21,692
Public order and safety	0	3,999
Education	3,379	29,050
Health	8,595	62,012
Social security and welfare	38,150	126,747
Housing and community amenities	33,144	6,180
Recreation and culture	276	3,809
Fuel and energy	1,535	6,464
Agriculture, forestry and fishing	395	2,953
Mining, manufacturing and construction	-2,128	2,245
Transport and communication	1,104	9,129
Other economic affairs		
A. Tourism and area promotion	0	177
B. Total labour and employment affairs	2,518	4,783
C. Immigration	0	2,740
D. Other economic affairs, nec(c)	18,570	2,354
Other purposes		
A. Public debt interest	0	11,421
B. Nominal superannuation interest	0	7,376
C. General purpose inter-governmental transactions	700	49,940
D. Natural disaster relief	3	1,516
E. Contingency reserve	0	0
Total(d)	111,334	377,739

(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 2011-12*.

(c) 'nec' means not elsewhere classified.

(d) Totals may not sum due to rounding.

1.4 Period covered by these estimates

The 2012 Tax Expenditures Statement generally uses the publication of the *2012-13 Mid-Year Economic and Fiscal Outlook* 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.