

Taxation Notes

Introduction to taxation and the Australian taxation system AND Overview of GST

Definition of Tax

- *Oxford Dictionary definition:*
 - 'Compulsory contribution to the support of government, levied on persons, property, income, commodities, transactions, etc'
- Taxpayers are compelled by law to pay taxes and are obliged to do so even though they may not necessarily receive any direct benefits in return

Functions of Tax

- *Revenue raising function:*
 - Redirects resources from citizens to government
 - Provides government with revenue for use in its spending programs
- *Social and political functions:*
 - Used to promote government objectives
 - Tax incentives – carrot to encourage certain behaviour
 - Tax burdens – stick to discourage certain behaviour
- *Economic functions*
 - Modifies consumer behaviour
 - Higher taxation leads to less spending (deflationary effect)
 - Lower taxation leads to more spending (inflationary effect)
- *Redistribution function*
 - Redistributes wealth among citizens

Tax System Design

- Tax system underpins a country's economic, social and political stability
- Unpopular taxes can lead to social and political unrest
- Society more likely to accept taxation if it:
 - Sees justification for the tax
 - Considers the level of tax appropriate

- Governments need to be able to forecast tax revenue for budgeting purposes
- Challenges facing Australia need to be taken into account in the design of its tax system

Adam Smith – *“The subject of every state ought to contribute towards the support of the government, as nearly as possible, in proportion to their respective abilities, that is, in proportion to the revenue which they respectively enjoy under the protection of the state”*

Features of a good tax system

- Clear fiscal and policy objectives
- Simplicity and certainty
- Stability
- Transparency and integrity
- Efficiency and flexibility
- Neutrality
- Equity
 - “Horizontal equity”
 - “Vertical equity”

Structural Features of Tax

- *Taxpayers*
 - The legal entities who are liable to pay the tax and from whom unpaid tax can be recovered
- *Tax base*
 - The property, transaction, activity or concept on which the tax is imposed
- *Tax periods*
 - The period in relation to which tax is paid
- *Tax rates*
 - May be single rate (eg flat rate) or differing rates (eg progressive rates)

Types of Taxes

- *Proportional taxes*
 - Imposed at the same rate for all taxpayers (eg GST)
- *Progressive taxes*

- Imposed at rates that increase with amount of tax base (eg income tax)
 - *Regressive taxes*
 - Imposed at rates that decrease with amount of tax base
- CAN BE FURTHER CLASSIFIED INTO:**
- *Direct tax*
 - Economic burden of tax is borne by person who pays the tax (eg income tax)
 - *Indirect tax*
 - Person who pays the tax is able to pass on the economic burden of tax to a third party (eg GST)

Types of Tax Rates

- *Marginal tax rate*
 - The rate of tax that is applied to the incremental amounts of the tax base
- *Average tax rate*

Taxpayer's total tax liability

Tax base

- *Effective tax rate*

Taxpayer's total tax liability

Taxpayer's total economic income

Jurisdiction to tax

- *Territorial approach – based on 'source'*
 - Worldwide approach – based on General jurisdictional rules:
 - 'source' and 'residence'
- *Australia adopts worldwide approach:*
 - Australian residents are generally taxed on their Australian and foreign source income
 - Foreign residents are generally taxed on their Australian source income

Sources of Tax Law

- *Statute*
- *Cases:*
 - High Court

- Full Federal Court
- Federal Court
- Administrative Appeals Tribunal

Australian Tax

- *Australia taxes individuals, rather than families*
- *No general account taken of taxpayer's dependants for tax purposes*
- *Nevertheless, some limited tax concessions apply to individuals with families*
- *Australia generally treats partnerships and trusts as flow-through entities*
- *Income is taxed in the hands of members*
- *Australia treats companies as opaque entities*
- *Companies and their members are taxed as separate entities (subject to imputation)*

Main Commonwealth Taxes

- *Income tax*
- *Temporary budget repair levy (TBRL)*
- *Medicare levy (ML)*
- *Medicare levy surcharge (MLS)*
- *Fringe benefits tax (FBT)*
- *Goods and services tax (GST)*

Tax Levels

- *Difficult to compare levels of taxation between countries because of differences in:*
 - Types of taxes imposed
 - Types of tax expenditure programs
 - Different tax bases

State and Territory Taxes

- *Payroll tax* – imposed on wages (including bonuses, allowances, superannuation contributions and certain fringe benefits) provided by employers to their employees
- *Land tax* – imposed on the taxable value of land owned in a State, with some exemptions
- *Stamp duty* – imposed on dutiable transactions, eg:

