

CHAPTER 7

TAXING AND CHARGING

Norfolk Island's revenue capacity was analysed before the High Court's ruling on 5 August 1997 that State business franchise fees on petroleum, liquor and tobacco were invalid. Since then, the Commonwealth and States have agreed that their total net tax effort will not change before 30 June 1988. As a result, our estimate of Norfolk's revenue capacity relative to the mainland has not been affected.

1. The financial capacity of the Norfolk Island Government is the extent to which it is able to raise revenue, from whatever source, to fund services for which it is, or might become, responsible. This chapter looks first at Norfolk Island's policies on raising revenue (that is, its effort), and then makes some estimates of its ability (that is, its capacity) to obtain revenue from:

- the tax bases it is using;
- the range of tax bases normally used on the mainland; and
- a more broadly based or global tax base, such as income, assets, or consumption.

2. As discussed in Chapter 2, the capacity of the Norfolk Island Government to raise revenue from its own sources has been estimated by applying taxes rates and charges, similar to those raised on the mainland, to the Island's tax bases. This process is modified if special circumstances that prevent Norfolk Island from imposing the standard (average) tax rates are thought to exist. An example is our assumption that, on cultural grounds, Norfolk has a capacity to raise revenue from lotteries but not from other forms of gambling.

3. This chapter deals with government revenue from all sources. No distinction is made between taxes, charges, interest earnings and dividends from government business enterprises (GBEs). Where appropriate, references to taxes should be understood to refer also to charges, interest earnings and dividends from GBEs. For Norfolk Island, total dividends from GBEs are deemed to be their total net operating surplus.

4. The total revenue figure shown in this chapter is lower than that shown in Chapter 5 because in this chapter we are only interested in the dividends from GBEs. Thus, only the net operating surplus is treated as revenue, whereas in Chapter 5 all GBE income was treated as revenue.

REVENUE RAISING CAPACITY

Financial and Related Policies of Government

5. Table 7-1 shows that in 1995-96, the Norfolk Island Government raised \$5571 revenue per capita, \$3342 (37 per cent) less than the \$8913 per capita raised by mainland Governments (Commonwealth, State and local). This lower revenue performance could be because:

- the community prefers a lower level of government service provision and therefore supports a smaller government sector (choosing to pay lower levels of tax);
- the Island is restricted to using narrower tax raising powers;
- the Island has chosen a different mix of taxes; or
- the policy of the Norfolk Island Government is to have low tax rates.

6. **Community preference.** The existence of a community preference on Norfolk Island for a lower level of government service provision was supported by some participants at both the May and July conferences. They believed that there is a high level of community voluntary effort on the Island that reduces the need for the government to provide as many services. Some submissions referred to this community effort as voluntary taxation.

7. A number of submissions provided information on a range of community contributions. During our discussions, we formed the impression that the level of community voluntary effort on Norfolk is larger than on the mainland, but that it would not amount to more than about \$200 000 worth of services a year.

8. We cannot be sure that the lower revenue performance is due to a community preference for a smaller government sector and a larger voluntary effort. However, it does appear to have some influence.

9. **Taxing powers.** Norfolk's lower revenue performance might arise because it is restricted to using narrower tax raising powers.

10. The revenue raising capacity of the States is constrained by the Constitution and Commonwealth law. They do not have the ability to access income direct through income tax and they cannot impose customs duties, excise or departure taxes. State tax regimes rely heavily on narrowly based indirect (or expenditure based) taxes. The only broad tax power available to them, Payroll Taxation, is their major source of tax revenue. The Commonwealth transfers revenue it has raised to the States to supplement their financial capacity.

Table 7-1 TAX REVENUES BY CATEGORY OF TAX, 1995-96

Category of tax	Norfolk Island	Mainland
	\$ pc	\$ pc
Taxation Revenue		
Direct taxes		
Health levy ^(a)	188	184
Income tax – residents	0	3 151
Income tax – companies	0	1 141
Broadly based indirect taxes		
Wholesales sales tax	0	714
Customs duty	1 421	172
Pay-roll taxation	0	554
Workers compensation levy ^(b)	116	0
Narrowly based indirect taxes		
Petroleum	170	85
Tobacco	0	144
Alcohol	31	40
Motor vehicle taxes	123	192
Gambling taxes	46	183
Financial institutions and stamp duties	603	339
Accommodation levies	111	0
Departure taxes	413	4
Landing fees	694	16
Other indirect taxes	293	1 032
Wealth taxes		
Land taxes	33	82
Municipal rates	0	280
Other wealth taxes	0	16
Total taxation revenue	4 242	8 330
Non-taxation revenue		
Interest earnings	231	178
Mining revenue	0	57
GBE dividends ^(c)	1 098	348
Total non-taxation revenue	1 329	583
Total revenue	5 571	8 913

(a) For Norfolk Island, the Healthcare Levy.

(b) For mainland governments, workers compensation levies are included in other indirect taxes.

(c) For Norfolk Island, the net operating surplus of GBEs (excluding the Healthcare Levy, Workers Compensation Levy and Landing Fees).

Sources: *Taxation Revenue, Australia, 1995-96*, ABS Cat No 5506.0. The Administration of Norfolk Island, *Financial Statements, Year Ended 30 June 1996*. *Budget Statements 1996-97, Budget Paper No. 1*, ABS Cat No 5506.0. Commonwealth Grants Commission, *Report on General Grant Relativities, 1997 Update*.

11. A DEST submission contained advice on the Norfolk Island Government's taxation power. This was that:

- the Norfolk Island Legislative Assembly has the power to pass laws imposing the full range of taxes and charges imposed on the mainland, provided such laws:
 - (a) (i) are for the purposes of Schedule 2 matters,
 - (ii) are for the purposes of Schedule 3 matters and are agreed to by the Commonwealth,
 - (iii) are for purposes outside the Schedules but are assented to by the Governor-General, and
 - (b) are not inconsistent with all or part of a Commonwealth Act, and
 - (c) do not purport to bind the Commonwealth; and
- the Assembly's power to levy taxes and charges is not otherwise limited.

12. We take this advice to mean that the revenue raising capacity of the Norfolk Island Government is subject to very few legislative constraints.

13. On Norfolk Island, the Commonwealth has vacated major taxing areas normally within its purview (notably sales tax and income tax). Commonwealth legislation levying customs duty and sales tax does not extend to the Island. Historically, the Commonwealth has advised the Administrator to assent to Island legislation raising customs duty. There is no sales tax on Norfolk. The *Income Taxation Assessment Act 1936* applies to Norfolk Island but exempts income derived by Island residents from sources within the Island. Application of the *Income Taxation Assessment Act* does not, of itself, prevent the Norfolk Island Government from developing an Island income tax regime — it would be a matter of drafting the local legislation in a way that was not inconsistent with the Commonwealth Act. Thus, the Island Government has had the opportunity to craft a tax regime to suit the Island's special circumstances.

14. One caveat to this is that the Commonwealth's attitude to an attempt by Norfolk Island to raise some major Commonwealth taxes — in particular, income tax — has not been tested. It would be open to the Commonwealth to circumvent an Island income tax by:

- withholding assent to Island legislation;
- advising the Governor-General to disallow the legislation under Section 23 of the *Norfolk Island Act 1979*; or
- introducing Commonwealth legislation to override the local legislation.

15. It is clear that restricted access to tax powers is not the reason for Norfolk's lower revenue performance and, for the purposes of this inquiry, we have assumed that the Norfolk Island Government has the capacity to impose the full range of taxes imposed on the mainland.

16. **Choice of taxes and rates.** In this and the following sections, we address the question of whether Norfolk's lower revenue performance is due to its choice of taxes and tax rates.

17. Looking first at the **mix of taxes**, Table 7-1 provides a summary of how taxes were collected on the Australian mainland and on Norfolk Island in 1995-96. Table 7-2 provides a list of the revenues raised on Norfolk and those raised on the mainland but not on Norfolk. The tables show that Norfolk Island imposes a very different range of taxes from governments on the mainland. In these tables, taxes are classified into:

- (i) direct taxes;
- (ii) broadly based indirect taxes;
- (iii) narrowly based indirect taxes;
- (iv) wealth taxes; and
- (v) non-taxation revenue¹.

18. Figures 7-1 and 7-2 show the percentage of revenue raised by each class of tax on the mainland and on Norfolk.

19. These figures and tables show the importance of:

- broadly based taxes (including income tax) on the mainland (mostly Commonwealth);
- the taxation of income and wealth on the mainland;
- narrowly based indirect taxes, which fall heavily on the tourist sector, on Norfolk Island; and
- business enterprise income on Norfolk Island.

20. About 66 per cent of mainland tax revenue was raised from broadly based taxes (income taxes, sales taxes and payroll taxes) in 1995-96. The figure for Norfolk Island was close to 31 per cent, comprising:

- Customs Duty (26 per cent of tax revenue);
- the Healthcare Levy (3 per cent of tax revenue); and
- the Workers Compensation Levy (2 per cent of tax revenue).

¹ This group includes charges, interest earnings and dividends from GBEs.

It is the compulsory nature of the Healthcare and Workers Compensation Levies that leads us to include them as taxes and the wide scope of their application to classify them as broadly based. Customs Duty is by far the largest revenue source for the Island.

Table 7-2 REVENUE RAISED ON NORFOLK ISLAND AND ON THE MAINLAND BUT NOT NORFOLK, 1995-96

Revenues raised on Norfolk	Additional revenues raised on the mainland
Direct taxes	
Healthcare levy	Income tax – residents Income tax – companies
Broadly based indirect taxes	
Customs duty ^(a)	Sales tax and other excise taxes
Workers compensation levy	Pay-roll taxation
Narrowly based indirect taxes	
Fuel levy	Tobacco franchise fees
Liquor licence fees	Stamp duty on motor vehicles registrations and transfers
Vehicle registrations and drivers' licences	Other gambling taxation
Lottery taxation	Other financial institutions levies
Financial institutions levy	
Stamp duty on cheques	
Conveyancing fees	
Accommodation levy	
Departure taxes	
Landing fees	
Company fees	
Other charges	
Wealth taxes	
Absentee landowners levy	Municipal rates Other land taxes
Non-taxation revenue	
Interest earnings	Mining revenue
Dividends from GBEs	

(a) For Norfolk, this includes customs duty levied on tobacco, alcohol and fuel.

21. Broadly based taxes, including income tax, offer a government a means of ensuring equity and fairness within its tax system. For example, they allow governments to impose higher taxes on those who earn higher incomes or who are wealthier.

Figure 7-1 SOURCES OF REVENUE, MAINLAND, 1995-96

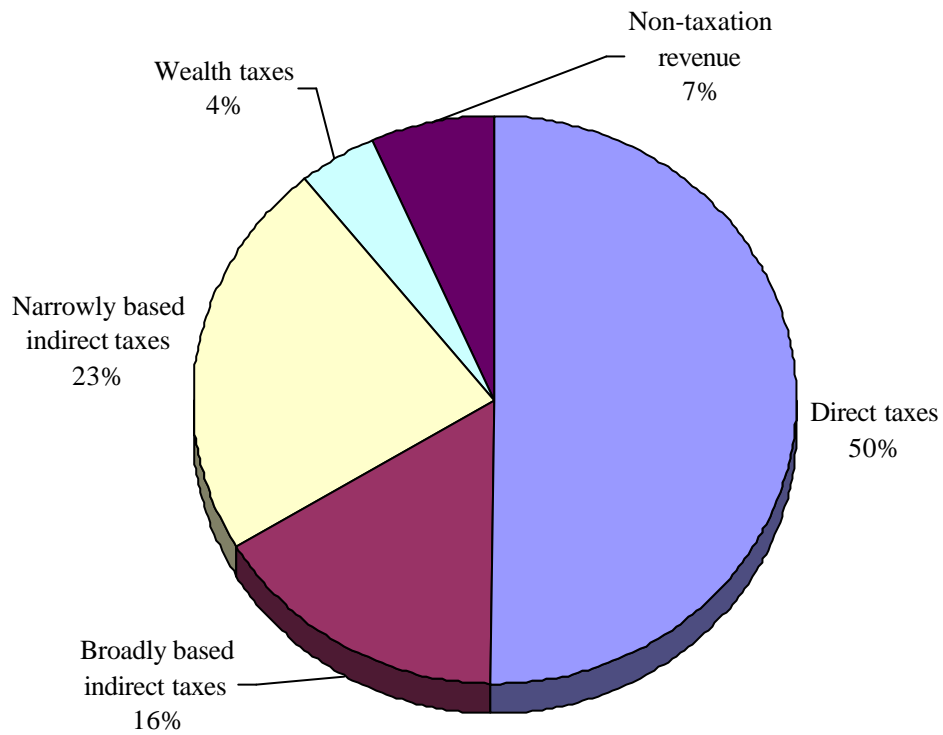
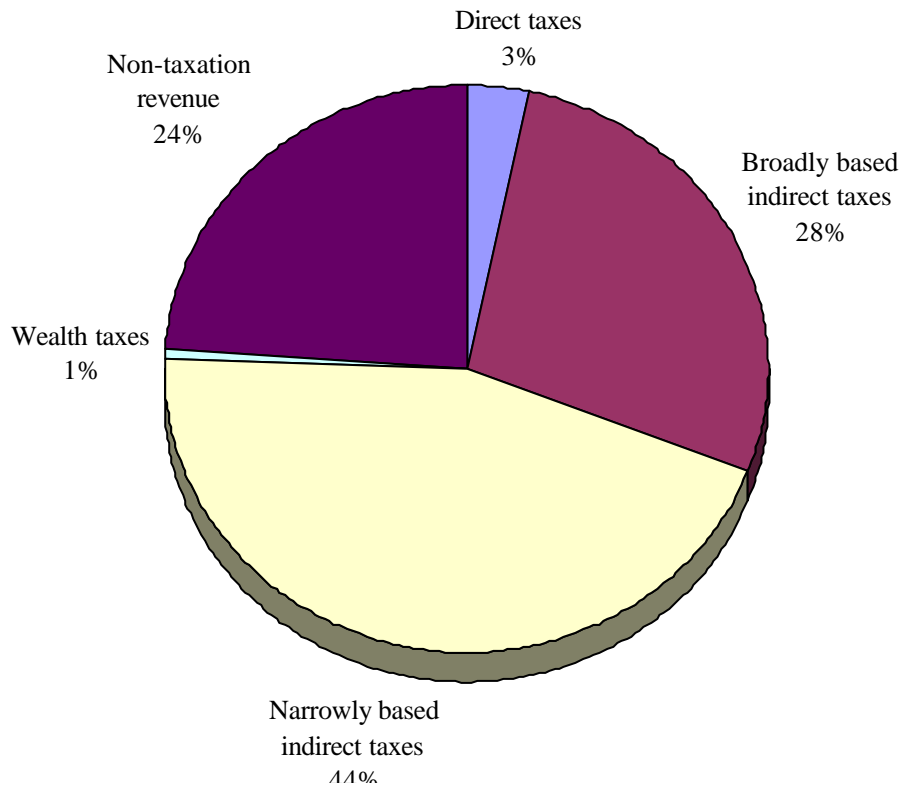


Figure 7-2 SOURCES OF REVENUE, NORFOLK ISLAND, 1995-96



22. Governments can tax income, wealth and expenditure. Most governments tax all three and have to find an appropriate balance between them. In 1995-96, the Commonwealth and States raised 54 per cent of their tax revenue by taxing income and wealth, whereas Norfolk Island raised only 4 per cent of its tax revenue from these sources. While the mainland may be over reliant on taxes on income, the Norfolk Island Government's capacity to develop an equitable and fair tax system seems to be limited by its policy of relying on expenditure based taxes. These can be distortionary (affecting some businesses but not others) and, in the extreme, can lead to some residents or businesses paying little or no tax. The structure of the Norfolk taxation regime is regressive; that is, it is highly likely that wealthier residents pay a lower proportion of their income or wealth in tax than poorer residents do.

23. A high proportion of the Island's tax revenue is raised from tourists. Three taxes are collected largely from tourists — Departure Tax, Landing Fees and the Accommodation Levy. In Chapter 4, the tourist share of these taxes is estimated at \$2 million, that is, about 22 per cent of the Island's total revenue. In addition, tourists contribute revenue through the Island's expenditure based taxes and it could be assumed that, as a minimum, this would match their average population share.

24. The taxation of tourists is not in itself bad. First, because tourists at any particular time comprise a large share of the Island's population, it would be reasonable for them to make some contribution towards the services they use during their stay — one example raised by the Norfolk Island Government is Landing Fees which it considers to be user pays charges for the purpose of financing future airport maintenance and capital requirements. Second, the taxation of tourists and others living elsewhere is a way for the Norfolk Island Government to export its tax burden to residents of other jurisdictions. Provided there are no serious adverse effects on its tourist trade, this is to the benefit of the Norfolk Island community.

25. However, our analysis of the figures in Table 7-1 does not support a suggestion made at the May conference that tourists are paying only a share of the tax burden proportionate to their numbers. In 1995-96, tourists comprised an average of 26 per cent of the number of people on the Island². Because they also pay indirect taxes, the tourist share of all taxes is much larger than the 22 per cent mentioned above. On a rough calculation, the figure is probably 40 per cent, not far short of the 46 per cent estimated in the recent Access Economics Report³.

26. Business enterprises are also an important source of recurrent revenue for the Norfolk Island Government. In 1995-96, 20 per cent of its revenue was obtained from GBEs⁴. The main revenue earners were the Liquor Supply Centre, Norfolk Island Telecom and the Norfolk Island Postal Service. These GBEs earned part of their revenues from tourists and foreigners. Compared to mainland governments, the Norfolk Island Government receives three times the revenue per capita from GBEs.

² Based on 1772 ordinary residents and an average tourist population figure of 632. Table 4.2 in Chapter 4 shows this calculation. The comparable figure for the period 1990-91 to 1995-96 is 25 per cent.

³ Access Economics Report, p35.

⁴ The 20 per cent figure does not include the Healthcare Levy, the Workers Compensation Levy or Landing Fees which are included elsewhere.

27. It is clear that Norfolk's choice of tax mix, with its much more limited range of taxes, partly explains its lower revenue performance.

28. Norfolk's revenue performance is also affected by its **tax rates**. We calculated average tax rates for Norfolk and the mainland by:

- (i) choosing an underlying tax base; and
- (ii) dividing revenue collected by the chosen tax base.

29. Table 7-3 lists the tax bases that were used to calculate the tax rates shown in Table 7-4 and also gives estimates of the size of those tax bases on Norfolk and the mainland. Actual tax bases are not available in a number of cases. Thus, we have chosen wages and salaries as the tax base for personal income tax because information on other forms of personal income on Norfolk is not available. We have also chosen wages and salaries as the tax base for the Workers Compensation Levy, even though it is imposed at the flat rate of 15 cents an hour worked by each employee. Because there is no Norfolk Island tax on tobacco sales, we estimated the tobacco tax base by increasing the value of tobacco imports (excluding re-exports) by 20 per cent.

30. Relevant aspects of Table 7-3 are:

- the mainland has a relatively larger tax base for Fuel Levy, Financial Institutions Levy, mining revenue and land taxes;
- Norfolk has a relatively larger tax base for all other taxes levied on the Island; and
- Norfolk has a relatively larger overall revenue base (gross product) than does the mainland.

31. To illustrate how average tax rates have been calculated, the average tax rate for the Workers Compensation levy was obtained by:

- taking the amount the Government raised through the Workers Compensation Levy in 1995-96 (\$204 678); and
- dividing it by the figure for total wages and salaries on Norfolk estimated in Chapter 4 to be \$24.3 million in 1995-96.

The average tax rate obtained was 0.84 per cent.

Table 7-3 TAX BASES, NORFOLK ISLAND AND THE MAINLAND, 1995-96

Category of tax	Specified tax base	Norfolk Island	Mainland
		\$pc	\$pc
Direct taxes			
Health levy	Wages and salaries	13 735	13 218
Income tax – residents	Wages and salaries	13 735	13 218
Income tax – companies	Private sector profit	22 553	10 342
Broadly based indirect taxes			
Sales tax	Gross product	45 343	26 911
Customs duty	Value of imports	13 910	4 244
Workers compensation levy	Wages and salaries	13 735	13 218
Payroll tax	Wages and salaries	13 735	13 218
Narrowly based indirect taxes			
Petroleum	Value of sales	852	2 370
Tobacco	Value of sales	160	154
Liquor	Value of sales	1 558	353
Motor taxes	No of registered vehicles	1.33	0.74
Tattersalls lotteries	Wages and salaries	13 735	13 218
Other gambling	Wages and salaries	13 735	13 218
Financial institutions taxes	Value of transactions	50 270	145 611
Conveyancing fees	Value of land	11 128	31 201
Company fees	Private sector profit	22 553	10 342
Accommodation levy	Number of tourists	16.81	0.21
Departure tax	Number of tourists	16.81	0.21
Landing fees	Number of travellers ^(a)	18.21	2.73
Other indirect taxes	Gross product	45 343	26 911
Wealth taxes			
Land taxes	Value of land	11 128	31 201
Municipal rates	Value of residential land	8 308	26 745
Other land taxes	Value of land	11 128	31 201
Non-taxation revenue			
Interest earnings	Gross product	45 343	26 911
Mining revenue	Value of sales	0	438
Dividends from GBEs	Gross product	45 343	26 911

(a) Both international and domestic.

32. Table 7-4 provides the estimates of average tax rates for a range of taxes applying on Norfolk Island and on the mainland⁵. It shows that, for most of the taxes imposed on the Island, Norfolk's average rate of tax is higher than on the mainland. This suggests that the Norfolk Island Government's low revenue performance is not because it imposes low rates in the taxes that it levies.

⁵ All these tax rates were calculated using the method discussed previously. Where the underlying tax base is number of people or vehicles, the average tax rate would be a dollar figure for each person or dollar figure for each vehicle rather than a percentage.

33. Its lower performance appears, therefore, to be due to the narrower range of taxes imposed than on the mainland, despite relatively larger tax bases across the board. The next sections explore these issues further. First, we look at the capacity of the Government to raise revenue from the range of taxes raised on the Island and then we examine its capacity to raise revenue from the wider range of taxes on the mainland.

Table 7-4 AVERAGE TAX RATES, NORFOLK ISLAND AND THE MAINLAND, 1995-96

Category of tax	Chosen tax base	Norfolk Island	Mainland
		% ^(a)	% ^(a)
Direct taxes			
Health levy	Wages and salaries	1.37	1.39
Income tax – residents	Wages and salaries	0.00	23.84
Income tax – companies	Private sector profit	0.00	11.03
Broadly based indirect taxes			
Sales tax	Gross product	0.00	14.38
Customs duty	Value of imports	10.21	4.06
Workers compensation levy	Wages and salaries	0.84	0.00
Payroll tax	Wages and salaries	0.00	4.19
Narrowly based indirect taxes			
Petroleum	Value of sales	20.00	3.59
Tobacco	Value of sales	0.00	93.60
Liquor	Value of sales	2.00	11.47
Motor taxes	No of registered vehicles	\$92.51	\$260.45
Tattersalls lotteries	Wages and salaries	0.33	0.26
Other gambling	Wages and salaries	0.00	1.12
Financial institutions taxes	Value of transactions	1.02	0.13
Conveyancing fees	Value of land	0.80	0.50
Company fees	Private sector profit	0.12	0.00
Accommodation levy	Number of tourists	\$6.62	\$1.51
Departure tax	Number of tourists	\$24.55	\$20.94
Landing fees	Number of travellers ^(b)	\$38.11	\$5.86
Other indirect taxes	Gross product	0.59	0.96
Wealth taxes			
Land taxes	Value of land	0.30	0.26
Municipal rates	Value of residential land	0.00	1.05
Other land taxes	Value of land	0.00	0.05
Non-taxation revenue			
Interest earnings	Gross product	0.51	0.66
Mining revenue	Value of sales	0.00	13.04
Dividends from GBEs	Gross product	2.42	1.29

(a) Unit of measurement is percentage. If the chosen tax base is number of people, the unit of measurement is dollars a person. If the chosen tax base is number of vehicles, the unit of measurement is dollars a vehicle.

(b) Both international and domestic travellers.

34. To simplify the presentation of the analyses in these sections, we have grouped taxes by the applicable tax base as follows:

- (i) taxes on personal incomes;
- (ii) taxes on expenditure;
- (iii) taxes on travellers;
- (iv) motor taxes;
- (v) land taxes;
- (vi) taxes on companies; and
- (vii) other taxes, charges and dividends.

While the analyses are presented using these tax groups, they were undertaken separately for each tax. Table 7-5 shows which taxes have been classified to each group.

35. **Summary.** Figures 7-3 and 7-4 show, for Norfolk Island and the mainland, the percentage of revenue collected from each tax group. They confirm the greater reliance on expenditure tax and taxation of travellers by the Norfolk Island Government compared with the mainland Governments' greater reliance on income tax (of individuals and companies) and land taxes.

Table 7-5 CLASSIFICATION OF TAXES, NORFOLK ISLAND AND THE MAINLAND

Tax group	Norfolk taxes	Mainland taxes
Taxes on personal incomes	Healthcare levy Workers compensation levy Tattersall's lotteries	Income tax – individuals Income tax – Medicare levy Pay-roll taxation Gambling - lotteries Gambling - other
Taxes on expenditure	Customs duty Fuel levy Liquor licence fees Financial institutions levy Stamp duty on cheques	Customs duty – imports and other Petroleum franchise fees Petroleum excise taxes Liquor franchise fees Tobacco franchise fees Financial institutions levy Stamp duty on cheques Other financial transaction taxes Mining revenue
Taxes on travellers	Accommodation levy Departure tax Landing fees	Accommodation levy Departure tax Landing fees
Motor taxes	Vehicle registrations and licences	Vehicle registrations and licences Stamp duty on registrations and transfers
Land taxes	Conveyancing fees Absentee landowners levy	Conveyancing fees Land tax Municipal rates Other land taxes
Taxes on companies	Company fees	Company fees Income tax –companies and other
Other taxes, charges and dividends	Interest earnings Operating surplus of GBEs Other charges	Interest earnings Dividends from GBEs Sales tax Excise tax – other Other fees and fines Other taxes

Figure 7-3 REVENUE BY TAX GROUP, NORFOLK ISLAND, 1995-96

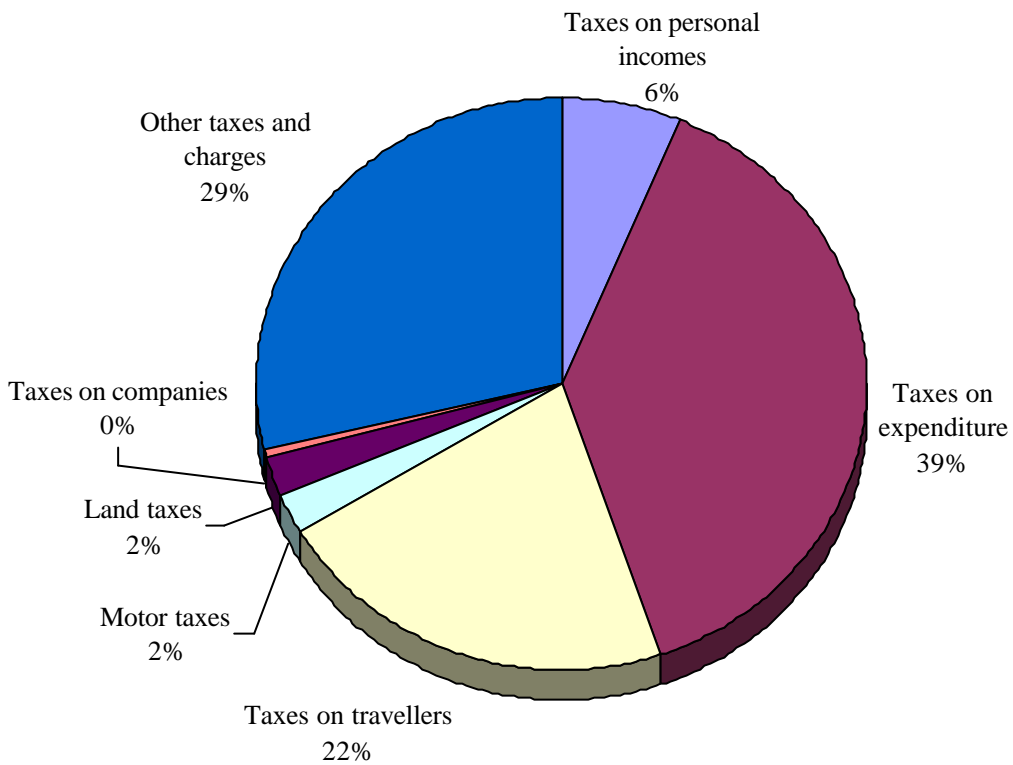
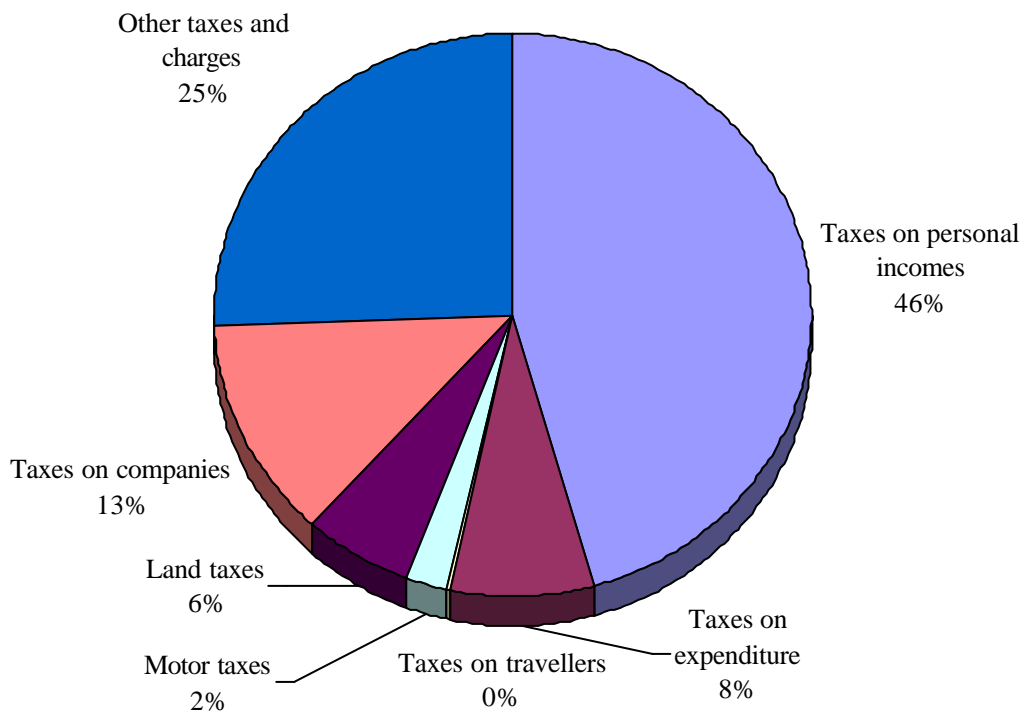


Figure 7-4 REVENUE BY TAX GROUP, MAINLAND, 1995-96



Taxes Raised on Norfolk Island

36. This section examines the Norfolk Island Government's financial capacity for the range of taxes imposed on the Island. Financial capacity is a measure of what a government could raise from a tax. For example, if wages per capita were higher on Norfolk Island than on the mainland, then a tax on wages should, if it were imposed at the same rate, raise more revenue per capita on Norfolk than on the mainland. From the Commission's perspective, financial capacity is more relevant than how much revenue is actually raised because it allows a comparison of how much revenue could be raised from different communities if their governments imposed the same tax burdens on them.

37. We have calculated Norfolk Island's financial capacity by applying the mainland tax rates, shown in Table 7-4, to the Norfolk Island tax bases shown in Table 7-3. For example, the mainland tax rate for conveyance fees is 0.50 per cent and for land tax is 0.26 per cent (see Table 7-3). The Norfolk Island land tax base is \$11 128 per capita (see Table 7-5). Thus, Norfolk's taxable capacity to raise similar land revenues is \$84 per capita (that is, 0.76 per cent times \$11 128).

38. Table 7-6 presents an analysis by tax group of the taxes raised on Norfolk Island. It shows that Norfolk raised \$5571 per capita from the taxes it imposes, more than twice the amount (\$2345 per capita) raised by mainland governments. The difference of \$3226 per capita (\$5571 less \$2345) is partly due to Norfolk's relatively higher tax bases and partly to its higher tax rates overall.

39. If Norfolk had imposed its taxes at mainland tax rates, it would have raised (because of its relatively larger tax bases) \$3027 per capita. Thus \$682 (\$3027 less \$2345) or about 20 per cent of the \$3226 per capita difference is attributable to greater taxable capacity. The remainder — \$2544 or about 80 per cent — is attributable to higher tax rates overall.

40. We conclude that Norfolk's overall lower revenue performance is not due to low rates of taxes imposed on the Island. On the contrary, for the range of taxes imposed, the Norfolk Island Government accesses the financial capacity available to it at greater than mainland severity.

Table 7-6 NORFOLK ISLAND'S ASSESSED FINANCIAL CAPACITY PER CAPITA FOR TAXES RAISED ON NORFOLK ISLAND, 1995-96

Tax group	Revenue raised		Effect of		
	Norfolk Island (1)	Mainland (2)	Norfolk's assessed capacity (3)	Norfolk's different tax rate (4)=(1)-(3)	Norfolk's different tax base (5)=(3)-(2)
	\$pc	\$pc	\$pc	\$pc	\$pc
Taxes on personal incomes	349	772	803	-454	31
Taxes on expenditure	2 136	403	810	1 326	407
Taxes on travellers	1 218	21	5	1 213	-16
Motor taxes	123	127	2	121	-125
Land taxes	122	236	84	38	-152
Taxes on companies ^(a)	26	0	0	26	0
Other taxes, charges and dividends	1 596	785	1 322	274	537
Total	5 571	2 345	3 027	2 544	682

Note: Totals may not add due to rounding.

(a) Company fees for Norfolk; on the mainland, company fees are included in other taxes, charges and dividends.

Taxes not Raised on Norfolk Island

41. A number of taxes applied on the mainland are not used on Norfolk. In these areas, Norfolk uses none of the capacity available to it. It is useful to ask what revenue the Norfolk Island Government could raise if it decided to impose the full range of taxes. Our estimate of the potential revenue from taxes not imposed on Norfolk Island is presented in Table 7-7. It is \$5929 per capita, a total of about \$10.5 million.

Table 7-7 ASSESSED NORFOLK ISLAND CAPACITY AND MAINLAND REVENUE COLLECTIONS PER CAPITA FOR TAXES NOT RAISED ON NORFOLK ISLAND, 1995-96

Tax group	Assessed capacity	Mainland
	\$pc	\$pc
Taxes on personal incomes	1 637	3 299
Taxes on expenditure	177	280
Taxes on travellers	0	0
Motor taxes	1	65
Land taxes	93	296
Taxes on companies	1 515	1 141
Other taxes, charges and dividends	2 506	1 488
Total	5 929	6 568

42. This estimate of financial capacity was assessed in a manner similar to that discussed earlier. It is conservative and is based on our assumptions that:

- for whatever reason, Norfolk would raise only half as much income tax as the mainland (per capita) if it imposed the same tax rates;
- on cultural grounds, Norfolk has no gambling base other than lotteries; and
- Norfolk has no capacity to earn mining revenue.

43. A rough estimate of Norfolk Island's financial capacity in 1995-96 from the full range of taxes imposed on the mainland is therefore \$8956 per capita, about \$15.9 million. This consists of \$3027 per capita for taxes raised (see Table 7-6) and \$5929 per capita for taxes not raised (see Table 7-7). It compares with the \$5571 per capita (\$9.9 million) it actually raised (see Table 7-1).

44. We conclude, therefore, that the main cause of Norfolk's lower revenue performance is the narrower range of taxes and charges imposed on the Island compared to mainland Governments.

An Alternative Broader Measure of Capacity

45. At the beginning of this chapter, it was noted that Norfolk Island's wider revenue raising powers, compared to the States, provided it with an opportunity to craft a tax regime to best suit the Island's special circumstances. It might be useful to estimate the Island's capacity on an overall basis — that is, to compare the ratio of total per capita public

sector revenue from all sources to total per capita gross product for Norfolk and for the mainland. This is done in Table 7-8. It confirms that the Norfolk Island Government has additional, unused taxation (financial) capacity when compared with governments on the mainland.

Table 7-8 BROADER MEASURE OF NORFOLK ISLAND CAPACITY, 1995-96

Category of tax		Norfolk Island	Mainland
Total public sector revenue (\$ per capita)		5 571	8 913
Total public sector revenue adjusted for Norfolk's special circumstances (\$ per capita)		5 571	6 469
Gross product (\$ per capita)	(1)	45 343	26 911
Ratio of adjusted revenue to gross product (%)		12.29	24.04
Mainland ratio of adjusted revenue to gross product (%)	(2)	24.04	
Broader measure of Norfolk Island capacity (\$ per capita)	(3)=(1)*(2)	10 900	

46. If the Norfolk Island Government raised the same proportion of revenue from gross product as on the mainland, it would have raised \$10 900 per capita, or approximately \$19.3 million. This is higher than the assessment based on individual taxes and charges which suggests that the Norfolk Island Government could raise \$15.9 million if it applied mainland tax rates, adjusted for Norfolk Island's special circumstances, to Norfolk tax bases.

47. The rest of this chapter uses the lower estimate.

The Norfolk Island Government's Tax Effort

48. Norfolk Island's financial capacity has thus been assessed as \$15.9 million or \$8956 per capita for:

- the range of taxes and charges imposed on Norfolk; and
- the range of taxes and charges imposed on the mainland but not on Norfolk.

Table 7-9 summarises these findings.

Table 7-9 FINANCIAL CAPACITY, NORFOLK ISLAND, 1995-96

Category of tax	Financial capacity	
	\$000	\$pc
Taxes, charges and dividends raised on Norfolk Island	5 364	3 027
Taxes, charges and dividends raised on the mainland but not Norfolk	10 506	5 929
All taxes, charges and dividends	15 870	8 956

49. Table 7-10 provides information on revenue raised by Norfolk Island in 1995-96, for the two groups shown in Table 7-9. It shows that Norfolk Island actually raised \$9.9 million or \$5571 per capita. Table 7-11 shows the Norfolk Island Government's revenue effort. This is calculated by dividing revenue raised by the assessed financial capacity. For example, the revenue effort for taxes, charges and dividends raised on Norfolk Island is equal to \$5571 per capita (Table 7-10) divided by \$3027 per capita (Table 7-9), that is, 184.1 or 184.1 per cent. Revenue effort gives an indication of the relative severity of tax rates. A revenue effort of more than one hundred per cent implies that Norfolk imposes a higher tax rate than is applied on the mainland.

Table 7-10 REVENUE RAISED, NORFOLK ISLAND, 1995-96

Category of tax	Revenue raised	
	\$000	\$ pc
Taxes, charges and dividends raised on Norfolk Island	9 872	5 571
Taxes, charges and dividends raised on the mainland but not Norfolk	0	0
Total revenue raised	9 872	5 571

Table 7-11 REVENUE EFFORT, NORFOLK ISLAND, 1995-96

Category of tax	Revenue effort
	%
Taxes, charges and dividends raised on Norfolk Island	184.1
Taxes, charges and dividends raised on the mainland but not Norfolk	0.0
Total revenue raised	62.2

50. This calculation confirms that, for the range of taxes and charges raised on Norfolk, the Norfolk Island Government imposes them at rates that are considerably higher than elsewhere. However, overall it seems that residents of the Island are paying only about 60 per cent of what they would pay if they lived on the mainland. Major taxes not imposed are:

- income tax; and
- sales tax (although Norfolk's relatively high Customs Duties mean that they might, to some extent, be performing the same function as sales tax).

Issues in Norfolk Island Government Revenue Raising

51. ***Tax evasion.*** We have some concerns about the systems employed by Norfolk to ensure payment of tax. Mainland governments make a big effort to ensure compliance with their tax laws. For Norfolk, our analysis of the Workers Compensation Levy indicates that, on the basis of amounts paid, the average hours worked would be less than 25 whereas the 1996 Census of Population and Housing indicated that it exceeded 35. The Norfolk Administration confirmed that this tax is levied on an honesty basis; there are no checks on whether employees are working more hours than claimed. It appears that some Norfolk employers are evading their liability. We do not know the extent of evasion of other taxes, but this is not the only case where the honesty system applies.

52. ***Mobility of tax bases.*** One of the difficulties for the Norfolk Island Government is the mobility of the population and its resources. Governments normally consider the mobility of tax bases when setting their tax rates. Some Norfolk Island taxes may be more mobile than their mainland counterparts. Financial Institutions Levy (FIL) seems to be an example in that modern communication and banking methods have enabled Norfolk businesses to bank outside the Territory. A 37 per cent fall in the level of transactions liable to pay the Island's FIL accompanied a four fold increase (to one per cent) in the levy in 1990. Experience with the Island's FIL indicates that taxpayers can adjust quickly to a tax change.

53. Table 7-12 provides a comparison of transactions liable for the FIL and importation of goods for the period 1989-90 to 1995-96. Imports are used as an indicator of economic activity because of the lack of other information. The table shows that, while imports fell by 14 per cent at one stage, by the end of 1995-96 they were 1 per cent above their 1989-90 level. The FIL tax base, however, was still over 30 per cent lower. As it seems that economic activity has not declined, most of the decline in the FIL tax base must be assumed to be due to tax minimisation.

Table 7-12 COMPARISON OF TRANSACTIONS LIABLE FOR THE FINANCIAL TRANSACTIONS LEVY AND IMPORTS OF GOODS

	1989-90	1990-91	1991-92	1992-93	1993-94	1994-95	1995-96
FIL levy (%)	0.25	1.00	1.00	1.00	1.00	1.00	1.00
FIL revenue raised (\$m)	0.3	1.2	1.1	0.9	0.8	0.8	0.9
FIL tax base (\$m)	129.3	116.4	109.3	91.3	83.3	81.3	89.1
Imports of goods (\$m)	24.4	25.9	24.4	21.0	20.9	24.8	24.6
Ratio of FIL tax base to imports	5.30	4.50	4.48	4.34	3.98	3.28	3.61

Source: Norfolk Island Government Submission, April 1997, pages 66 and 67. Import figures from Access Economics, *Norfolk Island: Recent Economic Performance, Present Situation and Future economic Viability. Is There A Case For Change?*, Canberra, March, p36.

54. Had the ratio of the FIL tax base to imports not declined, then the level of transactions liable to pay the FIL would have been over \$130 million rather than \$89.1 million, and the increased revenue to the government would have been about \$400 000 (or \$225 per capita). Access Economics estimated a level of taxable transactions of \$154.9 million after allowing for inflation. This would have led to an increase in government revenue of about \$650 000. Again their estimate is higher than the ours, but on any reckoning, it is obvious that there is much tax minimisation by Island residents. Given the extent of the FIL minimisation, it would be naive to believe that other taxes were not being minimised or avoided.

55. Taxes that are based on the usual place of residence of the taxpayer are usually the least mobile. Taxes on tourists are also immobile. In our view, the least mobile of the Norfolk Island tax bases are those relating to taxes on:

- inputs (such as Customs Duty, Workers Compensation Levy, Fuel Levy and motor vehicle registrations);
- individuals (such as the Healthcare Levy and Motor Vehicle Licences);
- the value of residential and commercial land; and
- tourists (such as Landing Fees, the Departure Tax and the Accommodation Levy).

56. We suggest that the Norfolk Island Government should look closely at tax mobility issues when any future restructure of the Norfolk taxation system is being considered. This would apply to any expenditure or Goods and Services Tax (GST). Given what happened when the FIL was increased, it is important to take into account the likelihood of sections of the community avoiding a GST by directing their discretionary spending off Norfolk.

57. **Choosing a tax regime.** Compared to the mainland, Norfolk Island has a lower revenue performance, due largely to the narrower range of taxes imposed on the Island. We have not recommended the introduction of specific taxes or specific increases in existing tax rates. These are matters for governments to decide. However, given the unusually wide range of revenue powers available to the Norfolk Island Government a number of observations can be made.

58. The Norfolk Island Government's reliance on narrowly based indirect taxes and GBE income means that its revenue growth is dependent upon increased expenditure, particularly by tourists. This leaves the Government, as well as the economy, vulnerable to the tourist sector. Thus, in a tourist driven economic decline, the Government might not have the resources to carry out its functions at present levels. A broadening of the Government's tax base would reduce its reliance on the tourist industry.

59. The Norfolk Island Government could broaden its tax base by increasing its taxation of income and/or wealth. The earlier analysis in this chapter showed that mainland governments raised 54 per cent of their revenue from taxes on income and wealth, whereas the Norfolk Island Government raised only 4 per cent from these sources.

60. **Income.** One submission suggested that the low level of wages on the Island meant that the community could not pay income tax. Of course, income tax applies to all forms of personal income, not just wages and salaries, and generally company income as well. Our estimates in Chapter 4 of wages and salaries per capita and gross profit per capita for Norfolk suggested that these were, in fact, higher than for the mainland.

61. Whether someone would be better or worse off if income tax were introduced on Norfolk would depend on:

- the extent to which wages and salaries levels were increased to compensate;
- the definition of income and the tax scale chosen; and
- how the Norfolk Island Government used the additional revenues.

For example, assuming that the overall tax collected stayed the same, the introduction of a progressive income tax to replace the Customs Duty would result in many people on Norfolk paying less tax. Those on higher incomes would probably pay more, resulting in a more equitable distribution of the tax burden.

62. **Wealth.** If the Norfolk Island Government were to extend its taxation to wealth, it could most readily do so by imposing municipal rates or land taxes similar to those imposed on the mainland. Table 7-13 shows the estimated value of residential and commercial land on the Island. These estimates are based on valuations of crown leasehold land. Table 7-13 also shows the tax payable if a tax of 2 per cent were levied on the estimated value of residential land (the same rate as the Absentee Landowners Levy) and a tax of 5 per cent were levied on the estimated value of commercial land. Land is immobile and land tax cannot be avoided.

Table 7-13 ESTIMATED VALUE OF LAND

Type of land	Estimated value of land	Tax payable ^(a)
	\$'000s	\$'000s
Residential	14 722	294
Commercial	4 996	250
Total	19 718	544

(a) Assuming tax levied at 2 per cent of estimated value of residential land and at 5 per cent of estimated value of commercial land.

63. In 1995-96, the Norfolk Island Government raised \$58 571 from its Absentee Landowners Levy. This is about 11 per cent of the estimate of tax payable shown in Table 7-13.

64. This discussion has shown that there is some capacity for the Norfolk Island Government to tax income and wealth on the Island. The existence of this capacity underlies our conclusion that the Norfolk Island Government has a lower relative revenue performance compared with mainland Governments. Nevertheless, the choice of tax mix and tax rates remain matters for governments to decide.

SUMMARY

65. Norfolk has considerable untapped revenue sources that the Government could access, if it wished, to provide better services and infrastructure to its constituency. The main reason for its low revenue performance is the narrower range of taxes and charges imposed on the Island; a number of tax bases are not used at all.

66. In the areas that the Norfolk Island Government does tax, its tax rates are high and indicate a revenue raising effort more than twice that found on the mainland. With very limited taxation of income and wealth, its tax regime is regressive.

67. In total, Norfolk Island is estimated to have a per capita revenue raising capacity close to 40 per cent higher than the mainland. This means that the Norfolk Government could raise over 60 per cent more revenue than it actually does.