



COMMONWEALTH GRANTS COMMISSION

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THE PAYROLL TAX ASSESSMENT

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INTRODUCTION

1. This paper addresses the issues related to Payroll Tax raised by the States in their submissions for the 2004 Review. It also presents a proposal for a simplification of the assessment, which has little effect on the existing equalisation outcome.

DESCRIPTION OF THE CATEGORY

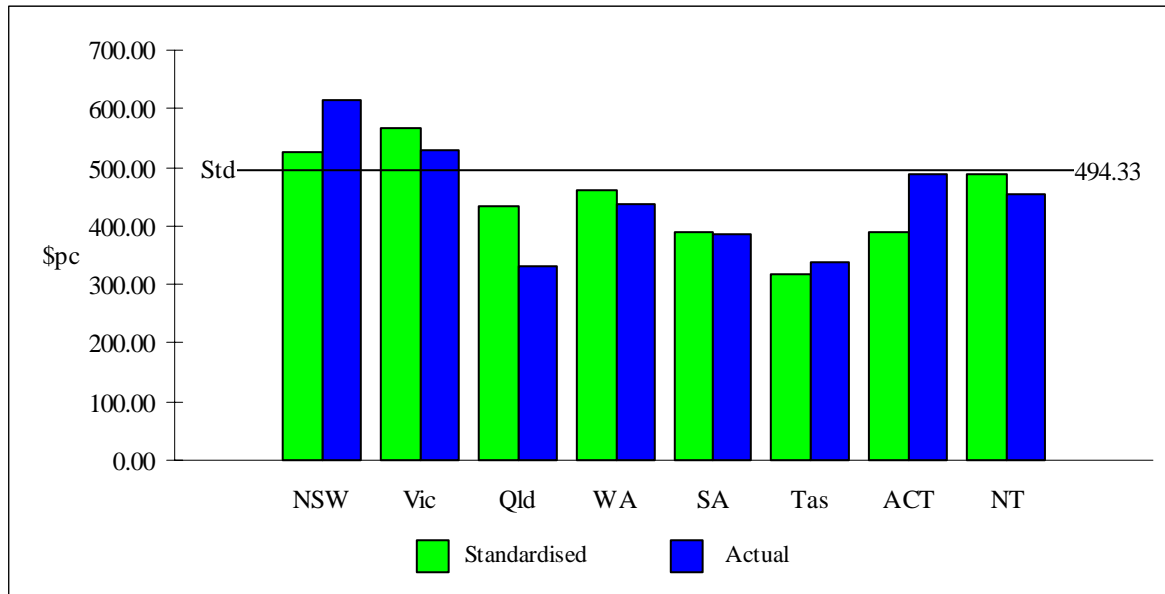
2. This category covers taxes levied on employer's payrolls. Payroll taxes paid by State general government sector agencies are excluded from the category, but payroll taxes collected from public trading enterprises (other than housing authorities which the Commission treats as welfare agencies)¹ are included. The Commission does not propose to change the coverage of the category for the 2004 Review.

CURRENT ASSESSMENT

3. Payroll tax is the largest State tax, with total collections of \$9526 million (an average of \$494.33 per capita) in 2000-01. This represented 20 per cent of State own-source revenue. In the 2002 Update, the payroll tax assessments redistributed \$504.5 million compared with an equal per capita distribution. Figure 1 summarises the 2000-01 assessments from the 2002 Update.

¹ The ABS uses the term Public Trading Enterprises (PTEs) to include public trading enterprises and public financial enterprises.

Figure 1 PAYROLL TAX: STANDARDISED, ACTUAL AND STANDARD REVENUES PER CAPITA, 2000-01



CURRENT METHOD OF ASSESSMENT

4. The revenue base is an estimate of the payrolls that would be subject to payroll tax under the standard tax policy. The estimate starts with data on Compensation of Employees (CE) for each State as published by the ABS. To better reflect what States actually tax, adjustments are made to exclude compensation to:

- (i) employees of small businesses — because all States exempt small businesses from the tax;
- (ii) employees of State general government sector — to ensure that State decisions on the size of their public service do not affect the assessments²;
- (iii) Commonwealth employees and members of the defence forces — because States cannot tax those wages; and
- (iv) employees of embassies and consulates — because States cannot tax those wages.

5. Payroll tax is levied on a progressive basis in all States. This gives States where an above average proportion of the total payroll is paid by large firms a greater capacity to raise revenue than States with relatively more small businesses. The assessment

² The payroll tax actually paid on these wages is also excluded from the expenditure standards used in assessing the relative costs of providing services.

therefore includes an adjustment for differences between States in the size distribution of their employers' payrolls.

6. The data used in the calculations come from several sources.
 - Data on compensation of employees come from the State National Accounts prepared by ABS.
 - Data required to exclude small businesses and general government agencies come from the ABS gross earnings collections.
 - Data for the size distribution adjustment are extracted from samples of taxpayers taken by each State revenue office.

MAJOR DEVELOPMENTS SINCE THE 1999 REVIEW

7. While there have been no major changes in State policies relating to payroll tax since the 1999 Review, States have generally moved to:

- (i) reduce the rate of tax;
- (ii) increase the exemption limit for small businesses; and
- (iii) broaden the tax base by including employee benefits other than wages, such as superannuation and fringe benefits.

MAJOR ISSUES RAISED IN STATE SUBMISSIONS

8. Victoria argued that the measure of the revenue base should be changed to a sub-global measure that is not affected by State policies on the minimum payrolls subject to the tax or tax rates. South Australia proposed refinements to the adjustment that excludes payrolls of small businesses. The Northern Territory suggested changes were necessary to the adjustment that allow for interstate differences in the size of employers' payrolls.

The Measure of the Revenue Base

9. Victoria argues that:
 - while all States apply a similar definition of the base, they have different tax rates and thresholds;
 - the actual wages paid in a State and the structure of businesses are sensitive to the payroll tax provisions — in particular, higher threshold

values encourage more small businesses and the total value of taxable wages are inversely related to the payroll tax rate; and

- it is not possible to accurately measure the value of taxable wages that would exist in each State if the standard tax policies were applied.

10. It concludes that the best method of excluding the effects of differences in State policy from the assessment is to measure the revenue base by using broad economic indicators, such as unadjusted Compensation of Employees, Gross Household Disposable Income or State population.

11. However, if the Commission decides to continue the existing approach, Victoria argues that an elasticity adjustment of -1 should be included in the revenue base measure to allow for the impact on wages of the difference between the actual tax rate in a State and the standard rate the Commission's assessments assume is applied.

The Threshold Adjustment

12. South Australia submitted that the Commission's approach of defining small businesses who are exempt from payroll tax as those with less than 20 employees is an inadequate proxy for the standard payroll-tax-threshold. It notes that since the tax legislation of all States defines the threshold in terms of dollars, the Commission's approach overstates the revenue base of States with below average wages and understates the base of States with above average wages. It proposes that the Commission discontinue the threshold adjustment or increase the firm size used for States such as Tasmania, South Australia and Queensland where wage levels are below the average.

Value Distribution Adjustment

13. The Northern Territory highlights potential problems with the wages data used in the value distribution adjustment. It notes that some States are shown as having taxable employers with payrolls below their threshold level. It considers that the adjustment produced using those data could be biased.

ISSUES TO BE ADDRESSED

The Revenue Base Measure

14. Except for Victoria, which proposed the use of sub-global measures of the revenue base, the States generally accept the thrust of the existing approach³.

15. The existing approach to measuring the payroll tax base:

- (i) reflects the tax base that States actually tax;
- (ii) can be adjusted to reflect the common features of the payroll tax policies of all States, that is to exempt small businesses and to impose progressive rates of tax (although Victoria implies this is affected by State policies);
- (iii) allows adjustments for those policies to be made using data that are reasonably robust (but the existing approaches can be improved).

16. A change to a sub-global measure of the revenue base, such as unadjusted Compensation of Employees, would mean that differences between States in the distribution of business by size would not be reflected in the assessment of relative revenue raising capacity. However, since all States exempt small businesses, such differences do affect their relative capacities to raise revenue. It is noted that using unadjusted Compensation of Employees as the revenue base would also mean that the payrolls of general government agencies would be included in the base. This would imply that the effects of State expenditure disabilities would affect the revenue base⁴.

17. A change to a sub-global measure of the revenue base may be desirable if it resolved general issues which may affect some revenue assessments, including payroll tax. Those general issues include:

- (i) whether there are differences between the States in policies on economic development and other matters that affect the relative size of their revenue bases; and
- (ii) whether revenue bases are sensitive to the level of tax imposed (that is, whether there should be elasticity adjustments).

³ New South Wales has noted that its preference is for one global assessment covering all revenue sources. While it has made arguments about its second best approach to measuring revenue bases in some categories, it has not commented on the payroll tax assessment.

⁴ States with higher (or lower) numbers of employees arising from, say, the above (or below) average number of Indigenous people in their populations would be assessed to have a higher (or lower) revenue capacity. Under the current approach this issue is avoided because the payrolls of general government agencies are excluded from the revenue base and payroll tax paid by general government agencies is excluded from the standard revenues.

18. However, those issues are unlikely to be resolved by a change to a sub-global base for payroll tax.

- (i) If State development policies affect narrowly defined revenue bases, such as the payrolls of medium and large businesses, they would also affect the broader measures of economic activity, which in part reflect employment or income.
- (ii) Similarly, if employment levels and hence business payrolls are affected by the rate of payroll tax, so would broader measures such as household disposable income, which largely reflect income of employees.

19. It is also noted that a move from the existing measure of the revenue base to sub-global measures would result in large changes to State grants, as shown in Table 1.

Table 1 GRANT CHANGES FROM U2002 UPDATE RESULTS IF SUB-GLOBAL MEASURES WERE ADOPTED

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Aust
	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m
Gross Household Disposable Income	51.8	203.5	-29.1	-20.3	-70.6	-29.9	-88.5	-17.0	255.3
Gross State Product	51.8	219.7	13.4	-141.8	-29.0	-12.1	-74.2	-27.7	284.9
Compensation of Employees	22.6	194.4	-4.8	-8.5	-30.9	-14.8	-127.2	-30.8	217.0
State Population	234.5	270.4	-203.7	-33.7	-141.8	-71.9	-40.1	-13.7	504.9

20. The Commission proposes to continue measuring the payroll tax revenue base in terms of an estimate of payrolls subject to tax because:

- (i) it reflects what States do in terms of what they tax and the general exemptions they provide; and
- (ii) while it requires some estimates to be made and there are some technical measurement issues, on the whole the measures are robust and can be improved.

Responsiveness of the Revenue Base to the Tax Rate

21. Victoria has argued that the size of the payroll tax revenue base is sensitive to the size of the small business exemption and the tax rate.

- (i) It provided data that compared the growth in payrolls for businesses with less than 20 employees and more than 20 employees in New South Wales and Victoria. The data indicated that growth in total employment was similar in the two States, but in New South Wales payrolls of small businesses grew faster than those of larger business while in Victoria growth of small and large businesses was much the

same. Victoria concluded that the data supported its assertion that the policy choices of New South Wales to have a high tax rate and a high threshold are encouraging faster growth of payroll tax exempt businesses and are distorting the Commission's assessments.

- (ii) It said that the States with the highest payroll tax rates (Tasmania, the ACT and the Northern Territory) are the ones that the Commission assessed to have the weakest growth in capacity⁵. Victoria submitted that, if the Commission does not use a sub-global measure of the revenue base, the assessments should include elasticity adjustments of –1, based on its short run results using the Monash University's Multi-Regional Forecasting (MMRF) model. It argued that such adjustments should ensure that the estimated value of taxable payrolls in each State reflects what it would have been if the standard tax rates had applied.

22. Whether the Commission should introduce an adjustment into its assessments for any such elasticity effect depends in part on:

- (i) the size of the differences between the actual tax rates in each State and the standard tax rate applied in the assessments; and
- (ii) the sensitivity of employment and payrolls to the tax rate.

23. Table 2 shows the main features of the tax in each State (the exemption level and the maximum tax rate) for 2000-01 and compares them with the standard rates applied in the assessments for the 2002 Update. The differences in the maximum tax rate between States are not as significant as the differences in the exemption threshold.

Table 2 ACTUAL PAYROLL TAX RATES AND STANDARD RATE APPLIED IN 2000-01 (FOR THE 2002 UPDATE)

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT Standard ^(a)	
Exemption level – annual payroll (\$'000)	600	515	850	675	456	1000	1250	600	640
Maximum payroll tax rate, %	6.2	5.45	4.8	5.56	5.67	6.3	6.85	6.6	5.69
Difference from average	0.51	-0.24	-0.89	-0.13	0.02	0.61	1.16	0.91	
Effective tax rate, %	6.07	4.86	3.96	4.94	5.17	5.57	6.53	4.84	5.20
Difference from standard	0.87	-0.34	-1.24	-0.26	-0.03	0.37	1.33	-0.36	

(a) Weighted averages, with each State's policy weighted according to the contribution its payrolls make to the Australian total.

⁵ Analysis of growth rates depends on the years covered, especially in cases where there may be year to year fluctuations in economic activity. The conclusions in the Victorian submission were based on consideration of data on movements over the years 1994-95 to 1999-2000 from the Commission's 2001 Update. If data on movements over the years 1996-97 to 2000-01 from the 2002 Update had been used a different conclusion may have been reached. Over those years, Victoria's capacity rose from 109.46 to 114.56 per cent but the capacity of the ACT rose from 69.53 to 78.52 per cent and that of the Northern Territory rose from 85.15 to 98.50 per cent. The capacity of Tasmania fell from 68.97 to 64.04 per cent.

24. *Sensitivity of employment and payrolls to the tax rate.* Many State governments are reducing the severity of payroll tax (by increasing threshold levels, reducing the tax rates or both) and justifying their action on the basis that it will stimulate employment. This suggests they generally believe that payroll tax rates have an effect on employment levels. While this view is supported by some people, especially employers, few empirical studies have been presented to measure the effects. Victoria's modelling is useful but it would be of more value if it were validated empirically using historical data for all States. Similarly, the different growth rates of the payrolls of small and large businesses in New South Wales and Victoria may be due to a range of influences other than the differences in the State policies on small business thresholds and tax rates⁶.

25. Commission staff have contacted a number of organisations seeking information but only the Victorian Employers' Chamber of Commerce and Industry (VECCI) has supplied data (derived from a survey conducted for its submission to the Harvey Review). VECCI's survey of its 7500 members indicated that most of them considered that payroll tax was the most important area for State tax relief aimed at improving individual business competitiveness. The VECCI concluded that payroll tax has a detrimental effect on key business performance indicators such as investment, profitability, and employment. However, it did not present any empirical evidence on the magnitude of those effects.

26. Conceptually, payroll tax and some other State taxes could have an impact on investment and employment. However, at this stage there is no strong empirical evidence to support an elasticity adjustment to payroll tax bases that is both material and robust. The Commission, therefore, is not inclined to introduce an elasticity adjustment into the payroll tax assessment. This position will be reviewed in the light of any empirical evidence States provide.

The Threshold Adjustment

27. All States exempt small businesses (defined by the size of their annual payroll) from payroll tax, but the threshold level differs from State to State. An adjustment to reflect this common policy is included in the assessments. Table 3 shows for each State the exemption level that applied on 1 July 2001 (in terms of payroll size), average weekly earnings and the threshold level converted to implied employee numbers⁷. The table also shows the standard threshold level used in the Commission's assessments.

⁶ The data Victoria provided (see Table 61 of Victoria Department of Treasury and Finance, *Major Submission to Commonwealth Grants Commission 2004 Review of State Revenue Sharing Relativities*, April 2002, Volume 1, p247) indicate that the rate of growth in payrolls of small business has increased in both States over the period 1997 to 2001, with a similar growth rate in both States in 2001. However, neither State varied its exemption limits over that period and the limits in both States are below the average limit applied by the Commission.

⁷ Assuming all employees are paid the average weekly earnings.

Table 3 PAYROLL TAX THRESHOLDS AND AVERAGE WEEKLY EARNINGS
– 1 JULY 2001

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Aust
Exemption level (threshold) – annual payroll (\$'000)	600	515	850	675	456	1 000	1 250	600	640 ^(a)
Average weekly earnings (\$)	703.5	644.1	636.2	638.9	628.9	576.6	758	679	658.1
Implied exemption level (no. of employees) using:									
Australia average threshold	17	19	19	19	20	21	16	18	20
State's actual threshold	17	16	26	21	14	34	32	17	19

(a) Weighted averages, with each State's policy weighted according to the contribution its payrolls make to the Australian total.

28. Table 3 shows that there are substantial differences among the States in the size of the tax-free threshold they apply. Under the Commission's usual assessment approach of basing its standards on a weighted average of State policies, the standard threshold would be about \$640 000. However, data for all employers classified by the size of their annual payrolls are not available. The only readily available source of data that classify employers by size is the ABS *Wage and Salary Earners* publication, which provides details of employers dissected by number of employees. Even those data are collected for only three size ranges (employers with 0 to 19 employees, 20 to 99 employees and 100 or more employees). The threshold closest to the States tax policy is less than 20 employees. Thus the Commission assessments do not precisely reflect the average State policy — they are the closest practical proxy.

29. However, this assessment approach mixes data expressed in two different units — gross earnings expressed in dollars and small businesses expressed in terms of employee numbers. Conceptually, this is undesirable and it introduces the problem that South Australia raises in its submission. That is, because average wages differ among States, the annual payrolls excluded from the assessments are higher in States such as New South Wales, the Northern Territory and the ACT where average earnings are higher, and lower in States like South Australia and Tasmania which have relatively low average earnings.

30. Conceptually, the assessments should use a different threshold in each State to reflect the differences in average earnings. However, data to support such a refinement are not available. Nor is it obvious how estimates of a possible refinement or its impact on the assessments might be made⁸.

31. The question then becomes whether a greater degree of equalisation is achieved by including a small businesses adjustment based on the existing proxy measure, or by excluding the adjustment altogether.

⁸ Simple proportional adjustments based on differences in average weekly earnings would introduce further judgement into the assessment because they would require additional assumptions about the variable to be estimated - the distribution of employers by size.

32. Table 4 shows for 2000-01 and for each State, the gross earnings of the private and PTE sector in each State, gross earnings of employers with less than 20 employees (excluding branch offices), the implied taxable gross earnings and taxable earnings as a proportion of total gross earnings.

Table 4 GROSS EARNINGS - 2000-01

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Aust
	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m
Gross earnings – private and PTE sectors	75 158	60 251	35 209	21 510	13 401	3 475	2 933	2 174	214 111
Gross earnings – employers with less than 20 employees	22 007	15 901	9 936	6 958	3 769	1 037	1 043	559	61 210
Taxable gross earnings	53 151	44 350	25 273	14 552	9 632	2 438	1 891	1 615	152 901
Taxable earnings as proportion of total gross earnings	0.71	0.74	0.72	0.68	0.72	0.70	0.64	0.74	0.71

Source: ABS *Wage and Salary Earners*, Product No. 6248.0, various quarters

33. Table 4 indicates that there are noticeable differences between the States in the proportion of gross earnings that would be subject to payroll tax under a uniform small businesses exemption policy. The difference between the highest and the lowest is about 14 per cent of the average. This is much higher than the difference implied by the average earnings (7.5 per cent derived by multiplying 5/20, the difference in threshold number of employees, and 30 per cent of average small businesses). This suggests that to remove the threshold adjustment would result a noticeable impact on the assessed State grants.

34. Table 5 indicates that deleting the small businesses adjustment from the assessments would have a noticeable impact on estimated State grants.

35. While the effect on each State's total notional FAG grant is small in percentage terms, the small businesses adjustment has a large impact on the payroll tax assessment and its contribution to the extent of redistribution from an EPC distribution⁹. It is not possible to predict the effect on the assessments of refining the small employer allowance as suggested by South Australia, but it is surmised that they would be small.

⁹ In the case of Western Australia, an assessment excluding the adjustment would imply that it had an above standard capacity to raise payroll tax.

Table 5 EFFECT ON 2002 UPDATE NOTIONAL FAG GRANTS OF DELETING SMALL BUSINESSES ADJUSTMENT

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Aust
	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m
Notional State grants									
2002 Update	7334.3	5257.1	4938.1	2314.8	2523.0	1067.7	491.2	1358.3	25284.6
Deleting small business adjustment	7308.2	5344.9	4921.8	2279.7	2532.3	1061.3	482.8	1353.5	25284.6
Grant Change	-26.1	87.9	-16.3	-35.2	9.2	-6.3	-8.4	-4.8	97.1
Grant Change	%	-0.4	1.7	-0.3	-1.5	0.4	-0.6	-1.7	-0.4

36. Overall, the Commission is inclined to the view that the inclusion of the small employer adjustment in the assessments improves equalisation, because it reflects the tax policies all States apply. Refinements to the adjustment that would address the issue raised by South Australia do not appear feasible.

Value Distribution Adjustment

37. Payroll tax is effectively levied on a progressive basis in all States. This means that differences between States in the value distribution of payrolls affects their relative capacities to raise payroll tax revenues. The Commission currently includes a value distribution adjustment in the assessments to allow for those effects. The data used to make this adjustment are obtained from samples of employers' payroll tax returns provided by each State revenue office.

38. The Northern Territory has noted that these adjustments could be miscalculated because the sample data for some States indicates that employers with payrolls of less than \$500 000 paid tax when the State exempts employers of that size from tax. This observation suggests that some data may be classified to incorrect value ranges¹⁰. Commission staff will discuss the data with the relevant States and appropriate adjustments will be made to the calculations, if necessary.

39. ***Data on Public Trading and Financial Enterprises (PTEs)***. To improve the accuracy of the assessments, aggregate gross earnings of employees of all public trading enterprises and public financial enterprises will be sought from the ABS. At present the assessments exclude data for PTEs in industries where the public sector is a minor player.

¹⁰ It is also possible that the data in question relate to payrolls of branch offices or employers who did not operate for the whole year. Such employers should be classified to value ranges on the basis of their Australia-wide total payrolls or their annual equivalent payroll, respectively.

SIMPLIFYING THE PAYROLL TAX ASSESSMENT

40. The Commission has previously indicated that it would attempt to simplify assessments in the 2004 Review if that could be achieved without major effects on the outcome or if it produced more robust assessments. The States also have often noted the complexity of the Commission's assessments and generally support simplification.

41. The following represents a proposal for a modest simplification of the payroll tax assessment that produces results similar to the current ones and is also:

- arithmetically simpler;
- less error prone; and
- easier to understand (more transparent).

The Current Assessment Framework

42. In the existing assessment, the revenue base is the estimated value of payrolls subject to tax (using ABS data on Compensation of Employees), adjusted:

- to exclude the Commonwealth Government and State general government sectors — this is done using ABS data on Gross Earnings to calculate the share of private sector businesses plus public trading enterprises in total gross earnings;
- to exclude small businesses — this is done using ABS data on Gross Earnings to calculate the share of private sector units with less than 20 employees in the total gross earnings of the private sector plus public trading enterprise; and
- to reflect interstate differences in the distribution of taxable payrolls by size of employer, using sample data supplied by the States.

43. There are problems with this assessment. It starts with data on Compensation of Employees from State national accounts. Those data match well with the legal tax base (because they include cash payments, fringe benefits and employer's superannuation contributions), but the data required for the adjustments listed above cannot be obtained from the same source. That data comes from two other sources (ABS Gross Earnings data and State Revenue Office sample payroll and receipts data). The differences in the scope of each data set mean numerous estimated adjustments are necessary. Mixing data from different sources is undesirable and each adjustment introduces a potential for error.

The Simplified Assessment Framework

44. A simpler assessment could be made by using ABS gross earnings data as the starting point (instead of Compensation of Employees). This approach would have a practical advantage in that the number of arithmetical computations in the assessments could be reduced by over one-third because gross earnings data:

- are simpler to work with;
- are available by sector (permitting the easy exclusion of Commonwealth and general government earnings and the inclusion of earnings of employees of all public trading and financial enterprises); and
- avoid the requirement for adjustments to exclude earnings of defence personnel and embassy employees.

45. The small businesses adjustment would continue to be made using the existing methods. Under the proposal, this adjustment would be based on the gross earnings data used for the main revenue base. However, the issue raised by South Australia would not be overcome. The value distribution adjustment would also be continued using existing processes.

46. Table 6 indicates that use of the simplified approach instead of the existing approach in the 2002 Update would have had little effect on the implied FAG grant distribution. However, the tables in Attachment A show that the small effect of the simplified approach appears to be due to averaging of the results of separate calculations for the five years of the assessment period. (That is, on a single year basis, the differences between the results of the two approaches are larger, but they tended to go in different directions across the five years of the assessment period.)

Table 6 IMPACT OF SIMPLIFIED PAYROLL TAX ASSESSMENT ON IMPLIED STATE GRANTS

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Aust
	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m
2002 Update	7334.3	5257.1	4938.1	2314.8	2523.0	1067.7	491.2	1358.3	25284.6
Simplified Option	7340.9	5259.1	4929.5	2305.4	2531.3	1064.7	493.9	1359.7	25284.6
Grant change	\$m								
	6.6	2.1	-8.6	-9.4	8.3	-3.0	2.7	1.4	21.0
	%								
	0.09	0.04	-0.17	-0.41	0.33	-0.28	0.55	0.10	

47. The main deficiency of the simplified assessment is that the proposed underlying measure of the revenue base (gross earnings) excludes fringe benefits and employer’s superannuation benefits which are subject to payroll tax in all States. Those benefits and payments are included in the current assessment — because the compensation of employees data includes them. However, the conceptual benefits of the current assessment may be more apparent than real because the limitations of the data on compensation of employees mean that many of the adjustments included in the assessments are based on gross earnings data.

48. The differences between the simplified assessment and the current assessment can be understood by looking at the underlying assumptions.

- (i) The current assessment implicitly assumes that for each State, gross earnings represents the same proportion of compensation of employees for:
- the general government sector and the private sector (including public trading enterprises); and
 - small and large businesses within the private sector.
- (ii) The simplified assessment implicitly assumes that gross earnings as a proportion of total compensation of employees for the private sector (including public trading enterprises) is the same for all States.

49. Neither assumption is correct and there is no prior knowledge to judge which assumption would have the lesser effect on the assessments.

50. Table 7 shows the average relationship between gross earnings and total compensation of employees across the five years 1996-97 to 2000-01. The table indicates that there are differences between States in the extent to which fringe benefits are a feature of remuneration. However, it also indicates that those differences are not large.

Table 7 GROSS EARNINGS AS A PROPORTION OF COMPENSATION OF EMPLOYEES (GE/CE excluding CE of defence and embassies)

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Aust
	%	%	%	%	%	%	%	%	%
Average 1996-97 to 2000-01	84	84	85	86	84	87	82	83	84

Summary

51. The revenue base measure used in the current assessment seems to better match what States tax than the base in the simplified approach. However, data limitations mean that in practice the advantage is not clear — both approaches involve doubtful assumptions.

52. The current and the simplified assessments produce very similar results over the five assessment years of the 2002 Update.

53. The simplified assessment would be more robust because it significantly reduces the number of computations involved in the assessment.

54. At this stage, the practical advantages of the simplified approach seem to outweigh any conceptual shortcomings.

ATTACHMENT A

Comparisons of Simplified and Actual Approaches to the Payroll Tax Assessment

1. Table A-1 shows, for each year in the 2002 Update assessment period, the difference between standardised revenue assessed using the existing approach to the payroll tax assessment and that assessed using the simplified approach. Table A-2 shows the results expressed in percentage terms (with standardised revenue assessed by the existing approach as the base).

2. The tables indicate that the size of the difference varies from year to year and that the direction of the difference varies across the years. However, the differences are not usually large in percentage terms.

Table A-1 DIFFERENCES IN STANDARDISED REVENUE

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT
	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m
1996-97	33.9	-8.80	-21.5	6.3	-12.8	6.7	-2.6	-1.4
1997-98	83.8	-22.8	-36.6	-4.8	-15.9	3.4	-4.1	-3.0
1998-99	42.1	-46.4	13.1	5.8	-6.9	-1.0	-2.3	-6.4
1999-2000	-66.6	12.3	50.3	4.8	-2.4	2.8	-2.4	1.6
2000-01	-142.1	63.2	41.1	31.6	1.4	1.8	-0.7	3.7
Average	-9.8	-0.4	9.3	8.7	-7.3	2.7	-2.4	-1.1

Table A-2 DIFFERENCE IN STANDARDISED REVENUE - PERCENTAGE

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT
	%	%	%	%	%	%	%	%
1996-97	1.2	-0.4	-1.7	0.9	-2.4	5.0	-2.9	-2.2
1997-98	2.8	-1.1	-2.8	-0.6	-3.1	2.3	-4.5	-4.4
1998-99	1.4	-2.0	1.0	0.7	-1.3	-0.7	-2.1	-8.8
1999-2000	-2.1	0.5	3.4	0.6	-0.4	1.9	-2.3	2.3
2000-01	-4.2	2.3	2.6	3.6	0.2	1.2	-0.6	3.8
Average	-0.2	-0.1	0.5	1.0	-1.4	1.9	-2.5	-1.9

3. Some of the year to year variation in the size of the difference is related to variations in gross earnings as a proportion of compensation of employees. Table A-3 shows these proportions for each assessment year. For example, the falls in the proportion for New South Wales in 1999-2000 and again in 2000-01 appear to be a major reason for the change in sign of the difference in standardised revenue produced by the two assessment approaches and the increasing size of the difference, as shown in Table A-1. Commission staff will discuss with the ABS possible reasons for the changes in gross earnings as a proportion of compensation of employees in 1999-2000 and 2000-01 for New South Wales and the Northern Territory.

Table A-3 GROSS EARNINGS AS A PROPORTION OF COMPENSATION OF EMPLOYEES (GE/CE excluding CE of defence and embassies)

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Aust
	%	%	%	%	%	%	%	%	%
1996-97	86	84	83	86	83	90	82	83	85
1997-98	87	84	82	84	82	87	81	81	84
1998-99	87	84	86	86	84	86	83	78	85
1999-2000	82	84	87	85	84	87	82	87	84
2000-01	80	86	86	87	84	86	83	88	84
Average	84	84	85	86	84	87	82	83	84