

Senate Standing Committee on Economics

ANSWERS TO QUESTIONS ON NOTICE

Treasury Portfolio

Budget Estimates

1 June – 3 June 2010

Question: BET 388

**Topic: Resource Rent Tax –
Markle & Shackelford Working Paper**

Hansard Page: Written

Senator EGGLESTON asked:

1. *The introduction of a resource rent tax was a major part of the budget and has been the subject of intense public debate. The policy was recommended in the report Australia's Future Tax System. The Revenue Group within Treasury provided support to the review panel (Annual Report, 2007-08, page 64). A particular piece of research has surfaced several times during the tax debate: a working paper by two American academics, Markle and Shackelford, dated June 2009. In the report on the tax system, the results of this paper are reported on page 169 as evidence for the effective tax rates paid by different industries in Australia and other countries. A table reproduces some of the working paper's results. The text says that "for Australia they find the highest effective tax rate is in the financial services and retail trade sectors (27 per cent) and the lowest in the information and mining sectors (14 and 17 per cent respectively)". The report further states that "tax disparities tend, at the margin, to cause resources to move into less-productive investments in tax-favoured industries".*
 - a) I refer to a working paper by two American academics, Markle and Shackelford, dated June 2009 which was the sole source of evidence in the tax review for the effective tax rates paid by different industries in Australia
 - b) Results from Markle and Shackelford were subsequently used in the Treasurer's economic note of 23 May 2010 to claim the effective tax rate for domestic mining companies was 13 per cent and for multinational mining companies in Australia, it is 17 per cent. The Deputy Prime Minister used these numbers in interviews, calling them "cold, hard facts".
 - c) What reviewing of this paper took place before including it in the tax review or providing the information to the Treasurer?
 - d) Did anyone bother to look at the methodology of the paper or the sample size for Australia?
 - e) Why rely on a survey method which was clearly very limited in regard to Australian mining?
 - f) In evidence last week the Secretary of Treasury told this committee that the tax review panel and "some people in Treasury" have been looking "at tax payable as a proportion of economic income rather than taxable income" "for some time" (page E9). Why wasn't work done by Treasury on this question of the effective tax rate, using the up to date data at its command?

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- g) Why has such an important question been addressed using the obviously insubstantial results on Australian mining contained in a draft working paper by two academics?
2. *For its Australian data, the paper uses a sample of financial statements for 1,234 firm-years, of which 96 are from New Zealand (footnote 24). Further, the observations are “firm-years”, that is financial statements for a particular firm in a particular year. The 494 observations for domestic Australian (and New Zealand) firm-years cover 9 years and the 740 observations for multinational Australian (and New Zealand) firm-years cover 20 years (table 3). Finally, there are 10 industry sectors covered in the study. Australian observations are 4.5% of the sample and mining observations are 3.6% of the sample. The number of Australian mining observations was clearly small.*
- a) In the revised version of the paper dated 22 March 2010, the number of Australian mining observations is less than 20. As a result no estimated effective tax rate is provided for Australian mining in table 4. That is, the two numbers – 13% and 17% – are no longer there.
- b) The authors of the working paper have stated that the usefulness of the results for policy “should not be overstated”. The sample “could have been as few as four mining companies”. And “using the table as if it delivered some precise measurement... was not the right thing to do”.
- c) When the new paper, dated 22 March 2010, came out why wasn't it read? Why wasn't the removal of the two figures noted so that the misleading references in the economic note and elsewhere were avoided in May?
- d) Would Treasury agree now that the paper should not have been used for the purpose it was used in the tax review and the Treasurer's economic note?
- e) Do you know of any other papers or analysis that corroborate these results?

Answer:

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(c) The Markle and Shackelford paper was published by the National Bureau of Economic Research (NBER). The NBER is a well regarded research organisation, with eminent members. The NBER has published papers by several Nobel laureates. The AFTS Secretariat reviewed the methodology of the Markle and Shackelford paper and considered the paper a credible international comparison of effective tax rates by industry. The results for Australia in the Markle and Shackelford paper are reflective of tax provisions available for different industries in Australia.

(d) Yes. The AFTS Secretariat and Treasury reviewed the methodology and considered it a credible international comparison of effective tax rates by industry.

(e) Surveys are a legitimate basis for analysis. Treasury's *Economic Roundup* article 'Disparities in average rates of company tax across industries' has similar results for the mining sector to the Markle and Shackelford paper based on publicly available tax

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and income data from the ATO and ABS. In addition, these results are corroborated by data from the Bloomberg Professional service for listed companies for 2006-07.

(f) Treasury's analysis was published in the *Economic Roundup* article 'Disparities in average rates of company tax across industries' on 24 May 2010. The analysis used data up to 2004-05 as it was the most fully enumerated data at the time the article was prepared. Data for more recent years were available from the ATO and the ABS, but was more likely to be subject to revisions (for instance, more recent tax data are likely to be revised for late lodgements and tax amendments). Treasury's analysis was subsequently updated to include data up to 2007-08. The results were published on 3 July 2010 in Treasury's *Economic Roundup* (Issue 2, 2010) and are broadly similar with the previous analysis.

(g) The Markle and Shackelford paper was cited in the AFTS report because the AFTS Secretariat considered the analysis a credible international comparison of effective tax rates by industry. The results in the Markle and Shackelford paper are consistent with tax provisions available to different industries in Australia. The NBER is a well regarded research institution. Treasury considers the authors well regarded in their field, in particular the lead author, Professor Douglas Shackelford, is a Distinguished Professor of Taxation at University of North Carolina's Kenan-Flagler Business School.

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(c) The Treasurer's Economic Note was based on Table B1-2 of the AFTS report which cites the Markle and Shackelford paper. The revised paper was not available at the time the AFTS report was provided to the Government. The results cited in the AFTS report are similar for the mining sector estimates derived by the Treasury using publicly available tax and income data from the ATO and ABS.

(d) See answer 1(g) above.

(e) See answer 1(e) above.