Business Tax Activity 4 Explaining business taxes

Years 11-12

TASK 3
SUPPLY-SIDE POLICIES: TAX REFORMS

Worksheet

Focus: Economics

YOU WILL:

- predict the impact of lowering company tax rates on aggregate supply, the government's macroeconomic goals and living standards
- interpret economic information and diagrams
- investigate a supply-side tax reform and use a cost-benefit approach to assess its effectiveness
- explain trade-offs associated with macroeconomic goals

YOU WILL NEED:

- *Fact sheet: Explaining business taxes*
- Access to the internet

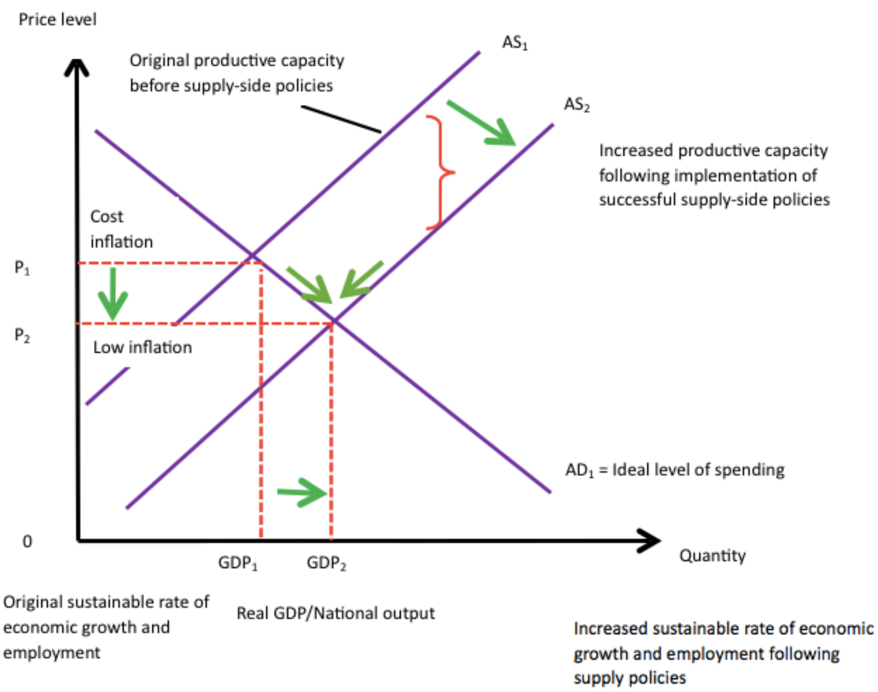
PART 1: CASE STUDY – LOWERING COMPANY TAX

Aggregate supply policies are used by governments to encourage individuals and firms to contribute to increasing national output, especially through improving productive capacity. Greater efficiency in turn helps to improve macroeconomic performance and living standards.

Tax reform is one microeconomic policy used by governments to affect aggregate supply, domestic macroeconomic goals and living standards.

The macroeconomic impacts of successful aggregate supply-side policies can be illustrated using an aggregate demand–supply diagram. A reduction in taxation results in an increase in Australia's productive capacity and shifts the whole aggregate supply to the right (the move from AS1 to AS2). Supply-side measures assist in raising the sustainable rate of economic growth (the shift from GDP1 to GDP2) and employment and lowering prices or cost inflation (the shift from P1 to P2).

Figure 1: Aggregate demand-supply diagram



Various governments have used tax reform as a supply-side measure to improve the productive capacity of Australian firms. One example is the Ten Year Enterprise Tax Plan.

Ten Year Enterprise Tax Plan — reducing the company tax rate to 25 per cent

Revenue ($m)					
	2015-16	2016-17	2017-18	2018-19	2019-20
Australian Taxation Office		-400.0	-500.0	-800.0	-950.0

The Government will reduce the company tax rate to 25 per cent over 10 years.

The tax rate for businesses with an annual aggregated turnover of less than $10.0 million will be 27.5 per cent from the 201617 income year. The threshold will then be progressively increased to ultimately have all companies at 27.5 per cent in the 202324 income year. The annual aggregated turnover thresholds for companies facing a tax rate of 27.5 per cent will be:

- $25.0 million in the 2017-18 income year;
- $50.0 million in the 2018-19 income year;
- $100.0 million in the 2019-20 income year;
- $250.0 million in the 2020-21 income year;
- $500.0 million in the 2021-22 income year; and
- $1 billion in the 2022-23 income year.

In the 2024-25 income year the company tax rate will be reduced to 27 per cent and then be reduced progressively by 1 percentage point per year until it reaches 25 per cent in the 202627 income year. Franking credits will be able to be distributed in line with the rate of tax paid by the company making the distribution.

A more competitive company tax rate will encourage investment, raise productivity, increase GDP and over time raise real wages and living standards.

This measure is expected to have a cost to revenue of $2.7 billion over the forward estimates period.

This measure forms part of the Government's Ten Year Enterprise Tax Plan, which will encourage Australians to work, save and invest.

Source: 2016-17 Budget – Budget Paper No 2, Part 1 Revenue Measures

MAKE PREDICTIONS

Read the excerpt from the 2016-17 Budget and predict the likely impact of this reform on aggregate supply and the government's macroeconomic goals and living standards by completing Table 1.

Table 1: Impact of cutting company tax rates

Aggregate supply	Cost inflation	Economic growth	Employment	Employment

PART 2: TAX REFORM AND TRADE-OFFS

Material and non-material living standards
Material living standards are related to our level of income and the quantity of goods and services we consume.
Non-material living standards relate to our wellbeing, or those factors that affect the quality of our daily lives such as freedom, happiness, quality of family life, justice, amount of leisure time, crime, and the state of the natural environment.

Supply-side policies are designed to improve national output or GDP. While producing and consuming more goods and services (economic growth) can lead to increased material standards of living, it can also lead to sacrificing aspects of our non-material standard of living (such as increased pollution or traffic congestion). There are also longer-term opportunity costs or sacrifices of economic growth, such as threatening the economic prosperity and opportunities of future generations.
Successive Australian governments have introduced a number of policies designed to improve the productive capacity of businesses. For example, aside from lowering company tax, in late 2014, the Australian coalition government abolished the following:

- The carbon tax (initially started at $23 per tonne of CO_2 emissions)
- MRRT: The minerals resource rent tax that was nominally at 30 per cent for coal and iron ore mining companies.

INVESTIGATE

Select one of these supply-side policies or choose another tax reform to investigate. Use the following steps to guide your inquiry:

1 Describe the reasons why supply-side policy you are investigating was introduced.

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2 Gather and evaluate data relevant to the supply-side policy. This data could include primary sources (statistics, surveys) or secondary sources (texts, newspaper articles, internet sources including websites, YouTube).

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3 Analyse the impact or likely impact of the supply-side policy using a cost-benefit approach (including a consideration of trade-offs) in relation to:

- economic growth
- environmental sustainability
- living standards (material and non-material)
- long-term economic prosperity.

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4 Justify your predictions.

Australian Government
Australian Taxation Office