BUSINESS START-UP COMPLIANCE COSTS: POLICY PERSPECTIVES

NTHATI RAMETSE AND JEFF POPE

Nthati Rametse is a doctoral candidate in the Department of Economics at Curtin University. Jeff Pope is an Associate Professor in the Department of Economics at Curtin University.

I Introduction

It is nearly half a decade since the Goods and Services Tax (GST)\(^1\) was introduced in Australia on 1 July 2000. Since then, most of the Australian tax reform issues still continue to be a “political play”. The government presented tax simplification as one of the related objectives of the tax reform. However, much of the concern from businesses, in particular, small business community, was on both GST start-up and recurrent compliance costs. Presently, start-up tax compliance costs of the GST may no longer be an important issue since they are mostly regarded as “sunk costs” that can never be recovered. Moreover, businesses are now focusing on GST recurrent compliance costs. Nonetheless, start-up compliance costs of any taxation system/regulation cannot be ignored as they are important for policy makers. Empirical evidence suggests that overall start-up tax compliance costs are significant and regressive.\(^2\) Furthermore, international findings also indicate that start-up compliance costs represent a significant amount of recurrent compliance costs.\(^3\) The taxation literature on start-up compliance costs is very limited, although non-taxation studies on start-up compliance costs do shed some light on the topic. The major objective of this article is to discuss the possible relationship between start-up compliance costs and recurrent compliance costs of the GST. It also seeks to present an evaluation of the importance of business start-up compliance costs.

The rest of the article is organised in four parts as follows. Section II reviews the terminology and the context of business start-up and recurrent compliance costs. Section III discusses the very limited literature on both the Australian and international business start-up compliance costs. Section IV presents some empirical evidence on start-up tax compliance costs of the GST for small businesses. Furthermore, studies on both GST start-up compliance costs and transitional compliance costs and their relationship to recurrent compliance costs are explored. Section V concludes the article with a focus on policy perspectives.

II Conceptual Issues

A An Overview of Compliance Costs

Compliance costs are those costs incurred by taxpayers, or third parties such as businesses, in meeting the requirement laid upon them in complying with a given tax structure, over and above payment of the tax itself.\(^4\) Similarly, business start-up costs are those costs incurred by businesses in preparing to comply with legislative prescriptions.\(^5\) Compliance costs of business taxation include professional fees, especially accounting and legal fees; “the value of time spent by business

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\(^1\) The Goods and Services Tax (GST) is also known as Value Added Tax (VAT) in other countries.


\(^5\) Tran-Nam, above n 3; J Pope and N Rametse, ‘Small Business and the Goods and Services Tax: Compliance Cost Issues’ (Working Paper, School of Economics and Finance, Curtin University, 2000); Rametse and Pope, above n 2.
taxpayers (including owner/partner/director, paid staff and unpaid helpers\(^6\)) to learn about and become thoroughly familiar with the new tax and its implications";\(^7\) computer hardware and software, and other physical resources.\(^8\)

Two concepts of tax compliance costs are normally distinguished in the literature, namely gross and net compliance costs. Gross compliance costs of particular concern to tax policy makers, represent the total resource cost to the economy before any offsetting benefits to taxpayers are taken into account. These offsets include the tax deductibility of the various costs incurred and the value of any cash flow benefits enjoyed by taxpayers. Cash flow benefits arise from the lawful delay in payment of tax to the tax authorities, and in the delay in remittance of tax revenue collected by them on behalf of the government.\(^9\) Managerial benefits to taxpayers arising from improved accounting procedures, together with tax deductibility, cash grants from government\(^10\) and cash flow benefits may also be an important offset, though for managerial benefit, quantification is very difficult.\(^11\) Thus net compliance costs are the actual or real costs imposed on the business sector after allowing for offsets, and what business focuses upon. A distinction is also made between start-up compliance costs and recurrent (or ongoing annual) costs.

**B Business start-up versus recurrent compliance costs**

Start-up costs are distinct from recurrent (or ongoing annual) costs. Whilst business start-up compliance costs “arise with the introduction of a new tax or a major change in tax”,\(^12\) recurrent costs are continuing costs. Recurrent/regular costs are incurred in running a tax system and do not include temporary costs, which are incurred by the tax officers and taxpayers in learning about the new tax system “over a period extending after a change commences”.\(^13\) Tran-Nam and Glover further clarify that aggregation of start-up costs and temporary costs is necessary because, although the two concepts are theoretically distinct, separating them with precision is very difficult.

Even when a particular tax has been well established to regard the compliance costs as regular/recurrent costs, some businesses will be starting to operate, hence experiencing tax start-up costs as they prepare to comply with the tax legislation for the first time. Thus, within the recurrent costs, there will be elements of start-up costs associated with changes in the taxpayer population.\(^14\) This may occur where either a new business is established or an existing business registers for GST for the first time.

**III INTERNATIONAL AND AUSTRALIAN BUSINESS START-UP COMPLIANCE COST STUDIES**

**A Overview**

To the best of our knowledge, the major start-up compliance cost studies undertaken before the Australian GST implementation date of 1 July, 2000 are two Canadian, one Mauritian, one

\(^{6}\) Tran-Nam, above n 3.


\(^{10}\) Tran-Nam, above n 3.

\(^{11}\) Rametse and Pope, above n 2, 410.

\(^{12}\) Sandford, Godwin and Hardwick, above n 4, 16.

\(^{13}\) Tran-Nam and Glover, above n 7, 502.

Australian and one British. Other United States studies\textsuperscript{15}, although not relevant to start-up tax compliance, are on start-up compliance costs of consumer financial regulations. Studies that are more relevant to start-up tax compliance costs of the GST are the Canadian Federation of Independent Business (CFIB),\textsuperscript{16} the Australian study\textsuperscript{17} and the Mauritian study.\textsuperscript{18} These studies, together with Gunz et al.\textsuperscript{19} (1995a, 1995b) are discussed briefly in this section.

The CFIB\textsuperscript{20} estimated small business GST start-up costs, Clare and Connor's study\textsuperscript{21} was on start-up compliance costs of the superannuation surcharge tax (SST) and Pillai\textsuperscript{22} researched the Mauritian GST start-up costs in the hotel industry. Amongst the various studies conducted by Sandford et al\textsuperscript{23} was the UK VAT recurrent compliance cost. Sandford et al\textsuperscript{24} further outline 33 major compliance costs studies. In Australia, most business start-up compliance cost studies relate to surveys that were undertaken before and after the GST was introduced.\textsuperscript{25}

B International literature on business start-up compliance costs

Research by Rametse and Pope\textsuperscript{26} is a major contribution to the international literature on (any) tax start-up costs, of which there is a surprising dearth of information. The development of Tax Impact Statements in various OECD countries in the 1990s is recognised.\textsuperscript{27} However, their depth in forecasting tax compliance costs is open to criticism, at least in the case of Australia,\textsuperscript{28} which omitted to recognise the regressivity of compliance costs. The Regulatory Impact Statement (RIS) is the early government impact statement that focuses on how the new tax law would impact on the taxpayer compliance costs as far as operating costs are concerned. The RIS\textsuperscript{29} did not provide any breakdown of its aggregate gross compliance cost estimate of $1.9 million for the year 2001-02 by size of business (small, medium and large).

Evans and Walpole researched the extent to which OECD members use taxation impact statements in the development of tax policies and legislation and found that:

\begin{itemize}
  \item \textsuperscript{15} As reviewed by G Elliehausen and BR Lowery, 'The Cost of Implementing Consumer Financial Regulations: An Analysis of Experience with the Truth in Savings Act' (Governors of the Federal Reserve System Staff Studies 170, 1997); available at: http://www.federalreserve.gov.
  \item \textsuperscript{17} R Clare and D Connor, 'The Cost of the Surcharge – more bad news' (ASFA Research Centre, Association of Superannuation Funds of Australia, Sydney, 1998).
  \item \textsuperscript{20} CFIB, above n 16.
  \item \textsuperscript{21} Clare and Connor, above n 17.
  \item \textsuperscript{22} Pillai, above n 18.
  \item \textsuperscript{23} Sandford, Godwin and Hardwick, above n 4.
  \item \textsuperscript{24} Ibid, 224-230.
  \item \textsuperscript{25} These studies are discussed in section III(E).
  \item \textsuperscript{26} Rametse and Pope, above n 2, 407-442.
  \item \textsuperscript{27} C Evans and M Walpole, Compliance Cost Control: A Review of Tax Impact Statements in the OECD (1999). See also AJ Sawyer, ‘Compliance Cost Impact Statements in New Zealand – How far have we come?: Tribute to Cedric Sandford’ (2002) 17(4) Australian Tax Forum 441-494
  \item \textsuperscript{29} Ibid.
\end{itemize}
Despite its commitment to the completion of taxation impacts statements, Australia compares poorly with other OECD countries in certain important respects. There is inadequate quantification of the likely costs of compliance for taxpayers (often inexplicably so), and there is inadequate consultation with business and other stakeholders outside the revenue authorities on the issues of taxpayer compliance costs.\textsuperscript{30}

Thus for any regulation, policy makers must recognise the regressivity of compliance costs. Pope and Rametse\textsuperscript{31} have identified around eleven international start-up compliance costs studies undertaken prior the Australian GST implementation on 1 July 2000, as shown in Table 1. It must be noted that there is a wide variation of the figures from other studies, for example, the United States studies. However, applying the rule of thumb, start-up compliance costs could be equivalent to one year’s recurrent compliance costs.

\textsuperscript{30} Evans and Walpole, above n 27, 7.
\textsuperscript{31} Pope and Rametse, above n 2.
<table>
<thead>
<tr>
<th>Country</th>
<th>Researcher</th>
<th>Regulation Researched</th>
<th>Research Method/Sample size/ Business Researched</th>
<th>Key Findings</th>
</tr>
</thead>
<tbody>
<tr>
<td>Canada</td>
<td>Canadian Federation of Independent Business(^{32})</td>
<td>Canadian start-up compliance costs of the GST.</td>
<td>Survey of 25,362 small businesses.</td>
<td>Start-up costs represented 45 percent of recurrent costs.</td>
</tr>
<tr>
<td>Canada</td>
<td>Gunz, Macnaughton and Wensley(^{33})</td>
<td>Start-up compliance costs of Canadian Research and Development tax incentives.</td>
<td>Survey of 51 companies.</td>
<td>Start-up costs represented 84 percent of recurrent costs.</td>
</tr>
<tr>
<td>Mauritius</td>
<td>Pillai(^{34})</td>
<td>Start-up compliance costs of the GST in the Mauritius hotel industry.</td>
<td>Survey of 82 small and large hotels.</td>
<td>Start-up costs represented 223 percent of recurrent compliance costs.</td>
</tr>
<tr>
<td>Australia</td>
<td>Clare and Connor(^{35})</td>
<td>The Costs of the Superannuation Surcharge Tax (SST).</td>
<td>Survey methodology and estimation analysis not reviewed.</td>
<td>Regressivity of start-up costs of SST.</td>
</tr>
<tr>
<td>Britain</td>
<td>National Audit Office(^{36})</td>
<td>Large business start-up costs for the GST component of the impact of the Single European Market.</td>
<td>Visits to Customs and Excise headquarters and 14 local offices.</td>
<td>Start-up costs were estimated at 72 percent of recurrent costs.</td>
</tr>
</tbody>
</table>

\(^{32}\) CFIB, above n 16.  
\(^{34}\) Pillai, above n 18.  
\(^{35}\) Clare and Connor, above n 17.  
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<th>Regulation Researched</th>
<th>Research Method/Sample size/ Business Researched</th>
<th>Key Findings</th>
</tr>
</thead>
<tbody>
<tr>
<td>USA</td>
<td>Murphy</td>
<td>Start-up compliance costs of the Equal Credit Opportunity Act.</td>
<td>Survey of 37 large commercial banks.</td>
<td>Economies of scale in legal and other compliance costs.</td>
</tr>
<tr>
<td>USA</td>
<td>Boyle</td>
<td>Start-up compliance costs of the Revised Truth Lending Act.</td>
<td>201 mortgage banks.</td>
<td>Start-up costs were 45 percent of the revised Act.</td>
</tr>
<tr>
<td>USA</td>
<td>Schroeder</td>
<td>Start-up compliance costs of implementing the Electronic Fund Transfer Act.</td>
<td>Used data from the Federal Reserve survey of 67 commercial banks.</td>
<td>18 percent of start-up costs were on management costs.</td>
</tr>
<tr>
<td>USA</td>
<td>Elliehausen and Lowery</td>
<td>Start-up compliance costs of the Truth in Savings Act.</td>
<td>Survey of 4,000 savings institutions.</td>
<td>Reported economies of scale of start-up compliance costs.</td>
</tr>
<tr>
<td>USA</td>
<td>Elliehausen and Lowery (2000)</td>
<td>The effect of the required changes on start-up compliance costs.</td>
<td>Not reviewed.</td>
<td>Start-up costs for the Truth in Savings were insensitive to the extent of changes required to implement the regulation.</td>
</tr>
</tbody>
</table>

40 Elliehausen and Lowery, above n 15.
C  The Canadian Studies

The CFIB\(^{43}\) undertook a survey of their members in the first year of the GST’s operation in Canada and received 25,362 responses. They estimated start-up costs of C$3.0 billion, representing 45 percent recurrent costs of C$6.6 billion, which was around 30 percent of tax revenue at that time.

Though one of the CFIB’s survey merits was its large sample size, their figures were widely criticized on the basis of selection bias and overestimation because they were a lobby group. Brooks,\(^{44}\) in particular, cautions that “these estimates may be influenced by selection bias and other threats to validity and reliability”. Plamondon and Associates,\(^{45}\) by contrast, found that Canadian GST recurrent compliance costs, expressed as a percentage of business turnover, were lower than those in New Zealand.

Economies of scale, which is revealed by most compliance costs studies, was also evident in the CFIB\(^{46}\) study as shown in Table 2.

### TABLE 2

**GST START-UP COSTS IN CANADA BY SIZE OF FIRM - 1991**\(^{47}\)

<table>
<thead>
<tr>
<th>Number of employees</th>
<th>Average cost per firm C$</th>
<th>Estimated total cost C$Million</th>
<th>Percentage of total Costs</th>
</tr>
</thead>
<tbody>
<tr>
<td>0-4</td>
<td>2,421</td>
<td>1,153</td>
<td>38</td>
</tr>
<tr>
<td>5-19</td>
<td>4,023</td>
<td>1,069</td>
<td>36</td>
</tr>
<tr>
<td>20-49</td>
<td>6,546</td>
<td>412</td>
<td>14</td>
</tr>
<tr>
<td>50-99</td>
<td>8,674</td>
<td>177</td>
<td>6</td>
</tr>
<tr>
<td>100+</td>
<td>10,389</td>
<td>179</td>
<td>6</td>
</tr>
<tr>
<td>Overall</td>
<td>3,964</td>
<td>2,990</td>
<td>100</td>
</tr>
</tbody>
</table>

Small businesses, defined in terms of employment size, comprising businesses with less than 20 employees, incurred 74 percent of the total cost compared to 6 percent for larger firms (more than 100 employees). It must be noted that the former account for 30 percent of total Canadian production.

Another Canadian study, though not related to GST, was on start-up compliance costs of Canadian research and development tax incentives.\(^{48}\) This study found that average start-up costs of 33 firms with a start-up year were $3,550. These comprised 84 percent of recurrent compliance costs, yet only represented 0.4 percent of the total research and development credit claimed. A further interpretation was that a firm has a “double year” of compliance costs in its start-up year, one of start-up costs and an almost equal amount of recurrent costs. Approximately, half of the start-up costs represented costs relating to external adviser’s costs. This confirms that start-up costs are

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43 CFIB, above n 16.
46 CFIB, above n 16, 8-9.
47 Source: Ibid. 9.
higher than recurrent costs because businesses may have gone to consultants to get them started. Thus at a later stage, businesses did not require assistance from these consultants once the firms became familiar with the program.

D The Mauritian study

In Mauritius, research on start-up costs and recurrent costs of VAT in the Mauritius hotel industry was undertaken. The estimated measurable compliance costs in 1998/99 for hotels in Mauritius was Rs 14.3 million, comprising of start-up costs of Rs 9.8 million and recurrent costs of Rs 4.5 million. Start-up tax compliance costs of VAT were around 69 percent of the total compliance costs, while the recurrent costs accounted for 31 percent. Thus start-up costs were more than twice as high as recurrent costs, representing around 223 percent of recurrent compliance costs. Part of the start-up costs were equipment costs and training costs, estimated at 28 percent and 18 percent respectively.

These figures however, are exclusive of time costs as apparently respondents had difficulty with the estimation of opportunity costs, hence omitted from the analysis. This study also confirmed the economies of scale and regressivity of compliance costs. Compliance costs expressed as percentage of turnover for less than Rs 12 million was estimated at sixteen times that of businesses with over Rs 180 million. Thus the very small hotels, with a turnover of Rs 7.2 million incurred the highest compliance costs of 1.78 percent compared with large hotels with turnover of Rs 310.3 million that incurred 0.11 percent. Furthermore, compliance costs for all hotels combined at turnover of Rs 103 million were 0.02 percent.

Segregation of these costs showed that start-up costs, as percentage of turnover were 1.39 percent for very small hotels and for large hotels, 0.07 percent. Recurrent costs for very small hotels were ten times that of large hotels with 0.40 percent as compared to 0.04 percent respectively. Thus in line with findings of other compliance costs studies, Pillai’s study found that both start-up and recurrent costs of VAT in Mauritius were regressive.

It is worth noting the importance of guiding respondents properly to segregate start-up costs from the recurrent costs. The joint cost issue must also be addressed, where equipment acquired for any tax under investigation could also be used for other normal business activities. This study does not reveal how respondents were guided to separate these costs. Since the study was conducted ten months after the introduction of the GST, it is possible that some elements of recurrent costs could have been included in start-up costs and vice versa if there was no proper guidance on the segregation of costs. Information on this can only be obtained from the questionnaire, which unfortunately was not provided with the report.

E Australian business start-up compliance cost studies

Apart from Clare and Connor’s study, which estimated start-up compliance cost of the SST, most Australian business start-up compliance costs studies relate to the GST and were estimated around 1998-2001. The GST compliance cost estimates for Australia were stipulated in the RIS. The Australian GST estimates were based on recurrent costs of the GST of other countries, in particular,

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59 Pillai, above n 18.
60 Ibid, 56.
61 Ibid, 58.
62 Clare and Connor, above n 17.
63 RIS, above n 28.
New Zealand. However, the government acknowledged that start-up costs might be of a similar magnitude to annual recurrent costs.

The pre-implementation debate on the GST attracted a variety of surveys on small business start-up compliance costs. Rametse and Pope are aware of around ten major studies that have been published to date concerning the GST implementation costs for small businesses (see Table 3). However, due to differing methodologies such as survey technique, sample sizes, wording of questions and ensuing reliability, the findings of these surveys must be treated with caution. These studies show a fairly wide range of cost estimates, in terms of direct costs and opportunity costs. Other differing factors are the number of businesses surveyed. Where there are a small number of respondents, this then raises a concern on the studies’ reliability and representativeness of the whole population of around 1.2 million small businesses in Australia in 2000.

These studies used different research methods (mainly telephone, questionnaire survey and case study) and particularly the varied treatment of time costs and joint cost issue. However, as it can be seen (Table 3), apart from Ernst and Young, RSM Bird Cameron and NARGA, there is evidence of similarity in terms of costs incurred. The most authoritative study by the Economic Development Committee, Parliament of Victoria, which used a synthesis of other studies, estimated GST start-up costs of $6,000 per small business. It must be noted that this study did not take into account the opportunity costs. If time spent was included, at an opportunity cost of $20, using Evans et al estimate, this figure would possibly increase by $2,000, resulting in the increased estimate of $8,000.

Furthermore, analysis of the 1999 estimates show figures that are much lower than the post-1999 estimates. This could be due to the fact that these surveys may have been based on expectations rather than actual experience. Thus, after the 1 July, 2000, small businesses would have known the actual implementation costs, hence provided fairly accurate figures. Furthermore, costs may have been overstated, for example, the Victoria University of Technology’s study, the time period of the study was from early June to mid November 2000. Thus costs may be inclusive of both start-up costs and recurrent costs.

54 Rametse and Pope, above n 2.
55 Pope and Rametse, above n 5.
60 C Evans, K Ritchie, B Tran-Nam and M Walpole, Taxpayer Costs of Compliance, (Australian Taxation Office, 1997), 11-12.
TABLE 3:
SUMMARY OF SMALL BUSINESS GST START-UP COMPLIANCE COST ESTIMATES FROM MAJOR STUDIES, 1999-2001

<table>
<thead>
<tr>
<th>Source (n)</th>
<th>Average start-up costs ($)</th>
<th>Average time spent (hours)</th>
<th>Number of respondents</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ernst &amp; Young⁶³</td>
<td>17,016</td>
<td>64</td>
<td>4</td>
</tr>
<tr>
<td>AC Nielsen⁶⁴</td>
<td>2,618</td>
<td>64</td>
<td>602</td>
</tr>
<tr>
<td>Pope et al⁶⁵</td>
<td>3,500</td>
<td>n/a</td>
<td>129</td>
</tr>
<tr>
<td>VECCI⁶⁶</td>
<td>6,814</td>
<td>80</td>
<td>328</td>
</tr>
<tr>
<td>VECCI² 000</td>
<td>5,000-20,000</td>
<td>142</td>
<td>70</td>
</tr>
<tr>
<td>RSM Bird Cameron⁶⁸</td>
<td>6,000</td>
<td>n/a</td>
<td>170</td>
</tr>
<tr>
<td>EDC, Victorian Parliament⁶⁹</td>
<td>12,380*</td>
<td>included above**</td>
<td>6</td>
</tr>
<tr>
<td>Victoria University of Technology⁷⁰</td>
<td>n/a</td>
<td>n/a</td>
<td>264</td>
</tr>
<tr>
<td>Patterson ⁷¹</td>
<td>5,587</td>
<td></td>
<td>285</td>
</tr>
<tr>
<td>NARGA² 2001</td>
<td>18,622</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>


⁶³ Ernst and Young, above n 56.


⁶⁸ RSM Bird Cameron, above n 57.


⁷⁰ Victoria University of Technology, above n 61.


⁷² NARGA, above n 58.
Notes: * Time period was from early June to mid November 2000, that is, up to the lodgement of the first quarterly BAS (GST) return. Costs are $6,012 excluding time costs. ** 170 hours, giving a cost of $6,368 at an average opportunity cost of $37.46 per hour (derived from the ‘employer hourly rate’). Time costs thus account for 51% of the average start-up costs of $12,380.
N/A indicates either not estimated or not cited. Implicitly time costs would be included in the monetary estimate.
1 Number of respondents refers to small business respondents only, and excludes respondents in other categories in some surveys, with the exception of the VECCI 1999 survey where a breakdown was not given. Cost and time estimates refer to small business only (and are mutually exclusive unless stated).
2 The Economic Development Committee, Parliament of Victoria, estimate was based on a synthesis of evidence from other studies and submissions. A high reliance appears to have been placed on the VECCI2000 survey findings, albeit with a conservative estimate cited.
3 There may be other smaller and/or unpublished studies not known to the authors.
4 A few studies have focused on large business or have not distinguished between large and small business, for example, PricewaterhouseCoopers (2001), and these are not included in this table but are discussed below.
The National Association of Retail Grocers of Australia Pty Ltd (NARGA) commissioned a study on both start-up and recurrent costs of the GST for independent grocers. Small businesses were measured in terms of annual turnover of $5 million, whilst medium-sized businesses annual turnover was between $5 million and $20 million. Start-up compliance costs for small businesses were estimated at $18,622 and for medium sized businesses at $44,704. It must be noted that careful comparative analysis must be treated with caution because of differing turnover measurement with other studies, particularly those that use the ATO measurement of small businesses with annual turnover of less than $10 million. Small independent retailers, as percentage of turnover, incurred start-up costs of 1.63 percent, while medium sized and large independent retailers incurred 0.58 and 0.17 percent respectively. This confirms the regressivity of the GST start-up compliance costs.

Another study, by Queensland Council of Social Services (QCSS) has been excluded from Table 3 because it is more of a recurrent compliance cost than a start-up compliance cost study since it covered a period of twelve months from July 2000 to July 2001. The QCSS study reveals that “the implementation of the GST and other parts of the New Tax System has cost this sector over $39 million and will cost a similar amount each year thereafter for ongoing (recurrent) costs...” However, the findings are similar to those of small businesses, high compliance costs, with a proportionately greater impact on smaller organisations.

Tran-Nam and Glover provide a critique of the QCSS study and assert the difficulty in assessing its reliability since the final questionnaire form was not included in the QCSS study. Thus information on guiding respondents to exclude recurrent costs from start-up costs was not available. Furthermore, the very well known problem identified by literature, of “accounting-taxation overlap” and disentangling equipment costs relating to the GST implementation and other normal business activities is normally scrutinised from the questionnaire.

A wide variation of GST start-up compliance costs reported by most of these studies could be attributable to expensive upgrades of computer equipment not related to the GST. This interpretation tends to be confirmed by the median estimates that are often below the mean estimates. Estimates also vary widely by type of industry, with retail/wholesale reporting the highest costs and entertainment, recreation, restaurants and personal services reporting the lowest.

It must be noted that these studies did not attempt to estimate temporary compliance costs of the GST. The only academic study that we are aware of and has estimated temporary compliance costs of the GST is by Tran-Nam and Glover. In estimating transitional costs, Tran-Nam and Glover included both commencement (start-up) and temporary (learning) costs. Their study was more of a quantitative focus and had a smaller number of small business participants.

The estimated transitional costs of tax reforms included GST related costs and other aspects of the tax reform such as the Business Activity Statement (BAS) and Pay-As-You-Go (PAYG). The

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73 NARGA, above n 58.
74 Ibid, 15.
76 An Australian GST start-up compliance cost study, for example, Rametse and Pope, would cover the period up until 30 June, 2000.
77 QCSS, above n 75, 4.
78 Tran-Nam and Glover, above n 7, 352.
79 VECCI, above n 67, Table 4.
80 Tran-Nam and Glover, above n 7.
mean gross transitional costs were estimated at $5,442 per small businesses and after considering tax deductibility benefits and the $200 direct subsidy, the estimated net transitional costs of tax reforms were $3,815 per business. Net costs expressed as percentage of average annual turnover in 1999-2000 and 2000-01 were 1.34 percent (gross) and 0.86 percent (net).

Petzke and Murphy\footnote{\textit{S} Petzke and D Murphy, ‘A Survey of Small Regional Businesses and the Impact of the Goods and Services Tax’ (Working paper, Charles Stuart University, 2001).} conducted a GST compliance cost study. This study surveyed small businesses in Albury Wodonga during September and October 2001. The research attempted to ascertain small business owners’ perception of the impact of the GST in the first twelve months of its implementation. Petzke and Murphy estimated average implementation costs estimated at $4,545 (without time costs) per business, comprising of additional staff costs of $2,019 and additional professional fees of $2,525 per business. Average time spent per business was 133 hours. This study, however, neither valued these hours in dollar terms nor addressed the common “joint cost” problem. If time was valued using an opportunity cost of $20\footnote{Evans, Ritchie, Tran-Nam and Walpole, above n 60, 11-12.} time costs would be $2,660, giving the total implementation compliance costs would be $7,205.

IV AUSTRALIAN GST EMPIRICAL EVIDENCE

Apart from Tran-Nam et al\footnote{B Tran-Nam, J Glover and S Wilkin, ‘The GST Recurrent Compliance Costs/Benefits of Small Business in Australia: A Case Study Approach’ (Paper presented at the Australasian Tax Teachers Association Conference, Flinders University, 29-31 January, 2004).}, to date, there is no academic GST recurrent compliance study in Australia that can be analysed to show the relationship between GST start-up compliance costs and recurrent compliance costs. In this section, an overview of the major GST start-up compliance cost for Western Australia small businesses\footnote{Rametse and Pope, above n 2.} and GST transitional compliance cost study\footnote{Tran-Nam and Glover, above n 7.} is presented. These studies are analysed within the context of small business GST recurrent compliance cost research by Tran-Nam et al\footnote{Tran-Nam, Glover and Wilkin, above n 83.}

A The West Australian GST Start-up Compliance Cost Study

Business start-up compliance estimates in Western Australia focused on small business and the GST. As reported in Rametse and Pope\footnote{Rametse and Pope, above n 2.}, small businesses incurred high costs in preparation for complying with the GST requirements. On average, small businesses incurred GST start-up costs (excluding their time costs) of $5,006. The costs were an average of 131 hours per firm in seeking professional accounting and information technology advice to introduce new systems and procedures. Time spent valued in dollars amounted to $2,620 (at an opportunity cost of $20 per hour), or 34 percent of total start-up costs of $7,626. Gross GST start-up costs, that is, before considering any offsets, were estimated at $7,626. This estimate comprises the cost of equipment, particularly computers and software, costs such as professional accounting and IT consultancy fees, training course fees, stationery and phone calls, and also (opportunity) time costs.

It must be noted that the opportunity cost of $20\footnote{Evans, Ritchie, Tran-Nam and Walpole, above n 60.} has since been reviewed to reflect the inflation of 8 per cent as at the period ending GST start-up compliance cost estimate (June 2000). Time costs
increased to $2,882 amounting to total estimated mean gross GST start-up compliance costs of $7,888. Most of this study’s results have been reported elsewhere89 and will not be repeated here.

B Relationship of Business start-up compliance costs to recurrent compliance costs

The GST formed part of the Australian new tax system and, it was expected that start-up compliance costs would be higher than the recurrent compliance costs. Furthermore, recurrent compliance costs would be lower as small businesses become familiar with the GST. Thus there is no doubt that a strong relationship of business start-up compliance costs to recurrent compliance costs exists. Analysis reveals the extent to which small business gross mean start-up compliance costs (with time) relates to recurrent GST compliance cost. Based on the study by Tran-Nam et al90 on the recurrent cost of the GST, the start-up tax compliance costs of the GST represent a significant amount of GST recurrent compliance costs. After two years of the implementation of the Australian GST, Tran-Nam et al91 estimated the recurrent GST compliance costs, covering the financial years 2000-2001 and 2001-2002.

Using a case study methodology, the researchers collected data from thirty one participants, predominantly from rural Victoria, NSW, Tasmania, Queensland, the ACT and the Northern Territory. The preliminary results of this study estimated the mean gross GST recurrent compliance costs per small business at $2,481. After considering offsets such as tax deductibility and cash flow benefits, the net recurrent GST compliance costs were estimated at $1,244 per small business.

Earlier on, for the period 1999-2000, the gross transitional costs of the GST were estimated at $7,673, a figure which is in line with Rametse and Pope study’s92 gross mean GST start-up compliance costs of $7,888. However, Tran-Nam et al93 believed that the mean gross GST recurrent compliance costs were still higher and as such, the figure could be inclusive of some elements of transitional costs. Thus transitional difficulties are still evident for small businesses.

It is clear that start-up compliance costs of $7,888 estimated by Rametse and Pope94 and transitional costs of $7,673 estimated by Tran-Nam and Glover95 are around six times higher than the Tran-Nam et al96 recurrent compliance costs estimate of $1,244 per small business. It must be noted that both start-up compliance costs and transitional compliance cost figures do not include a deduction of government’s $200 voucher subsidy.

As compared to Rametse and Pope study,97 which covers only start-up compliance costs, Tran-Nam and Glover98 transitional costs include both start-up compliance costs and temporary compliance costs.99 These authors define temporary compliance cost as “the value of additional time required

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90 Tran-Nam, Glover and Wilkin, above n 83.
91 Ibid.
92 Rametse and Pope, above n 2.
93 Tran-Nam, Glover and Wilkin, above n 83.
94 Rametse and Pope, above n 2.
95 Tran-Nam and Glover, above n 7.
96 Tran-Nam, Glover and Wilkin, above n 83.
97 Rametse and Pope, above n 2.
98 Tran-Nam and Glover, above n 7.
by staff over a period extending after a change commences in order for them to comply and familiarise themselves with new regulations”. Thus their slightly lower transitional cost figure as compared to Rametse and Pope’s start-up compliance cost figure may justify that small businesses were beginning to be familiar with the GST requirements.

Another potential relationship of start-up compliance costs to recurrent compliance costs, though may be weaker, relates to managerial benefits arising from the use of computers. The increased level of small businesses, using computers, not only for record-keeping and GST compliance, but for their business generally is significant. Rametse and Pope’s study also covers acquisition of computers for GST compliance (as start-up compliance costs) and its relationship to recurrent costs. It is expected that acquiring computers for GST compliance would result in lower recurrent compliance costs due to benefits from the use of technology in other business areas and better management. The authors are in the process of finalising interviews and data analysis on managerial benefits and are keen to disseminate their findings as soon as possible.

C GST Start-up Compliance Aggregation Difficulties

The estimation of aggregate start-up compliance cost of the GST for the Australian small businesses is a dicey situation. It requires stratified small business data by either annual turnover or employment size for grossing up purposes. However, for comparability intention, Rametse and Pope’s study requires stratification data by annual turnover rather than employment size since it follows the ATO’s definition of small business. This data can only be obtained from the ATO, which “for confidentiality purposes” is unwilling to provide it.

In order to gross-up, it is appropriate to use the number of small businesses registered for GST before the GST implementation date on 1 July 2000. However, this has the potential of inflating aggregate GST start-up compliance costs because it is evident that many businesses may operate several firms as one business. If extrapolation of gross GST start-up compliance costs was based on an estimate of around 1.2 million Australian small businesses in 2000, GST start-up compliance costs would be around $9 billion. However, to obtain a more reliable estimation, small business aggregate gross GST start-up compliance costs can be calculated by extrapolating on the basis of the number of small businesses in Australia and weighted against Australian small business GST registrants. Rametse and Pope are in the process of estimating a more reliable aggregate gross GST start-up compliance costs figure for Australian small businesses.

V CONCLUSIONS AND POLICY PERSPECTIVES

Though business start-up compliance costs are “sunk costs” and can never be recovered they are important to policy makers. Countries yet to introduce their new taxes need to know about the

100 Ibid, 502.
101 Rametse and Pope, above n 2.
102 Ibid.
103 Ibid.
106 Rametse and Pope, above n 2.
magnitude of start-up compliance costs. Though the United States start-up compliance costs studies
do not relate to tax whatsoever, their contribution to literature is acknowledged.

It is evident that business start-up compliance costs relative to recurrent compliance costs are
significant. Gross mean GST start-up compliance costs estimated by Rametse and Pope\textsuperscript{107} and
Tran-Nam and Glover\textsuperscript{108} transitional compliance cost study are around six times more than Tran-
Nam \textit{et al} recurrent compliance cost study. This contradicts Government prediction that start-up
compliance costs may be of a similar magnitude to recurrent compliance costs.\textsuperscript{109}

The government had estimated start-up compliance costs for all businesses at around $2 billion. If
extrapolation of gross GST start-up compliance costs was based on an estimate of around 1.2
million Australian small businesses in 2000, small business GST start-up compliance costs would
be around $9 billion. Pillai\textsuperscript{110} found that start-up compliance costs were more than twice as high as
recurrent costs, at 223 percent. Gunz \textit{et al}\textsuperscript{111} estimated start-up costs at 84 percent of recurrent costs
while National Audit Office\textsuperscript{112} found start-up costs to represent 72 percent of recurrent costs.

Estimation of managerial benefits relative to GST start-up compliance costs is a challenging task.
Higher start-up costs may represent an investment in the latest technology yielding lower recurrent
compliance costs. This relationship is analysed in the context of start-up costs. The longer-term
benefits may justify the Government’s policy of a low GST registration threshold and offset to high
initial costs.

Policy makers should recognize the significance of compliance costs and without their cooperation
(making data available to researchers) researchers may experience estimation difficulties. As such,
unless careful analysis is applied, various parties may question the reliability as well as the
credibility of the research in question.

\textsuperscript{107} Ibid.
\textsuperscript{108} Tran-Nam and Glover, above n 7.
\textsuperscript{109} RIS, above n 28.
\textsuperscript{110} Pillai, above n 18.
\textsuperscript{111} Gunz, Macnaughton and Wensley (1995), above n 19.
\textsuperscript{112} National Audit Office, above n 36.