THE GST RECURRENT COMPLIANCE
COSTS/BENEFITS OF SMALL BUSINESS IN AUSTRALIA:
A CASE STUDY APPROACH

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I INTRODUCTION AND BACKGROUND OF THE STUDY

Re-election of the Howard-led Coalition Government in October 1998 with a platform including a substantial new tax was unprecedented in Australian federal history. Governments had previously failed to overcome public resistance to major indirect tax reform in 1975, 1985 and 1993. Central to the government’s 1998 tax reform package was a 10 per cent, broad-based consumption tax known as the ‘Goods and Services Tax’ (GST). GST Bills introduced by the government in December 1998 were amended and passed by the Senate in July 1999. The new tax first became effective in Australia on 1 July 2000.

Prior to the introduction of the GST, the government claimed that its relevant tax reform, described in ‘A New Tax System’ (ANTS), would bring substantial benefits to Australia. The claim sharply divided the opinion of tax academics and tax practitioners. Expert witnesses giving evidence before a 1999 Senate inquiry provided equally strong support for and in opposition to the GST.

Now the GST has operated for more than three years. It is opportune to assess ANTS, inter alia, under the simplicity criterion of good tax policy. Two things should be mentioned at the outset. First, all five criteria of good tax policy (equity, efficiency, flexibility and transparency) should be applied simultaneously in the evaluation of the ANTS claims. This paper, then, should not be interpreted as a full evaluation of ANTS. Rather, it should be regarded as an attempt to contribute to a specific aspect of the ongoing assessment of ANTS. Secondly, it is known that from the outset both the government’s pre-1998 promise that ANTS will ‘collect revenue in a … simpler … way’, and post-1998 claim that the replacement of the Wholesale Sales Tax (WST)

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3 Ibid, 10.
and a range of state taxes by the GST will ‘reduce compliance costs for business’, were untrue and misleading. It has been argued that the GST imposes not only a substantial transitional compliance cost but also a large increase in the recurrent compliance costs. However, estimates of the GST-induced increase in recurrent compliance costs are prospective, mostly based on the New Zealand experience.

The aim of this paper is to present preliminary results of a study of the recurrent costs/benefits of the GST—confined to the Australian small business sector. Small business is acknowledged to bear a disproportionate burden of tax compliance costs, giving the GST, to a degree, a regressive effect. Unlike larger businesses, small businesses are often logistically and administratively under-equipped to cope with new taxes such as the GST.

This paper evolves from an Australian Research Council (ARC) Linkage project involving: two academic institutions, Atax of UNSW and the Law Faculty of Monash University; and three industry partners, National Farmers’ Federation (NFF), Council of Small Business Organisations of Australia (COSBOA) and Taxpayers Australia (TA). The principal aim of the project is to study the impact of compliance costs/benefits of tax reform on small business, especially those in rural areas. More specifically, the project seeks to examine the simplification impact of ANTS, including the so-called Ralph reform proposals. A previous paper arising from this project reported on the transitional compliance costs of the GST.

Section II of the paper discusses conceptual issues related to small business and recurrent compliance costs. Difficulties with obtaining reliable estimates are identified and analysed. The rationale and methodology of the case study approach adopted in this study are explained in Section III. Qualitative findings obtained from the case studies are summarised in Section IV. Some preliminary findings on estimates of GST recurrent compliance costs incurred by businesses included in the case study follow in Section V. Section VI makes some tentative comparisons with results obtained in previous studies. Concluding remarks are then given in the final section.

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II CONCEPTUAL ISSUES

A Small Business

Since this study is confined to small business, it seems appropriate to start with a discussion on the meaning, characteristics, identification and measurement of small business. A business is traditionally regarded as small if it has some of the following organisational or management characteristics:

- It is independently owned and operated;
- It is closely controlled by owners/managers who also contribute most, if not all of the working capital; and
- Principal decision-making functions rest with the owners/managers.8

Essentially qualitative characteristics such as these are inherently problematic. For practical purposes, small business is often measured in terms of business size—usually the number of employees that a business has, or the size of its turnover. The Australian Bureau of Statistics (ABS) defines small businesses in terms of employment. A non-agricultural, private sector business is small if it is either a non-manufacturing business employing less than 20 employees, or manufacturing business employing less than 100 employees. About 95.9 per cent of total non-agricultural businesses are small pursuant to this definition.9 However, the employment size definition is not used by the ABS for the agricultural sector. Instead, a measure called the Estimated Value of Agricultural Operations (EVAO) has been developed, to reflect the area of crops sown, the number of livestock and crops produced/livestock sales during a given year. Some 88 per cent of all private sector agricultural businesses are accordingly said to be small.10

The Ralph Review, following the Australian Taxation Office (ATO), used a definition of small business based on turnover.11 Businesses with an annual turnover or receipts of less than $1 million, exclusive of GST, are to be eligible to be taxed under the Simplified Tax System (STS) as small businesses. Over 96 per cent of businesses (representing over 1.075 million businesses in 1999–2000) are said to have an annual turnover of less than $1 million.12 In order to facilitate critical comparisons and analysis of the Review, this article will adopt the same turnover definition of small business as the Review. In any case, the ABS employment definition has a comparable sample range.

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9 ABS, 1999 Year Book (1999) derives the ratio 1 004 200/1 046 900 = 95.9 per cent; cf ratio of 894 500/929 500 = 96.23 per cent.
11 See n 6, Recommendation 17.1 at p 575.
It is worthwhile to note that there are other practical ways of defining small business. For example, the size of PAYE tax deductions is a possible candidate. Thus, the New Zealand’s Inland Revenue Department (IRD) defines a small employer as an employer making gross annual PAYE deductions of less than NZ$100 000. It is not difficult to see that the IRD’s definition of a small employer encompasses both the number of employees and the wage levels (which tend to vary in proportion to business revenue). Gross annual PAYE deductions of less than $100 000 is quite compatible with an annual GST-exclusive turnover of less than $1 million. In this sense, the IRD’s definition is perhaps a better way to define the size of business than either number of employees alone or turnover alone.

B Compliance Costs

1 Components of Compliance Costs

It is appropriate to begin with a universally accepted definition of tax compliance costs. According to a leading authority:14

Compliance costs are defined as those costs incurred by taxpayers, or third parties, such as businesses, in meeting the requirements laid upon them in complying with a given tax structure.

Although this definition will be further elaborated and refined in the remainder of this section, it will be employed as a useful starting point of analysis.

From the above definition, it can immediately be deduced that compliance costs to business taxpayers typically include:

- The value of time losses by taxpayers, internal staff and unpaid helpers in dealing with business tax affairs;
- The costs of external tax advisers; and
- Any non-labour costs such as specific travel relating to tax compliance activity, the cost of tax publications, stationery, postage, telephone and facsimile, the use of office and equipment such as computers for tax purposes, etc.

Sandford et al also included psychological costs in the definition of tax compliance costs. Psychological costs refer to the stress, anxiety and frustration experienced by taxpayers in dealing with their tax affairs. Psychological costs are extremely difficult, if not impossible, to measure and have not yet figured in empirical studies. They may be highly relevant to tax legislative change during the transitional stage but less so for recurrent compliance costs. Nevertheless, some attempts will be made in this study to assess psychological costs qualitatively.

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15 Ibid, 16–18.
2 Recurrent Compliance Costs v Transitional Compliance Costs

Sandford et al also distinguished a number of tax compliance cost categories. These include:

- commencement costs;
- temporary costs; and
- regular costs.

Commencement costs are typically referred to as start up costs in the Australian literature, and this practice will be maintained here. For example, a typical start-up compliance cost may be the expenses of initial training of staff to deal with a proposed tax change. A temporary compliance cost may then be the value of additional time required by staff over a period extending after a change commences in order for them to comply and familiarise themselves with new regulations. Regular (or recurrent) costs will correspondingly equal the value of time expended by staff to comply with tax changes with which they are now familiar.

3 Gross Business Compliance Costs v Net Business Compliance Costs

The literature recognises offsets to compliance costs. Under this approach, the term ‘gross’ business recurrent compliance costs is used to refer to the opportunity costs of resources expended by businesses in their compliance with the new tax after the transition period. The components of the gross business transitional costs are elaborated previously. The term ‘net’ business transitional costs then refers to the costs incurred by business taxpayers after all offsetting benefits have been taken into account. In the context of the Australian GST, these offsetting benefits include:

- Tax deductions (business compliance cost activities are tax deductible);
- Cash flow benefits (mismatch in timing of when GST is collected by business and when it is remitted to the ATO); and
- Managerial benefits: tax compliance may generate marginal benefits to business taxpayers in the form of improved business decision-making. These benefits may be brought about by the need to have stringent record keeping in order to comply with the requirements of the tax laws. Managerial benefits theoretically exist but are difficult to quantify, and are typically omitted in empirical studies. Important exceptions include Sandford et al and National Audit Office of the UK, which suggest that the values of managerial benefits can be quite considerable.

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16 Ibid, 13–14.
17 This period is known as the ‘transitional period’.
18 Above n 14, 13–14.
4 Incremental Compliance Costs v Total Compliance Costs

The conceptual framework has so far focused on total compliance costs. But given the nature of the study, the estimation of prevailing total compliance costs before and after the introduction of the GST may not be as important as knowledge as to whether total compliance costs have either decreased, increased, or remained unchanged in response to the GST. Thus, this paper will focus on incremental costs.

5 Practical Difficulties in Measuring Recurrent Tax Compliance Costs

Recurrent compliance costs are difficult to estimate in practice for a number of empirical reasons:

- Boundaries between recurrent and transitional compliance costs are not always well defined. It may be impossible for business taxpayers to allocate costs to the correct category with confidence.
- Economic inputs are not perfectly divisible. One item of expenditure may satisfy several business purposes. For example, a firm may purchase a new computer for stock control and invoicing as well as handling its GST requirements. How much of the costs of running this computer can be attributed to GST compliance costs? This problematic task of cost allocation is analogous to the well-known accounting-taxation overlap debate in the tax compliance cost literature.
- Many tax changes being implemented over a relatively short time period in Australia. The GST, BAS, Australian Business Number (ABN), Pay As You Go (PAYG), Simplified Tax System (STS) and other measures were all introduced either at the same time, or in quick succession. It is difficult for business taxpayers to ascribe recurrent costs to particular types of tax reform.
- Valuation of the time spent by unpaid helpers is also a problem. The problem also exists, but to a lesser extent, with self-employed persons, such as sole traders or partners.

Practical issues, of which the foregoing are only some, suggest that the study of recurrent compliance costs must be conducted carefully in order to achieve meaningful and reliable results.

III RESEARCH METHODOLOGY

A Scope of the Study

The primary purpose of this paper’s study is to obtain a general picture of the recurrent costs incurred by small businesses—especially those located in the rural sector—in complying with the GST. Small business is in practice normally defined in terms of various criteria such as turnover, number of employees, physical characteristics or PAYE tax bill, as discussed above. Using turnover to define small business, it is worthwhile noting that the ATO classifies small businesses as those entities (excluding superannuation funds) with an annual total income of less than $10 million,21 while the

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Review of Business Taxation regards businesses with an annual receipt of less than $1 million, exclusive of GST, as small. Since the ultimate objective of this ongoing study is to evaluate the Review, this paper initially adopted the same definition of small business as that in the Review. However, it was soon discovered that for rural businesses, the $1 million limit is almost always exceeded even though the enterprises in question employed only two or three persons. For future studies, an expansion of the definition of small business to entities with a greater annual receipt may be advisable. The periods under study include the 1999–2000, 2000–01 and 2001–02 financial years.

B Choice of Data Gathering Techniques

Basically, there are two main approaches to studies of this kind:

- large-scale mail surveys; or
- in-depth case studies.

Both of these methods have been employed in the Australian context. For example, the pioneering work on tax compliance costs in Australia by Pope et al. used the mail survey method, whereas the case study approach was utilised in another earlier study led by Wallschuzky.

The main disadvantages of large-scale mail surveys are that:

- they are costly to conduct; and
- the assistance of the ATO is required in order to obtain a random, representative sample of business taxpayers.

The major advantage of the large-scale survey is that the sample data, combined with other information and relevant macro-statistics from the ATO, can be used to generalise to the entire economy. This kind of approach is necessary in evaluating the economy-wide simplification impact of the tax reform. If this method is adopted, ideally, there should have been two surveys, six months before and one year after the introduction of the GST, to capture as much information about the transitional costs as possible.

The case study approach was adopted by the present authors for the following reasons:

- They have limited resources and no access to the ATO’s taxpayer files;
- Concern with contemporary events are best explored by the case study method; and
- It is more useful to study the same taxpayers over the entire life of the project.

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22 Above n 6, 575.
The case study approach does not allow the results to be generalised to the entire economy. But it does present the likely scenarios faced by a range of businesses in different circumstances. Further, such an approach is useful in obtaining qualitative data that may identify particular areas where compliance costs imposed on business taxpayers could be reduced.

C Selection of Participants

The participants in this project were supplied by the three industry partners (above). Not surprisingly, it was initially difficult to find suitable participants to cover the wide range of characteristics considered as relevant by the research team. Ultimately, a total of 53 business taxpayers agreed to participate in the project (26 primary producers supplied by the NFF, 14 small business participants by COSBOA and 13 by TA). However, since the participants are spread throughout Australia, the study has so far only collected data from 31 of them.

A cross-section of participants were selected from Victoria, NSW, Tasmania, Queensland, the ACT and the Northern Territory. At the time of this paper, twelve businesses had been interviewed from the farming sector and ten from non-farming industries. Farming businesses included dairy, beef, sheep and poultry farmers, graziers, a rice farmer, a citrus fruit farmer and a grape-grower. Those businesses from the non-farming sector included financial advisers, accountants, shopkeepers, a sign writer, an association manager, a furniture re-upholsterer, a bookshop owner, a pharmacist and an artist.

Since conducting the study of transitional costs, one business is now defunct, another has been sold and amalgamated as part of a larger business, and, at the time of the last interview, another farmer was preparing for the sale of his farm. At the time of this report, a little over two-thirds (twenty-two) of the respondents had been interviewed.

D Mail Questionnaire and Interviews

Relevant data was gathered from participants by means of a questionnaire, supplemented by face-to-face and telephone interviews. The questionnaire was extensively discussed within the research team, and subjected to pilot testing before being sent to participants by email and ordinary mail. The joint cost problem discussed earlier was dealt with by researchers during interviews.

The purpose of the follow-up interviews was to verify the quantitative data obtained from the questionnaire and to gather additional qualitative comments. In terms of quantitative data, the issue of joint costs was emphasised and participants were guided to focus only on the recurrent costs of tax reform. As far as qualitative comments were concerned, the emphasis was on how tax reform could be made more ‘friendly’ to those directly affected.

26 Small business taxpayers, many of them owners or partners, were reluctant to commit their time to a multi-stage project.
IV QUALITATIVE FINDINGS

A Evaluating the Problems of Tax Reform

Nine respondents to the questionnaire reported continuing transitional difficulties with the GST. These respondents were mainly farmers. However, as members of the overall majority of respondents declared that they were sufficiently familiar with GST, the following difficulties can be classed as of a recurrent nature.

1 Lack of Time

Respondents were often unable to keep up-to-date with paperwork. GST tax reform was seen by some small business operators as something preventing them from overseeing day-to-day business affairs. Two non-farming small business proprietors remarked:

We have had a couple of major problems but we have too much work to do in the business to worry about these problems. Like most small business owners we spend too much time working on our business tax matters rather than on our business itself.

Bookshop owner, Caloundra, Qld

The general feeling is that we're just tax collectors. It's really hard at our level. We don't have time to think about what we're doing, we just do it. I think we've been taken away from what we're here for.

Shopkeeper, Yanackie, Vic.

The need to prepare and retain copies of GST compliance paperwork was regarded as onerous by small business operators who did not have easy access to administrative resources.

How do you expect a small business (couple or single) without office staff to have the facility to do all of this extra work when they are working in the business. Most of these people do not have a photocopier but we are expected to keep copies of everything!

Farmer, Yinnar, Victoria

Reading and understanding industry-specific GST rulings was also onerous for some respondents. A Victorian farmer observed:

I still get lots of paper from the ATO which clarify which things have GST on them and which don’t. I guess I’m expected to read them all but there are too many and I don’t have time to read them all. I know it’s a drop in the ocean compared with what’s out there. It would just be much simpler if everything had GST on it.

Farmer, Illabo, NSW
One small business proprietor said that she chose monthly GST BAS reporting because of its cash-flow advantages. Lack of time prevented her from continuing with this choice.

We changed from monthly to quarterly because of a lack of time to complete the monthly BAS. It was due 3 weeks after the end of the end of the month. There were no extensions and it was too constricting. It was just too short a time to get the paperwork completed.

Poultry farmer and small business accountant, Ellalong, NSW

Accountants as respondents recounted comparable problems experienced by their small business clients.

There’s too much to explain to people and my clients just can’t take it in. You’re asking them to make decisions that in a lot of cases they can’t reverse. For example, if you go into the STS and then opt out, you can’t go back in for 5 years. That’s a far-reaching decision. But people are just overwhelmed and they are unable to think through the consequences.

Accountant, Darwin, NT

2 Increased Stress Levels

A majority of the participants had been uncomfortably stressed as a result of GST tax reform. Stress levels varied from moderate to considerable. In most cases, stress levels were not offset by any personal benefit arising as a result of tax reform. Respondents also reported that stress levels varied throughout the year, increasing around the time of the BAS or when the BAS conflicted with other busy periods, for example, shearing and grain harvesting. Notably, the majority of respondents reported that their stress levels had decreased over the 2002–03 period.

Because I do all the BAS and IAS myself, the stress level is high. Before, the accountant dealt with the ATO. Now I do too—I do my best but there's always a worry that I've got something wrong!

Farmer, Glen Innes, NSW

Part of the stress is trying to convince my husband of what he needs to comply with and be careful about regarding the GST. I try to explain to my husband that if you get one thing wrong and you are audited, you’re gone but he’ll say ‘Oh, they won’t know’. ‘They have computers’, I say, ‘linked in with our other information, like our super and worker’s comp.’ It’s the whole ‘Big Brother’ thing—everything is tied up together—you only have to make one mistake and they can catch you up. I’m really nervous about being audited, my accountant tells me that he’s never seen so many audits as he’s seen recently.

Farmer, Barraba, NSW

The level of changes that small businesses had to do was immense. GST on its own would have been quite enough. People needed a couple of years to get over it before they brought in all the other changes.

Grape-grower, Denman, NSW
3 Higher Tax Adviser Fees

External tax advisory costs increased for almost all respondents.

Most businesses just aren’t big enough to absorb all these external costs . . . generally, the benefits don’t outweigh the costs. I’ve had four clients that have said that it is too hard and shut down. One was a doctor and he said that it just wasn’t worth his effort. He’s now gone to work interstate as an employee in general practice. He used to work on the outskirts of Darwin and there’s no doctor there now. It was purely GST-related. So there’s an impact on rural people that can get forgotten.

Accountant, Darwin, NT

Some respondents said that accountants had used the GST as a pretext for charging higher fees. ‘My accountant charges like a wounded bull for any advice I ask him for,’ one NSW farmer commented.

While I think that some accountant firms did a very good job of educating small businesses about the GST, I think that there are a lot out there that simply made an awful lot of money out of it and I believe that organisations like COSBOA, independent retailers organisation and other small business organisations, would have done a far better job with the money that was available. More money should have been spent on small business organisations. We’re not in these groups for money or personal gain. We’re in it because we consider the effects on small business. Accountants and their firms, they are in it to make money and that’s exactly what they did with the GST.

Store-owner, Myaree, WA

The intention of the GST was that people would be forced to do their own bookkeeping and know more about their businesses. The reality is that the people who were already keeping records are still doing so and the ‘shoe-box’ people are still sending it all to the accountant. For these people there is no benefit, just an increase in costs. There may be a few farmers who weren’t keeping records and have been brought in line by the GST, but I suspect these are few and far between. The VB [shoebox] farmers, on the other hand, have increased costs but their knowledge about their business is no better.

Farmer and bookkeeper, Coolup, WA

Only a single respondent recorded a surprising decrease in accountancy fees following introduction of the GST. This was said to be the result of changing from a Sydney accountant to a locally based firm.
4 ATO Alterations to the BAS Form

Changes in the BAS were of concern to nearly all respondents.

The first two [BASs] were abominations of things but we got used to them. Then the b____s changed them, we got used to that and they changed them again! The critical thing would be to find a formula and stick to it. [The ATO] was the worst organisation to design the BAS form. Many of my clients still use the original version and that’s their choice.

Farmer and bookkeeper, Coolup, WA

A small minority (two respondents) suggest further changing the layout of the BAS— but back to the original version.

I think the new form that the ATO adopted is actually more confusing. It doesn't flow as easily as the older one did. The way the old BAS form was structured made it easier to find add up payments and calculate the GST. I think it would be simpler to go back to the old form.

Poultry farmer and small business accountant, Ellalong, NSW

Terminology used in the BAS was sometimes troublesome.

Keep things in English! I can't get my head around all the terms like "payee" and "payer". I have a hard enough time with "employee" and "employer." I don't use that sort of terminology in day-to-day life.

Farmer, Illabo, NSW

5 Other Commercial Decisions Based on New Tax Deadlines

It appears that non-tax entities may be basing unrealistic expectations on their customers’ compliance with GST accounting requirements. Small businesses are forced to adhere to the new standards for unrelated commercial reasons. One NSW farmer, for example, said that her bank now, for the first time, expected farm finances to be finalised in July.

The expectation now is that our tax is to be up-to-date to the minute. We wanted to borrow money for a truck in May and the bank wouldn't approve it until we had provided our yearly financial statements. The upshot of this is that we now can't borrow money at the 'wrong' time of year.

Farmer, Gogeldrie, NSW

6 Other Problems

The GST, for example, unequally treats economically equivalent credit arrangements for the acquisition of farm equipment, according to whether it is leased, hire-purchased or hypothecated. Lease and hire arrangements attract proportionally more GST than outright purchase subject to a chattel mortgage.
A NSW grazier recounted problems that he had experienced in dealing with the NSW Wheat Board. Transactions for the purchase of grain from local farmers in NSW are treated as loans until the grain is on-sold to a third party. Or again, on a smaller scale, another small business person was concerned about tax invoices issued on thermal paper which fades over time. ‘Who is responsible when the ATO audit me and find only blank pieces of paper?’

Farming respondents have said that the shape of the GST could have been improved through better consultation with farmers as a ‘grassroots level’:

What the tax office should have done was get a few of the real people from the bush to go through it with them. Then they would have been able to bring about reform in a more appropriate way and earn some mileage with the farming community.

Farmer, Lismore, NSW

There was also some discussion of the perceived new role of small business as being ‘unpaid tax collectors’ for the government. One farmer, in particular, resented what he called the ‘three month loan’ that he considered he was effectively making the ATO.

I’m still very cranky about that. It affects those of us who sell food, although, amazingly, the other growers I’ve spoken to don’t seem to be too upset about it. There’s been very little public comment on it—I’m surprised that the Opposition hasn’t got stuck into it. They seem to have missed it completely.

Farmer, Lismore, NSW

B Respondent Comments on the Benefits of GST Tax Reform

1 Decreased Time Costs of Tax Compliance

Only a small number of participants reported a significant decrease (over 20 hours) in the internal time costs of tax compliance since the introduction of the GST. One of them a Victorian farmer, attributed his reduction in time costs solely to tax reform.

Record keeping requirements are easy now that we have systems that are working and the benefits have been huge . . . I use the accounts system where I transfer the payments and receipts from my GST account directly to the last page. I find this easy and straightforward—many others fill in all of the boxes and if I had to do that I would find it a real chore and far more time consuming. I gratefully acknowledge the ATO's willingness to allow me to do this.

Farmer, Clunes, Victoria

2 Better Business Decisions

Tax reform had brought about significant managerial benefits for small business, in the view of some respondents.
My overall business is much stronger as a result of my improved knowledge—I spend more time at the computer inputting information which I then find myself inadvertently testing, analysing, making up ‘what if?’ scenarios, etc. We have recently gone through the process of applying for finance to allow our business to expand and have found the level of record keeping extremely beneficial. The fact that everything is up-to-date has made us very nimble—financiers like up-to-date cash flow statements and I can now provide them at the touch of a button. In general, I find the GST and STS combined a far more business friendly situation (given the benefits of compliance requirements) than the old system where I was one to largely leave the bookwork until a ‘rainy day’ in June.

Farmer, Clunes, Victoria

Because I have to kept the cashbook every three months (instead of once a year for four nights in January), I’m getting the benefit of the fact that all the receipts aren’t in a shoebox, they have to be on the computer. [My husband] also likes seeing in black and white how many cattle he’s sold, etc. You can see how much money has actually been made. Most of my friends are saying they’ve never been so organised.

Farmer's wife and bookkeeper, Barraba, NSW

Because of the decision I made to put in the scanning system [directly attributable] to tax reform, I am now getting so much more information.

Mini-mart owner, Margate, WA

All bar one of the respondents who acknowledged a managerial benefit in GST tax reform, were unable to quantify the benefit in dollar terms. The exception was a small business retailer who reported savings for his business in the vicinity of $100 000. Respondents not experiencing any personal benefits pointed to benefits enjoyed by other local businesses or their clients:

I’m very aware of the fact that it [taxation reform] has helped a lot of micro-businesses. For example, a lot of hairdressers [in our area] took up or upgraded computer systems as a result of the GST. Instead of being just a booking system, it became a financial system. This has improved efficiency in a lot of the salons.

Association Management, Hobart, Tasmania

C Participant Suggestions for Reducing GST Compliance Costs

1 Extension of BAS Deadlines

Several respondents saw the need for greater flexibility in BAS deadlines.

Reconciliation of the BAS is particularly difficult towards the end of the financial year. Not only do you have the end of the financial year where you have to do stocktake and so on, but in Darwin we also have our four-week school holidays because that’s our good weather season. An extra two weeks here would be sufficient.

Accountant, Darwin, NT
Twenty-eight-day deadlines are too tight, particularly with deadlines falling during school holidays or if a clerk or bookkeeper is on leave.

Farmer, Coolup, WA

Postponement of the BAS until after all credit statements had been received was a common practice. This often resulted in tight deadlines. In the words of one small business accountant:

If we had until the fifth of the following month, it would make all the difference.

Accountant, Darwin, NT

Farmers filing BAS statements from remote areas contended with the problems of limited postal access.

Postal delivery to our region [Pinjarra, WA] is once a week and many farmers have little or no access to the Internet. Twenty-eight days is too tight a deadline.

Farmer, Coolup, WA

Farmers noted difficulties with filing BAS statements when deadlines conflicted with seasonal activities such as grain harvesting in January or shearing in April. A farmer from Clunes, Victoria suggested that taxpayers individually should be able to negotiate different quarterly arrangements with the ATO, so as to lessen compliance requirements in months of seasonal high activity.

2 Need for a Comprehensive GST Base

Almost all respondents expressed a preference for a GST without exemptions. However, there was also acknowledgment of the difficulties that a regressive consumption tax would cause disadvantaged Australians.

There would need to be compensation for people on lower-incomes and this would need to be immediate. But it would be the best outcome for small businesses.

Shop-owner, Myaree, WA

3 The Ability to Self-Correct Errors in BAS Statements

Taxpayer errors in the BAS were a headache for several participants. One NSW farmer took exception to the fact, as he put it, that the ATO would always contact him when he was a couple of dollars out in his BAS:

Most of the time it’s just my computer rounding things up to the highest decimal. I really think they could be focussing on more important things!

Farmer, Illabo, NSW

There should be an option to correct small errors (under $100) on the BAS form. Perhaps a box to tick to show adjustment of a previous BAS. You shouldn't need to ring the tax office for every small error.

Artist, Langwarrin, Victoria
4 Continuing the Presence of Field Officers

Two respondents advocated more individual assistance to small businesses. A larger number of ATO field officers would assist in educating small businesses about easier systems available to them, for example, the STS.

There needs to be greater face-to-face assistance for small businesses from the ATO. Perhaps a resurgence of the role of the [ATO] field officers. I think parliament overestimated the ability of small businesses to handle reforms. Not in an intellectual sense but in the amount of time small business have and their priorities.

Association Manager, Hobart, Tasmania

One NSW farmer, who remained in contact with one of the ATO field officers, commented on the benefits of ongoing advice:

I phoned her up the other day to find out about the rules and regulations with lime marketing—I wanted to ask her how best to grapple with a particular problem—and once again, she was very helpful. The ATO has gems scattered with people like this [sic] and they are worth their weight in gold.

Farmer, Lismore, NSW

Other suggestions included: freepost envelopes (Artist, Langwarrin, Victoria); more people manning the ATO Hotline, ‘It takes far too long to speak to them—I’m better off ringing my accountant’, (Farmer, Glen Innes, NSW); and an improved ATO website, ‘It’s hard to find the information you need’ (Farmer, Illabo, NSW).

A final point was made by a retailer who ran a convenience store in Western Australia. He suggested the inclusion of manufacturer-inserted barcodes onto the packaging of retail items—to signal whether or not an item was subject to GST.

V QUANTITATIVE FINDINGS

A Participants’ Business Profile

Twenty-two participants sent back their completed questionnaires and/or were interviewed. Their business profile is summarised in Table 1.
Table 1: Participants’ business profile

<table>
<thead>
<tr>
<th>Attribute</th>
<th>Summary Statistics</th>
</tr>
</thead>
<tbody>
<tr>
<td>Legal form</td>
<td>Sole trader: 5, Partnership: 10, Companies: 5, Trusts: 2</td>
</tr>
<tr>
<td>Location of business</td>
<td>NSW: 8, VIC: 8, QLD: 1, WA: 2, TAS: 1, ACT: 1, NT: 1</td>
</tr>
<tr>
<td>Main business activity</td>
<td>Primary: 12, Secondary: 2, Service: 8</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Attribute</th>
<th>Min</th>
<th>Max</th>
<th>Mean</th>
<th>Median</th>
</tr>
</thead>
<tbody>
<tr>
<td>2000–01 Turnover ($)</td>
<td>5950</td>
<td>1500000</td>
<td>414425</td>
<td>296000</td>
</tr>
<tr>
<td>Estimated taxable income ($)</td>
<td>0</td>
<td>190000</td>
<td>55128</td>
<td>45000</td>
</tr>
<tr>
<td>Number of owners/partners/</td>
<td>1</td>
<td>2</td>
<td>1.68</td>
<td>2</td>
</tr>
<tr>
<td>directors/trustees</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Number of employees/contractors</td>
<td>0</td>
<td>20</td>
<td>3.50</td>
<td>2</td>
</tr>
<tr>
<td>Number of unpaid helpers</td>
<td>0</td>
<td>3</td>
<td>0.27</td>
<td>0</td>
</tr>
</tbody>
</table>

Source: Authors’ own survey.

B Participants’ Accounting and Taxation Profile

All 22 participants were registered for GST. Among them, 14 (64 per cent) submitted BASs only and the remaining 8 (36 per cent) submitted both BAS and Instalment Activity Statements (IASs). It is found that 20 (91 per cent) of participants submitted their BASs/IASs quarterly and 2 (9 per cent) submitted monthly.

As expected, most of the participants (20 out of 22 or 91 per cent) used a cash accounting system. As far as the use of business financial statements is concerned, more participants considered tax requirements as the most important use of financial statements than other reasons, as indicated in Table 2.

Table 2: Ranking of use of financial statements*

<table>
<thead>
<tr>
<th></th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tax requirements</td>
<td>12</td>
<td>7</td>
<td>2</td>
<td>0</td>
</tr>
<tr>
<td>Managerial decision making</td>
<td>8</td>
<td>11</td>
<td>2</td>
<td>0</td>
</tr>
<tr>
<td>Use by banks, lenders, etc</td>
<td>3</td>
<td>3</td>
<td>17</td>
<td>0</td>
</tr>
<tr>
<td>Other</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>21</td>
</tr>
</tbody>
</table>

Source: Authors’ own survey.

Notes:
* 1 is most important and 4 is least important
One participant ranked all four uses equally and was deleted from Table 2.

Table 2 appears to support the conventional wisdom that most small businesses produce financial statements mainly to satisfy their tax requirements. However, the very high ranking of managerial decision making serves to reinforce the difficulty of the accounting-tax overlap debate in tax compliance cost studies.
C Estimates of Participants’ Recurrent Costs/Benefits

The case study approach described in Section 3 yields information on time spent on business tax affairs, fees paid to professional tax advisers, and computer-related costs for 2001–02 and 2002–03. In order to generate estimates of recurrent gross and net business transitional costs, some further information/assumptions are required:

- The external adviser, computer-related and other costs relating to GST compliance are deduced by multiplying the respective external adviser, computer-related and other compliance costs of all taxes by the proportion of time spent on GST over time spent on all taxes;
- Time valuation: to value time, we use the hourly wage rates obtained from the 1997 ATAX study, adjusting for inflation. For small businesses, these rates are $33, $30, $20 and $15 for owners, managers, clerks and unpaid helpers, respectively.
- Marginal tax rate: the marginal tax rate varies depending on the legal form and taxable income of business.
- To calculate cash flow benefits, we assume average cash-flow benefit periods of 5 and 10.5 weeks for monthly and quarterly BAS submission, respectively. The interest is conveniently assumed to be 7 per cent per annum.

The data obtained from the study is combined with the information/assumptions above to generate gross and net participants’ recurrent costs as a result of the GST-based tax reform. These results are summarised in Table 3.

Table 3: Estimates of participants’ annual recurrent GST compliance costs

<table>
<thead>
<tr>
<th>Component</th>
<th>Min</th>
<th>Max</th>
<th>Mean</th>
<th>Median</th>
</tr>
</thead>
<tbody>
<tr>
<td>External adviser costs ($)</td>
<td>0</td>
<td>3327</td>
<td>859</td>
<td>569</td>
</tr>
<tr>
<td>Internal wage costs ($)</td>
<td>0</td>
<td>1080</td>
<td>148</td>
<td>0</td>
</tr>
<tr>
<td>Value of time loss ($)</td>
<td>0</td>
<td>5940</td>
<td>1201</td>
<td>726</td>
</tr>
<tr>
<td>Computer-related costs</td>
<td>0</td>
<td>1006</td>
<td>105</td>
<td>0</td>
</tr>
<tr>
<td>Other costs</td>
<td>0</td>
<td>1215</td>
<td>167</td>
<td>56</td>
</tr>
<tr>
<td>Gross recurrent costs ($)</td>
<td>0</td>
<td>7856</td>
<td>2481</td>
<td>2443</td>
</tr>
<tr>
<td>Tax deductibility benefits</td>
<td></td>
<td></td>
<td></td>
<td>744</td>
</tr>
<tr>
<td>Cash flow benefits</td>
<td></td>
<td></td>
<td></td>
<td>493</td>
</tr>
<tr>
<td><strong>Net recurrent costs ($)</strong></td>
<td>0</td>
<td></td>
<td></td>
<td>1244</td>
</tr>
</tbody>
</table>

Source: Authors’ own survey

Notes:
- Internal wages costs refer to wages paid to employees including managers, accountants, programmers and clerks.
- Value of time loss refers to the opportunity costs of time spent by owners/partners/directors/trustees and unpaid helpers.
- Preliminary only.
- Totals may not add up due to rounding off.

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The recurrent costs in Table 3 ($2481 (mean) and $2443 (median)) are much smaller than the transitional costs found in an earlier phase of the project ($7673 (mean) and $4500 (median)). Nevertheless, the average gross recurrent costs of the GST are still quite high to small businesses, suggesting that these costs still include some elements of transitional costs. This is consistent with the qualitative finding that some small businesses are still having transitional difficulties with the GST. In other words, the GST system has not fully bedded down and it will take several more years to gain a more accurate measure of GST recurrent costs.

The break down of participants’ mean gross recurrent costs is presented in Table 4.

**Table 4: Distribution of participants’ mean gross recurrent compliance costs**

<table>
<thead>
<tr>
<th>Component</th>
<th>% of total</th>
</tr>
</thead>
<tbody>
<tr>
<td>External adviser costs</td>
<td>35</td>
</tr>
<tr>
<td>Internal wages</td>
<td>6</td>
</tr>
<tr>
<td>Value of time lost</td>
<td>48</td>
</tr>
<tr>
<td>Computer-related costs</td>
<td>4</td>
</tr>
<tr>
<td>Other costs</td>
<td>7</td>
</tr>
<tr>
<td>Gross recurrent compliance costs</td>
<td>100</td>
</tr>
</tbody>
</table>

Source: Table 3.

As expected, the value of time lost was the most important single category of cost, accounting for about 48 per cent of the total costs. Somewhat surprisingly, the costs of computer and other equipment represented the least important (4 per cent).

**VI COMPARISONS WITH PREVIOUS STUDIES**

It is important to bear in mind that, for a variety of reasons, strict comparisons between the results here with those obtained in previous studies may not be valid. An obvious reason is that the results obtained here are based on a small number of case studies and cannot be extrapolated to the entire economy.

_A Australian Studies_

To the best of our knowledge, apart from this study, there are no current researches in recurrent compliance costs of the GST in Australia. It is perhaps too premature to conduct a large-scale mail survey for such a study. In the absence of comparable information and in view of the government’s claim about the simplicity of ANTS, it is perhaps worthwhile to compare the recurrent compliance costs of the now abolished WST and the GST. For tax policy purposes, the appropriate concept is gross compliance costs.

In a major study of the compliance costs of the Australian federal tax system by large-scale surveys, an ATAX team lead by Chris Evans estimated the gross compliance costs of the WST to be $737 million in 1994–95.\(^{28}\) Using an annual cost inflation rate...
of 5 per cent, the estimate of the gross WST compliance costs would be $1089 million in 2002–03. In its Impact Regulation Statement accompanying the ANTS Bills, the government estimated the net compliance costs of the state taxes to be abolished at about $220 million to businesses in 2001–02. Assuming that tax deductibility and cash flow benefits are worth half of that total, the gross recurrent compliance costs of the repealed state taxes would be about $330 million. This is a very plausible estimate because the estimated compliance costs– revenue ratio for state taxes (to be abolished) is similar to that of the WST. Adjusting for 5 per cent annual inflation, the compliance costs of abolished state taxes would translate to about $346 million in 2001–02. Adding the two corresponding figures together, the repeal of the WST and some state taxes would have saved the Australian economy about $1435 million in 2002–03.

There are about 1 million separate businesses in Australia corresponding to about 2 million GST registered businesses. If we are willing to extrapolate on the basis of the average gross recurrent compliance costs in Table 3, the gross recurrent compliance costs of the GST in Australia would easily exceed $2500 million in 2002–03. This figure is at least $1 billion more than the corresponding compliance costs of the abolished WST and State taxes. However, it should be born in mind that the WST only involved about 75,000 large firms. So $1.089 billion of costs in the aggregate means an average cost of about $14,520 per WST registrant. In short, the compliance burden under ANTS is now greater than before reform but it spreads much more widely, that is, ANTS is burden-broadening.

B International Studies on GST and VAT

1 New Zealand Experience

A major and authoritative study of the compliance costs associated with business taxes including the GST in New Zealand by Sandford and Hasseldine was published in 1992. Using the mail questionnaire approach and based on a sample of 2700 respondents, Sandford and Hasseldine estimated the total, gross compliance costs of the GST to be NZ$453 million or 7.3 per cent of GST net revenue in 1990–91. This translated to an average annual gross compliance cost of about NZ$1290 (= $452,957,000/351,236) in 1990–91. Since the GST was first introduced in NZ in 1986, it seems reasonable to take this estimate as representing recurrent compliance costs only. Assuming that compliance costs grow by 5 per cent per annum, this would give rise to an average cost of NZ$2317 in 2002–03. Using average weekly earnings (AWE) data for New Zealand and Australia, it is found that for the period 1991–98, NZ$1 labour cost in New Zealand translated to A$0.8842 in Australia. Based on this relative wage information, an estimate of recurrent GST compliance costs of $2048 per firm is

31 Statistics New Zealand, Key Statistics, various issues, ABS Statistics New Zealand, Wellington; and Key Statistics and Year Book, Australia, (1991–99), ABS Canberra. The Australian data refers to total AWE of all employees (full-time and part-time) while it is not clear whether the New Zealand data refers to total AWE of all employees or full-time employees only.
obtained for Australia in 2002–03. Considering that the estimate of recurrent compliance costs in Table 3 still contains some transitional elements, there is a broad agreement between the New Zealand study and the present study.

2 UK Experience

The Bath mail-survey study led by Sandford estimated that, in 1986–87, the compliance costs of the UK Value Added Tax (VAT) were about £791 million, accounting for 3.7 per cent of VAT collected (£21.4 billion). This compliance costs/revenue ratio appears to be much lower than the same ratio in Australia now. A possible reason is that VAT in 1986–87 was an ‘old’ tax in the UK, so all transitional issues had been resolved. The GST in Australia in 2002–03 was a still a very young tax and many GST registered taxpayers are still on their learning curves.

3 The Canadian Experience

In 1992 Plamondon & Associate was commissioned by the Department of Finance to undertake a study of the GST compliance costs for small business in Canada. Utilising the interview approach and based on a sample of 200 participants, Plamondon & Associate derived surprisingly low estimates, ranging from Can$219 (for business with turnover below Can$100 000) to Can$17 659 (for business with turnover from Can$500 000 to $999 000) in 1992. The gross compliance costs relative to GST collected were all below 1 per cent for different business sizes. These estimates were too low and incompatible with the results obtained in other countries. This may have arisen as a result of differences in research methodology, in particular the question of how to allocate overall compliance costs to different tax types.

VII SUMMARY CONCLUSION

Australia entered the twenty-first century with a substantially reformed indirect tax system. Prior to the replacement of the WST and some state taxes by the GST on 1 July 2000, there had been a heated debate about the desirability or otherwise of the GST. The community of tax academics and tax experts was divided with strong support both for and against the GST-based tax reform. However, despite the federal government’s assurance of its concern for tax simplification, replacement of the WST by the GST substantially raised operating costs, especially tax compliance costs, for Australian small business.

The findings of an ongoing case study sponsored by the ARC with participation from the NFF, COSBOA and TA are as follows. On average, based on 22 case studies, small business incurred gross recurrent costs of $2481 (mean) or $2443 (median). These are much smaller than their corresponding transitional costs of $7673 (mean) and $4500 (median). Subtracting tax deductibility and cash-flow benefits, the net recurrent compliance costs of the GST for small business was estimated to be $1244 on average.

32 Above n 23, 75.
34 Above n 2, 131–52.
The main category of transitional costs was value of time lost, followed by external adviser costs.

In addition to monetary costs, small business taxpayers also appeared to suffer some psychological costs. Broadly speaking, it may be concluded that:

- Small business, especially the farm sector, has not fully come to grips with the GST on a day-to-day basis. Transitional issues still exist.
- Current estimates of the GST recurrent costs are on the high side but should decline over time as business becomes more familiar with it.
- The ATO should consider implementing some of the suggestions from respondents of this study in order to make the GST friendlier to small businesses in their capacity as tax collectors.