Why The Left Should Back A GST Rise

28 June 2013

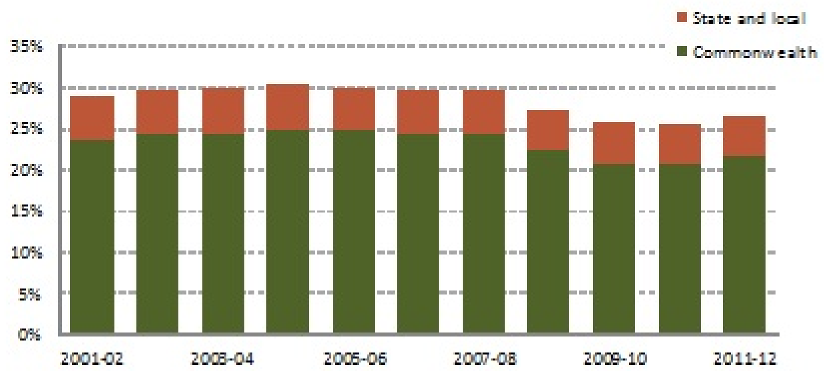
The states need cash and a GST increase might be the best way to do it. Could Kevin Rudd pull off the politically distasteful? Ian McAuley makes the case

Kevin Rudd is back, and, as Bernard Keane wrote in Crikey this week, he has a clean slate when it comes to policy. Building on the big-ticket policy items set up by Julia Gillard, Rudd might have the opportunity to work on a few neglected areas, either before the election or, should he win it, during his second tilt at the prime ministership.

One such neglected issue is taxation – the very issue that got Rudd into hot water in the first place. Tony Abbott and shock-jock journalists have successfully conveyed the impression that our taxes are high: two-thirds of people surveyed by the Australia Institute believe that Australia is a "high tax" country, while only 2 per cent correctly identify Australia as having almost the lowest taxes among the 30 countries in the OECD.

In fact, an analysis of ABS taxation statistics shows that Australian taxes have fallen sharply from their peak in 2004-05, when the Howard government was enjoying a boom spurred by rapidly rising commodity prices and a property boom. In that year our taxes – Commonwealth, state and local – reached 30.3 per cent of GDP, before falling to 25.6 per cent of GDP in 2001-11 and only slowly creeping up since. (See Figure 1 below.)

Figure 1: Australian taxes as % of GDP

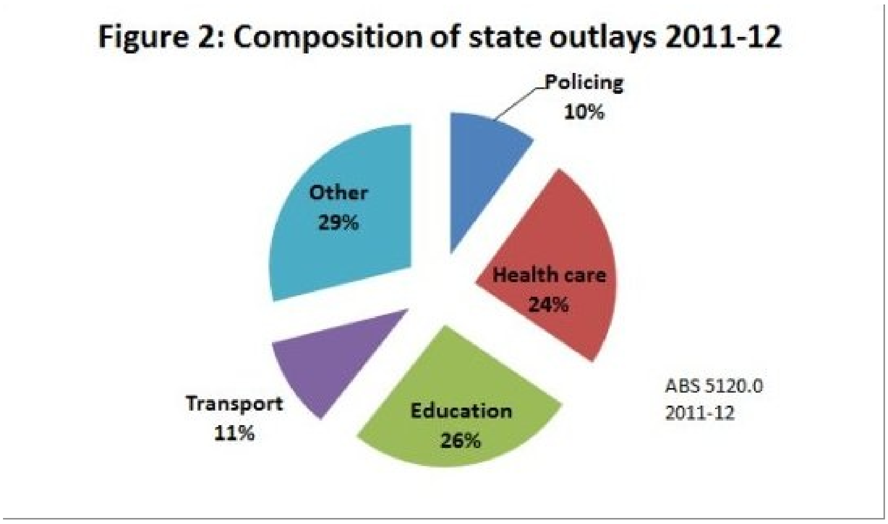


Had Wayne Swan enjoyed the taxation revenue that flowed into Costello's coffers, the Commonwealth Budget would have had an extra $197 billion in revenue over the four years to June 2012 – enough to fund the NBN, the Pacific Highway and an east coast fast train, with some left over, and with no net debt (assuming those assets remained on the Commonwealth balance sheet). Perhaps Chris Bowen will be luckier, although it seems unlikely.

While Commonwealth revenues have suffered, so too have state and local revenues. By the same calculation as I have used for the Commonwealth, state governments lost $22 billion over that period from their own tax bases, and they lost another $24 billion in GST revenue – money which is collected by the Commonwealth, but passed through to the states.

That's why state premiers are crying poor, and why, apart from Campbell Newman's intransigence and the usual squabbling, are attracted to the Gonski reforms. When there is money on offer they care little about the partisan alignment of the Canberra government.

In general, state governments survive or fall on the quality of their services. Health care and education absorb half of all state expenditure and policing takes another 10 per cent (see Figure 2). These are all skill-intensive services, for which labour costs are a major part of expenditure. It may be convenient for some on the left to condemn the hard line state governments are taking towards nurses and teachers, but that hard line is more a fiscal imperative than an ideological stance. (Again, Queensland must be excused from assumptions of fiscal rationality.)



There are rumblings from state premiers about their share of GST funding, particularly from Western Australia which, because of its potential to raise royalty income, gets a much lower share of funding than other states. The Grants Commission recommendations for the coming year (which the Commonwealth usually follows) are for Western Australia to get back only 45 cents per dollar of GST collected, while at the other extreme the Northern Territory will get $5.31 per dollar collected and Tasmania $1.61.

Redistributing GST away from the Grants Commission formulae would be politically difficult, particularly in view of the fact that Tasmania has the same Senate representation as larger states, and it has a number of swinging House of Representative seats.

And it's hard to imagine that GST revenue will come back to its earlier levels. When the Howard government introduced the GST in 2000, it was definitely a "growth tax". Incomes were rising, and people were running down their savings, particularly by borrowing against rising house prices. It was a boom period, but that boom ended in 2008.

Although real incomes are still rising, people have become more cautious about going into debt – the GFC and stabilising house prices have had a sobering effect. Some items exempt from GST, particularly health care and education, have been subject to relatively high price rises, and this has meant less expenditure on items on which GST is levied. And, to the marketers' chagrin, there is emerging among many young people what the advertisers call a "post materialist" lifestyle. For many, shopping is losing its attraction.

An Abbott government is already considering increasing the rate of GST. Julia Gillard's predictable response was to prepare to launch a scare campaign. But there are a few reasons why progressives might support an increase to the GST.

The textbook economic wisdom is that consumption taxes are more regressive than other forms of tax, particularly income tax. The better-off devote a larger share of income to saving and a lower share to consumption. That means consumption taxes take proportionately more from a household with low income than from a household with high income. That is no mere abstract theory. Australia's GST is regressive, even allowing for exemption of most food and health care.

But the GST is much harder to avoid than other taxes, and, apart from local government rates, it is virtually the only tax collected from wealthy "self-funded" retirees, thanks to the undeserved breaks granted in Costello's final budget, which have been so hard for the present government to wind back.

There is also a case for abolishing or paring back certain exemptions. As incomes have risen across the board, food is taking a smaller share of our expenditure: in 1988-89 food took 18.1 per cent of household expenditure; in 2009-10 that was down to 16.5 per cent. The same reduction in food's prominence has happened in all income bands. There is also a good case for applying GST to private health insurance to arrest its uptake, before it inflicts more damage on our public hospitals. After all, other insurers are subject to GST.

Most importantly, GST goes to state governments, who provide those services which form the most important part of the "social wage", particularly health, education, transport and public housing, which all have redistributive benefits as well as a strengthening of our social and human capital. States don't squander money on military equipment or on middle-class welfare. And they have no incentive to subsidise private health insurers to suck resources out of public hospitals.

A higher or more inclusive GST is not the only way to improve state revenues. But the general point is that there are political and constitutional imperatives for the states to be responsive to people's needs. If Abbott pitches a rise, perhaps Rudd could show leadership; instead of beating up a GST increase as a bogeyman, he could sell it as an antidote to the neoliberal sell-off of public services. A rise may not be politically popular, but it may be necessary.