THE GST : A TAX IN NOBODY'S INTEREST

Address by Gareth Evans, Deputy Opposition Leader and Shadow Treasurer, to NCOSS Seminar, *Tax Reform: In Whose Interest?*, Sydney, 30 July 1998.

ACOSS President Michael Raper has in the past 24 hours expressed doubts about the welfare lobby's capacity to support the Coalition's GST, but he is also saying that ACOSS will defer a verdict until all the detail is on the table, and signalling that any opposition would not be as fierce as it was in 1993.

Let me say very directly to him that on all the evidence we now have about the shape of the GST the Coalition is determined to impose, it's time for ACOSS and its constituent bodies to abandon once and for all their dalliance with the Government on this issue. The needs of lower income, needy and disadvantaged Australians - can only be served by opposing outright the Coalition's proposal.

While some of the detail remains to be filled in, assiduous Government leaking in the last few days has made it clear that what is proposed is a 10 per cent GST, taxing for the time all the basic necessities of life - food, clothing and shelter - and a huge range of other goods and services as well; with exclusions confined to health, education and some community services. The adverse impact of all of this supposedly to be compensated by a miscellany of personal income tax cuts and other measures, some to be paid for by GST proceeds and others from the budget surplus.

How does all this stand up against ACOSS's five-point "Equity Test" which was the central theme of its *Agenda for Tax Reform*, released last month? Let's look at each of these points in turn:

1. Consumption tax changes must be part of a comprehensive and progressive package which includes substantial income tax reform to close unfair tax loopholes and shelters.

It is reasonable to assume that Coalition action on closing income tax loopholes will be minimal and most, if not all, of the other specific recommendations of ACOSS to broaden the direct tax base seem likely to be ignored. It seems likely that there will be some action taken to align company and trust tax rates - but this is one of only *nine* measures to deal with the use and abuse of discretionary trusts, in particular by high wealth individuals, that the ATO has recommended to government. Action on all but one of these has been completely stalled since Peter Costello has been Treasurer, and there is no reason to believe things will change.

2. There must be no increase in the proportion of public revenue derived from consumption tax as a result of the changes.

It is difficult to see that the GST will do anything *other* than to raise the proportion of public revenue derived from consumption taxes. At the rate, and with the exclusions, proposed, the GST will raise much more revenue than that necessary to replace the existing Wholesale Sales Tax and State financial duties, and to make fuel excise cuts of the order suggested. At the same time there is no suggestion that the share of revenue derived from income tax will rise: with the tax cut election bribes proposed in this area, the contrary will probably be the case.

3. Consumption tax changes must not increase the average cost of living for low income people so as to leave them substantially reliant on "compensation measures" to maintain their living standards.

This principle will obviously be breached. The GST will unquestionably increase the cost of living for low income people. The welfare groups themselves tell us that food makes up around 40 per cent of low income household budgets, and food will certainly now be taxed. Clothing will be taxed. Rent, which takes up another third, on average, of low income family budgets, will also be hit by the GST: even if rent is declared technically "exempt", landlords will still be subject to GST on the council rates that they pay, and on the fixtures and fittings and maintenance they provide, and all of that will in practice be passed straight on to tenants.

Add to that all the other chemists' and other goods that will be taxed for the first time; add to that all the basic services that will taxed for the first time - like phone calls, and gas and electricity bills, and train and bus fares, and trips to the footy and the movies; and you have a horror story for low income earners.

They will *certainly* depend on compensation measures. But no-one can be sure these will deal adequately with any or all cases to begin with - given, among other things, the differences between people's ages, health, gender and location. And absolutely no-one can guarantee that, whatever may be the situation at the outset, compensation will *stay* adequate in the future. It certainly hasn't in New Zealand and elsewhere.

With John Howard's promise - both before and after the last election - that he would "never ever" introduce a GST at all, why should anyone trust him when he says he won't change the rate. And why should anyone trust him that compensation for those hurt by a GST will be both adequate and sustained over time?

4. Access to social and community services which are essential to the well-being of people on low incomes must not be restricted by consumption tax changes.

It's not clear what community services, other than child care, and possibly some aged care, will be completely excluded from the operation of a GST by being zero-rated. Certainly access to community and social services will not be improved by the GST, even if they are zero-rated. At best we can expect no change in this area; at worst there will be a detrimental impact.

The Lord Mayor of Brisbane yesterday pointed out just how many basic services - apart from those covered by rate bills - are provided these days by Councils on a fee-for-service basis, including sporting ground hire and swimming pool access and dog registration systems and cemetery plots. I don't think anyone has suggested that *these* community services will be zero-rated, and they will all become more expensive for ordinary families as a result.

5. There must be a firm and enforceable legislative guarantee that tax rates on consumption will not increase, at least in the medium term.

As ACOSS has itself now acknowledged, there is absolutely no way the rate of a GST can be guaranteed not to rise, short of incorporating it by referendum in the Constitution. No Australian Parliament can bind its successors. A law can be made by the Commonwealth Parliament which says, as the Coalition is , that a particular rate can only be increased if all the States agree. But that law can itself be repealed or amended by the Commonwealth Parliament at any time, without any reference at all to what the States think!

Governments all round the world have cheerfully ignored promises, express or implied at the time of the GST's introduction, not to raise the rate. For example, it's gone in New Zealand from 10 to 121/2 per cent, in the UK from 10 to 171/2 per cent, and in Denmark from 10 to a whopping 25 per cent!

If the overall tax take stays as it is, the results of introducing a GST will simply be to transfer a large chunk of the revenue-raising burden from business to households. Shifting the tax burden from business to households is not an achievement that the leadership of ACOSS should want to have engraved on its collective epitaph. Of course that shift is what makes business, or at least big business (which doesn't have to worry about compliance costs) such a big booster of a GST - although the Business Coalition is starting to look more and more frayed around the edges these days, with, for example, the Housing Industry Association abandoning ship, the publishing and book-selling industries strongly opposed to a GST, the insurance sector unhappy, and the tourism and hospitality industry very deeply worried by what is happening.

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There are those, of course, who claim that whatever the weakness of the *equity* arguments for a GST, it does have some significant benefits for the economy as a whole to which we all - not just the business community - should be duly sensitive.

But the *economic* arguments against a GST are just as compelling as the equity ones, as Peter Costello frankly acknowledged not so long ago when he called a GST "snake oil":

> - First, on jobs and growth: there is no causal link that can credibly be identified between the existence of a GST and lower unemployment. The US, whose experience has been quoted much less often by the Coalition than Swaziland's, is the healthiest economy in the world, but doesn't have a GST. The most compelling consideration for Australia at the

moment is that a GST is a job killer, in that it is bound to directly discourage job creation in the services sector, where most of our hope for rapid future employment growth lies.

- Secondly, on savings, we have Treasury Secretary Ted Evans's word for it that while every economic text book may tell you that shifting the burden towards indirect tax will significantly aid national saving, you won't find that convincingly demonstrated in studies of international economic experience.

- Thirdly, on inflation, we have the word last year of Associate Professor Neil Warren who the Prime Minister, rightly, said in Parliament recently was one of the greatest tax experts in the country - that a 10 per cent GST with a comprehensive base would add 5.6 per cent to the CPI! At a time of looming major current account deficit problems this is hardly the time to be contemplating a major new source of inflationary pressure.

- Fourthly, on exports, we have the 1995 researcher Matthew Ryan - the Treasurer's former senior adviser and now number two on his taskforce - concluding that there is essentially no trade effect in moving to a destination-based tax like the GST from origin-based taxes which are embedded in export prices. And you have the reality that a WST adds only a little over one per cent in costs to our $110 billion in annual exports - not the $5 billion that the Prime Minister asserted recently in Parliament. Payroll tax is more significant, but the Coalition - in apparent collusion with the States on this issue - is not proposing to touch that.

- Fifthly, there is no credible basis on which one can assert that a GST will ensure better taxation of the black economy. Again there is no overseas experience which helps the argument for a GST, and plenty - like Canada's - which serves to undermine it. The better view is that whatever may be picked up by people now in the black economy making taxable purchases outside it, this is more than outweighed by new transactions - particularly in the personal and household services area - moving *into* the black.

- Sixthly, there is the disproportionate burden in compliance costs born by small business with the introduction of a GST. Not only will there be over a million new unpaid tax collection points, but the OECD estimates the relative compliance burden at up to 30 times greater than that for big business. Even relatively modest dollar costs - although they have been estimated as high at $7,000 per annum for the average small business by the National Tax and Accountants Association - really mean something to small business on very narrow profit margins.

- The seventh deadly economic sin involved in a GST, and by no means the least, is simply that it may all be a waste of time, in the sense that at the very time the argument is raging most fiercely, indirect taxes of this kind may be on their way to obsolescence. The OECD has recently published a paper concluding that "improvements in electronic commerce are likely to make the base for consumption taxes, such as the VAT or sales taxes, more geographically mobile and harder to trace".

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But what of the question of *revenue adequacy*, of which ACOSS has from the outset made so much? Is it the case that, however much we might be sceptical or scathing about its economic utility, and concerned about its equity impact, nonetheless government will just *need* to tax services in the future if it is to sustain an adequate revenue base for expenditure on social security, health, education and lots of other public goods?

The Labor Party is of course concerned to ensure the adequacy of our revenue base - just as much as we are concerned with tax equity and efficiency issues - but we don't buy the argument that this base is in any trouble now or for the foreseeable future.

This year's Budget Papers [Table D2 page 2-71] show that Commonwealth tax receipts are totally stable over the whole forward estimates period. Last year the Commonwealth collected 24.1 per cent of GDP as taxes; this year the figure is budgeted at 24.0 per cent, then at 23.9 per cent in the following year, increasing back to 24 per cent in 2001-02 and 24.1 per cent in 2002-03.

Rather than painting a picture of a rapidly crumbling tax base, this shows the real situation - namely that the current tax base is adequate and will continue to be adequate, without any discretionary broadening of the base, as far as projections are published into the future. The argument that the current base is not sustainable is comprehensively rebutted by this data.

On the specific question of the adequacy of indirect tax base, and the wholesale sales tax in particular, what does the evidence show? Budget Paper No. 1 [Table 7 on page 5-14] shows that the total "other tax" to be collected over the forward estimates is estimated at 6.1 per cent of GDP this year, 6 per cent next year and 5.9 per cent for the succeeding years. This is hardly evidence of a collapse in revenue, and simply reinforces Labor's point that there is no need for an unfair new tax base which will hurt ordinary Australians.

All of this is, moreover, in the context of an underlying budget surplus, which Labor was just as keen as the Coalition to achieve (and would have achieved over the last two and a half years with much less pain - but that's another story). So not only do we have a stable and adequate tax base, but we also are in the relatively rare position of raising adequate revenue to finance the projected spending programs of government.

It is worth adding, so far as the other governments in our Federation are concerned, that the national fiscal outlook document prepared for the Premiers' Conference tells us that the aggregate State/Territory sector is in fiscal balance over the forward estimates period without any change in its taxation base.

The other obvious point to make about the contribution of a GST to maintaining an adequate revenue base is that if it is indeed the case that, as the OECD and lots of other have suggested, electronic commerce is rapidly making all forms of indirect tax collection obsolescent, this is an extraordinary time to be arguing, when your primary object is to protect the revenue, for greater reliance on a consumption tax.

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The tax debate is of course not just about the virtues and vices of a GST. It's about a proper overall regime for *business taxation*, and specific measures and incentives in that area, about which we will have a good deal to say in our own tax package when it is released. And it's certainly about making the present *personal income tax* system work more efficiently and fairly. ACOSS is right when it says, as it did in last month's statement, that the main task in tax reform is the repair of the income tax base. And it's right to call for the removal of poverty traps confronting ordinary families.

Labor believes that the personal income tax system needs to be improved in four main ways. As I've said many times already, we won't be drawn into a demeaning tax auction at the next election, trying to outdo the Coalition with bigger and glitzier tax cut bribes, while leaving the Australian community with more and more inadequate services. But we will take action where it's needed, and give help where it's needed.

First, we do need to address - and will address through our proposed Tax Credit for Working Families - the problem of very high effective marginal tax rates being paid by low to middle-income earners as a result of the interaction of present tax and social security scales, which involve significant poverty traps and disincentives to work. Many families are keeping less than 20 cents of every extra dollar they earn, losing over 30 cents in tax and 50 cents in family payments. Our tax credit will be directly linked to earned family income and number of children; it will be generous; it will reward people who work; and it will encourage people to move from welfare to work.

Secondly, we need to ensure that average weekly earners do not, as a result of bracket creep, pay higher marginal tax rates than they should. Throughout our term in office we made many targeted changes to the tax scales to address the bracket creep problem; if we hadn't, we'd be collecting $30 billion more revenue today! Despite the Treasurer's repeated claims to this effect, *nobody* is about to pay one dollar in two in tax: not even honest multi-millionaires pay that. But Average Weekly Ordinary Time Earnings will shortly cross the $38,000 threshold, which means a marginal tax rate of 43 per cent, and that is unacceptably high for this group.

Thirdly, we need to address the erosion of the PAYE system by people who essentially remain employees establishing themselves as independent contractors, often now in the legal guise of trusts, companies, or partnerships. This is partly a matter of better compliance with existing law, but some further legislative changes will be necessary to ensure equal tax treatment of those doing for all practical purposes identical jobs.

Fourthly, there is a need yet again to seriously address the problem of tax avoidance, especially by high wealth individuals through discretionary family trusts like those used by Senator Parer and so many of the Coalition front and back bench, and its financial supporters. Last month, for example, I announced that we would implement in government six of the specific legislative proposals recommended to the Government by the ATO, which I referred to earlier, and on which the Coalition has taken no action whatsoever. This should go a long way toward solving the trust misuse problem, and collecting the many hundreds of millions of dollars annually which the Tax Office estimates as being recoverable just from Australia's one hundred wealthiest individuals alone.

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Tax reform is always bound to produce winners and losers, and it's notoriously the case that the winners tend to regard their wins as no more than their due, while the losers scream blue murder. That's why tax reform is always so difficult, and why it rarely makes sense to promote it with high profile crusades, as distinct from just quietly getting on with the job in government - as Labor did.

But intelligent tax reform can ensure that the benefits flow to where they are most needed, that no new inequities are created, and that those who lose out are doing so because the concessions or exemptions or rates or rules on which they are relying are no longer defensible in terms of the broader community interest.

That's not the kind of tax reform the Coalition is about, nor can it be while the GST remains the centrepiece of their reform ambitions.

But this kind of intelligent tax reform is the kind the Labor Party will be promoting, and we think it's time that everyone - including ACOSS and its constituents - came aboard.