



A GST reform package

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Federal Relations and Tax Reform Workshop
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A GST Reform Package

Why should we reform GST?

- Budget repair – more efficient (and palatable) than further increases in income tax
- Stability of tax base – GST not been the growth the tax the states were promised

Governments no longer have the dollars to “buy reform”

Can we design a workable compensation package?

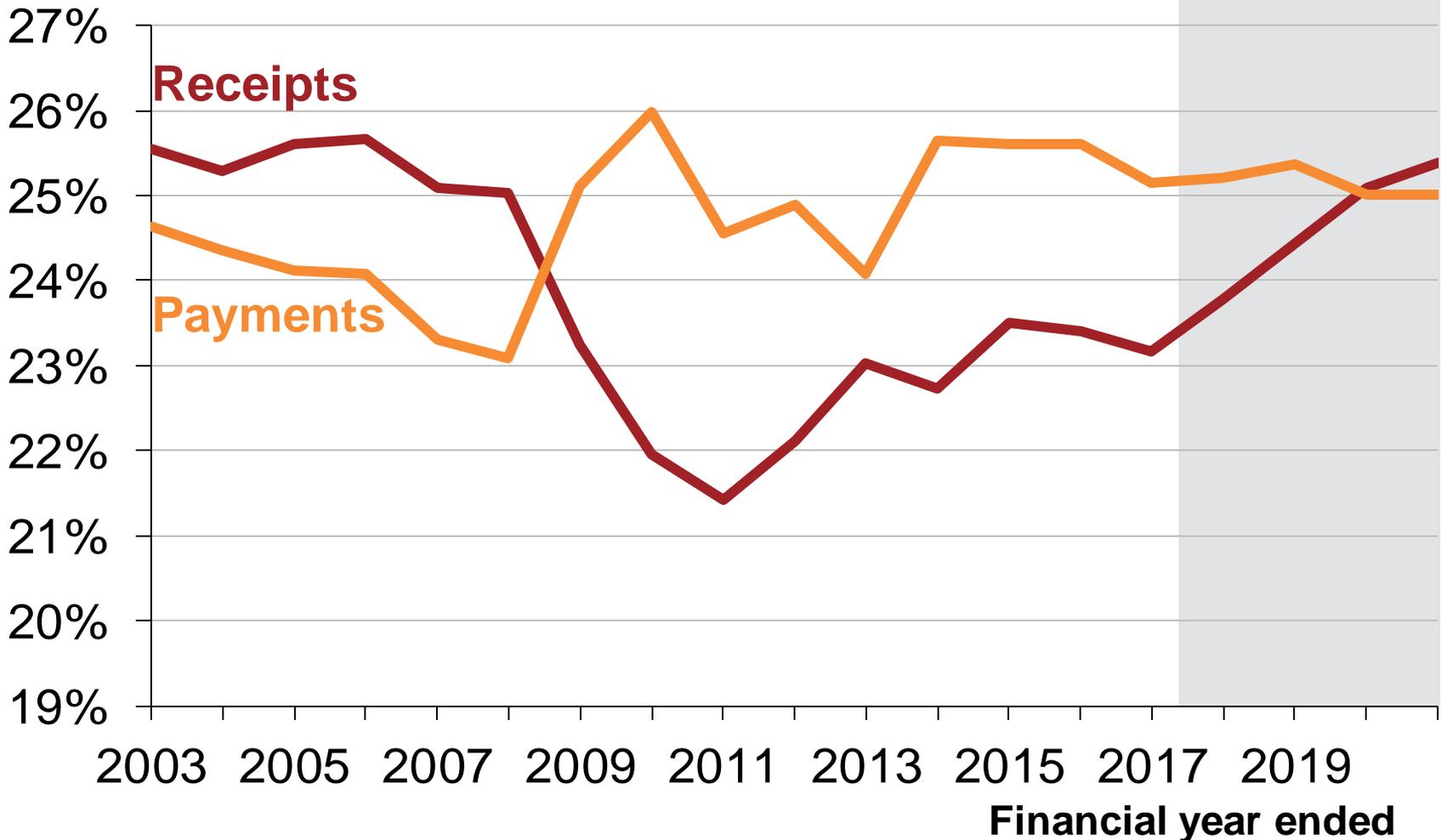
- Compensation can never be perfectly targeted
- Fairness and political pragmatism suggest:
 - On average at least fully compensate bottom 20%
 - Tax cuts for low and middle brackets

Dividing the pie

- Very different backdrop to 2001: this time Commonwealth government has budget issues
- Needs to be “something in it” for both levels of government
- Assuming 50:50 split – would require Commonwealth to cut tied grants to schools or hospitals

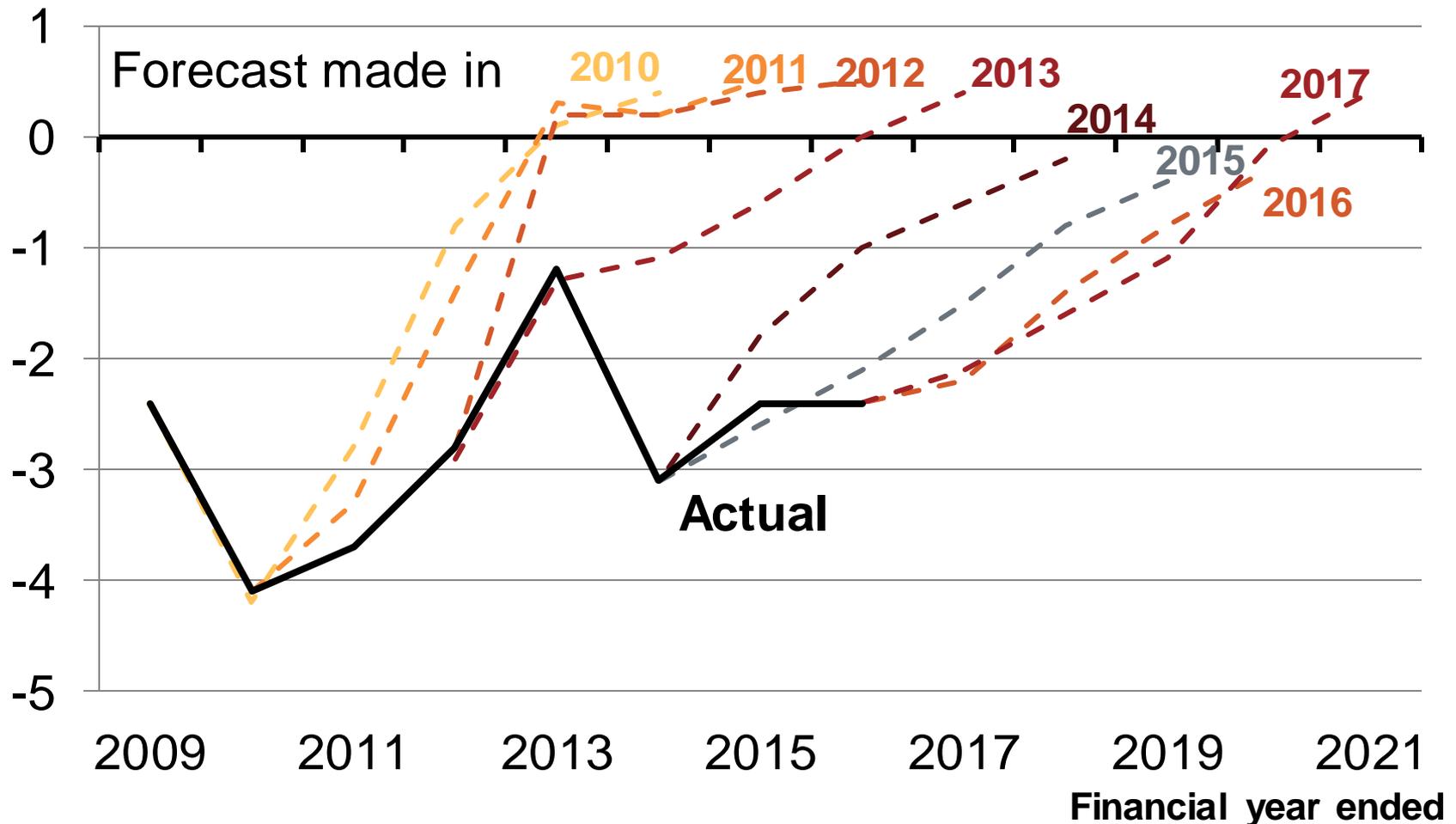
Commonwealth government running deficits for 9 years

Commonwealth expenditures and revenues per cent of nominal GDP



And forecast surpluses have not been achieved

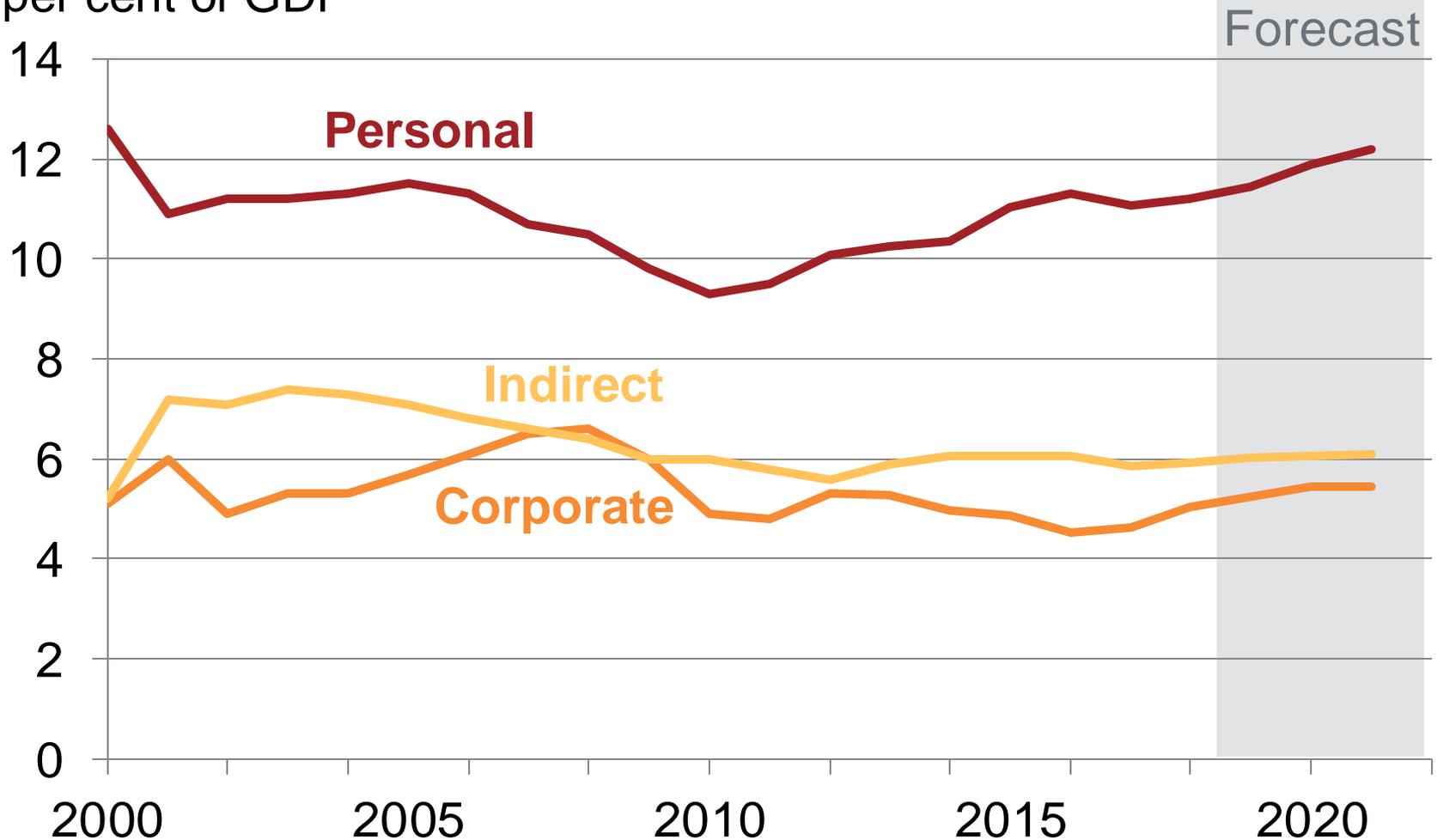
Actual and forecast Commonwealth underlying cash balance, per cent of GDP



Revenue increase is driven by personal income tax growth

Commonwealth taxation trends

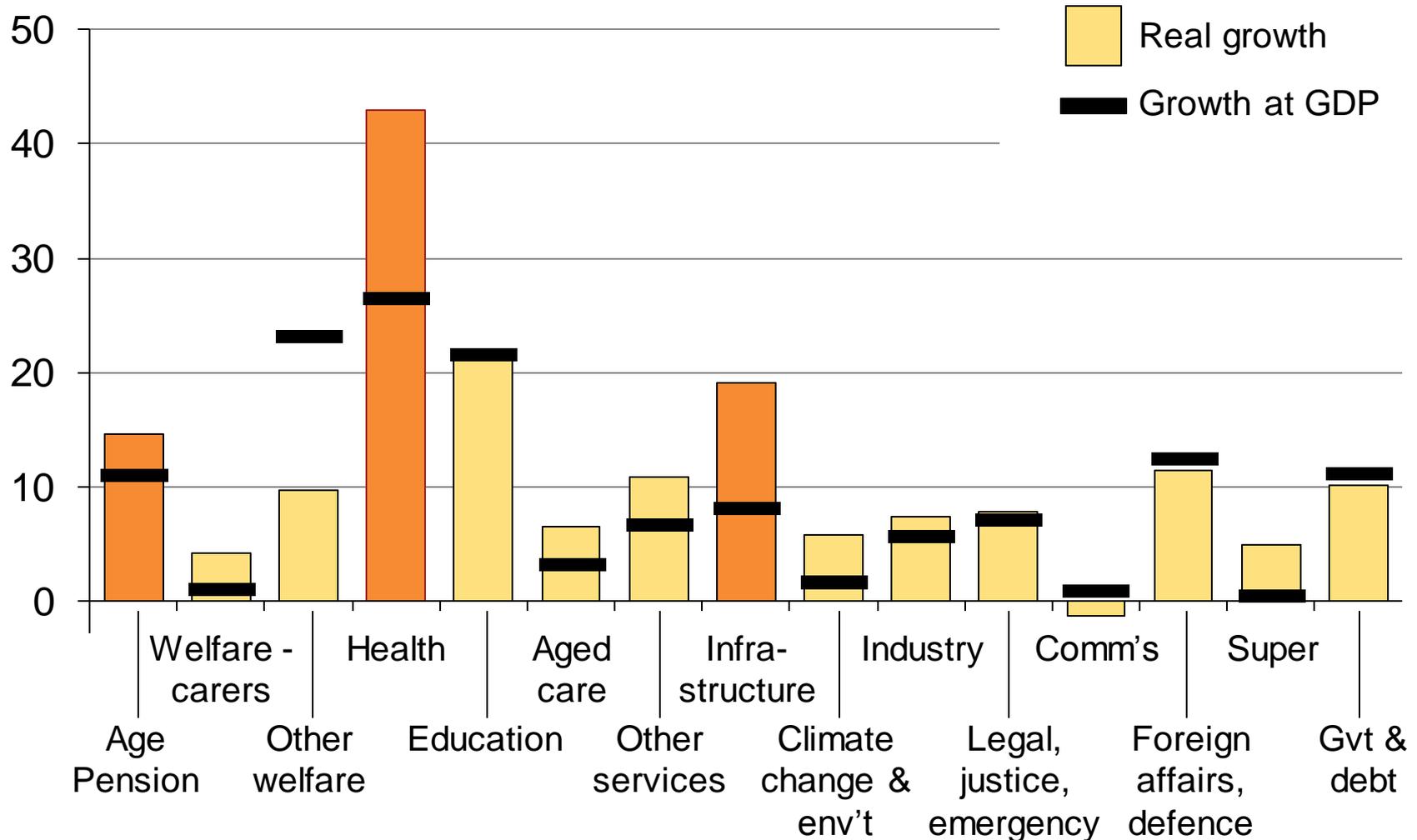
per cent of GDP



State government budgets face long term pressure from growing health spending

Real change in government recurrent expenditure, 2003 to 2014

\$2013 bn



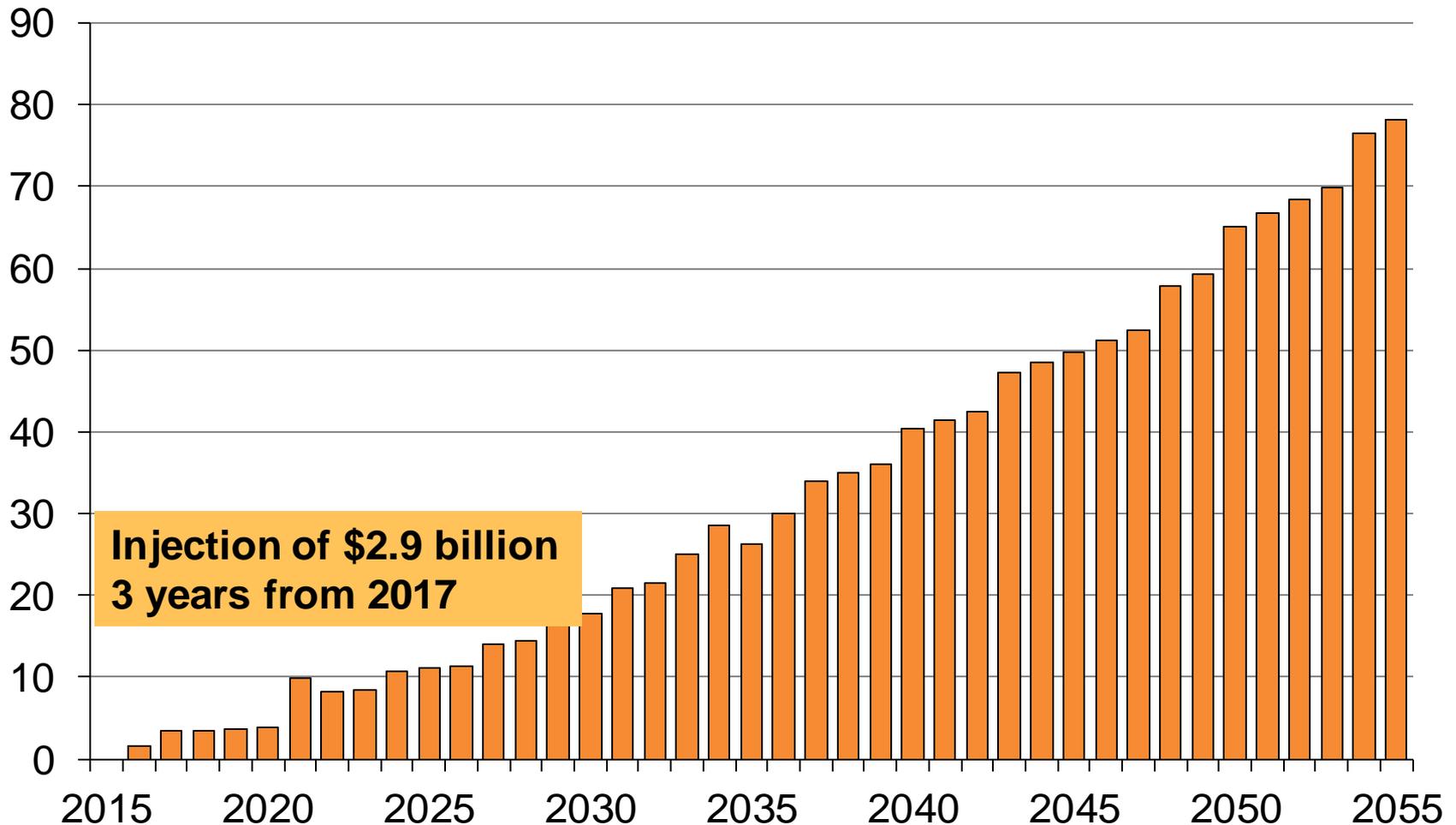
Note: Based on analysis of Commonwealth, NSW, Vic, Qld and WA data. Categories that changed by less than \$1 billion not shown.

Source: Grattan Institute, *Budget Pressures 2014*

And Commonwealth funding for hospitals is highly uncertain

Forecast Commonwealth health funding withdrawn from states

2013-14 \$ billion



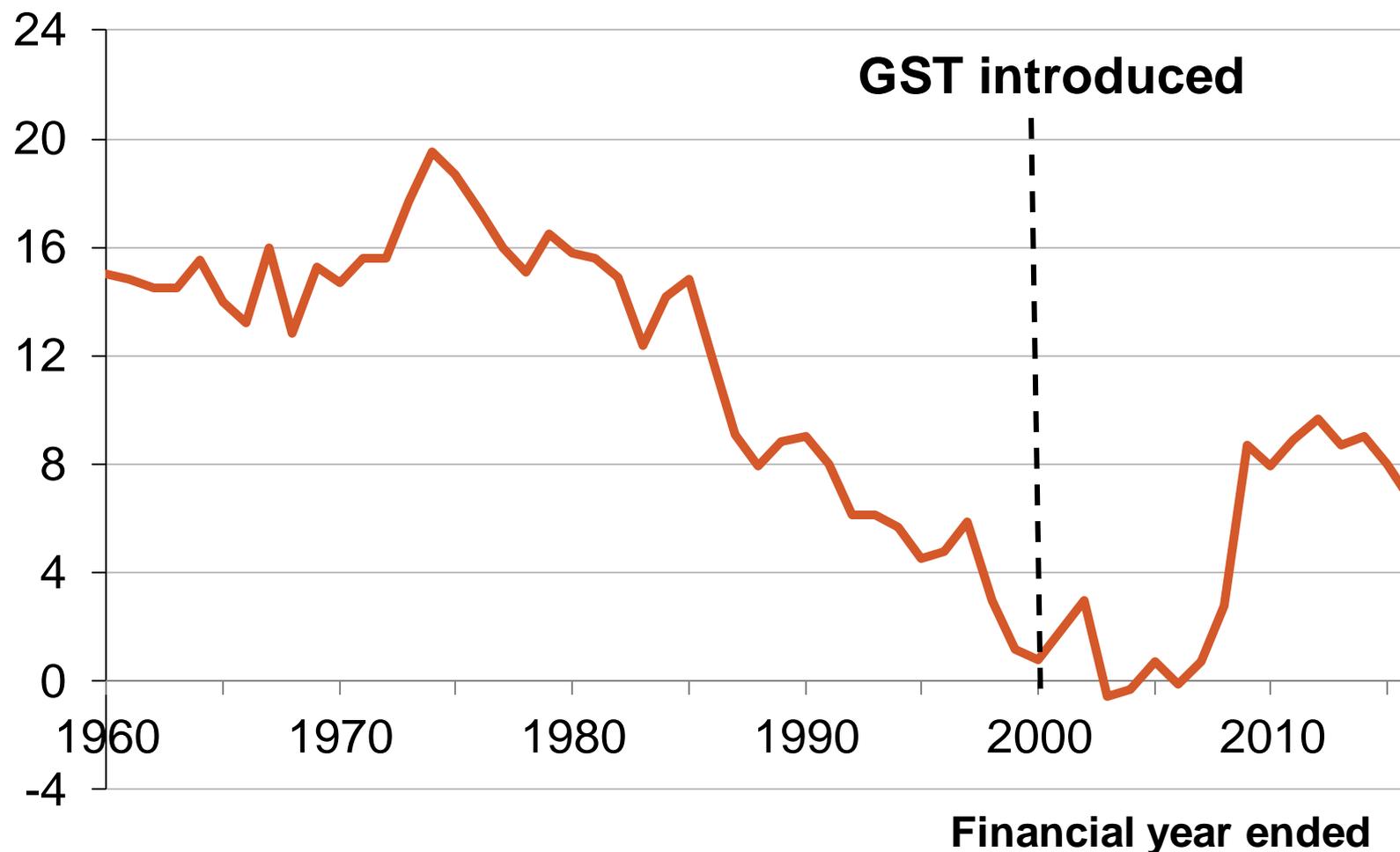
Note: Estimates of health funding withdrawn from the states based on difference in Australian Government spending under the 'proposed policy'; and 'previous policy' scenarios modelled in the Intergenerational Report.

Source: Treasury (2015), Intergenerational Report

GST has not been the growth tax the states were promised: savings rates increased

Household saving rates

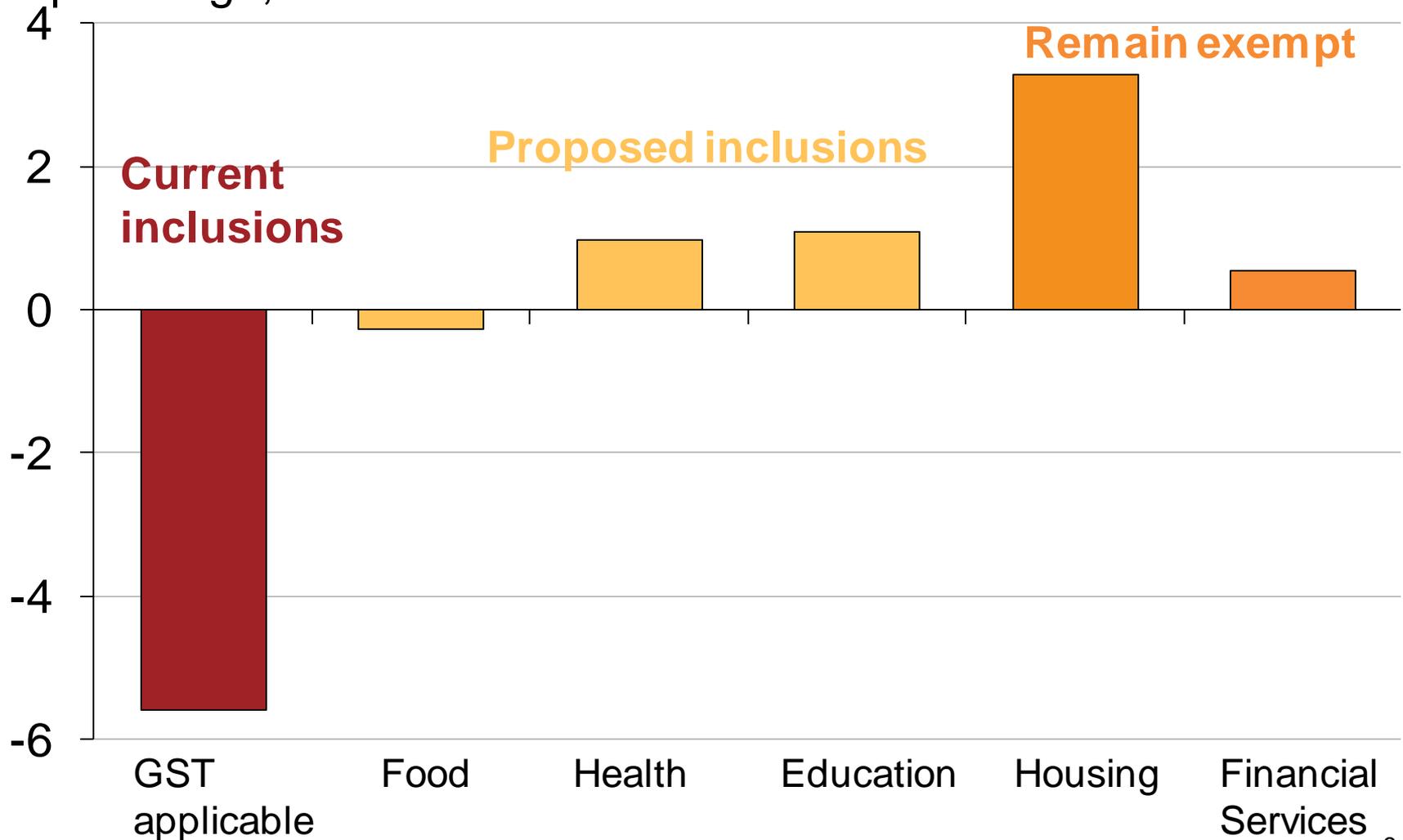
Per cent of household disposable income



And spending share of good and services subject to GST has fallen

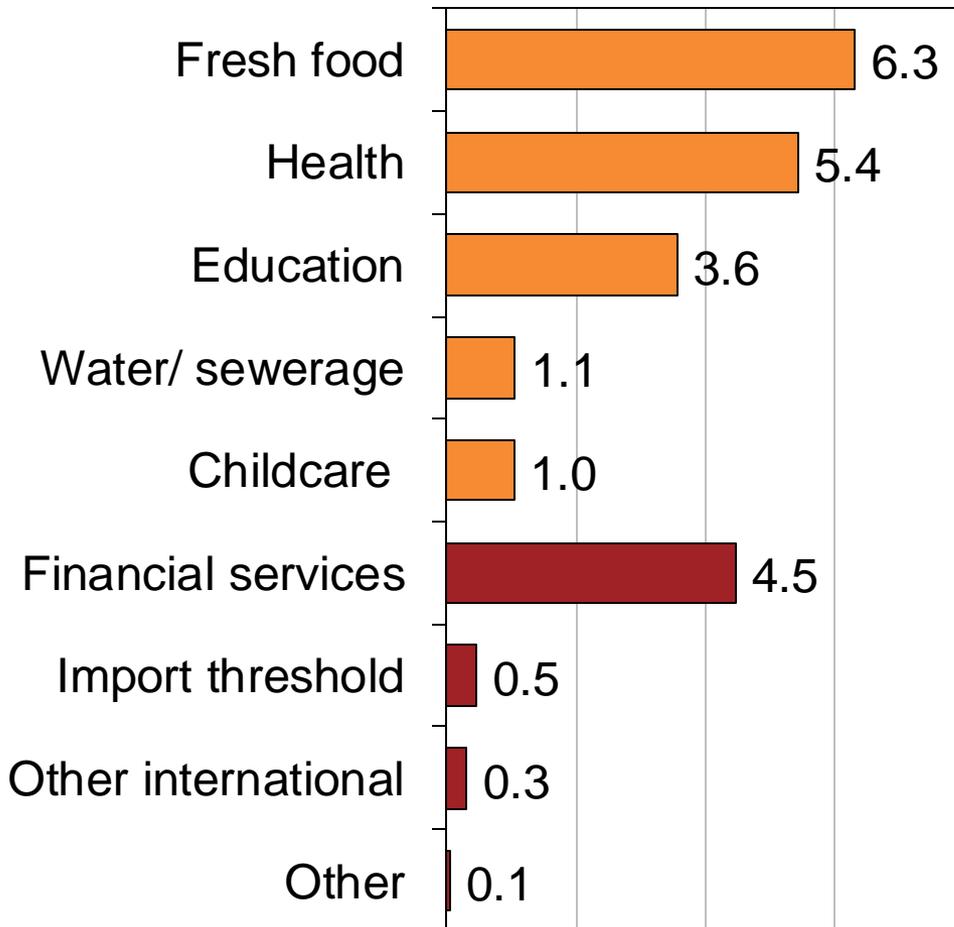
Change in HH consumption expenditure

Ppt change, 2005-6 to 2014-15



Model two proposals: broaden base and increase rate

Potential GST revenue of excluded items (2014-15), \$ bn



Proposal 1: Broaden the base

- Broaden the base to include fresh food, education, health childcare, water and sewage
- Raise around **\$17 billion** (2014-15)

Proposal 2: Increase the rate to 15%

- Raise **\$27 billion** (2014-15)

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Leaders have become accustomed to “buying reform”



Typical families with either one or both parents in the workforce, will be \$40 to \$50 a week better off even after the GST.

**GST
(2000)**

**CPRS
(2009)**

No low income family will be worse off and 90% of them ... will receive windfall compensation.



But generosity comes with a price tag

GST (2000)

GST raised **\$30 billion**

Compensation:

- **\$25 billion** - other taxes (wholesale sales and state indirect taxes) abolished (or proposed to be)
- **\$13 billion** reduction in personal income taxes
- **\$2 billion** increase pensions and social security changes
- **\$2.5 billion** increase in family payments

Total household overcompensation estimated around **\$12 billion year**

CPRS

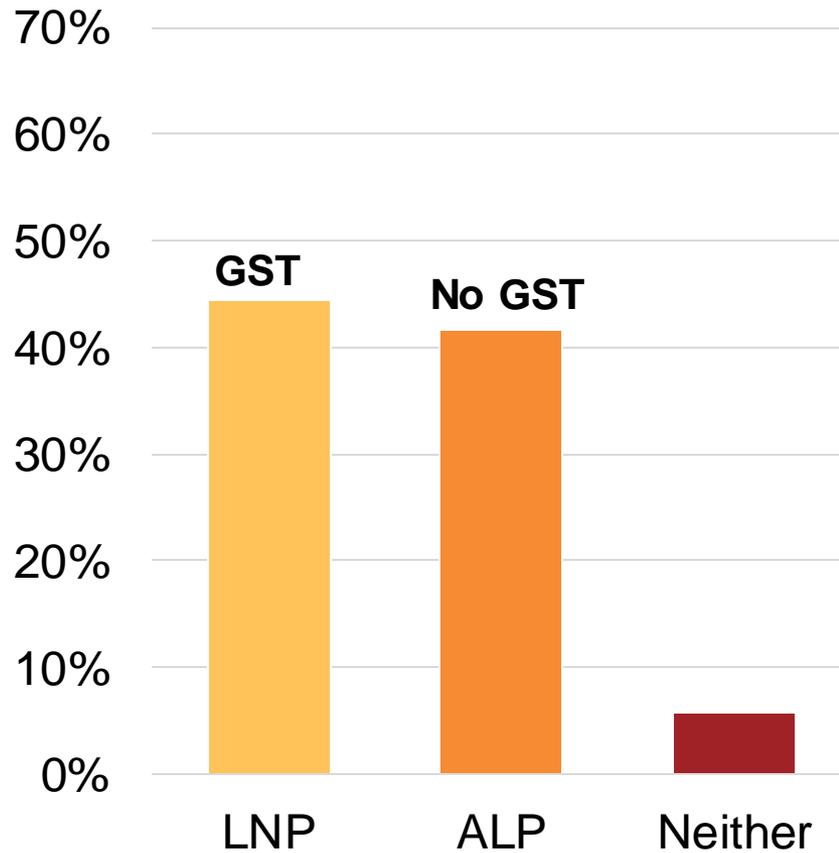
CPRS raised **\$4 billion**

Compensation:

- Objective: fully to offset the cost of living increased for low income households and meeting a share of increase in costs for middle income households
- **\$2 billion** – household compensation inc higher family payments, pensions, tax cuts
- Fund ease transition costs business and community organisations
- Package **overcompensated households** – average assistance **\$10.10 per week**, average cost increases **\$9.90 per week**

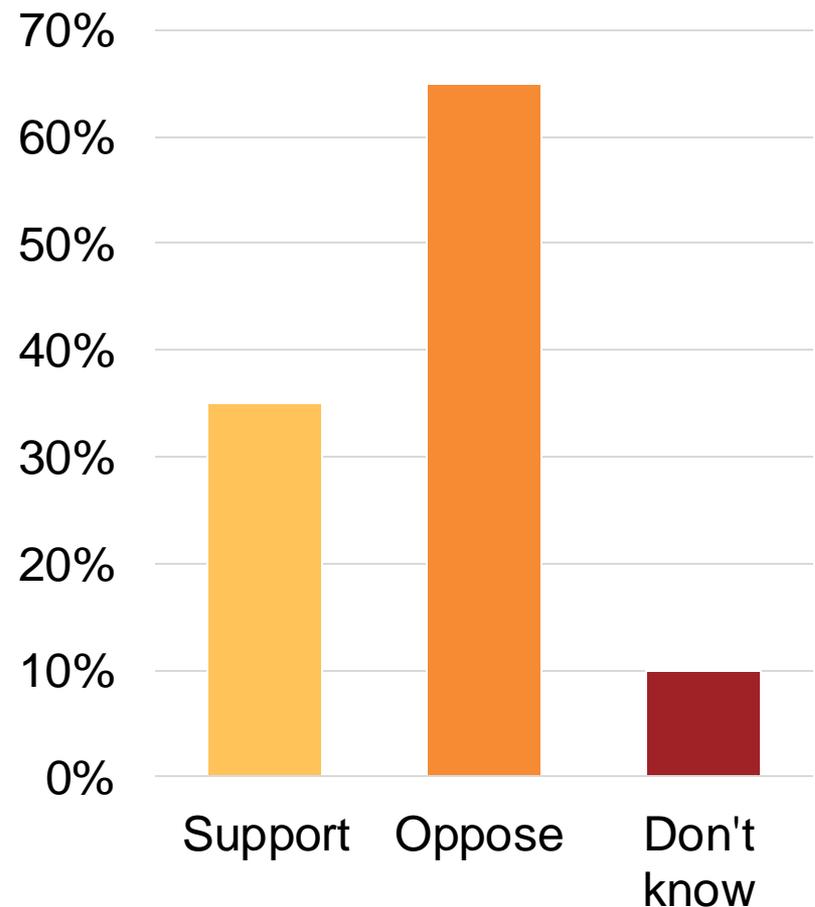
GST not popular even with generous compensation and highly unpopular without

Percentage who agreed with party GST policy, **1998**



Source: Grattan analysis of the Australian Election Study (1998)

Percentage who support increase GST, **2017**



Source: Grattan analysis of Essential Media (2017)

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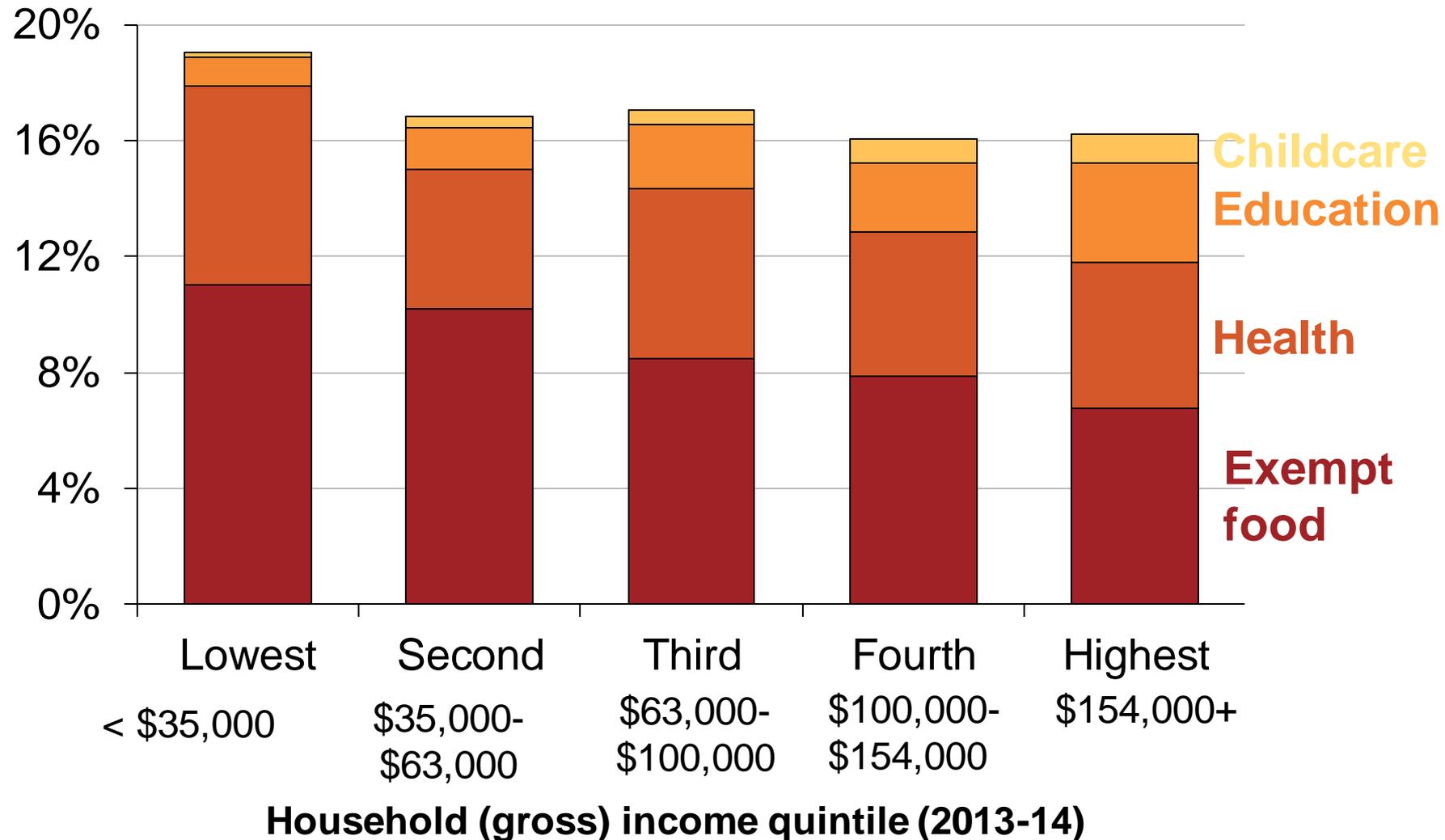
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GST is regressive (as share of income) but not as share of spending

Percentage of households by main source of income, 2013-14



Designing a compensation package

Objectives:

- Address **fairness** concerns – protect most vulnerable
- **Political pragmatism** requires some compensation for middle income households
- **Minimising cost of compensation** so there is some net revenue for government

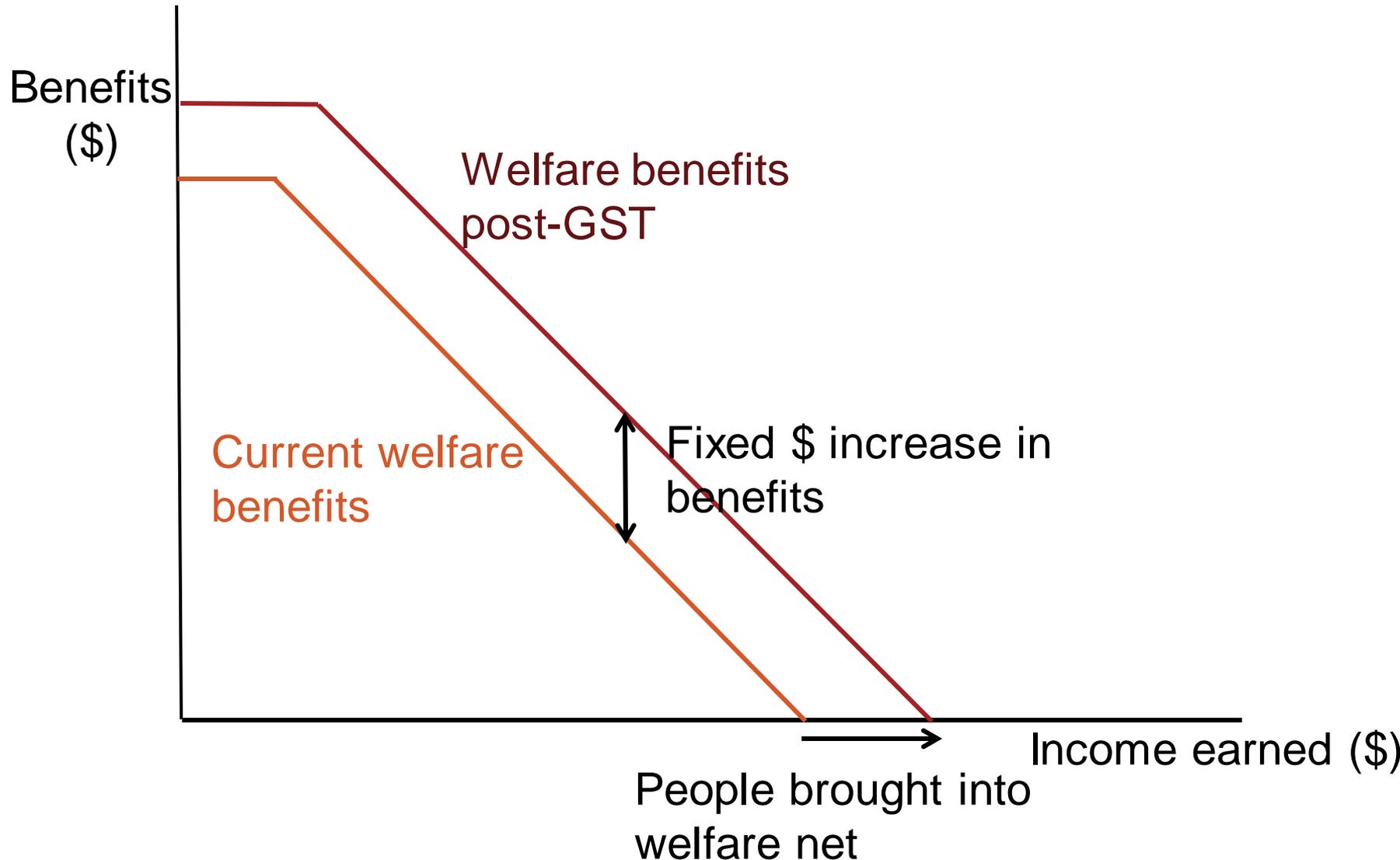
Design:

- **On average** bottom 20 per cent of households are **at least fully compensated** for the tax increase
- **Most households** earning up to \$100,000 are compensated **for at least 75 per cent** of the tax increase

Fairness is absolutely critical. Any package of reforms which is not and is not seen as fair will not and cannot achieve the public support without which it simply will not succeed.

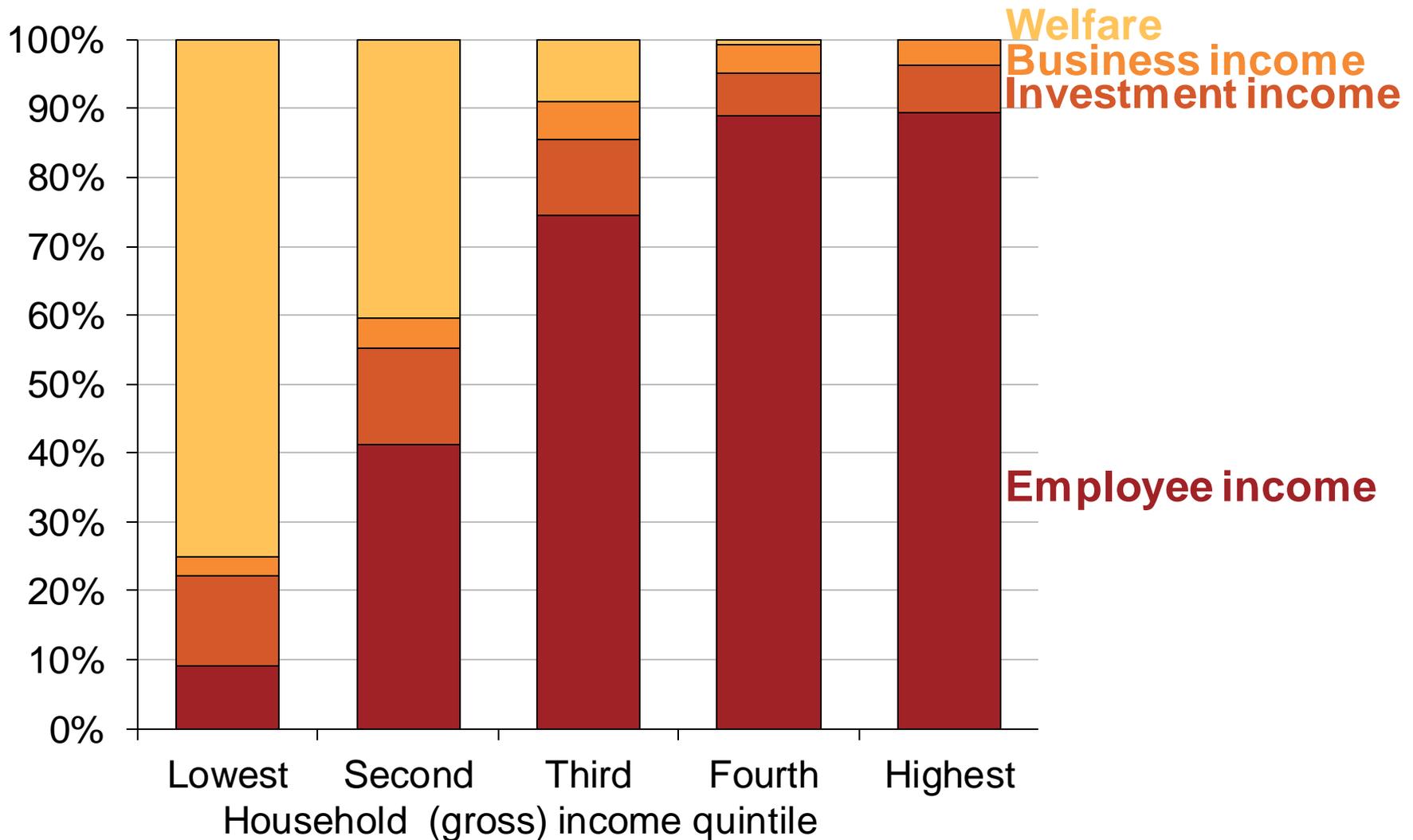


Fixed \$ increase in welfare payments maintains marginal work incentive (for most)



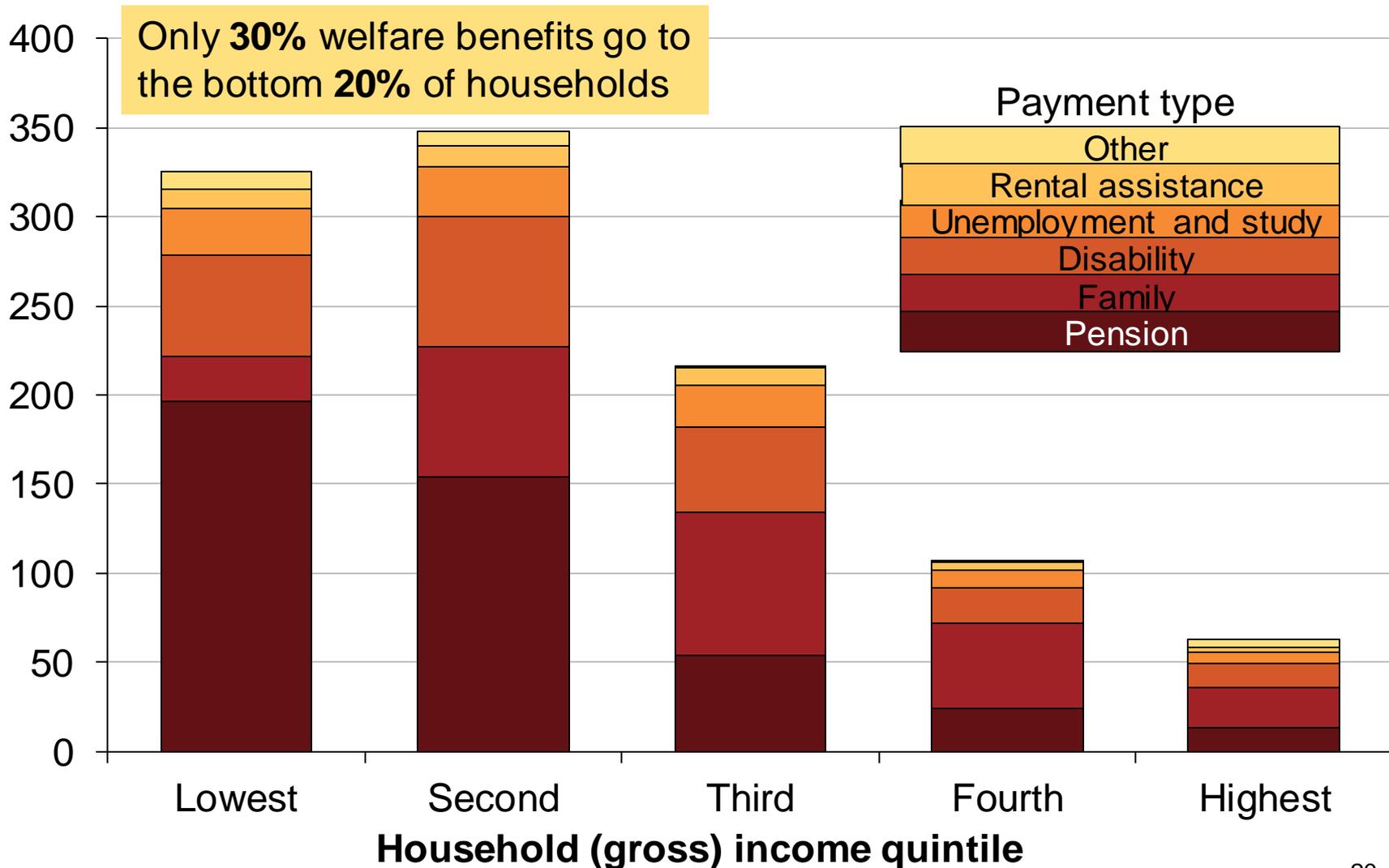
Government benefits are the main source of income for the poorest households

Percentage of households by main source of income, 2013-14



BUT compensation will be imperfectly targeted

Average welfare payments per week, 2013-14



Compensation package (15% GST)

Welfare

- **\$8 billion** (30% of revenue) from higher GST on higher welfare payments
- **5% increase in base rate** of all welfare payments

Tax

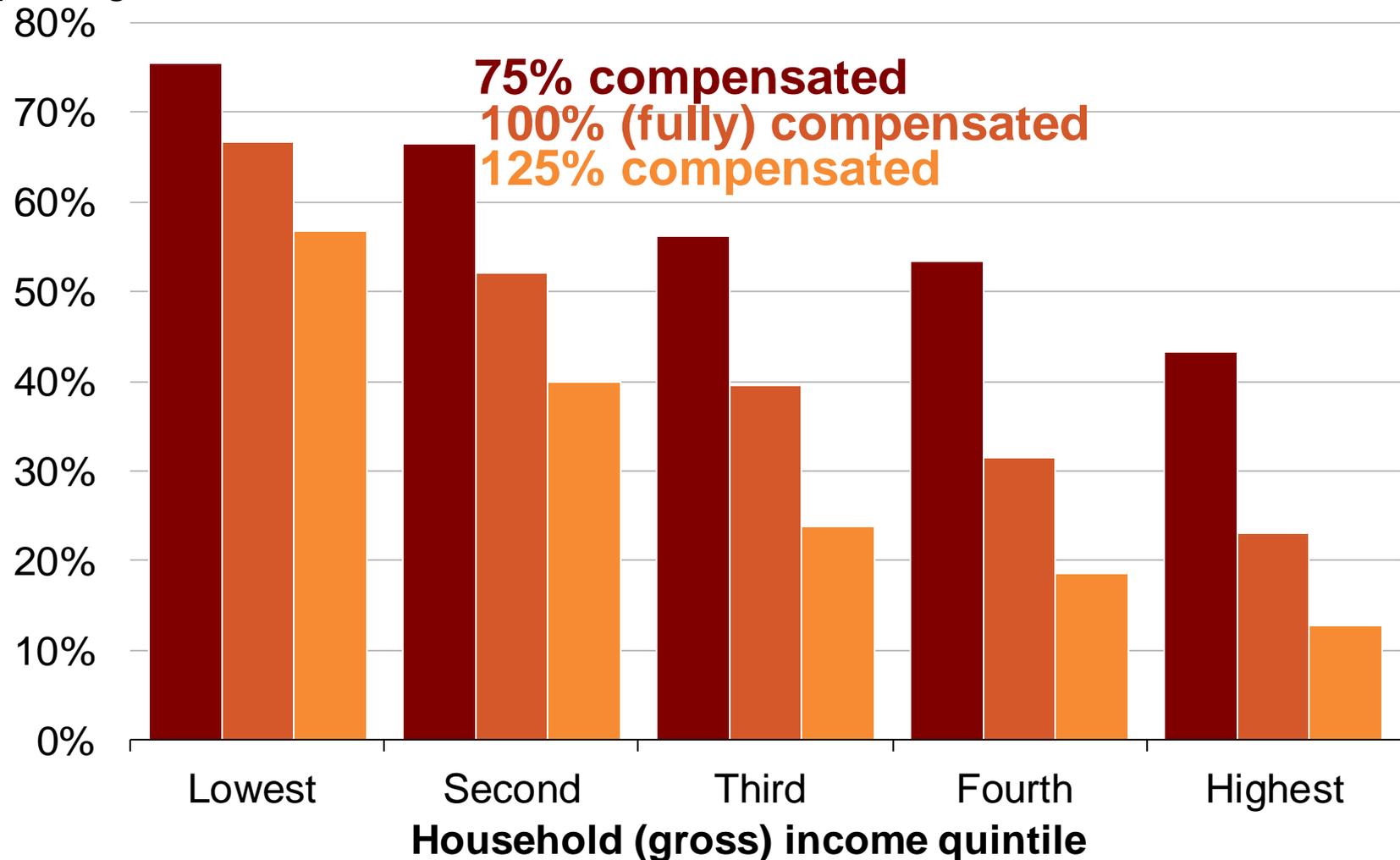
- **\$8 billion** (30% of revenue) on tax cuts
- Focus on low and middle tax cuts – biggest impact on participation

Tax bracket	2015/16 tax rate	Rates with higher GST	Rates broader GST
0-\$18,200	0	0%	0%
\$18,201-\$37,000	19%	16.5%	17.5%
\$37,001-\$80,000	32.5%	30.5%	31.5%
\$80,001-\$180,000	37%	37%	37%
\$180,001 and over	45%	45%	45%

- Leaves **\$11 billion** (40% revenue) for budget repair

Two out of three of the poorest households will be better off

Percentage of each quintile at least compensated by the about shown by our package



Drilling down.....

Impact of GST compensation package on selected benefits and households

Benefit	Household type	Average change in disposable income (%)	Proportion under compensated
Full Age pension	Couple, home-owners	0%	36%
Newstart	Couple, 2 children, renter	0.8%	9%
Disability	Single, no other income, renter	1.4%	21%

Note: This analysis is based on welfare patterns and spending from 2009-10 because this is the most recent year for which spending data at the household level are available.

Source: Grattan analysis

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Why and how should we reform GST?

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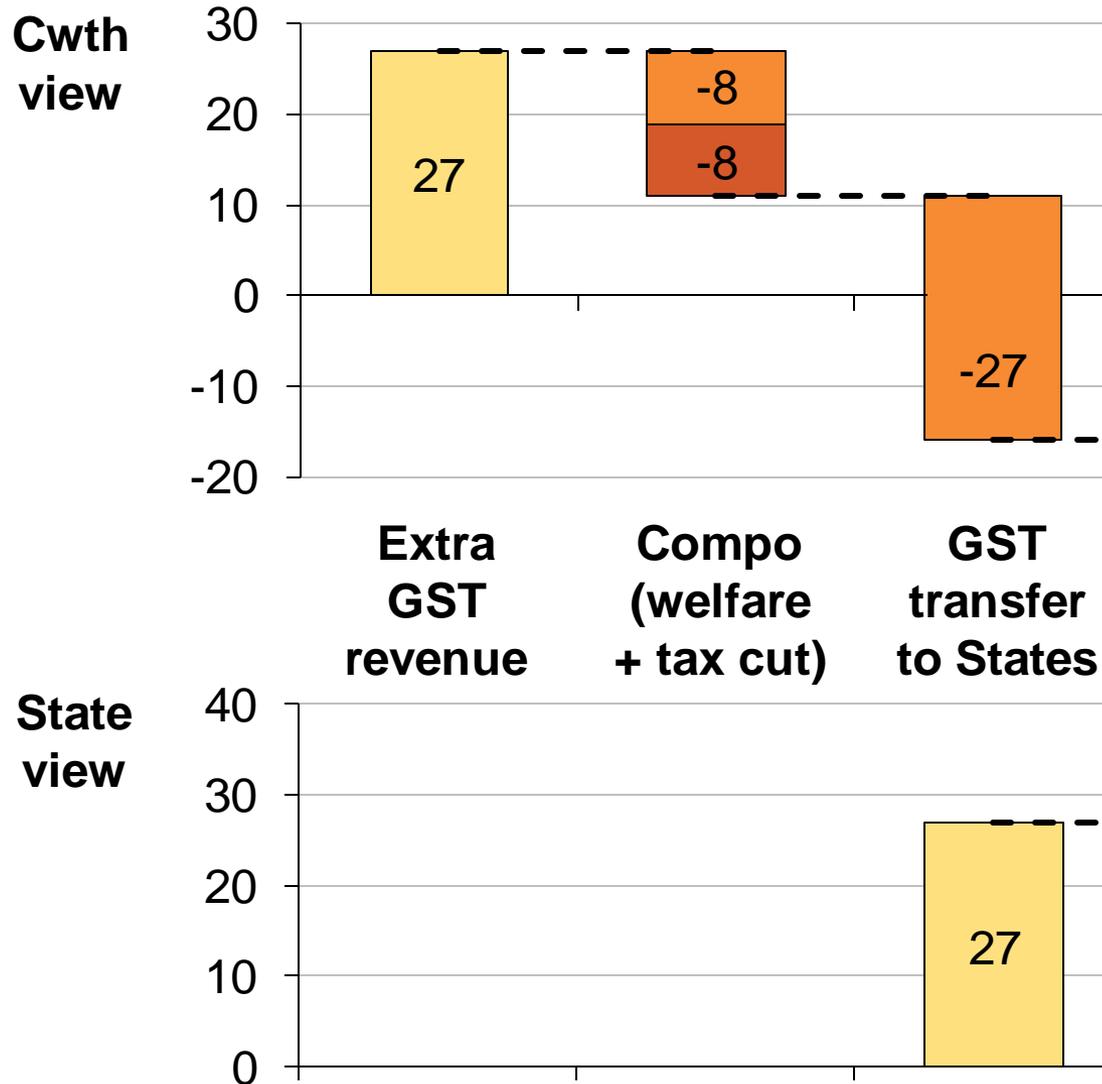
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Dividing the pie....

All GST goes to the States

Budgetary changes, 2014-15, \$billion/yr



Why would States agree to receive only a proportion of GST revenue?

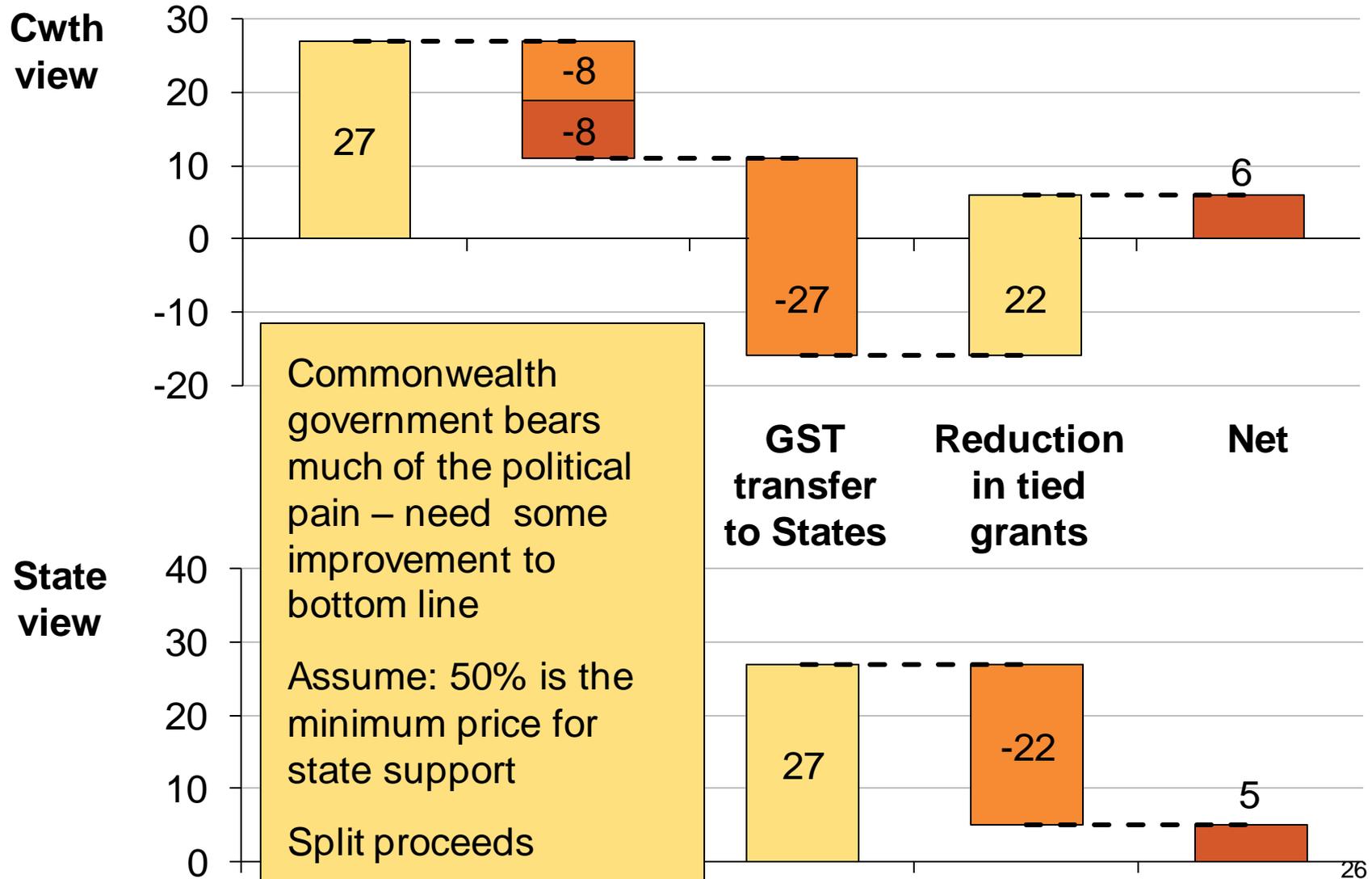
“A slippery slope to Commonwealth taking a bigger slice in future”

BUT from Commonwealth perspective \$16 billion down

Dividing the pie....

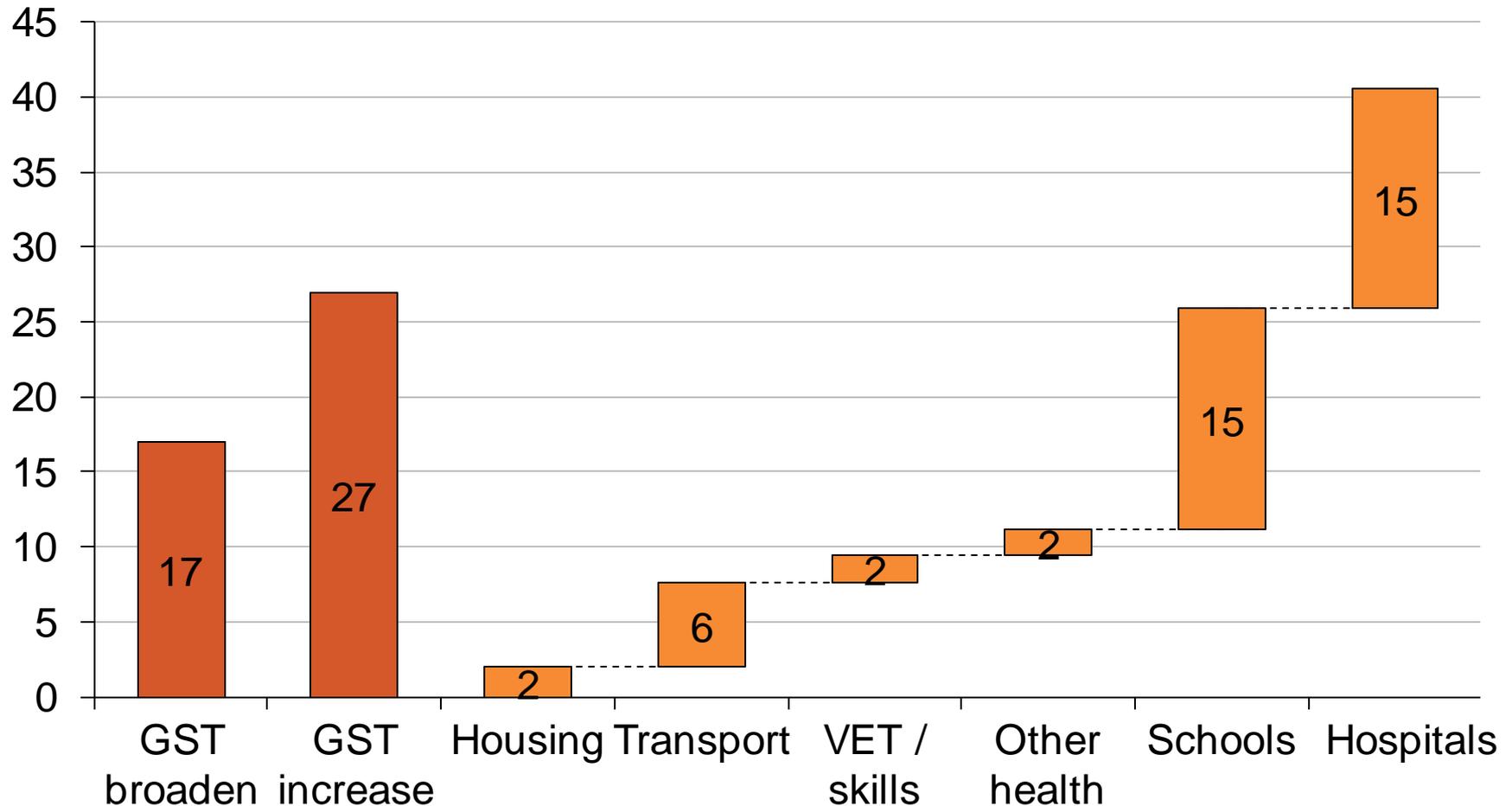
Effect on budgets must be positive

Budgetary changes, 2014-15, \$billion/yr



GST broadening or increase implies reductions in schools or hospitals tied grants

Budgetary impacts of GST and tied grant changes, 2014-15, \$billion/yr



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