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## REVIEWS

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### Different Perspectives on the GST

*Binh Tran Nam (ed), Tax Reform and the GST, an International Perspective, Prospect Media Pty Ltd, 1998 (ATAX Seminar Papers)*

*Reviewed by Howard Pender*

Anyone wishing to enter the current Australian tax debate should have, firmly in their head, opinions as to the merits of the various tax bases (labour, income, consumption etc.) on criteria such as economic efficiency and fairness. The six major contributors to this book have conflicting views as to the public policy desirability of introducing a GST in Australia. However, their views on the relative size of the administrative and efficiency burden of the various tax possibilities exhibit a fair degree of harmony. If they were a committee of curators of an art gallery their disagreement would be more about public taste than the artistic meaning or the price tag to put on the works of particular artists.

It is useful to distinguish two kinds of efficiency burden of tax. The administrative burden is the cost of the effort devoted by government officials and taxpayers to record keeping, compliance and payments processing associated with the tax. I will label the administrative burden of a particular tax base 'AB (base)'. For example, 'AB (GST)' denotes the administrative burden of a GST expressed as a proportion of revenue raised. The second burden, the 'marginal excess burden' is a measure of the additional economic cost of a tax (as a fraction of the additional revenue raised) resulting from changes in behaviour. The figure below summarises my own view as to the magnitude of these burdens. It is better to interpret the numbers as a reflection of rank than ascribe too much significance to the actual values.

#### **The Efficiency (MEB) and Administrative (AB) Burden of Various Tax Bases in Australia (percentages)**

	<b>MEB</b>	<b>AB</b>
Income from Business Capital	50	20
Income from Labour	25	5-10
GST	10 to 15	3 to 5
Wholesale Sales Tax (WST)	15	3

Source: Pender (1998:Ch.8).

Four of the major contributors to this book devote much of their discussion to justifying their slant on the size of the numbers set out above or the inference for policy they take from those numbers.

Tony Rumble focuses on demonstrating the MEB (GST) is much less than the MEB (business taxes including the miscellaneous state taxes which impact on business). He supports a GST but he is most concerned to emphasise the high MEB of tax on income from capital and the high administrative burden flowing from attempts to raise further revenue from that base. He feels efficiency as a criterion is underrated in the current Australian tax debate particularly awareness of the likely level of the MEB of business tax which results from the high level of capital mobility.

David Vos and Patrick Gallagher focus on the MEB and AB comparisons between the WST and a GST. They place the AB (WST) significantly less than the AB (GST). (Though they point out that some small scale traders face a high burden under the WST). Much of their discussion can be paraphrased as 'look at these things which make up the MEB and AB of the current WST'. Regarding the MEB (WST) they contend it is higher than the likely MEB (GST) because of the cascading of input prices and the GST rebate of inputs for exporters. They devote little attention to the likely MEB of a GST.

Neil Brooks, by contrast, in Chapter 7 sets out an anti-GST case. He notes many proponents (like Vos and Gallagher) overstate the efficiency benefit of a GST over a WST. He correctly points out that the arguments that a GST results in less distortion to savings, labour supply and international competitiveness are commonly overstated, and have been overstated in the pro-GST material distributed by the Australian Government. He also asserts the administrative burden of a GST is higher than that for a WST.

Neil Warren in Chapter 6 provides an effective reply to Neil Brooks on behalf of the pro-GST case. He points out the correct comparison on the MEB criterion is not simply WST and GST. His counterfactual for the 'fail to introduce a GST' situation is 'extract more revenue from the current WST base' without compensation. An extreme version of his argument could be paraphrased as follows. 'Suppose the MEB (GST) roughly equalled the MEB (WST) in 1993. Failure to introduce the GST in 1993 resulted in increases in WST rates and other State and Commonwealth indirect tax rates. Low income earners were not compensated for these increased tax rates. On the basis of the household expenditure survey pattern of expenditure a compensated GST would have been more (vertically) equitable than what occurred. As the WST rates increase the MEB increased so that now the MEB of an equi-revenue GST is less than that of the current WST and the situation, in the future, if a GST is not introduced will only get worse.'

By contrast with Rumble, Warren's focus is 'within the indirect tax base'. His reply to Brooks ('sure there isn't much in the MEBs but they're diverging, sure GSTs are regressive but increased WST rates won't be compensated for') is

only valid if his premise ('more money will have to be extracted from the indirect tax base') is accurate as a prediction for the future.

The two other major contributors take different tacks. Gull Izmir notes that the MEB of a payroll tax (PRT) is similar to that of a broad based consumption tax so that much of the 'let's have a GST to replace PRT' argument is flawed, from the efficiency perspective. Izmir also acknowledges the high MEB of most of the non-PRT State taxes. Much of the remainder of Izmir's chapter is devoted to the proposition 'the Commonwealth should organise tax base sharing' for the Australian States. Izmir does not differentiate between the various tax bases with regard to this proposition. At the international level the geographic nexus of income from capital (transfer pricing), general consumption (Internet trade) and even labour (Australian Super contributions paid in New Zealand) is already coming under stress. Izmir does not appear to have heard Rumble's 'think in a global economy' message, much less applied it within Australia.

Cedric Sandford's discussion in Chapter 5 takes a 'social science explanation' approach rather than advocacy. Sandford asks why so many countries have introduced a GST despite its high AB, potential regressivity and the weakness of some of the indirect tax efficiency comparisons. Sandford's question is not 'why not swap a GST for a WST?' but 'why has a GST (as opposed to a retail sales tax) become so prevalent?'. Sandford's main conclusion is that a GST is a better revenue raiser for a given efficiency cost.

Three of the six contributors support a GST though for different reasons. To my mind Rumble's argument is the most convincing and enduring. Neil Brooks, the single opponent of a GST, proposes alternatives based on broadening both the income from capital base (such as the abolition of negative gearing) and the income from labour (for example, FBT) base. If Australia was a closed economy then personally I would support both Brooks's proposals. But it is not. Aggregate labour income depends on our capital stock. It, in turn depends on the international competitiveness of our business tax regime. The GST is a minor tax design issue by comparison with the questions raised by fully accepting an open economy paradigm. There is another art gallery opening down the road, which artists will they exhibit?

## Reference

Pender, H. (1998), *The Joy of Tax*, Australian Tax Research Foundation, Sydney.

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