

Concessions have put a dent in the budget

Tax breaks need reining in: report

Savings

Katie Walsh

The \$111 billion in tax concessions paid each year must be cut if the federal government is to repair the budget, an economic analysis funded by the Minerals Council of Australia argues.

This year tax breaks for superannuation savings will hit \$32 billion, overtaking capital gains tax breaks for housing as the most expensive concession, and is expected to grow at 5 per cent a year over the next two decades.

"The merits of each concession should be periodically re-established," **Stephen Anthony**, director of budget policy and forecasting at economics consulting firm Macroeconomics writes. "All of the concessions should be treated in the same way as direct budget expenditures for the purposes of program evaluation."

Concessions of all sizes have hit the

budget hard, Mr Anthony said. In the latest tax expenditures statement, they number to 363 and make up one third of budget revenue.

After superannuation and housing comes the cost of goods and services tax exemptions for food, education, health and financial supplies, due to cost more than \$15 billion in the 2013 tax year.

The federal government has announced plans to slash concessions on super accounts earning more than \$100,000 a year in the pension stage but has pledged to otherwise leave super alone.

The Coalition is set to cut an exemption for low-income earners if voted into government in September but otherwise steer clear of the area.

Mr Anthony says an expert panel could review tax concession programs in each budget, in addition to major spending and other costs.

Treasury could "score" the perform-

Targets

Possible budget cuts

- Scrap alternative energy programs. **Save \$100m**
- First Home Owners Grant. **Save \$771m**
- Cut staff in federal health and education. **Save \$249m**
- Cut irrigation infrastructure and water buy backs handouts. **Save up to \$4.7bn**
- Tighten defence procurement. **Save \$80m to \$800m**
- Scrap drug subsidies for wealthy pensioners. **Save \$28m**
- Cut staff in Defence Materiel Organisation and AusAID by half. **Save \$390m**
- Scrap the School Kids bonus. **Save \$1.2bn**
- Scrap the Caring for Country scheme. **Save \$2bn over five years**
- Cut Family Tax Benefit B to households earning over \$120,000. **Save \$811m**
- Cut corporate welfare; industry subsidies cost **\$18bn a year**

SOURCE: MACROECONOMICS

ance of all tax expenditures and provide a new budget paper setting out details on the top 20 areas of spending and tax breaks that face a growth risk.

The paper says the "fiscal largesse" of successive governments over the past decade, flush with funds from a commodities boom that added an extra

\$160 billion to the bottom-line in the last seven years, Macroeconomics says.

Corporate tax receipts have suffered since the financial crisis and are predicted to worsen, hemorrhaging by \$7 billion more than estimated this year.

While crediting Treasurer **Wayne Swan** for tightening personal tax offsets

as part of "crucial longer-term structural budget reforms", he says the government erred in linking the rise in superannuation payments to 12 per cent to the mining tax: the latter could fall \$6 billion short by 2020.

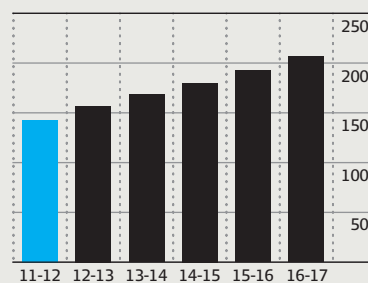
Among "wasteful spending" that the government could slash were bonus payments to parents of school kids (\$1.2 billion in savings in 2013-4), some family tax benefits (\$811 million), the up to \$14,000 handed to first home buyers (\$771 million), and duplicative energy programs (\$100 million).

Another \$28 million in savings is possible if pension eligibility rules – which allow a retiree who has \$1 million in super to get access to cut-price drugs using a health card – are tightened.

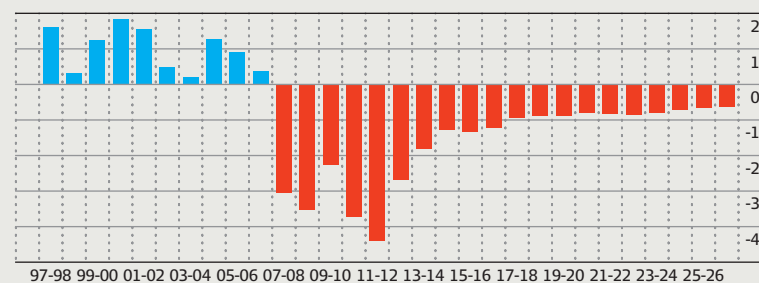
On the flipside, personal tax rates could benefit from a cut – but one funded by reigned-in spending on social security, pooling all welfare benefits into one means-tested payment.

In the red

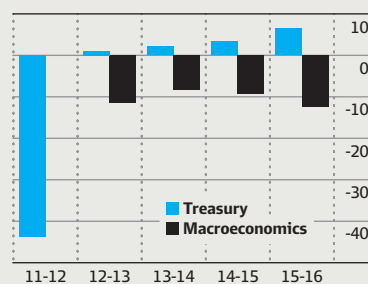
Commonwealth net debt (\$bn)



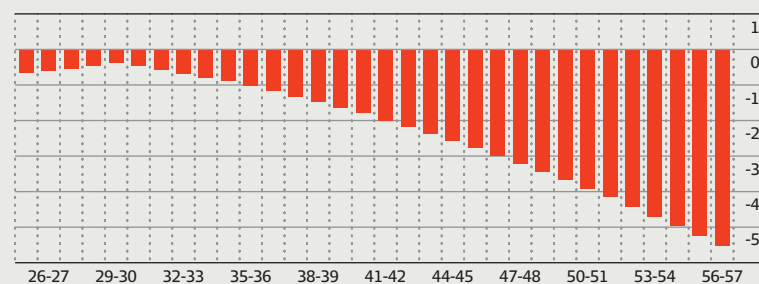
Structural budget balance projections to 2026-27 (% GDP)



Budget forecast comparison (\$bn)



Budget forecast comparison (% GDP)



SOURCE: MACROECONOMICS

From page 1 Labor's budget black hole

from **Geoff Carmody**, a leading private sector economist and co-founder of Access Economics, canvasses options such as an immediate \$14 billion spending cut, including by curbing billions in "corporate welfare" to dying industries such as car making.

Minerals Council chief executive **John Kunkel** said the report highlighted the scale of revenue that had flowed into government coffers from the mining boom and the "degree to which this has been frittered away by poor-quality spending".

"The MCA thought it important to ensure future governments are held to account on spending, and not resort to the lazy option of more taxes on industries that support Australia's prosperity," Dr Kunkel said.

A spokesman for Treasurer **Wayne Swan** said there was no doubt this year's budget was being brought down "in some extremely challenging and unusual circumstances".

"We'll continue to strike the right balance of making room for smart investments that support jobs and growth of the future while continuing our fiscal consolidation in a balanced and responsible way," he said.

The report comes just days after both sides of politics signalled they were

backing away from delivering surpluses in coming years.

Labor is understood to be struggling to find ways of generating a surplus in any of the so-called "forward estimates" years, which run through to 2016-17, because revenue collections are at least \$7.5 billion short of what was forecast six months ago.

Market economists and budget experts are tipping a deficit for 2012-13 of \$10 billion to as much as \$25 billion. At the same time, Opposition Leader **Tony Abbott** has declared "all bets are off" on a Coalition pledge to deliver a surplus in its first year in office.

Concern is now growing among business groups and budget experts

It is clear that Australia's fiscal strategy is in need of an overhaul.

Stephen Anthony, Macroeconomics

that failure to find a credible path back to surplus could result in Australia losing its coveted AAA credit rating.

The Grattan Institute published research on Monday suggesting that federal and state budgets would be generating combined deficits of at least \$80 billion a year by next decade unless spending was cut.

Macroeconomics argues that Australia's political parties should deepen

their commitment to surpluses over the economic cycle by pledging so-called structural budget balance.

Mr Anthony said the lack of a structural target meant successive governments had been "free to engage in fiscal largesse while still meeting their fiscal strategy objective".

"There was no acknowledgement of the windfall element of tax revenues under the strategy and no tally kept of the magnitude of these impacts on the budget," he said. "Windfall receipts were frittered a way."

The Labor government has recently complained that the falling terms of trade and the high dollar have delivered a "sledgehammer" to expected revenues. But budget experts say revenues are returning to their longer term levels following falls in the terms of trade since September 2011 of 17 per cent.

Mr Anthony said the situation was so bad that even an extended period of spending restraint – involving a 2 per cent cap on outlays for the next four years, plus a 2.5 per cent limit thereafter – would make it difficult for Labor to restore the structural balance.

"Such low spending growth has not been achieved by Australian governments for any sustained period of time over the last 50 years," he said.

Mr Anthony calls for an amendment to the Charter of Budget Honesty Act that would require the government to subject every new spending proposal worth more than \$50 million a year to an independent cost-benefit analysis.

Deficits demand tax hikes, say economists

Tax

Jason Murphy

An Abbott government would have to raise taxes as well as cut spending if the budget is to be returned to a structural balance, economists say.

Australia faces years of deficits as government spending increases faster than growth in revenues, and economists warn that cutting spending will not be enough to reverse the damage done to the nation's finances.

"I'd prefer that the government explored options for reducing spending before looking at revenue options, but I accept that they will need to do both," Bank of America Merrill Lynch economist **Saul Eslake** told *The Australian Financial Review*.

A Grattan Institute report on Monday said federal and state governments face a "decade of deficits" of \$60 billion, or 4 per cent of GDP, unless there are big spending cuts. It also argues that tax increases need to be part of the mix. "History suggests that successful budget repair invariably involves both tax increases and expenditure reductions," the report says.

BT Financial Group chief economist **Chris Caton** said if he wins the election, Opposition Leader **Tony Abbott** would have the political opportunity to raise other taxes early in his first term as prime minister. "A first term government with a big majority could argue that this is what it has to do to 'fix the mess left by its predecessors'," he said.

Mr Caton argued the ratio of tax to GDP, which the government estimates at 23 per cent, "suggests we are under-taxed".

The federal government has spent more than it raised in revenue since the start of the global financial crisis.

Shadow treasurer **Joe Hockey** told the *AFR* that the budget gap would be made up on the expenditure side if the Coalition wins the September election.

"The Coalition will restore budget sustainability by reducing spending, not by raising taxes. Our commitment is to abolish taxes – the carbon tax and the mining tax, with no plans for new or increased taxes beyond our previous announcement of a paid parental leave levy," he said.

Mr Eslake said there was a conflict between the Coalition's philosophy and

reality. "The incoming government is ostensibly committed to lowering taxes as a matter of philosophical principle," he said. "Despite this they are proposing to increase the tax paid by 3200 or so large companies by 1.5 percentage points in order to pay for Tony Abbott's 'signature' paid parental leave policy – so the philosophical commitment not to raise taxes isn't immutable," he said.

Mr Eslake said the policy is more in keeping with a philosophy of "hostility towards big companies" than a traditional Coalition approach.

Any tax increases should not come by raising rates, he said. "I would very much prefer to see them looking at broadening the base of existing taxes – especially personal income tax and GST – by removing exemptions, concessions, and other forms of differential treatment, before considering any increases in rates of tax."

Grattan Institute chief executive **John Daley** said a new government would need to be explicit that everyone

Will the incoming government hike taxes? My answer to that ... I hope so.

John Daley, CEO Grattan Institute

would feel the pain of budget repair.

"Will the incoming government hike taxes? My answer to that ... I hope so. Because given the situation we are in, they are going to need to both increase taxes and reduce expenditure," he said.

Mr Daley nominated "tax expenditures" – the big loopholes in the tax system – as the place to make big revenue gains. The biggest ones are superannuation, exemptions from capital gains tax for property and the GST exemptions for food, education and health.

HSBC chief economist **Paul Bloxham** believes GST could change as part of a broader tax overhaul.

"We need to see a restructuring of the tax system, so no doubt that will involve some hikes as well as some cuts."

ACIL Allen consulting director **Stephen Bartos**, said a government that wants to raise taxes without a political backlash should use specific levies, or so-called hypothecated taxes.