# POLICY PAPER No. 9 · September 2018

## Voting for a Living: A shift in Australian politics from selling policies to buying votes?

**Robert Carling and Terrence O'Brien** 



THE CENTRE FOR INDEPENDENT STUDIES .



A catalogue record for this book is available from the National Library of Australia

## Voting for a Living: A shift in Australian politics from selling policies to buying votes?

**Robert Carling and Terrence O'Brien** 





**POLICY Paper 9** 

## Contents

Introduction1
The `voting for a living' theory2
What would we see if Australia is now 'voting for a living'? Some hypotheses2
Measuring the forces 'voting for a living'3
Net benefits5
Changes over time
Public employment9
Bringing it all together — the 'voting for a living' population
Evidence of voting for a living10
What is to be done?11
Appendix A: The fiscal incidence study, 'Government Benefits, Taxes and Household Income'12
Endnotes13

*"The state is that great fiction by which everyone tries to live at the expense of everyone else."* Frédéric Bastiat, *"The State", Journal des débats, September 25, 1848.* 

#### Introduction

The size of government in Australia and many other countries has expanded as a long-term trend, and attempts to check the trend have been rare and of mixed success.<sup>1</sup> Various theories have been advanced to explain the trend—none of which can provide a complete explanation, but each of which contributes something to our understanding.<sup>2</sup>

This paper focuses on one such theory; which holds that the growth of government has become selfsustaining through the emergence of a segment of the population that both enjoys sufficient direct support from government and is large enough that political parties shape their policies to curry its favour. This theory has its origins in public choice literature: that growth of government results from the sum of individuals' choices at the ballot box, other forms of political activity in our democratic system, and political parties' responses and encouragement.

In particular, we are interested in the sub-set of government activities that impinge most directly on household budgets through the tax/transfer system. This system is often analysed for its effects on income distribution and the economic incentives that people face. In this paper we focus on political incentives, although the ultimate reasons for that interest are concerns about the economic and social consequences of those incentives. The economic consequences include the greater difficulty in balancing budgets as government keeps expanding; the pressure for higher taxation, which saps incentive and individual initiative; and the retardation of economic growth. The social consequences include demotivation and loss of personal accountability associated with dependence on government; and political friction and polarisation as the political contest becomes increasingly focused on distribution rather than growth.

We may have reached the point that such a large segment of society — whether measured by people, households or voters — are beneficiaries of government that big government and its further growth feeds on itself because of the strong resistance to any withdrawal of existing benefits, the lure of more benefits and reinforcement by the advocacy industry that has grown up around the welfare state.

To put this another way, government may have grown to the point that there is a large segment of the population — perhaps even a majority — facing incentives to 'vote for a living' rather than to 'work for a living' by adding value to resources through market-tested employment in the private sector. Less pejoratively, this group has also been labelled "zero net taxpayers", although these words fail to capture the fact that most in this group are not zero but negative net taxpayers.<sup>3</sup> If such a group becomes large enough, politics changes to cater for it.

#### The 'voting for a living' theory

Public (or 'collective') choice literature was the modern intellectual home of 'voting for a living' theory. As defined by the Library of Economics and Liberty, public choice applies the theories and methods of economics to the analysis of political behaviour. It assumes that people are guided chiefly by self-interest and that their political behaviour is motivated by the same factors that motivate their behaviour in private markets. "Voters 'vote their pocketbooks', supporting candidates and ballot propositions they think will make them personally better off; bureaucrats strive to advance their own careers; and politicians seek election or re-election to office."<sup>4</sup> The concepts and ideas underlying 'voting for a living' are not new. They have been discussed in the US context for many years, including notoriously by Mitt Romney, a presidential candidate in 2012.<sup>5</sup> Variants of the idea have also been advanced in Australia, as reviewed by Whiteford.<sup>6</sup>

This theory does not deny the case for social benefits or the virtue of much public sector employment. Rather, the questions for social benefits are how many, how much, for whom and employing how many? Nor does it ascribe self-interest as the only factor motivating political behaviour. Rather, it is one significant motivating force — for political parties as much as for voters — and the question is how important it may have become.

## What would we see if Australia is now 'voting for a living'? Some hypotheses

What would we predict would happen in a world where there was a majority 'voting for a living'? To test the theory, we need some falsifiable hypotheses — among which might be the following:

- 1. Political parties will emphasise policies relying on public expenditure growth, and favour income redistribution over economic growth.
- Proposed policies from all parties will increasingly favour tax increases targeted on a diminishing minority who pay tax in net terms on their income from private employment; especially tax increases on the disenfranchised and unpopular, such as 'rich foreign multinationals', or 'big banks'.
- 3. As political parties seek to sustain expenditure growth on a majority with tax increases on only a diminishing minority they will become more short-sighted, understating the risks of demographic ageing, protracted fiscal deficits, a build-up in national debt and of a future international slowdown. Voters will be led to believe, if only by misdirection, that their net benefit receipts are secure in any event.

- 4. As political parties compete for the support of the median voter, the tendency will be for government taxes and transfers to grow to favour the middle of the income distribution — even those with significant private income.
- Policy development by political parties will become increasingly a matter of exaggerating benefits to the median voter, disguising costs to net taxpayers, and supressing analysis that shows policy will not meet its stated purpose. Consequently, public inquiry, competent social cost-benefit analysis, and contestable advice will all tend to decline.
- 6. The gap between the politically-stated purpose of policies and the actual outcomes of those polices may progressively widen. For example, policies purporting to support the disadvantaged may primarily fund service providers rather than correct the source of the disadvantage.
- Major parties will tend to 'double down' on past policies, either without analysing past outcomes or despite evidence they have demonstrably failed.

- 8. Voting blocs of public employees will become more influential in party politics. Teachers will support not only more spending on education, but also more on nurses, police, ambulance staff and fire services. The state-owned broadcaster will support them all. This natural mutual support within the public sector will gain institutional strength from all these areas of employment being heavily unionised.
- 9. As public employee and public sector union influence becomes more politically influential through 'voting for a living', consequences may emerge not only in growth in public employment numbers, but also in relatively fast public sector wage growth and in generous, pace-setting terms of public sector employment.
- 10. State and territory governments will experience the forces noted in #1 to #9 above no less than the Commonwealth, and those jurisdictions with the largest public sectors may develop the foregoing policy trends faster than jurisdictions with larger shares of private employment and greater proportions of net taxpayers.

Any of these hypotheses, taken individually, may have some other contributing cause or causes as well as 'voting for a living' and the political responses to it. But the 'voting for a living' theory is striking in its potential to explain all 10 observations, and also the changing 'tone' of Australian political debate, with more fractious 'zero sum' debate about distribution and less of constructive 'positive sum' debate about raising incomes for all.

#### Measuring the forces 'voting for a living'

How could we estimate the size of the pool of voters potentially tempted to 'vote for a living' in Australia today?

We surmise that a tendency by segments of households or individuals to support higher government expenditure out of self-interest is most likely to be associated with the following characteristics:

- 1. A significant degree of dependency on social benefits provided by government.
- A low contribution through taxation to the overall costs of government – particularly if it is low relative to the household benefits received.
- 3. Dependency on public sector employment.
- 4. Private sector employment in activities heavily dependent on government subsidies.
- Interaction of the above effects for example, households whose income is derived mainly from government employment or subsidy and are also significant recipients of social benefits.

There is an abundance of data available to help quantify the first three, but the fourth category is much more difficult to quantify. The advocacy industry that has grown up to protect and advance the welfare state might also be considered part of the 'voting for a living' population—albeit also difficult to quantify.<sup>7</sup>

The main sources of data are in various Australian Bureau of Statistics (ABS) publications, and especially the fiscal incidence study *Government Benefits, Taxes and Household Income*, which shows the effects of government benefits and taxes on the distribution of income among private households. This study is updated only every six years and with a significant lag. The late-June 2018 release of 2015-16 data in this series was the catalyst for the current paper. Appendix A provides further detail of the ABS's methodology.

The ABS fiscal incidence studies shed light on a range of issues, including: the growth of household income and its components over time; quantification of income inequality; and how the tax/transfer system works to reshape the income distribution. Box 1 draws out from the fiscal incidence study some interesting results on these topics. However, the main interest of this paper is in what the study may tell us about the prospective size of the 'voting for a living' population.

## Box 1: How much do different taxes and benefits reshape the income distribution?

The ABS's fiscal incidence study allows the calculation of measures of income inequality to estimate:

- first, the inequality that would arise from private incomes alone, without any taxes and transfers;
- second, the effect of each major category of government redistributive intervention (transfers in cash, income tax, transfers in kind, and selected taxes on production such as GST and stamp duties); and
- lastly, the total effect on final income after all taxes and transfers.

The ABS uses the most common summary of income inequality, the Gini coefficient, which potentially ranges between 0 and 1. A Gini coefficient closer to 0 represents a more equal income distribution than a Gini closer to 1.

Among G20 countries, Australia has a middling Gini rank, but has long been acknowledged to have a comparatively efficient tax and benefit system. Because Australia relies more heavily on income-testing benefits than other OECD economies, it achieves a large difference between income inequality before and after taxes and transfers, at a relatively low cost in terms of tax burden as a share of GDP, and much lower social expenditure as a share of GDP. For example, France's Gini is about 0.29, while Australia's is about 0.34; but France's tax-to-GDP ratio is 45%, compared to Australia's 28%.<sup>8</sup>

Table 1 below summarises the changes effected in the Australian income distribution over the last decade by each major category of taxes and benefits in the ABS methodology. The ABS notes there has been effectively no change between 2009-10 and 2015-16 in the Gini coefficient for final incomes. In both those snapshots, the tax and benefit system has reduced inequality in initial private income by about 43-44%.

However, from 2003-04 to 2015-16 there has been a slight change, with most of that change occurring before 2009-10:

- The initial distribution of private income widened about 2%.
- The contribution to the overall redistributive effort within each year from cash transfers fell, and the impact of transfers in kind rose.
- The redistributive contribution from the tax system rose a little, from about 16% of the total redistributive effort in 2003-04 to about 19% in 2015-16.
- The lesser redistributive effort of transfers in cash and kind slightly outweighed the increased effort from the tax system. So the distribution of equivalised final incomes widened slightly, with the Gini rising 9% from 0.23 to 0.25.

		2003-04		2009-10		2015-16	
Income components and taxes	ABS Income concepts	Gini coefficient	% contribution to overall equalisation	Gini coefficient	% contribution to overall equalisation	Gini coefficient	% contribution to overall equalisation
Wages, salaries, investment income, imputed rent	Equivalised private income	0.434	n.a.	0.446	n.a.	0.442	n.a.
ADD cash transfers	Equivalised gross income	0.335	48%	0.357	46%	0.361	42%
SUBTRACT income tax	Equivalised disposable income	0.292	21%	0.320	19%	0.316	23%
ADD transfers in kind	Equivalised disposable income (incl. social transfers in kind)	0.217	36%	0.243	40%	0.241	39%
SUBTRACT GST, stamp duty etc	Equivalised final income	0.228	-5%	0.252	-5%	0.249	-4%
% Gini coefficient reduction, all taxes and transfers		47%		43%		44%	

#### Table 1: Tax and transfer impacts on Gini coefficients; 2003-04, 2009-10 and 2015-16

Source: ABS 6537.0 Government Benefits, Taxes and Household Income, Australia: Summary of Results, 2015-16; released 20 June 2018.

The ABS fiscal incidence study identifies government benefits with sufficiently close connection to the beneficiaries to be able to allocate those dollar benefits to households. Such benefits comprise just over half of all government expenditure at all levels of government in Australia.

Within the totality of social benefits, the ABS distinguishes between social benefits in cash—which are pensions and allowances paid as general income support to individuals—and social transfers in kind—which provide health, education, and other benefits such as Medicare, child care subsidies and free school education. (Interestingly, academic studies of welfare typically consider only cash transfers that constitute the majority of the recipient's income to be welfare; social transfers in kind are not counted as welfare in many studies.)<sup>9</sup>

On the tax side, the ABS study allocates income tax (direct taxation) and various taxes on production (indirect taxation) such as GST to households on the basis that these are the taxes most directly felt by households—though as a basic principle of taxation theory the incidence of almost all, if not all, taxation ultimately falls on households even if, in the first instance, it is levied on other sectors such as business.

This can all be summarised with the following equation:

- A. Private income
- B. Plus social assistance benefits in cash
- C. Equals gross income
- D. Minus income tax paid
- E. Equals disposable income
- F. Plus social transfers in kind
- G. Equals disposable income plus social transfers in kind
- H. Minus selected indirect taxes
- I. Equals final income

In what follows, we focus on social benefits in net terms after deduction of taxes (items B, D, F and H).

#### Net benefits

The view people take of their dependency on government (and the potential attractiveness or otherwise of increasing that dependency) will depend not only on the benefits received but also on the taxes they pay.

The ABS uses the distinction between direct and indirect taxation to define two measures of net benefits: <u>net cash benefits</u>, which are gross cash benefits as defined above less income tax paid (or (B - D) in the equation above); and <u>net total benefits</u>, which are total benefits as defined above less both income tax and selected indirect taxes the ABS is able to assign to households (or (B - D) + (F - H) in the equation).

Figure 1 shows the distribution of the benefit (B) and tax (D) components of net cash benefits across the income distribution in 2015-16, while Figure 2 shows the net of the two (B – D). In all cases, the results are expressed as dollars per week averages for each quintile.

The distribution of income tax is heavily skewed to higher incomes as a result of the tax-free threshold, other concessions, and the graduated scale of marginal rates. Taking the whole population aged 18 and above, 46% pay no income tax at all after deductions and offsets are factored in. Among those of working age (18 – 64) this proportion is lower, but still about 38%.<sup>10</sup> Looking at households rather than individuals, in 2015–16 the lowest two quintiles accounted for less than 9% of all income tax paid, and the top two quintiles for 80%. As Figures 1 and 2 show, the income tax paid by the lowest two quintiles is much lower than cash benefits received, whereas tax paid is clearly higher than benefits for the top two quintiles. In the middle, the two are about equal. It is not possible to discern from the ABS data what percentage of all households are net beneficiaries in these terms, but other researchers have suggested that in the recent past as many as 48% of households received at least as much in cash benefits as they paid in income tax.<sup>11</sup>

Figures 3 and 4 show comparable measures based on the broader definitions of benefits to include the in-kind form (F) and of taxes to include selected indirect taxes (H). The picture is dramatically different compared with net cash benefits. As a result of inkind benefits being both higher and more evenly distributed across households—and despite the broader measure of taxes being less progressive than income tax alone—the net beneficiary status extends to the middle income quintile as well as the first and second. Even in the fourth quintile, although tax paid is greater than benefits received, the margin is small relative to the total of either tax or benefits.

This suggests the existence of a large pool of households receiving more in benefits than they

## Figure 1: CASH BENEFITS & INCOME TAX 2015-16 \$ pw by income quintile



Source: ABS, Government Benefits, Taxes and Household Income, Australia 2015-16 (ABS Cat. No. 6537.0)





Source: ABS, Household Income and Wealth, Australia 2015-16 (ABS Cat. No. 6523.0)

are paying in taxes. It is not possible to determine from the averaged data presented in Figures 3 and 4 precisely what proportion of households is in a net beneficiary position, but other data provided by the ABS suggests it is slightly above 50%.<sup>12</sup>

It should be emphasised that the existence of some number of net beneficiary households — on either the

narrow or broad definition — is to be expected, is not controversial, and is indeed desirable. Households that would be needy on the basis of their private income are the intended beneficiaries of progressive taxes and targeted welfare spending. Rather, the question is one of how far up the income distribution the status of `net beneficiary' extends and whether this creates



#### Figure 3: ALL BENEFITS & TAXES 2015-16 \$ pw by income quintile

Source: ABS, Government Benefits, Taxes and Household Income, Australia 2015-16 (ABS Cat. No. 6537.0)



#### Figure 4: NET EFFECT OF ALL BENEFITS & TAXES ON FINAL INCOME 2015-16 \$ pw by income quintile

Source: ABS, Government Benefits, Taxes and Household Income, Australia 2015-16 (ABS Cat. No. 6537.0)

incentives for political parties to seek to entrench majority support; either through increases in benefits concentrated on the middle and lower quintiles or increases in taxation concentrated on the upper quintiles.

The influence in-kind benefits have on political behaviour is open to debate. On the one hand, their value is larger than cash benefits for all income quintiles, and for the third, fourth and top quintiles, very much larger. On the other hand, households may not place the same value on in-kind benefits as they do cash benefits, and they may have only a vague idea of the value of in-kind benefits to them in any given year.

This point could work either way—they may be just as likely to have an inflated notion of the value of in-kind benefits as they are to under-value them. For health expenditure in particular, households may place a very high 'insurance value' on the availability of good medical and hospital care in the event of accident or serious ill health. Certainly, the importance attached to health and education benefits in voter surveys and in election campaigns suggests households value them highly—and political parties have responded by increasing expenditure on health and education programs massively, with only weak if any means testing and little if any linkage to improved outcomes.

The last point is a reminder that even though households may lack precise quantification of how the tax/transfer system affects them, political parties don't ignore the attraction of offering bigger transfers in kind. Individual voters do not need to be wellinformed and programmed calculating machines with a precise measure of the extent to which 'big government' benefits or costs them. It is necessary only that political professionals armed with focus group and polling data know how to appeal to each sub-group of net beneficiaries to create the impression their benefits from government will increase, or that voting for the other party will cause their benefits to shrink (think 'Mediscare').

#### Changes over time

Although the ABS has been producing estimates of government benefits and taxes allocated to households at five or six year intervals going back over 30 years to 1984, changes in definitions and methodologies limit our ability to make comparisons over time. However, there is a reasonably high degree of comparability among the earlier years (up to 1998–99) and among the last three observations (back to 2003–04).

To give a rough impression from the two sets of data, Figure 5 shows both net cash benefits and net total benefits back to 1984. For simplicity, the focus is on



Figure 5: MIDDLE QUINTILE NET BENEFITS as % of net income, since 1984

Source: ABS, Government Benefits, Taxes and Household Income, Australia 2015-16 and 1998-99 (ABS Cat. No. 6537.0)

the middle income quintile, as it is there that the largest shifts in net benefit position have occurred.

In the 1980s, the middle quintile was a significant net cash contributor, but has since been close to balance between cash benefits and income tax paid. On the broader measure of benefits and taxes, the middle quintile shifted from close to balance in the 1980s to being a substantial net beneficiary in the 1990s and retains that position in the most recent observations. This is consistent with other findings reported above concerning the rapid growth of in-kind benefits over time, and the concentration of this growth in the middle and higher quintiles. Although it is difficult to make comparisons over time, the data suggest that if net beneficiary status motivates voters in favour of higher benefits and political parties to design policies to cater for this demand, this effect may have strengthened since the 1980s with the spread of benefits in both cash and kind to the middle class.

Benefit dependency as measured may change over time for a variety of reasons, including obviously policies to change benefit rates and eligibility rules. But it can also change even without policy changes, just because demographic, economic or behavioural changes increase uptake of existing policies.

#### Public employment

Support for the 'voting for a living' hypothesis may also be found in public sector employment—not because public sector employees would be net beneficiaries in the tax/benefit calculus (or at least, not many of them), but because they owe their jobs and career advancement to government expenditure and regulatory activity. This is not to imply that public sector work is worthless or inferior to private sector work. Rather, the point is simply that people employed in the public sector may respond to public spending proposals in political parties' platforms with less of an eye to the effectiveness of the policy in terms of its stated objectives, and more with an eye to their own careers (think of teachers and their involvement in the 'I give a Gonski' campaign).

There is survey-based evidence that public sector workers are more likely than private sector workers to vote Labor and more likely to favour higher government spending over lower taxes, although this tendency may be related to some other factor such as post-school qualifications rather than the employment sector *per se*.<sup>13</sup> Be that as it may, public sector employment in June 2016 was 16% of total employment and 11% of the voting age population—a figure that is little changed from earlier comparable periods.

If we simply add this group to the net beneficiary groups discussed in earlier sections, there may be some double counting. However, given that average cash remuneration in the public sector was \$76,600 in 2015-16, there are unlikely to be many households containing public sector workers that are also net beneficiaries of government benefits and taxation. Private income in the middle income guintile averaged \$73,000 in 2015-16, but with an average of 1.3 employees per household, so only \$56,200 'equivalised', or per person. A full-time public servant earning the public sector average wage would likely be in the top two quintiles of households, not the bottom three. Part-time public sector workers - who comprise about one-quarter of total public sector employment - would be the most likely to be included in net beneficiary households.

# Bringing it all together — the 'voting for a living' population

Just over 50% of households are net beneficiaries of the tax/transfer system as (broadly) defined above. In addition, many of the 1.9 million public sector employees—by virtue of their relatively high wage and salary incomes—would live in households not in the net beneficiary population. Taking these two groups together, there is a clear majority of households—perhaps around 60%—that may be motivated to support policies of higher public expenditure and taxation based on their dependence on social transfers and public sector wages and salaries for a living.

That is not to say that the same proportion of voters are so motivated, as it is not households that vote but individuals of voting age. As lower income households on average have fewer members of voting age (for example, as few as 1.3 in the lowest income quintile) than higher income households (2.6 in the highest quintile), the population of voting age in net beneficiary households comprises less than half the total population of voting age — probably close to 40%. Combining these with individuals in public employment, the 'voting for a living' population may be around 50% of the total.

These do not include the other categories we identified at the outset — namely, those in private sector employment heavily dependent on government subsidies and those involved in relevant advocacy

activities. While beyond the scope of this paper to quantify, these groups would be substantial.

These conclusions may be criticised on the grounds that the preferences of the net beneficiary population would be largely neutralised by the net contributor population in a situation where the two are roughly equal. However even if net beneficiaries plus government employees are not yet a dominant majority, they are significantly large, and their defence of existing benefits and advocacy for more spending are likely to be well organised and vigorously pursued.

For example teachers, teacher unions, parents of children in public schools and the ABC all support the agenda for strong growth in government education spending; apparently regardless of whether education outcomes are rising or falling.

In contrast, the objections by net taxpayers to ineffective growth in education spending are a much more disparate force. (When was the last time there was a voter demonstration against a wasteful government policy, a personal tax increase, or a failure fully to index income tax thresholds?)

This contrast between beneficiaries and contributors in the public finance system is rather like the explanation that used to be offered of the persistence of industry protection in Australia—the winners were concentrated and vocal; the losers diffuse and silent.

### Evidence of voting for a living

The factors that influence people to vote as they do—and to participate more broadly in the democratic process—are many and complex. Being a net beneficiary of the tax/transfer system is only one such factor. Moreover, we do not suggest that net beneficiaries would vote consistently as a block for one party. Rather, it is a matter of what their policy preferences are, and how political parties may be motivated over time to design policies to appeal to those preferences. The cumulative effect of these preferences—and of how they condition political parties' to behave—is that benefits become entrenched and enhanced over time, with all parties participating in the bidding for votes and winning the favour of overall majorities at different elections.

For this reason, it is difficult to discern any partisan pattern of 'voting for a living' at any point in time. Perhaps more revealing are the results of voter policy preferences. For example, the latest version of the annual tax survey of Per Capita think tank reveals the following:

- Almost 70% agree that government should spend a lot or a little more (and more 'a lot' than 'a little') on public services;
- More than 75% favour spending more on health and education, and more than 50% on social security (functions that together account for more than 60% of all government spending);
- But the only item for which a majority would be prepared to pay higher taxes is 'better health and aged care services';
- Rather, the favourite tax increases are 'reducing corporate tax avoidance' and 'raising tax on the top 5% earners'. Tax increases that would affect everyone, such as raising income tax rates and increasing the GST, are supported by less than 15% of respondents.<sup>14</sup>

The ultimate test is one of observed political trends: are the hypotheses outlined above as a consequence of 'voting for a living' being observed more and more in Australian politics over time?

#### What is to be done?

If more people now vote for a living than work for a living, what is to be done?

We can at least begin to understand one important cause of our policy problems, understand why current problems have proven intractable, and see what sort of policies and politics would help return Australia to its strong reformist recent past.

It is fair to say no political party ever set out to deliberately create a 'voting for a living' support base. It is not a policy target. As Professor Peter Whiteford has written in his magisterial survey of the interactions of the tax and benefit systems: "The share of 'zero net taxpayers' in the population is in a sense an 'accidental statistic'. It is the by-product of other decisions ..."<sup>15</sup>

However, while it is a by-product, it is in our view a step too far to argue, as Whiteford does, that it is not a useful concept. In the realm of policymaking, it is useful as a manifestation of problems with policies that have been adopted in isolation for various purposes, but have intersected in unintended ways to cause unanticipated distortions.

Corrective policies and politics might include:

- Transparent enumeration of the problem and debate about it, of the kind this paper aims to carry forward.
- Sharpened inter-generational fiscal modelling to show how an irreversible downward spiral of bad policies increases the risk of economic crisis.
- Renewed focus on broadening tax bases, flattening progressive rates and lowering or eliminating the income tax-free threshold.
- Renewed focus on removing middle class welfare in the forms of transfers in kind which contribute disproportionately to the middle

deciles of the income distribution being net beneficiaries rather than net taxpayers.

- Tighter means testing of benefits.
- Lowering the share of government spending in GDP, which is the aim of the CIS TARGET30 campaign.<sup>16</sup>
- Shifting the political competition away from spending more on education, health and the like to a focus on the effectiveness of current levels of spending.
- Putting a lid on public sector employment and the strong growth in its pay and conditions.

A little of the above is being done, but it is more the case that Australia is now set on the path of increased taxation—if not explicit, then by stealth through personal income tax bracket creep. While some correction to this process has now been legislated, the great bulk of the correction will not begin to take effect until 2022. In the meantime, combined personal income tax and GST revenues are estimated to increase by 40% from 2015-16 (the data point of the current ABS fiscal incidence study) to 2021–22 (the next likely data point).<sup>17</sup> This is an even faster rate of increase than that in Commonwealth expenditure on social security and welfare, education and health-which helps explain how the budget can return to surplus even with strong growth in expenditure.

If these projections are realised, they suggest that if there is to be any reduction in the 'voting for a living' population in the years ahead, it will be a result of increased taxation across the board. However, it is hardly the best way for it to come about and is likely to be temporary as growth of spending on government benefits reasserts itself as the dominant force in the longer term.

### Appendix A: The fiscal incidence study, 'Government Benefits, Taxes and Household Income'

The Australian Bureau of Statistics describes its fiscal incidence study in the following terms.

This publication presents results from a Fiscal Incidence Study undertaken to show the effects of government benefits and taxes on the distribution of income among private households in Australia in 2015-16. Previous studies were conducted in 1984, 1988-89, 1993-94, 1998-99, 2003-04 and 2009-10.

Household income is increased directly by the Australian government through social assistance benefits in the form of cash payments, such as the age pension and family tax benefit, and indirectly by government expenditures such as those on health and education. On the other hand, household income is reduced by taxes on personal income (direct taxes) and by taxes on production (indirect taxes) passed on in the prices households pay for goods and services. This study shows the effect on household incomes after taking both government benefits and taxes into account.

The FIS excludes government taxes and expenditure that do not relate directly to particular types of households or household expenditure, such as government revenue from corporate taxes and spending on defence, public order and safety, transport and communications.

The three major data sources used in the FIS were the 2015-16 ABS Household Expenditure Survey, ABS Government Finance Statistics, and Input-Output tables from the Australian System of National Accounts.

The fiscal incidence study takes private income as the starting point and then works through to gross income, disposable income, disposable income including transfers in-kind, and final income. This progression is schematically described as follows by the ABS:

#### COMPONENTS OF FINAL INCOME



Source: 6537.0 - Government Benefits, Taxes and Household Income, Australia, 2015-16, 20 June 2018.

The ABS study is not confined to Commonwealth taxes and benefits. Some state and local taxes and benefits are also included. Just over 50% of total general government sector expenses are included on the benefit side, and just under 60% of total taxes on the taxation side.

#### Endnotes

- 1 Robert Carling, *From Reform to Retreat: 30 Years of Australian Fiscal Policy*, Centre for Independent Studies Occasional Paper 161, Sydney, 10 December 2017.
- 2 Stephen Kirchner, *Why Does Government Grow?* Policy Monograph 117 (The Centre for Independent Studies, 2011).
- 3 Peter Whiteford (2016), *Should we be worried about "Zero Net Taxpayers"*? Policy Brief 5/2016, Tax and Transfer Policy Institute, Crawford School of Public Policy, ANU.
- 4 The Library of Economics and Liberty, www. econlib.org/library/Enc/PublicChoice
- 5 Glen Levy, *Mitt Romney's '47 percent' Gaffe Tops Yale's Quotes of the Year*, Time, 13 December 2012
- 6 Whiteford, op cit.
- 7 One might conceptually scope the 'advocacy industry' by summing the staff of advocacy groups whose members are not government employees. Getup, ACOSS, refugee advocacy groups, teachers unions, and so on. Obviously the numbers would be large. ABC staff would not be included in such an exercise as they are already counted as government employees.
- 8 OECD Revenue Statistics 2017, http://www. oecd.org/tax/revenue-statistics-france.pdf . The Australian Gini coefficient cited here is from OECD sources (https://data.oecd.org/inequality/ income-inequality.htm) and is not comparable to the Ginis cited in the ABS fiscal incidence study and Table 1.

- 9 Roger Wilkins and Inga Lass, The Household, Income and Labour Dynamics in Australia Survey: Selected Findings from Waves 1 to 16, Melbourne Institute, University of Melbourne, pp 39-41, especially Box 3.7, 'Welfare Payments'.
- 10 John Daley, *et al*, *A fairer super system: assessing the 2016 tax reforms,* Grattan Institute, Melbourne, 2016.
- 11 Whiteford, op cit, 14.
- 12 Australian Bureau of Statistics, Government Benefits, Taxes and Household Income, Australia, 2015-16, (Cat. No. 6537.0), Income Redistribution and Inequality, Graph 4 — Distribution of Net Benefits to Households, 2015-16, and plotting points provided to authors.
- 13 Peter Saunders, 'The Rise of the Opinionators', *Policy* 22:2 (Winter 2006), 3-10.
- 14 Per Capita Tax Survey 2018, www.percapita.org. au/our\_work/per-capita-tax-survey-2018/
- 15 Whiteford op cit, 35.
- 16 Simon Cowan, et al, TARGET30 Towards Smaller Government and Future Prosperity, The Centre for Independent Studies, Sydney, 2013.
- 17 Commonwealth Budget 2018-19, Budget Paper 1, Statements 5 and 6.

#### About the Authors



#### **Robert Carling**

Robert Carling is a Senior Fellow at The Centre for Independent Studies where he undertakes research into a wide range of public finance issues, writes papers for publication, and regularly comments in the media on taxation and other budget issues. Before joining the CIS, Robert was a senior official with the New South Wales Treasury, the Commonwealth Treasury, the IMF and the World Bank.



#### Terrence O'Brien

Terrence O'Brien is a retired public servant who has worked for some 40 years in the Commonwealth Treasury, Office of National Assessments, Productivity Commission and at the OECD and World Bank.

POLICY Paper 9 (PP9) • ISSN: 2209-2447 • ISBN: 978-1-925744-26-2

#### THE CENTRE FOR INDEPENDENT STUDIES

Published September 2018 by The Centre for Independent Studies Limited. Views expressed are those of the authors and do not necessarily reflect the views of the Centre's staff, advisors, directors or officers.

 $\ensuremath{\mathbb{C}}$  The Centre for Independent Studies (ABN 15 001 495 012)

This publication is available from The Centre for Independent Studies. Visit www.cis.org.au.