Penalised for Success: Perils of Having A Low Voter Base

Why is it that a state which has a small voting base is penalised for having a successful world class mining industry?

The politics surrounding Resource Rent Tax in the Henry Tax Review, launched May 2, 2010, and the upcoming federal election campaign in part provide the answer.

However, it is clear that the public response has not been what the Prime Minister expected.

Proposing a Resource Rent Tax on so-called "super" profits seems a great way to spread around the wealth.

That is what the politically correct political class sees as their duty, namely to distribute the largess from the successful Australian mining industry, predominantly located in Western Australia, to Australia's rust belt states of Victoria and New South Wales.

We will ignore that the fact that this is based on assumed perpetual growth of China and then India which is confidently represented by straight lines going upwards.

But this is not really about optimistic projections, rather the implications of a high-spending government in Canberra and its relationship with the most western state in the Commonwealth.

In federal elections, the votes of outer-suburban, mortgage belt, middle Australia are paramount.

The problem is that Western Australia does not have enough of them.

Sydney's and Melbourne's Western suburbs outnumber WA's seats at least eight-fold.

So it's there that governments in Canberra are made and unmade.

WA still has the States' house which is meant to act as a constitutional safeguard for smaller states.

The issue is that the Senators in this State's house have long since shifted allegiance to political parties rather than their home state.

This leads to the more interesting issue about how we got into this mess in the first place.

In 1975, an emerging economist with experience in Melanesia and schooled in Canberra academia co-authored an article titled "Taxing of Natural Resources Projects".

In it he wrote: "The central task of economic management in the resource based industries is thus to maximise the contribution that these industries make to government revenue."

His name was Ross Garnaut who went on to develop an economic argument around the apparent "Neutrality of the Resources Rent Tax" (RRT).

Possibly, in his various encounters with a then young Queenslander who, not coincidentally, was studying in Canberra, Garnaut explained the logic of resource rent taxes and other environmentally-linked taxing opportunities.

Garnaut still has immense influence within the Canberra halls of power and that young Queenslander is now the Prime Minister.

The arguments against a RRT are not new either.

In 1983, Dr Michael Porter wrote: "The fundamental flaw in this argument, however, is that *prior* to sinking a well or drilling a hole is precisely the prospect of some sort of bonanza which encourages the miners to continue in areas other than those of high mineral prospectively. A special taxation on super profits, then is actually a tax on the marginal mining prospect – and at some time in their lives, *all* mines are marginal, just as early in life Phar Lap was just another horse. A 35 percent "super tax" on the winners of horse races, for example, would deter the entry of almost all marginal horses; so too special taxation of the mining sector must have the inevitable consequence of deterring all by the most highly prospective mineral activities."

To be fair it should be stated that Garnaut and Porter have both been consistent.

As chairman of a major mining company, Garnaut has supported the RRT.

Certainly a company director supporting a tax he has believed in for the past four decades is a sign of consistency, as generally company directors seek lower rather than higher taxes, especially in their own industry.

Porter has also been consistent and said in a letter to the *Australian Financial Review* on May 6, 2010, that: "A so-called super tax is a tax on success and effort."

While Western Australia has a low voting base, it should not be penalised for success.

At least there is consistently bad and consistently good thinking on the RRT and there remains an ability to do something about it.

For now.

What can be done?

1) **Reject the Parameters of the RRT Debate**: Prime Minister Rudd has attempted to define the debate about the rate and implementation of the mining "super" tax. Entering into this debate is wrong. The philosophy behind tax, enterprise and equity should be the focus of the response to the RRT. The need for a specific federal resources tax should be fundamentally disputed.

2) **Focus on Where Votes Count**: A drawback of having a small state population is that you do not get many votes in the House of Representatives. However, the Senate has equal representation for all of the states. As South Australian Senator Nick Xenophon has shown, breaking the monopoly of major party candidates is healthy for your home state.

3) **Firewall State Services and Funding Streams**: Greater fiscal and operational independence of core state services (as per the 1901 Constitution) is important to be able to resist moves such as the RRT. Avoiding creeping erosion of state capabilities places you in a much stronger bargaining position than if you are completely reliant on Canberra.

4) **Promote the Minerals and Energy Sector to the Public**: For a sector which already pays so much tax; employs hundreds of thousands of Australians; and is transforming the nature of the overall economy, there is surprisingly little public awareness or understanding of how it actually works. If the unions can successfully run marginal seat campaigns on little more than ideology, why can't the mining community simply convey the facts to the public? Certainly this is now happening, but the metaphorical horse has already bolted and much remedial work needs to be done.

5) **Read the Constitution**: The minerals are owned by the Crown, but it is the Crown in terms of states. Therefore it is up to the State to determine the royalties payable on minerals extracted from that State. Comparisons to the petroleum tax are inappropriate from a constitutional perspective.

-Andrew Pickford is a Senior Fellow at Mannkal Economic Education Foundation