

Taxation and The Size of Government in Australia: Current Trends and Future Prospects

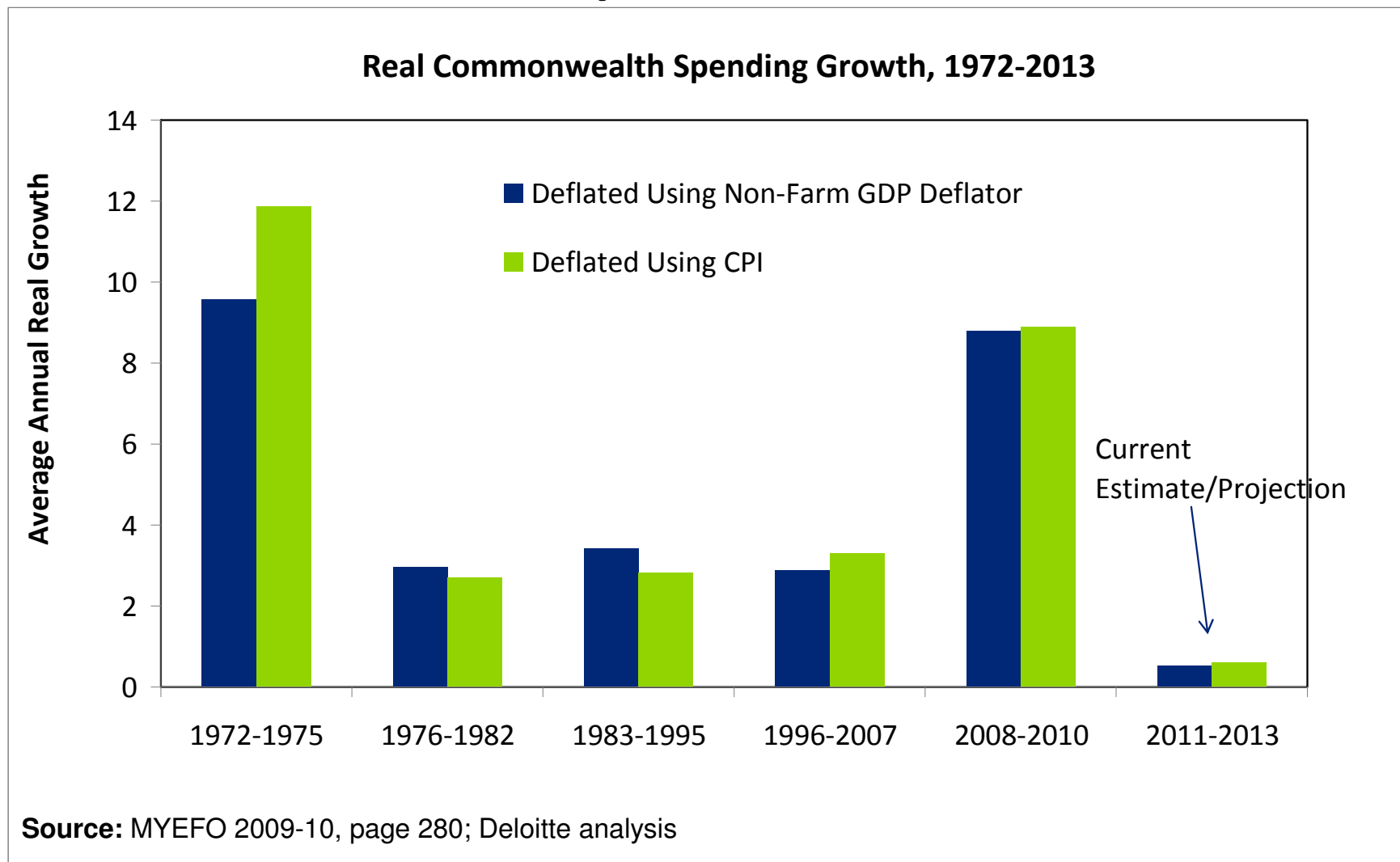
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8 April 2010

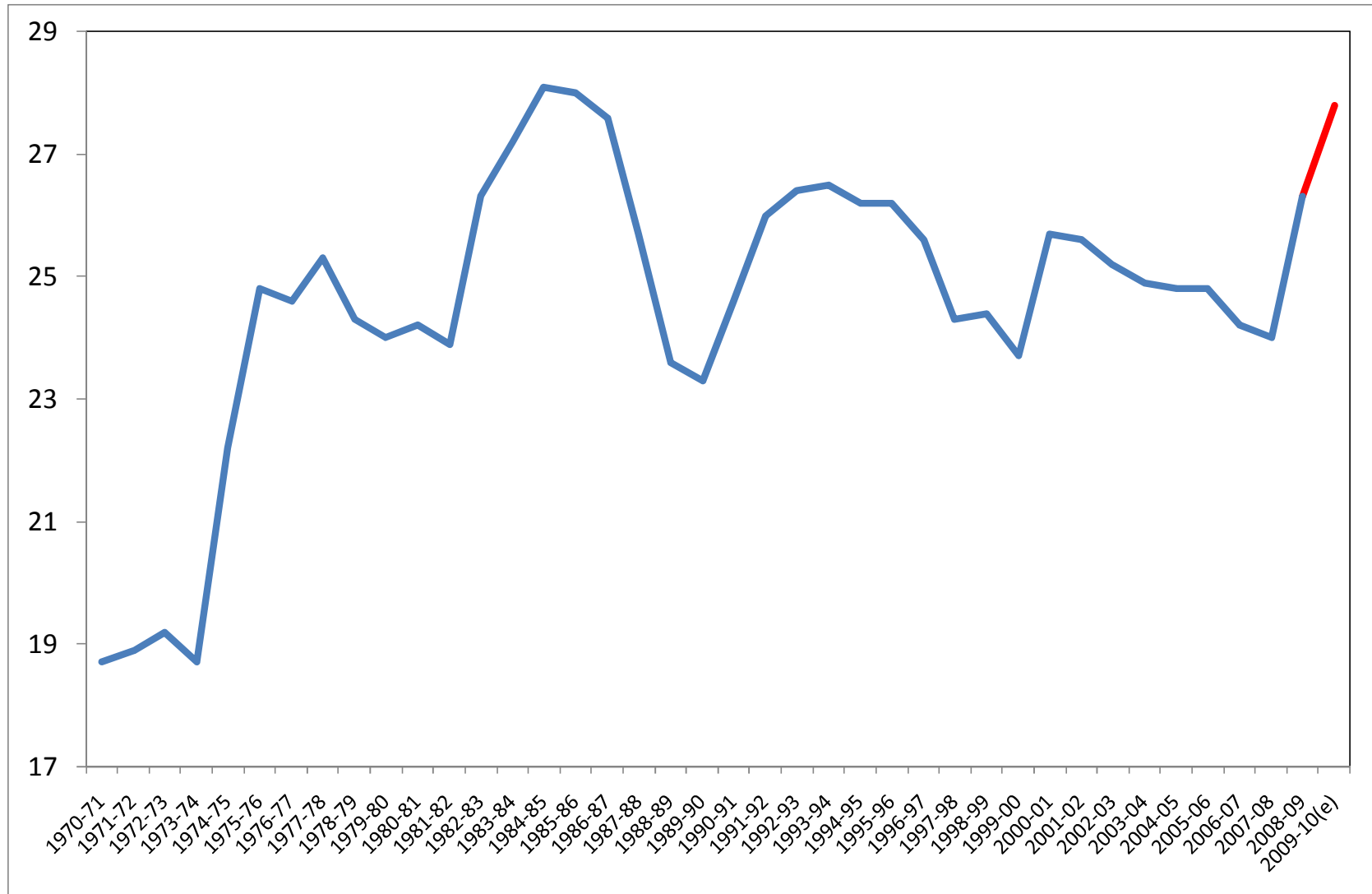
Outline

1. Current Trends and Future Prospects in Spending
2. Why Does it Matter? The Economic Costs of Spending, Taxation and Regulation
3. Current Trends and Future Prospects in Taxation
4. Current Trends and Future Prospects in the Volume of Regulation
5. Conclusion

Real Commonwealth Spending Growth, 1972-2013

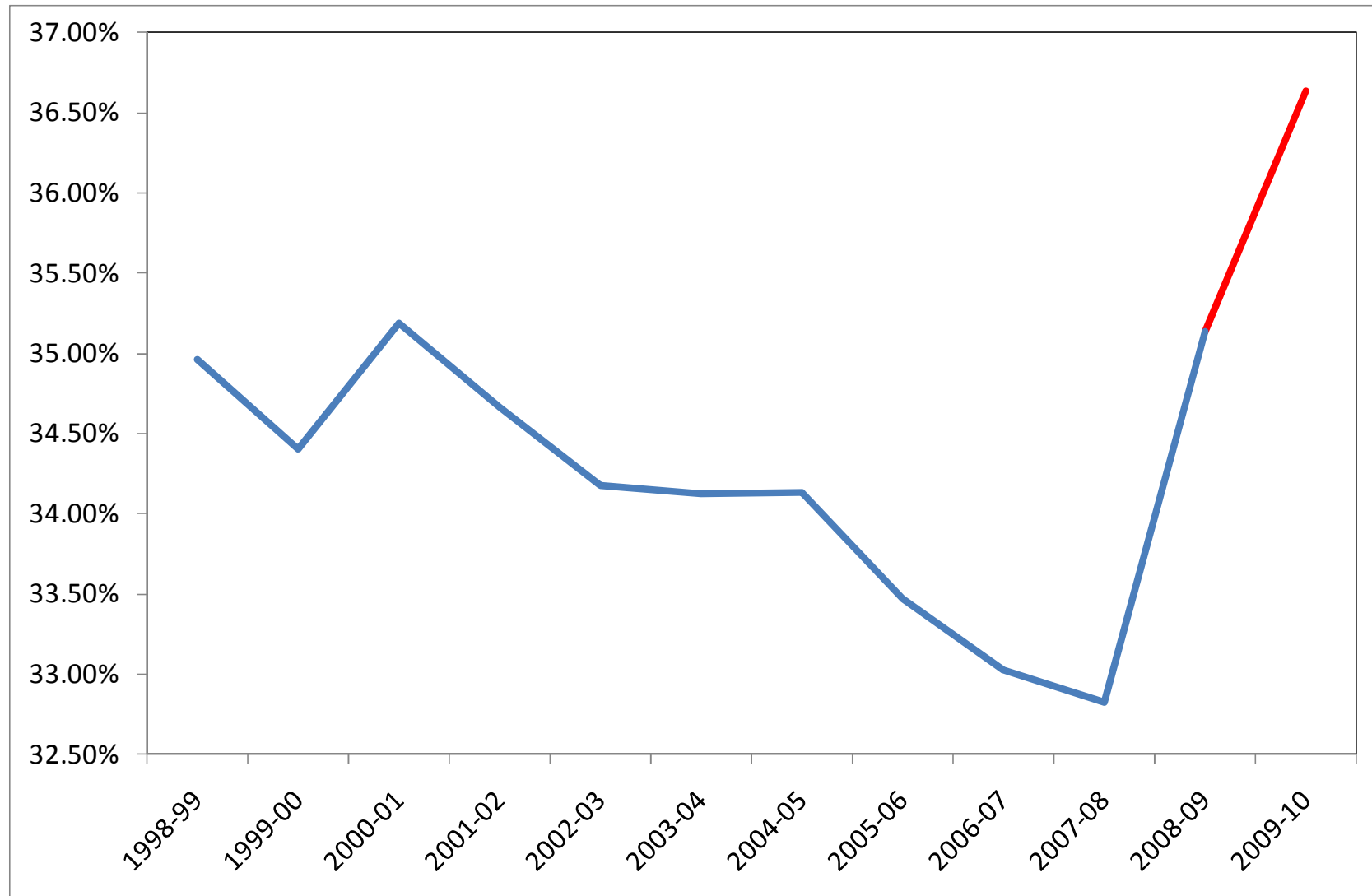


Commonwealth Government Spending: Proportion of GDP



Source: MYEFO 2009-10

All Government Spending: Proportion of GDP



Source: ABS, Government Finance Statistics; National Accounts; MYEFO 2009-10

Why Does it Matter?

- Higher government spending:
 - Leads to higher taxes
 - Reduces household disposable income
 - Reduces private saving
 - Reduces investment
 - Reduces economic growth
 - Reduces living standards below what they would otherwise be

Why Does it Matter?

- Note also that these are just the costs of taxation.
 - Spending can have its own adverse economic effects (eg distortionary subsidies) , but these are separate from the costs of raising revenue.
- Government spending can have benefits, but these costs of taxation should not be ignored.
- If the costs exceed the benefits, the community as a whole is poorer.

The Costs of Taxation

- Deadweight Costs of Taxation: Taxes “eat up” some of the possible gains from trade.
 - Simple example: Suppose that you are willing to pay \$10 for a shirt, and it costs the producer \$5 to make.
 - Then the total possible gains from trade are $\$10 - \$5 = \$5$, and trade will only be undertaken if it is expected to be mutually beneficial.

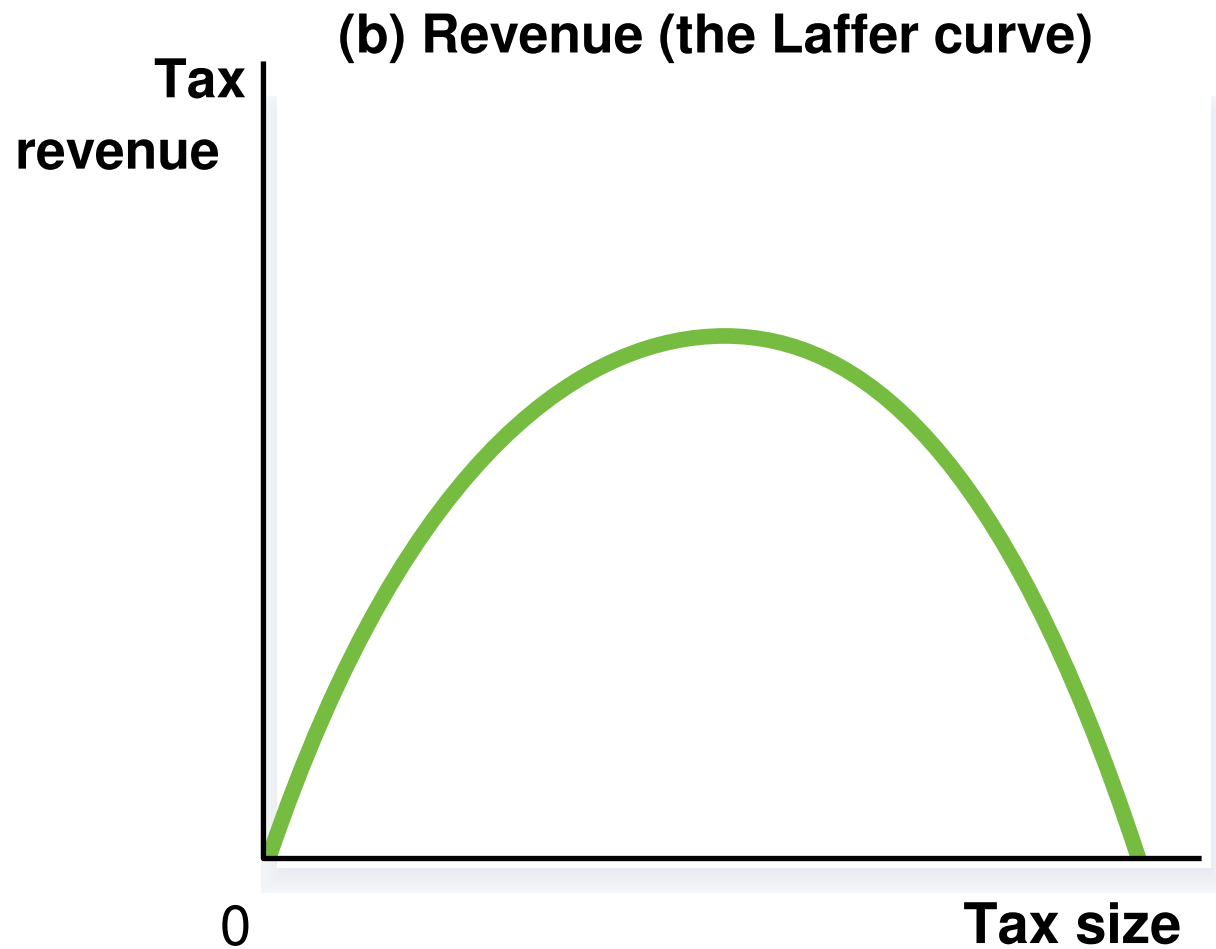
Costs of Taxation

- But now suppose there is a shirt tax of \$6. Then the size of the tax is so large that the gains from trade are completely eat up by the tax.
- A mutually beneficial exchange is no longer possible.
- Note here that the tax destroys all the possible gains from trade, as well as raising no revenue!

Deadweight loss and tax revenue

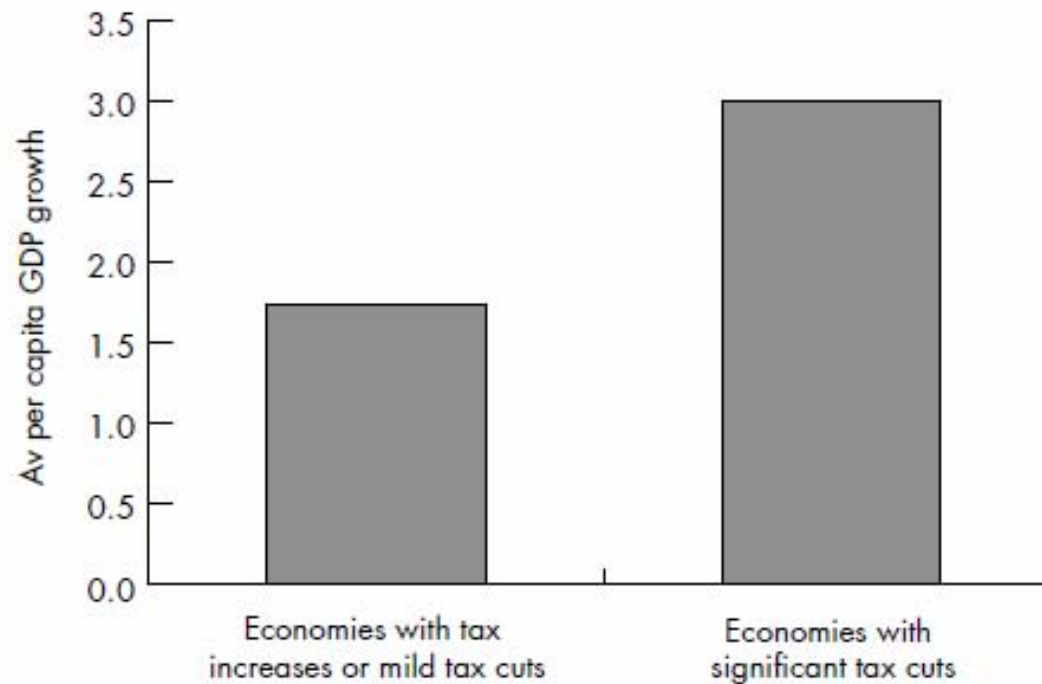


Deadweight loss and tax revenue



Income Tax Cuts and Economic Growth

Figure 3. Income Tax Cuts and Per Capita Economic Growth
Average Performance of OECD Countries, 1980-2000



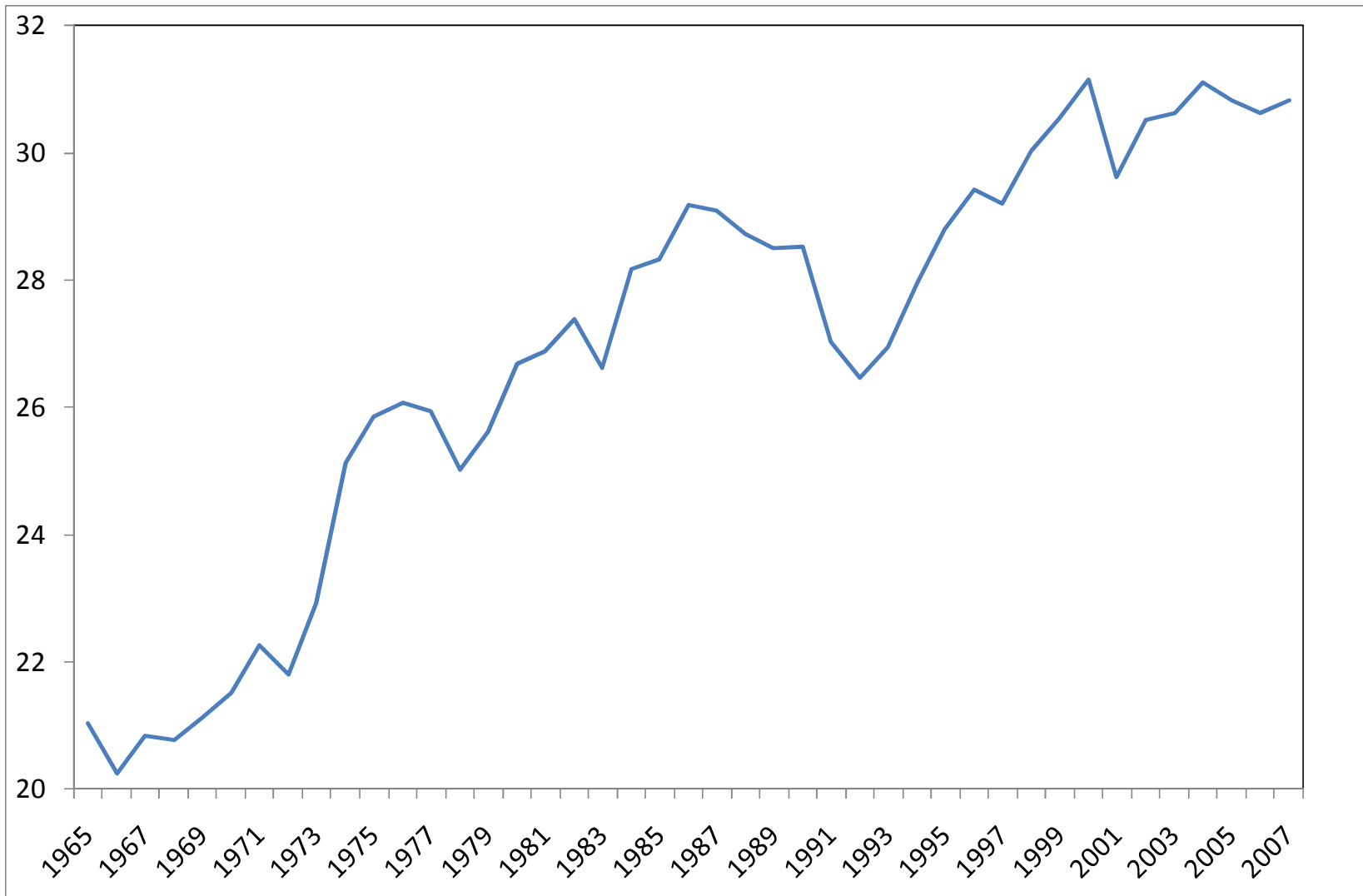
Sources: Fraser Institute, *Economic Freedom of the World*, various issues; Penn World Tables 6.1, Real GDP Per Capita 1980-2000, see <http://dc2.chass.utoronto.ca/pwt/>

Other Costs of Taxation

- Other Costs:
 - Administrative Costs
 - Enforcement Costs
 - Compliance Costs
 - Evasion Costs
 - Lobbying Costs

Tax Revenue/GDP

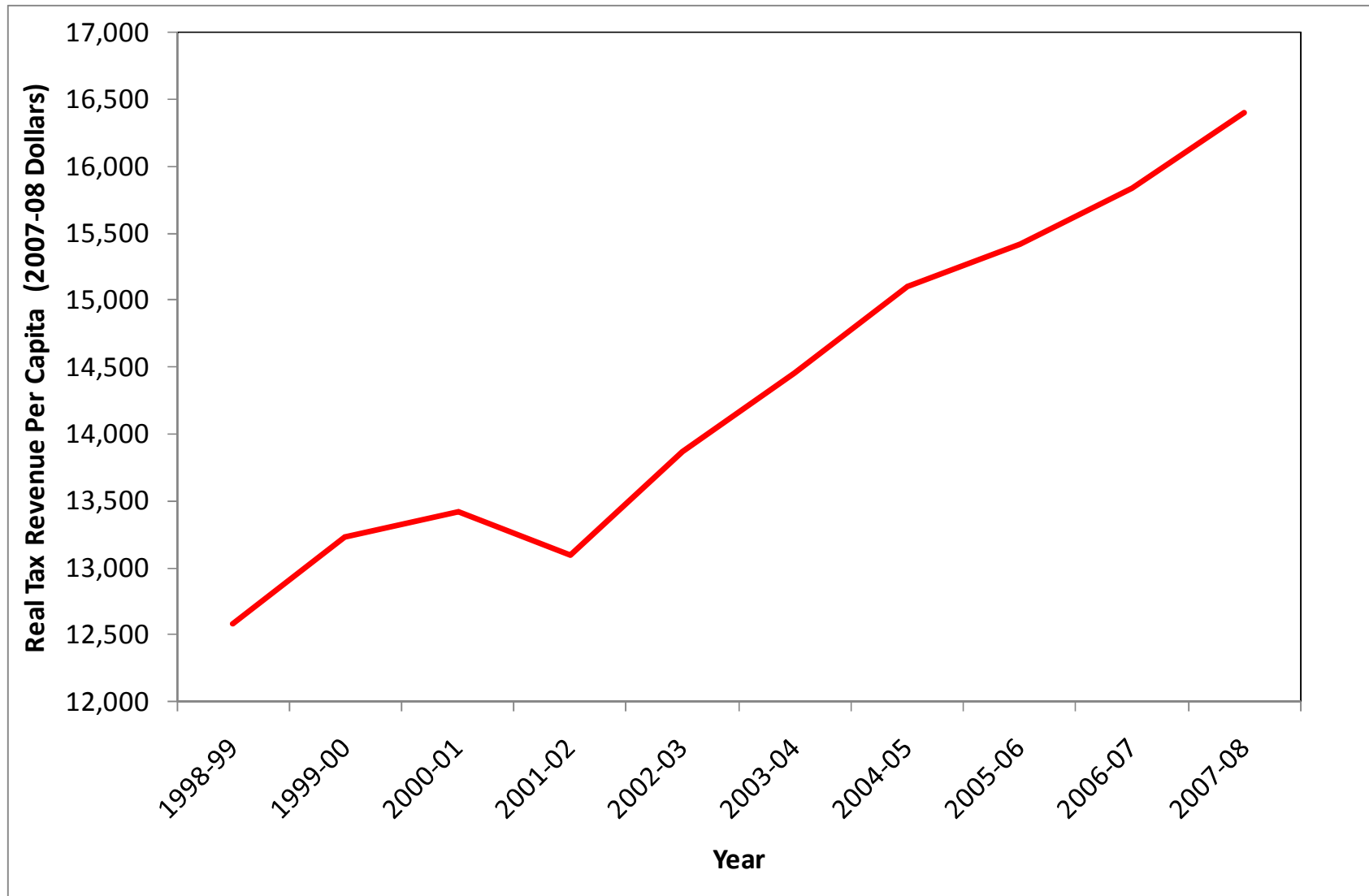
All Levels of Government



Source: OECD

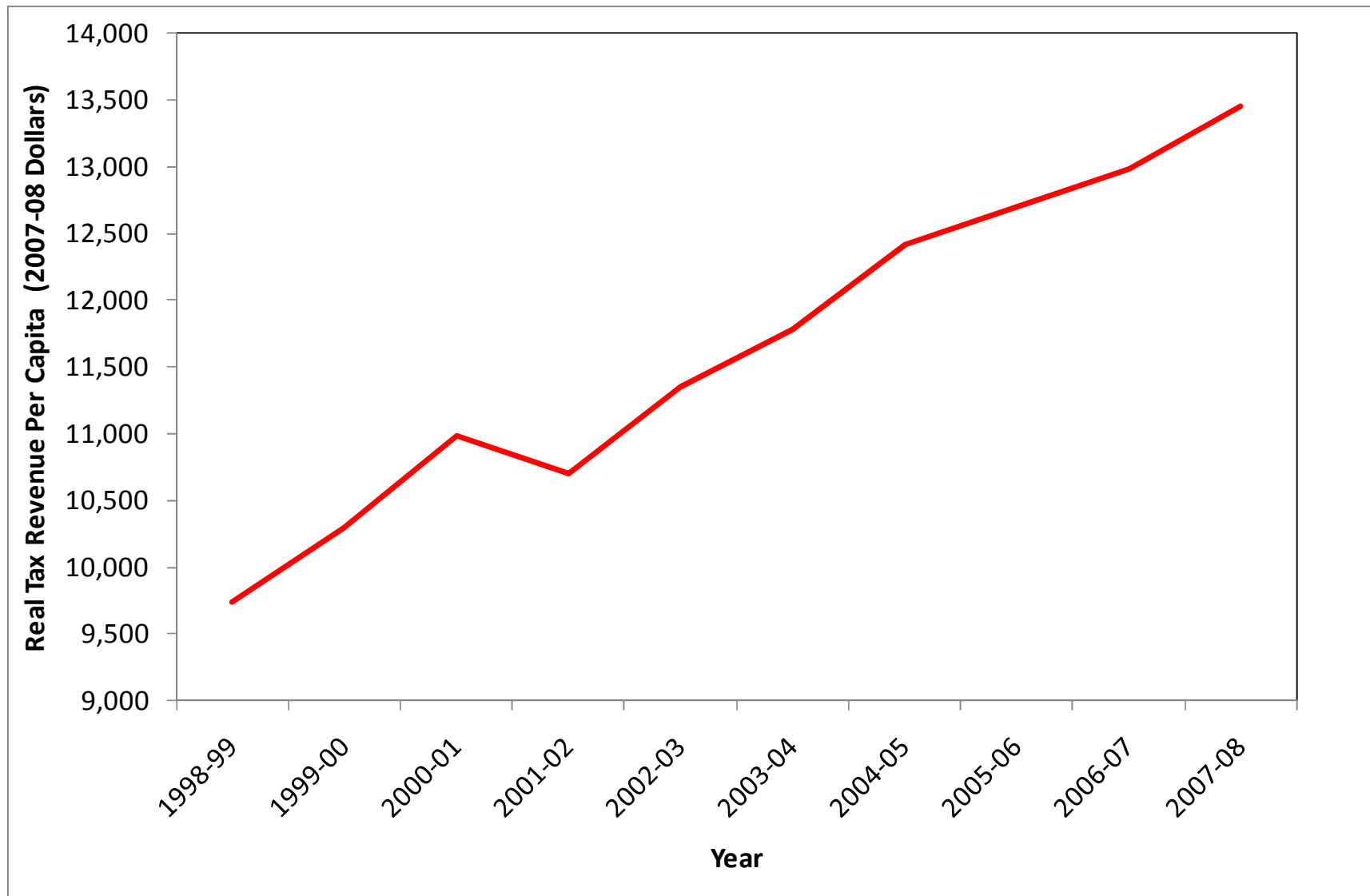
Taxation: Current Trends

Real Tax Revenue per Capita, All Levels of Government



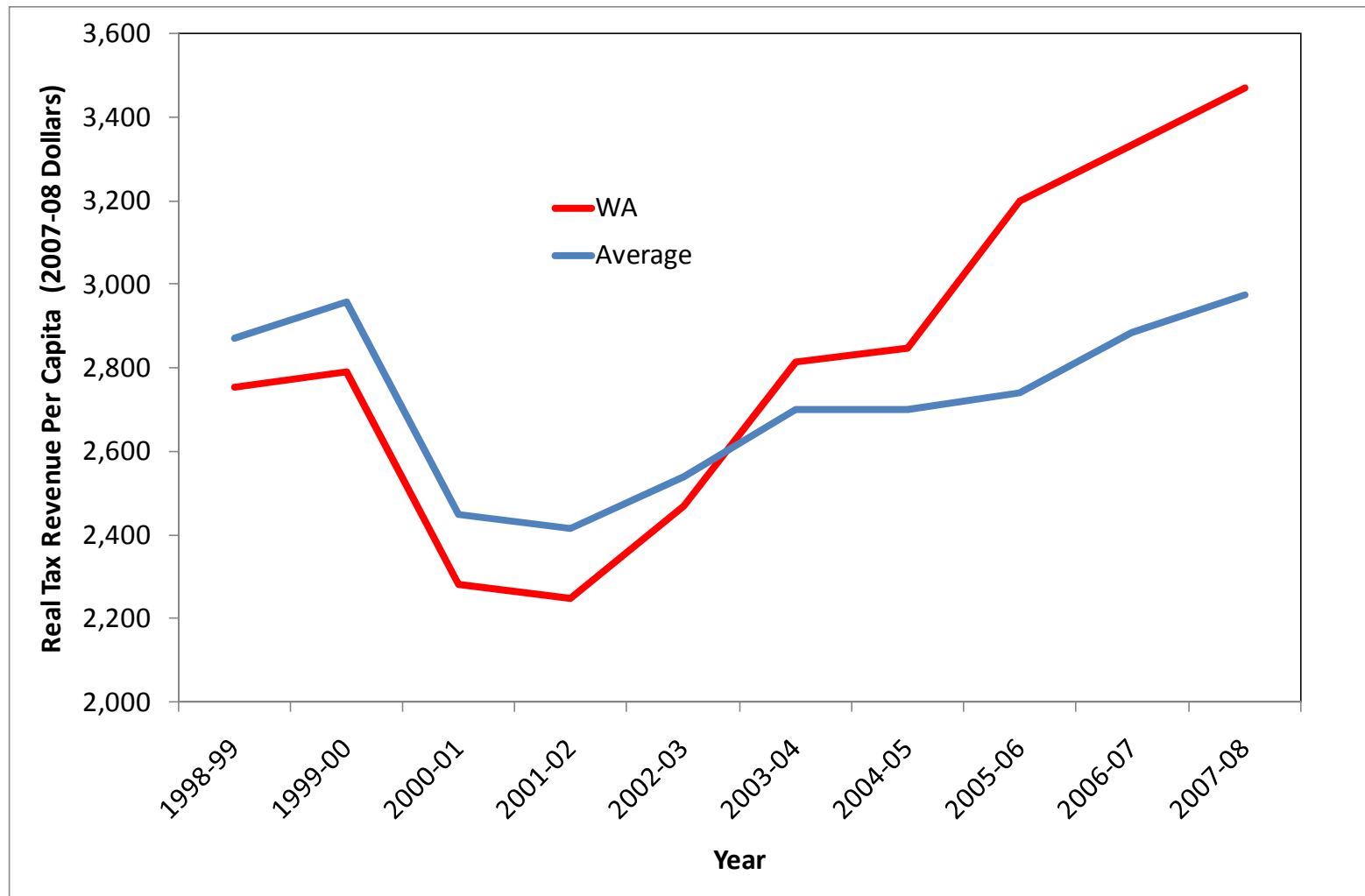
Source: ABS, Taxation Revenue, Australia, 2007-08; ABS CPI

Real Taxation Revenue per Capita: Commonwealth Government

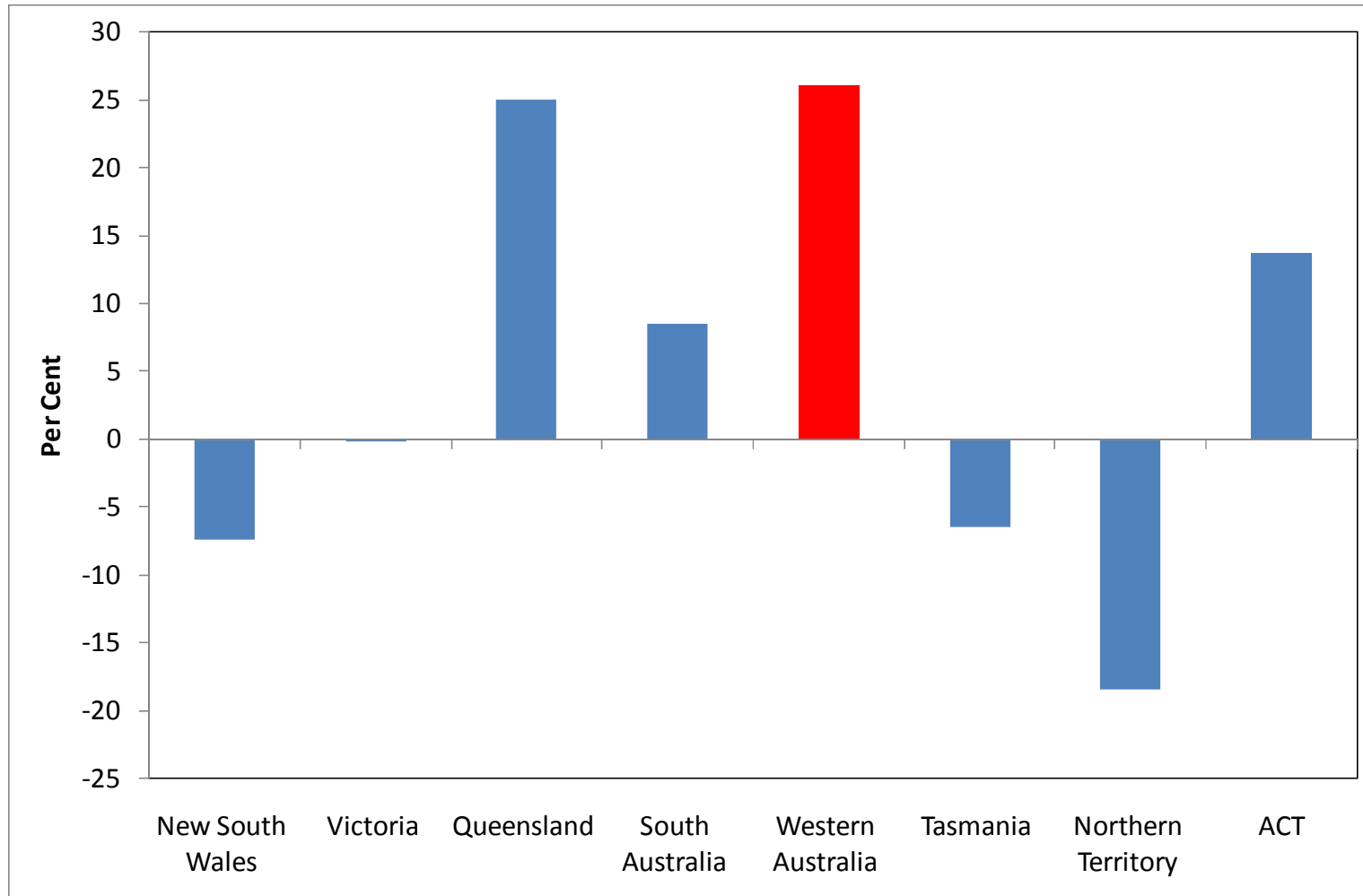


Source: ABS, Taxation Revenue, Australia, 2007-08; ABS CPI

Real Taxation Revenue per Capita: States

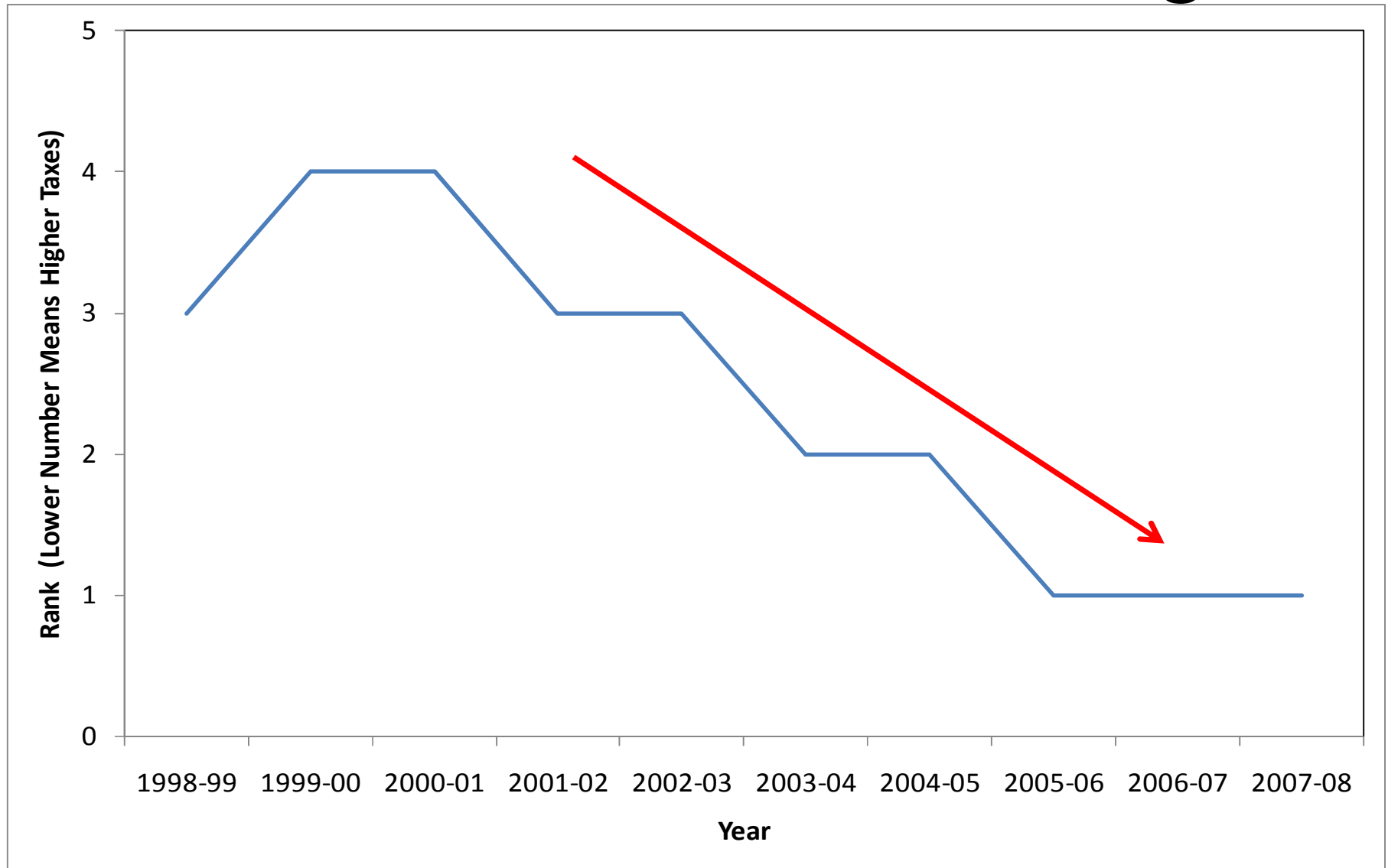


The States: Growth in Real Taxation Revenue Per Capita, 1998-99 to 2007-08



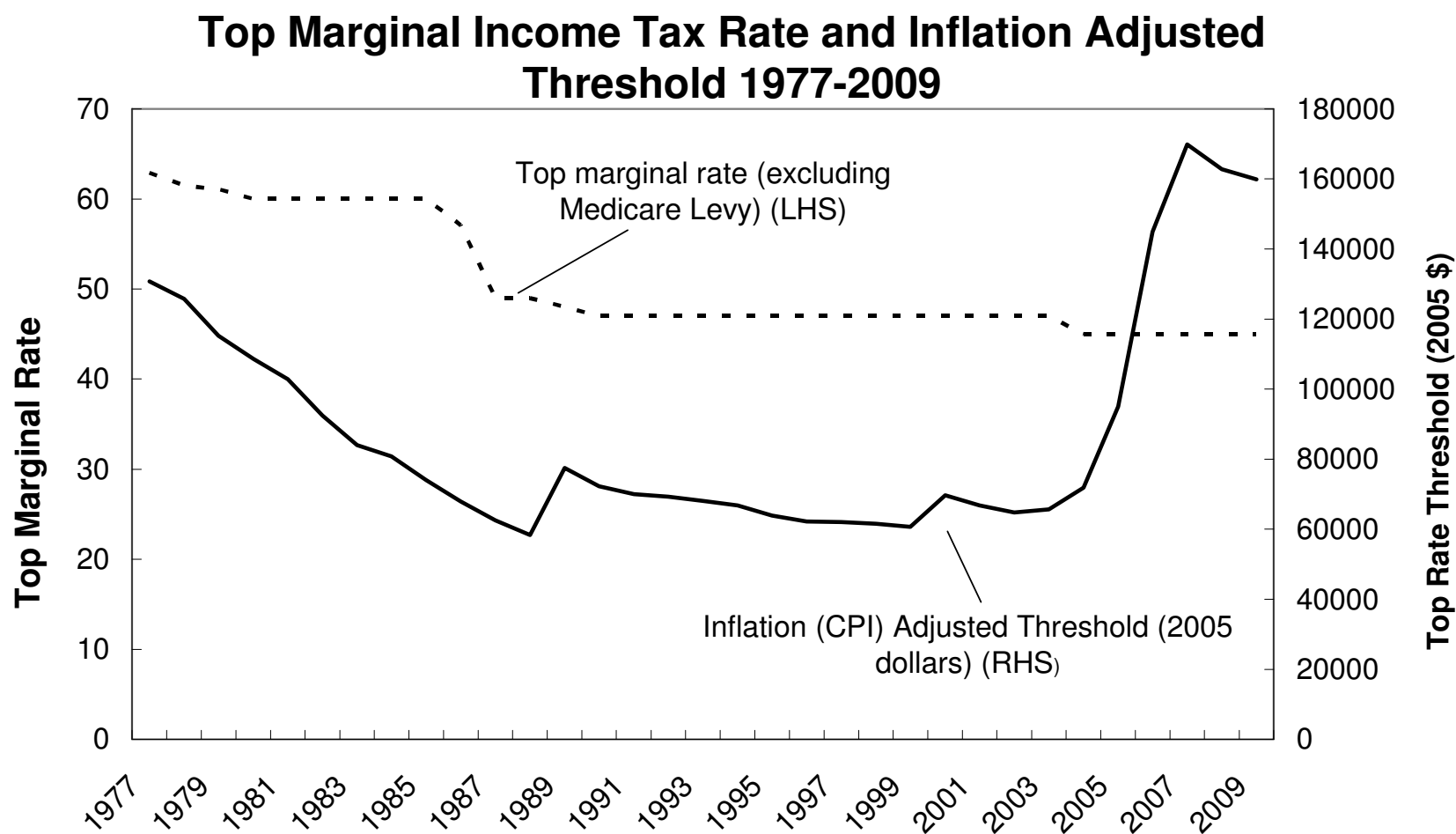
Source: ABS, Taxation Revenue, Australia, 2007-08; ABS CPI

Western Australia's Ranking



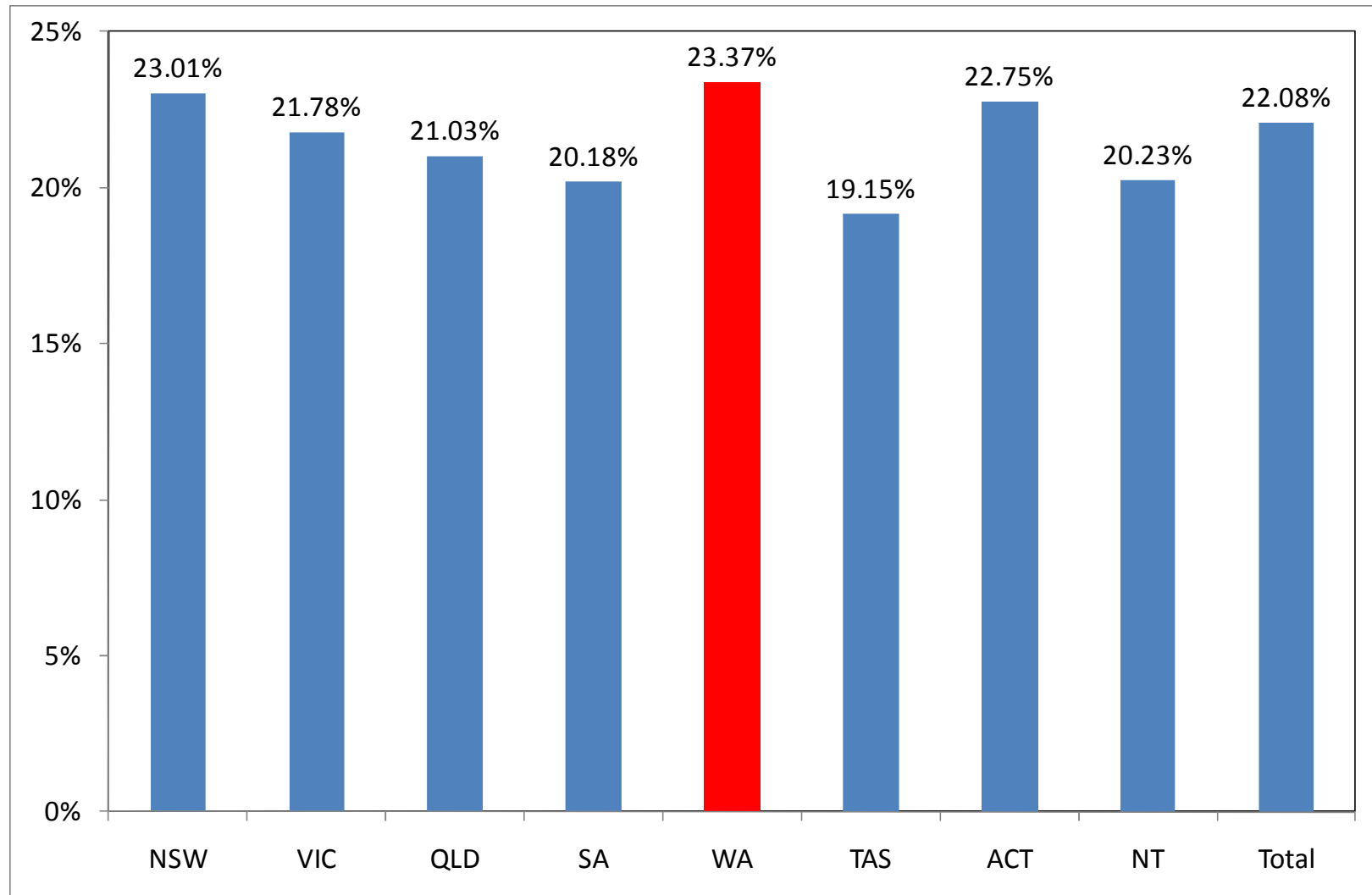
Source: ABS, Taxation Revenue, Australia, 2007-08; author's own calculations

Top Marginal Personal Income Tax Rate and Threshold 1977-2009



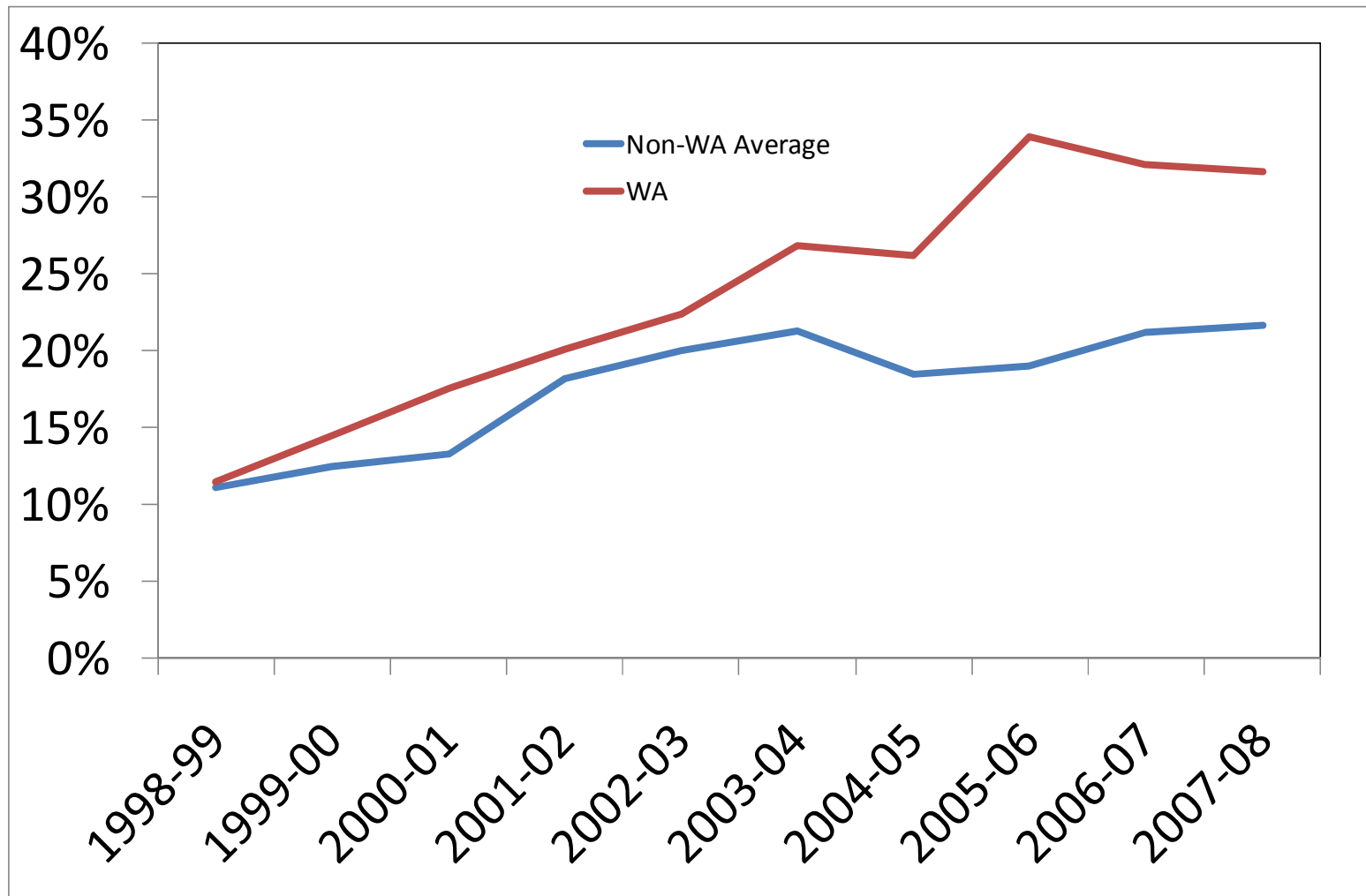
Source: Parliamentary Library; Australian Bureau of Statistics; Deloitte analysis

Average Personal Income Tax Paid Per Taxpayer: State Comparison



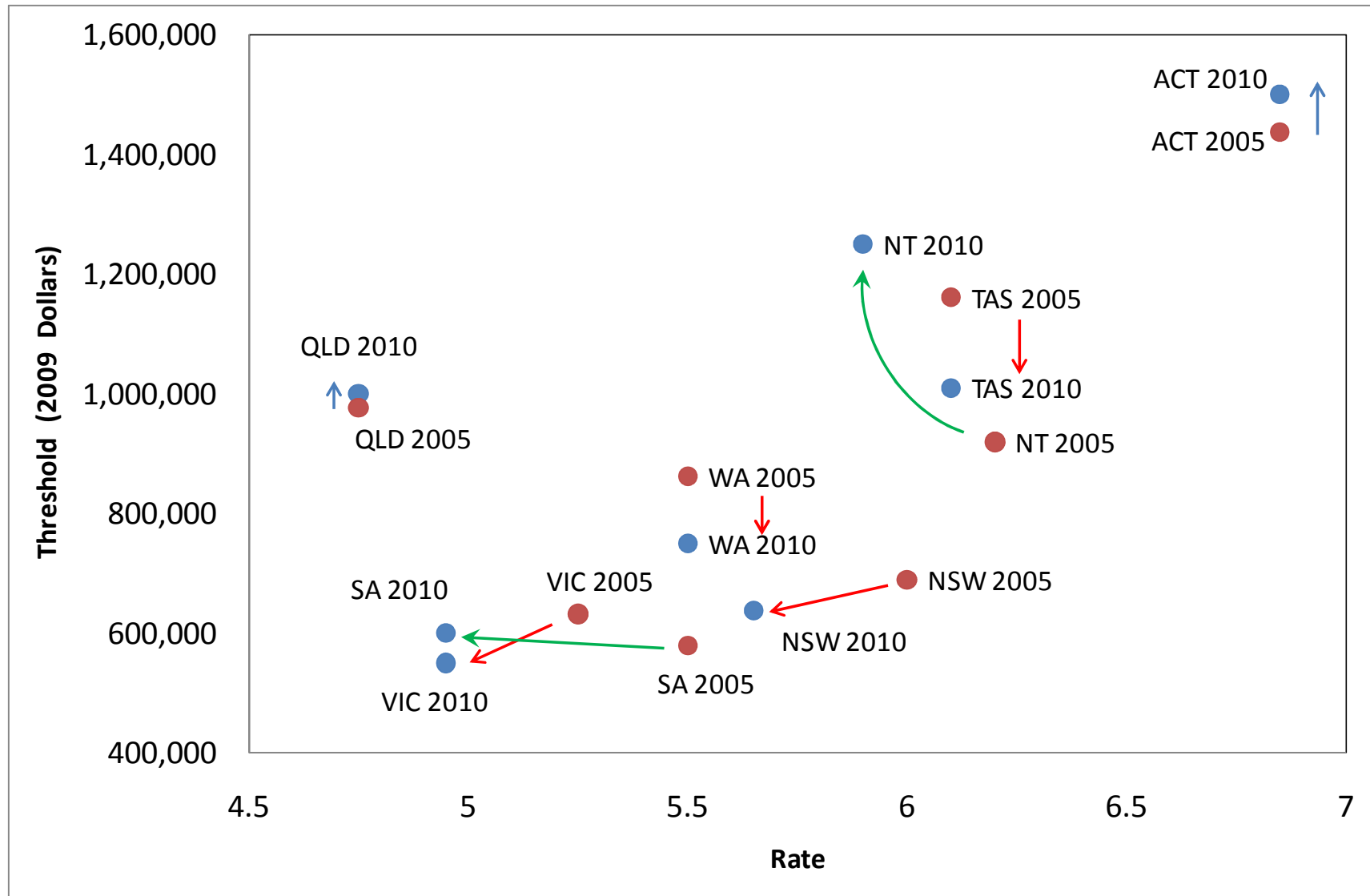
Source: Australian Taxation Office, Taxation Statistics, 2007-08.

Fraction of Tax Revenue from Stamp Duty on Conveyances



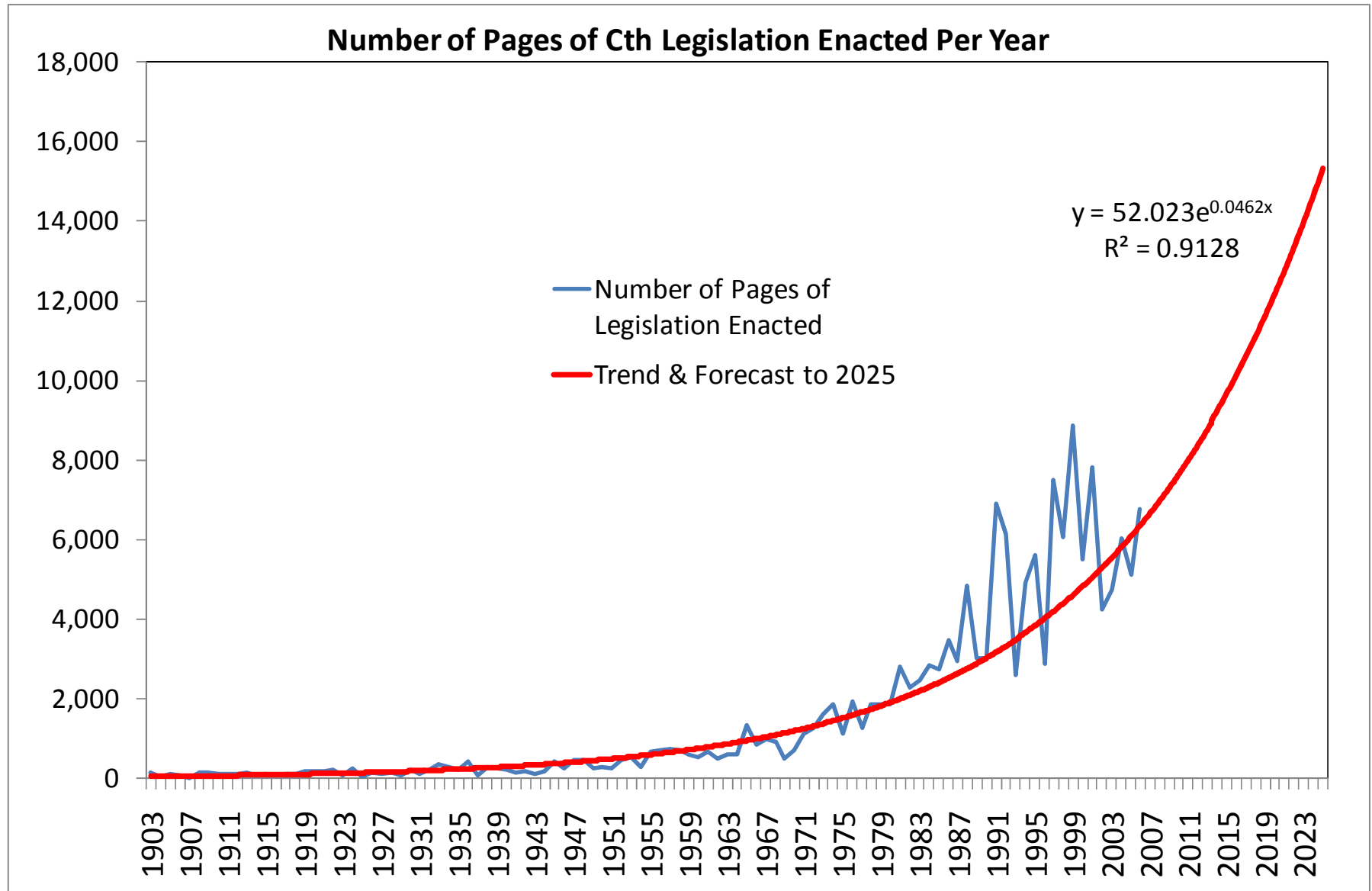
Source: ABS, Taxation Revenue, Australia, 2007-08; author's own calculations

Payroll Tax Rates and Thresholds



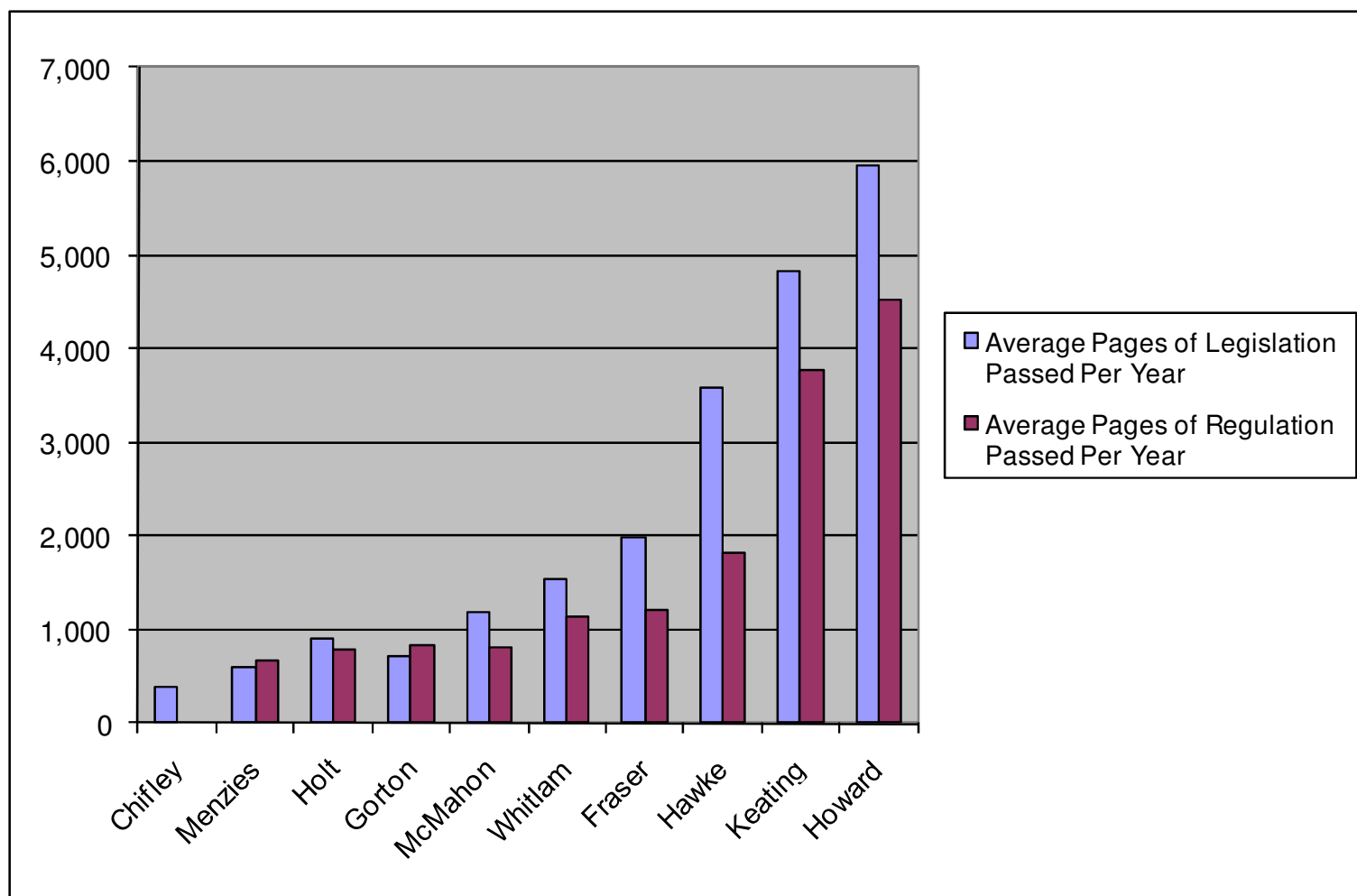
Source: State Revenue Offices; ABS CPI; author's own calculations

Volume of Legislation: Commonwealth



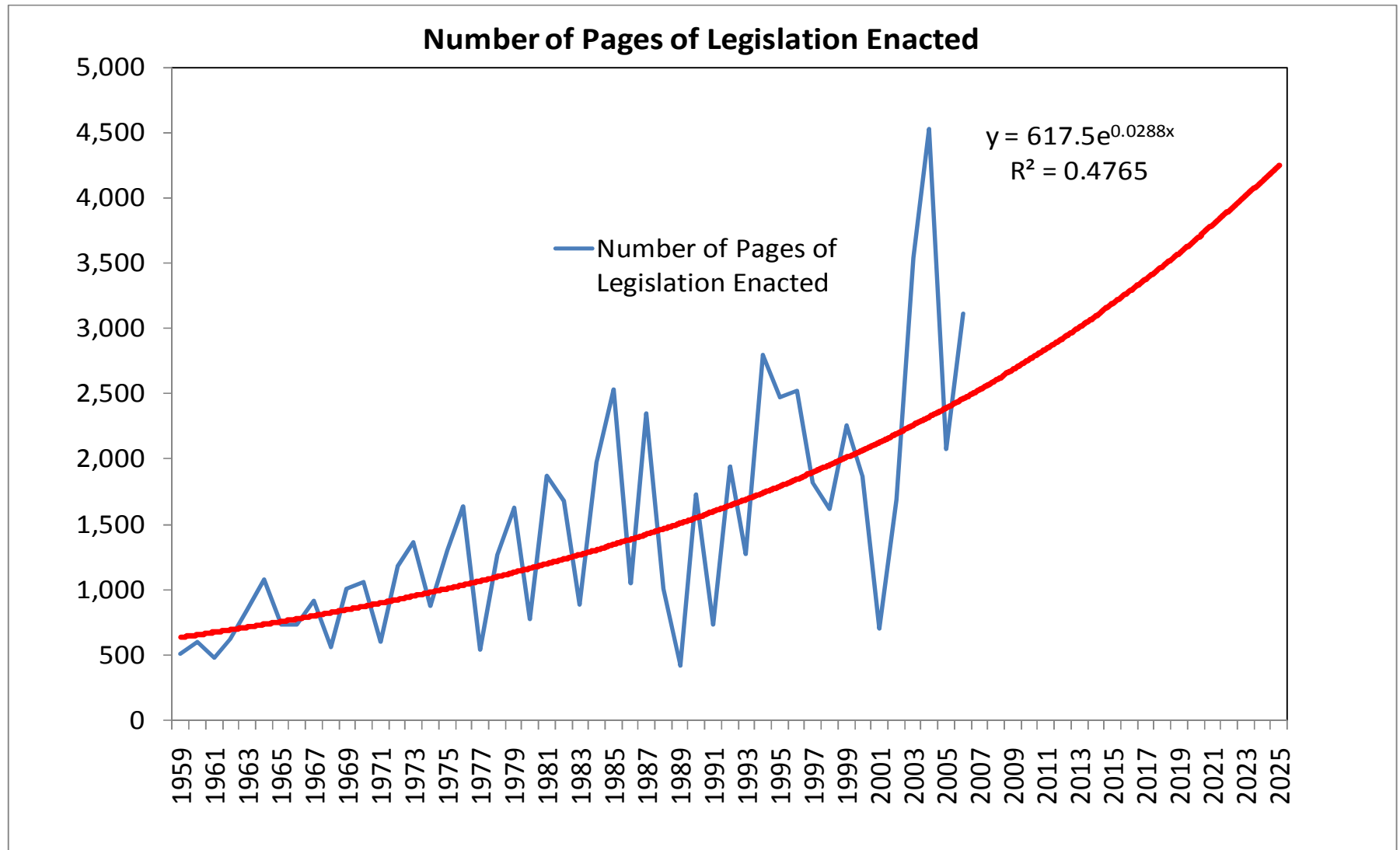
Source: Institute for Public Affairs; author's own calculations

Volume of Regulation and Legislation



Source: Institute for Public Affairs

Volume of Legislation: WA



Source: Institute for Public Affairs; author's own calculations

Conclusion

- The size of government and the burden of taxes have tended to grow faster than GDP.
- The cost of taxation increases with the square of the tax, so the total cost and marginal cost of taxation has also tended to rise.
- The volume of regulation is increasing at a roughly constant growth rate, but also faster than GDP.