

Tasmania: An imperative for reform

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Introduction

There is no published economic history for Tasmania because we have no future. *—Hobart bookseller*

Tasmania has significant natural resources such as arable land, mineral deposits and plentiful sources of hydro electricity that could power a modern, dynamic economy. The state also has a lifestyle the envy of those living on the mainland, and a beautiful natural environment that draws in visitors from around the globe.

With all this promise, the Tasmanian economic prospects should be healthy and vibrant. Yet, former Federal Minister Peter Nixon concluded in his 1997 review that:

I have found an economy with serious problems and an overwhelming inertia against taking the actions needed to achieve the opportunities which would turn the State around.¹

In the decade since then, however, little has changed.

A popular view is that Tasmania's geographic position on the Australian periphery explains its systemically poor economic performance. This, however, ignores the very real impact of a legacy of poor policy choices by the State government—for example, in terms of taxation, expenditure and public sector staffing.

Despite the much vaunted objectives of the current government to fashion a 'New Tasmania', the reality is that Tasmania also could easily become a mendicant state. Indeed some might argue that it has done so already. Tasmania is highly dependent on mainland Australia for financial assistance.

This paper sets out the basis for this view and recommends that the Tasmanian community commences a wide ranging debate about the future Tasmanians want to have for themselves.

With all this promise, the Tasmanian economic prospects should be healthy and vibrant.

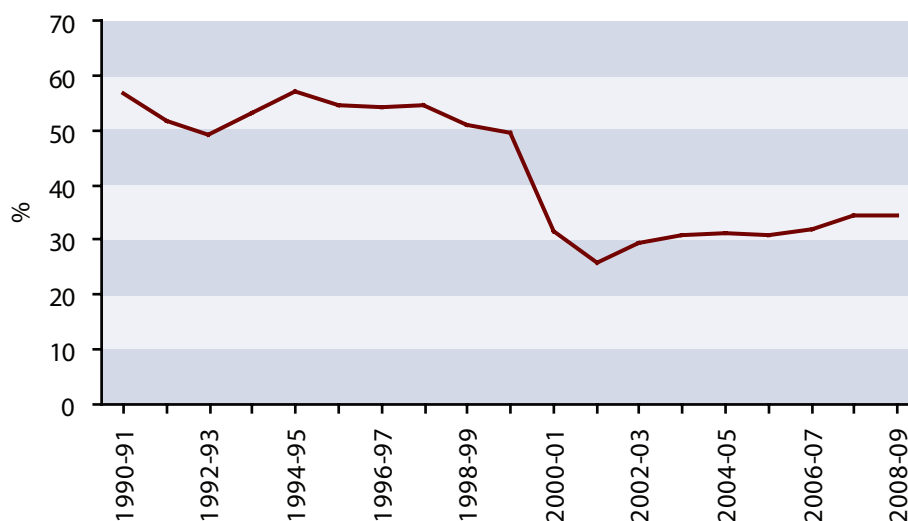
1. *The Nixon Report: Tasmania into the 21st Century*, p. iv

Tasmania is dependent on the mainland

This financial year Tasmanian own-tax revenue will comprise just 34.4 per cent of Commonwealth assistance. That figure has declined remarkably since the early 1990s when it was above 50 per cent. To be fair, the introduction of the GST has had an impact on own-tax revenue, nonetheless the other states and territories are far more self-reliant than is Tasmania. An equivalent figure for Victoria in 2006–07 is 77.4 per cent.

The only State or Territory with a lower own-tax revenue is the Northern Territory. In other words, the provision of government services in Tasmania is very highly subsidised by the rest of Australia. The bulk of the money coming from the Commonwealth is not Specific Purpose Payments, but rather in the form of General Revenue Assistance (now GST payments and previously as Financial Assistance Grants).

Figure One: Tasmanian Own Tax Revenue as % of Commonwealth Assistance



Source: Tasmanian Budget Papers

Just how much money does Tasmania get?

In this financial year Tasmania will receive \$1.7 billion in General Revenue Assistance and \$864 million in Specific Purpose Payments. Strictly speaking, the Specific Purpose Payments are Commonwealth spending in Tasmania and should not be counted when examining the choices of the Tasmanian government and community. Tasmania has received a substantial sum of money from the Commonwealth in General Revenue Assistance alone. In 2007 dollars, Tasmania has received over \$42 billion in General Revenue Assistance since 1970.

To place that figure into context, we calculate what would have happened had that money been invested in the Australian Stock Market over time rather than been paid to the Tasmanian government. A portfolio of Australian shares would have been worth over \$100 billion (excluding dividends) by the end of 2007. Assuming a dividend-yield of four per cent, that implies a cash return of \$4 billion in 2007. In 2006–07 Tasmania had a Gross State Product (GSP) of \$19 billion. So the income from a portfolio of stocks would have accounted for just over 20 per cent of Tasmanian GSP.

Tasmania is highly reliant on mainland funding. Similarly, it is not appropriate to argue that the mainland funding is a trivial sum of money. Certainly, that stock portfolio would have lost value over the course of 2008; nonetheless it is probably fair to argue that on balance all that mainland funding has been consumed by Tasmanians in the form of government services.

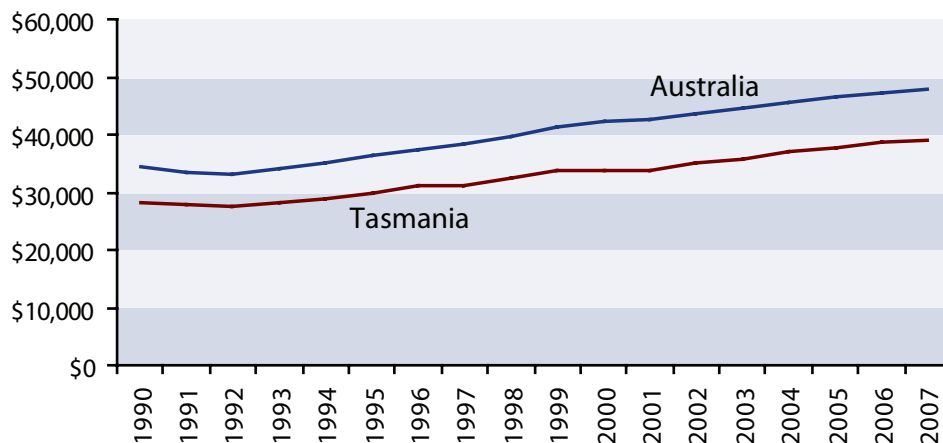
In 2007 dollars, Tasmania has received over \$42 billion in General Revenue Assistance since 1970.

Tasmanian economic growth

On a per capita basis Tasmanians are the poorest Australians in the Commonwealth. Figure two shows a comparison on per capita Tasmanian Gross State Product (GSP) and per capita Australian Gross Domestic Product (GDP) for the period 1990–2007. In 2007 Tasmanian GSP was just under \$40,000—the corresponding figure for Australia as a whole was just under \$48,000. Australia as a whole had a GDP per capita of \$40,000 in 1998. As a rough and ready guide (ignoring inflation) the average Tasmanian is ten years behind the average mainland Australian.

An additional point worth highlighting is that the gap between Tasmania and the mainland has widened. GDP per capita for Australia has grown faster than Tasmanian GSP per capita. This can be seen in the increasing gap between Tasmania and Australia in Figure Two.

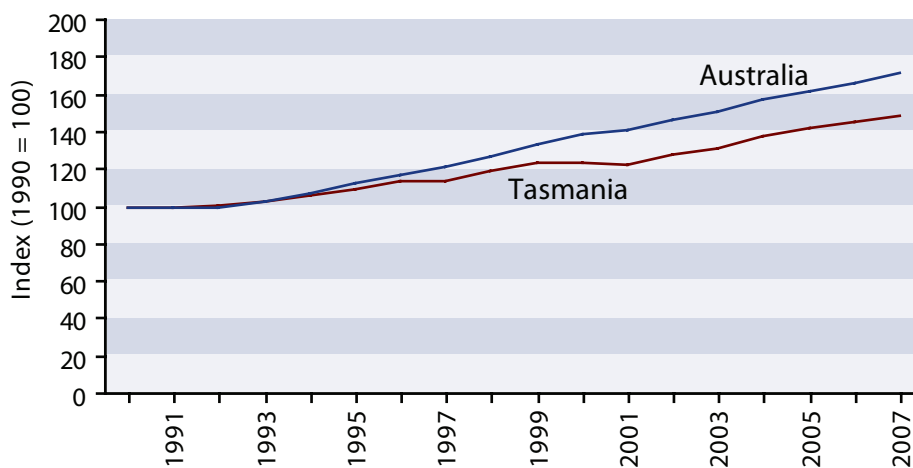
Figure Two: Tasmania Gross State Product per capita and Australian Gross Domestic Product per capita



Source: ABS Cat. 5220.0

Figure Three shows relative growth rates in Tasmanian GSP and Australian GDP over the period 1990–2007. Australian economic growth far exceeds that of Tasmania. On a State by State basis (analysis not shown) Tasmania has kept pace with South Australia, but otherwise has lagged far behind the other States and Territories.

Figure Three: Growth in Tasmania Gross State Product and Australian Gross Domestic Product



Source: Derived from ABS Cat. 5220.0

On a State by State basis Tasmania has kept pace with South Australia, but otherwise has lagged far behind.

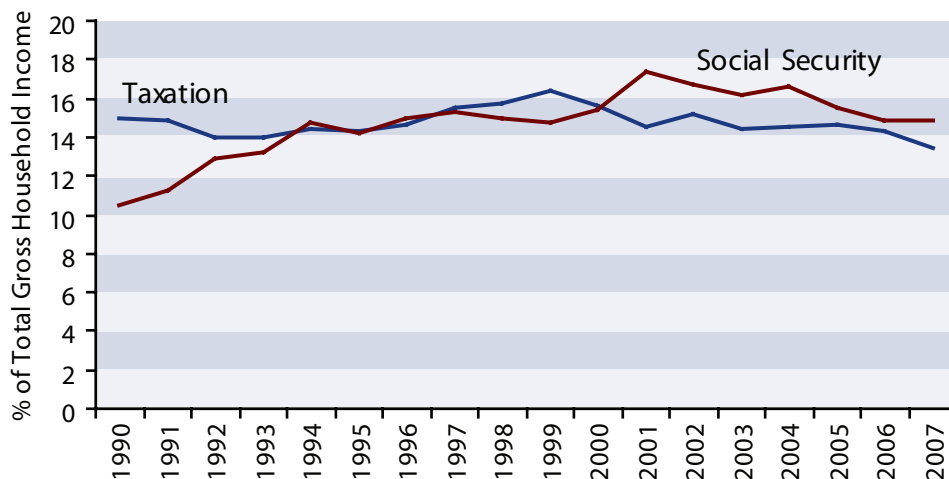
Tasmanians are highly dependent on welfare

A particularly troubling comparison is to look at how much Tasmanian households receive in Social Security and to compare that with how much they pay in income taxes (and other Commonwealth taxes).²

Since 2000 Tasmanians have, on average, received more in Social Security benefits than they have paid in taxation. This is a very different picture than that for the rest of Australia (not shown). Indeed it is this analysis that most starkly highlights the dependency that Tasmania has formed on the rest of Australia.

2. Taxation is defined as the sum of Income Tax Payable and Other Current Taxes and Social Security is defined as the sum of Workers Compensation and Social Assistance Benefits.

Figure Four: Taxation and Social Security as a percentage of Gross Household Income



Source: Derived from ABS Cat. 5220.0

The ‘Tasmanian problem’

In a comprehensive analysis of Tasmania Jeffery Rae identified four ‘fundamental and underlying causes’ of the economic malaise that has beset Tasmania.³ These were:

- The disadvantage of time and space;
- Flawed institutional arrangements;
- Poor policy choices by State and Commonwealth governments; and,
- Cultural impediments to performance.

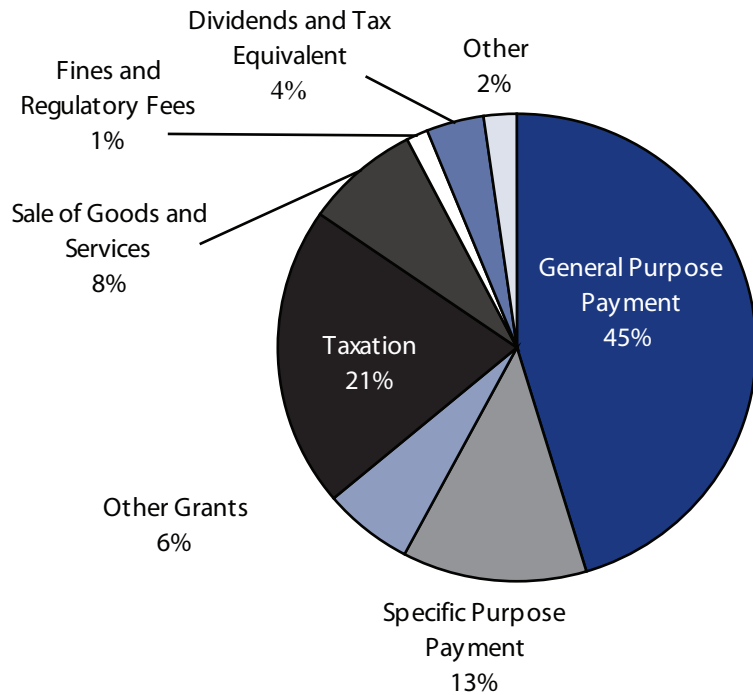
There are no good policy measures that can overcome the problem of Tasmania’s geographic isolation. The historic ‘solution’ has been to subsidise transport costs—this in our opinion is not a wise long-term policy. Consideration of Tasmania’s institutional arrangements is somewhat beyond the scope of this paper and the subsequent analysis of taxation and expenditure. The size of the Tasmanian bureaucracy, however, does form part of our current brief and is discussed below. Similarly, cultural impediments to performance is also far beyond our brief. In the discussion below we concentrate on policy choices.

Revenue

The Tasmanian government receives most of its revenue from the Commonwealth. This is in the form of either General Purpose Grants or other specific grants. Tasmanian taxation only made up 21 per cent of Tasmanian government revenue in 2007–08. Approximately 64 per cent of the Tasmanian government revenue in 2007–08 was from sources other than the Tasmanian government.

3. Jeffery Rae, 2002, *The Tasmanian Experience: Lessons for New Zealand*, New Zealand Business Roundtable, www.nzbr.org.nz. The term “Tasmanian Problem” was coined by Peter Nixon.

**Figure Five: Tasmanian Government Revenue
(2007–08)**



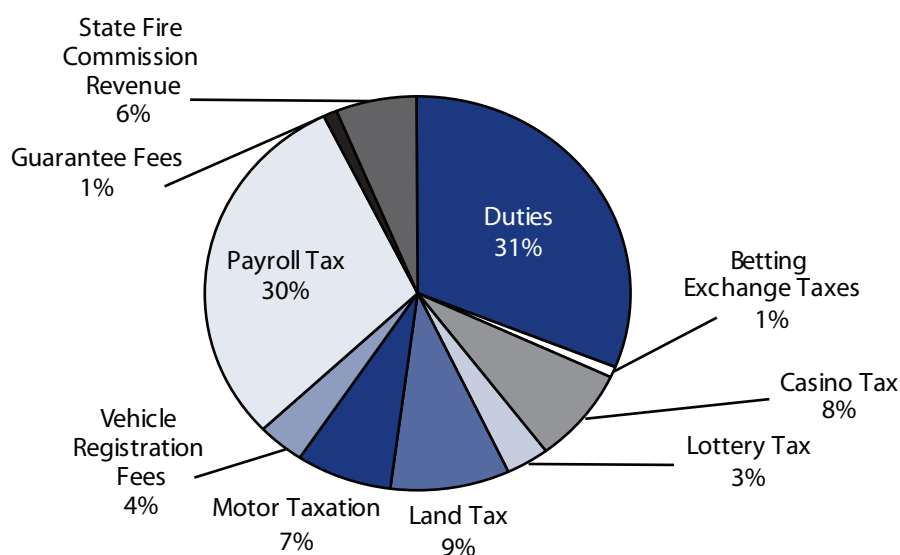
Source: Derived from ABS Cat. 5220.0

It is possible to levy taxation on income, wealth, consumption, and transactions. Head or poll taxes could also be levied, yet these are remarkably unpopular and are not generally used in modern economies. Australian States and Territories do not levy income taxes—the Commonwealth undertook that power during WWII and has not relinquished it.

Similarly, the States and Territories do not levy consumption taxes—the Australian constitution forbids the States and Territories from levying excise taxes and the High Court has interpreted that prohibition generously. The General Purpose Payment (the General Revenue Assistance) consists of Tasmania's share of the Commonwealth Goods and Services Tax which is a consumption tax.

Australian States and Territories are basically limited in their ability to raise taxation revenue. In large part they can only levy taxes on wealth or transactions. Figure Six sets out the sources of Tasmanian taxation revenue.

Figure Six: Tasmanian Taxation Revenue 2007–08



Source: Tasmanian Budget Papers

The bulk of Tasmanian tax revenue comes from taxation on transactions. Duties and Payroll tax between them make up 61 per cent of tax revenue. These two taxes are highly sensitive to economic conditions with the Payroll Tax ultimately being a tax on employment. Land tax is a tax on wealth.

The Commonwealth Grants Commission evaluates both Revenue Raising Capacity and Revenue Raising Effort on the part of each State and Territory (see Table One).⁴

4. Revenue Raising Capacity is a ratio indicating the capacity to raise revenue relative to the Australian average. It is measured by dividing assessed revenue per capita by average revenue per capita. A score greater than 100 indicates that a State or Territory has a capacity to raise revenue above the Australian average. Revenue Raising Effort is a ratio indicating the actual effort made to raise revenue relative to the Australian average effort. It is measured by dividing actual per capita revenue by assessed revenue per capita. A score greater than 100 indicates that a State or Territory is making an effort to raise revenue above the Australian average.

Table One: Taxation Revenue Raising Effort, 2006–07

	Revenue capacity	Revenue effort
Payroll tax	65.8	98.3
Land tax revenue	23.0	253.3
Stamp duty on conveyances	54.3	95.5
Gambling taxation	93.1	82.3
Insurance taxation	63.6	104.8
Heavy vehicle registration fees and taxes	94.1	115.3
Light vehicle registration fees and taxes	112.3	77.7
Stamp duty on motor vehicle registrations and transfers	83.5	98.5
Other revenue	100	32.3
Total taxation	66.7	95.5

Source: Commonwealth Grants Commission

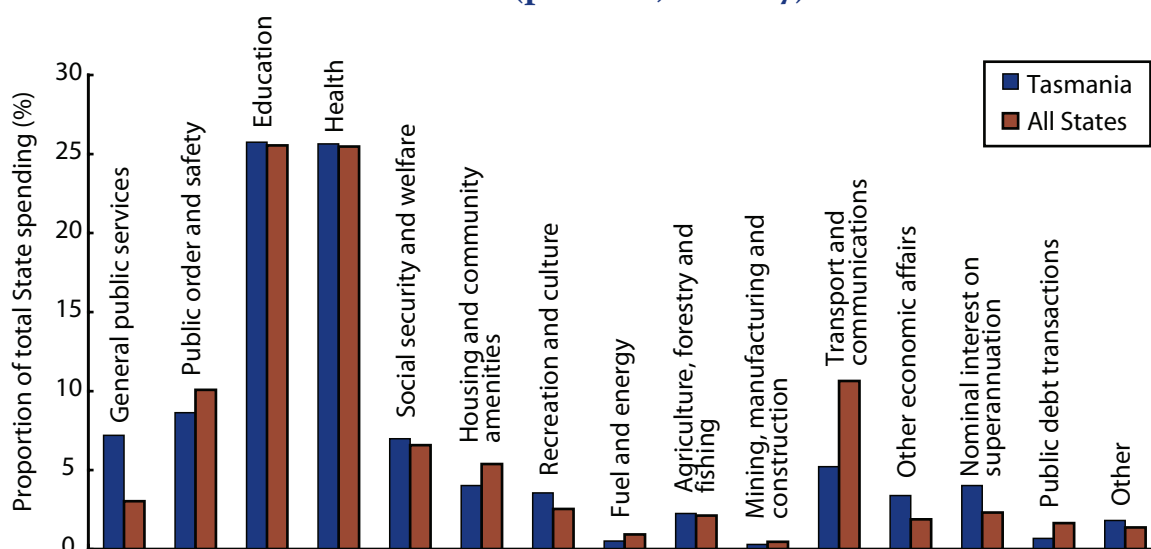
The figure that is most problematic in Table One relates to Land Tax revenue. Relative to the rest of Australia Tasmania has little ability to raise revenue from a Land Tax, yet goes to great effort to do so. While the Land Tax makes up just nine per cent of Tasmanian taxation revenue it is a candidate for reform.

Expenditure

Tasmania, like other Australian States and Territories, spends most of its budget on areas such as Health and Education. Figure Seven shows a comparison of government spending between Tasmania and the average for all States and Territories.

The functional composition of Tasmanian general government sector expenses were broadly similar to that of other States. Tasmania spent more on general public services, as a proportion of total expenditure, than the other States. This item includes outlays on general administration and regulatory functions. On the other hand, the Tasmania general government sector spent proportionately less on transportation services.

Figure Seven: Government Spending in Tasmania and other States and Territories (per cent, 2006 07)

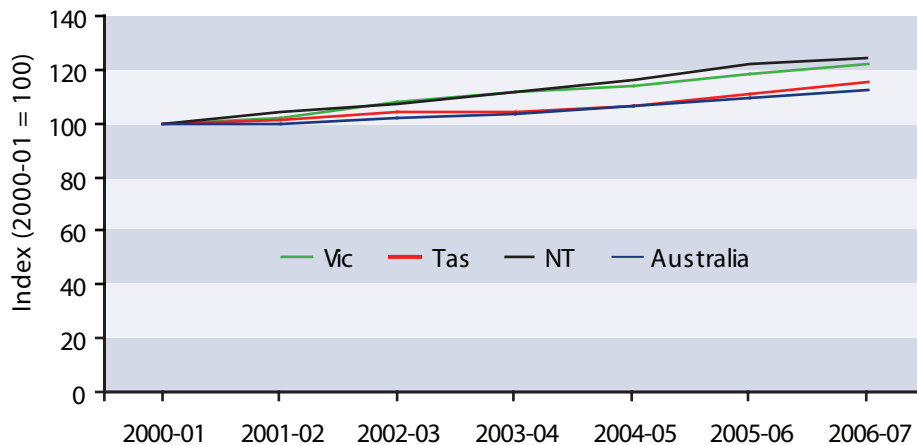


Source: ABS Cat. 5512.0

Bureaucracy

Given Tasmania's significant levels of expenditure on general public services, further examination of trends in the State bureaucracy is warranted. The ABS provides information on the total number of State public servants. In 2006–07, there were about 37,000 public servants employed by the Tasmanian government. This represented an increase of about 5,000 people compared to 2000–01 (an average annual growth rate of about 2 per cent). The growth in Tasmanian public sector employment has been the third highest after the Northern Territory and Victoria.

Figure Eight: Public Sector Employment Growth (2000–01 – 2006–07)



Source: ABS Cat. 6248.0.55.001

Growth in Tasmanian public sector employment has been the third highest after the Northern Territory and Victoria.

Taxpayers are not receiving sufficient return from the government's relaxed stance concerning its labour inputs.

The difficulty with increased public sector employment comes from the fact that it has grown faster than total employment over the period 2000–01 to 2006–07. In Tasmania public sector employment has grown faster than has total employment. For 2006–07 we estimate that Tasmanian general government sector employee expenses comprised 47.5 per cent of total expenses—the highest proportion in Australia.

It is important to consider what Tasmanian taxpayers are getting for the increasing money poured into the bureaucracy. Take one of the big ticket items of government spending—public hospital services. Despite an increase in public hospital beds per 1,000 population:

- the percentage of public hospital elective patients who had to wait for more than twelve months for treatment increased from 2000–01.
- the proportion of public hospital emergency patients seen on time declined from 2004–05.
- the median waiting time for treatment in emergency departments had risen from 2004–05.

Similar issues have arisen in school education, another big spending area for the Tasmanian government. Despite a reduction in student to staff ratios in schools, the performance of Tasmanian students against eight of the nine reading, writing and numeracy skill benchmark tests have deteriorated since 2001.

The fact that the State has gone backwards on some important performance indicators suggests that taxpayers are not receiving sufficient return from the government's relaxed stance concerning its labour inputs.

The imperative for reform

The Tasmanian economy is highly exposed to the current economic crisis confronting Australia as a whole. In particular the Tasmanian budget can expect to come under severe strain. On the revenue side the Tasmanian government is highly dependent on GST money and inefficient taxes, while on the expenditure side the government has promised pay-parity with the mainland. This is looking to have been a very expensive commitment.

With Australia facing a potential recession and a decline in employment the Tasmanian economy is particularly at risk. The State government has come to rely on GST revenue always growing. As consumer spending declines, however, so must GST revenue receipts. The Tasmanian government has considered itself a big winner out of the GST redistribution between States. An economic downturn could see the State lose its expected quantum of funds from the Commonwealth. Economic reality has the potential to hit the State's fiscal settings hard.

Of course, the States themselves are not to blame for their perilous financial situation. The Commonwealth has long constrained States in their ability to be self-sufficient, or at least to being more self-reliant. Australia's fiscal federalism is still mired in decisions made during WWII.

Tasmanians have the right to choose their economic destiny and should not be Commonwealth mendicants. Specific purpose payments and general purpose payments should be icing on the fiscal cake. Instead they are the bread and butter in the budget. This implies that Tasmanians need to explore ways whereby they can increase their own self-reliance.

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Tasmanians should look to growing the tax base through increases to economic activity.

Increasing the tax burden is not ideal—that would only act to suppress much needed economic activity. Rather Tasmanians should look to growing the tax base through increases to economic activity. Part of that must be an increase in labour productivity.

The State government's preparedness to throw 'money at walls' in the midst of a downturn does nothing to solve the underlying structural causes of Tasmania's systemic economic underperformance. Instead, a whole-of-community debate about the fundamental kinds of policy choices to secure Tasmania's future needs to occur. Do Tasmanians want to stay on the 'low road' of low economic growth, fiscal dependence on Canberra and top-heavy State tax and spending? Alternatively, do they want to eschew the formula for poor performance, and instead do what is necessary to propel the State toward a new plane of economic excellence?

There is no better time than now to undertake the debate about State economic policy, when all ideas and assumptions are up for contest.