IPA REVIEW JANUARY/MARCH 1981. Vol. 35 No.1

Institute of Public Affairs 401 Collins St. Melbourne 3000 Tel. 61 2029

Editorial-
GOOD AND NOT SO GOOD

The Prime Minister's scathing attack on tax avoidance and extremist unionism (in an address to the Victorian State Council of the Liberal Party) is the sort of leadership Australia desperately needs.

The Government's rejection of tax reform is a serious error. The Treasurer's statement, on 13th March, again trots out the old fallacy that Australians are not heavily taxed.

In an address to the Victorian State Council of the Liberal Party on March 15, the Prime Minister attacked the unrestrained pursuit of self-interest by sections of the Australian community. He singled out particularly the "cynical pursuit of power by extremist union leaders" and what he described as "abhorrent tax avoidance schemes" which he stigmatized as "an abdication of community responsibility". He called for greater recognition throughout the community of "responsible and moral behaviour in dealing with one's fellow citizens". Respect for others and the observance of decent moral standards, he asserted, were at the heart of liberalism.

This is the kind of forthright leadership which the I.P.A. has been advocating and of which Australia stands desperately in need. The Prime Minister's remarks will be applauded by all responsible and right-thinking Australians. The truth is that the problems we face have their seeds not so much in economics or politics as in basic morality.

We are not going to achieve a better deal for all Australians, or overcome inflation and unemployment, or progress to higher living standards, unless we act and work responsibly and honourably and curb our unthinking, self-centred demands.

The seat of our troubles lies not in Canberra but within ourselves. "The great society" can be made only **by us**, the people. It cannot be manufactured **for us** by Governments, no matter how wise or well intentioned. What Governments, can, and should, do is to create the environment which will call forth the best qualities that lie, too often dormant, within us. Actions speak louder than words. Deeds, as well as exhortations, are necessary. Then will we, as a nation, begin to achieve our truly enormous potential.

☆ ☆ ☆ ☆ ☆

The Government is undoubtedly moving in the right direction in the strong stand it is now taking on irresponsible, destructive industrial action and on the widespread and morally damaging practice of tax avoidance.

We are not convinced it is moving in the right direction in its approach to tax reform (or lack of it). The Statement on Taxation (released by the Treasurer on March 13) is clearly intended to provide support for the Government's decision not to put into effect a combination of reduced personal taxation and compensatory increases in indirect taxes. In this respect the Statement is not convincing.

But the Statement also, surprisingly, persists in the view — long since surely exploded — that Australians carry a lighter burden of tax than practically any other Western industrial country. It resorts to the usual absurdly simplistic comparison of percentages of total tax revenues to G.D.P. It shows that in 1978 the Australian figure was 28.8 per cent, compared with an average 35.8 per cent for 22 O.E.C.D. countries. The Statement also shows that personal income tax in Australia in 1978 amounted to 12.6 per cent of G.D.P. as against an O.E.C.D. average of 14.5 per cent.

Thus the Treasurer's Statement is concerned not merely to establish that, taking into account all taxes, Australia is more lightly taxed than other countries; it also endeavours to refute the notion, widely held, that our burden of personal income tax is far too heavy and is imposing a serious disincentive to enterprise and work.

We do not intend to deal here in detail with the fallacies in this kind of reasoning. (We have done that on many occasions and those interested should refer to the July/September 1980 "Review"). Suffice to say now that the Government's figures especially those relating to personal income tax, will not convince most Australians that the taxes they pay are not exorbitant. The "tax revolt", implicit in specific tax avoidance schemes and the huge "underground economy", surely demonstrates that most Australians **feel** their personal taxes to be excessive.

The cardinal difference between the European countries and Australia is that the peoples of the former are now habituated to a society where the great part of their needs in welfare, retirement, health and education are provided by the State. Despite expanding welfare, Australians, taken as a whole, still expect to pay for a substantial part of these needs out of their own pockets, for example through life and health insurance, and contributions to private superannuation schemes. These payments are no less a burden to Australians than are the specific social security contributions (which amount to some 15 per cent of G.D.P. in France and 12.5 per cent in Germany). It is only by including these contributions as a "tax" that the Treasurer's statement is able to show that personal tax is higher, on average in the O.E.C.D. countries than it is in Australia. One might fairly argue that the contributions Australians make to such things as private superannuation and health insurance funds should be added to the total of Australians' personal taxes if a proper comparison is to be made. The truth, of course, is that the Government's comparisons are meaningless because they are dealing with widely differing economic and social structures.

A central tenet of liberalism is "freedom of choice" and there can be few more important freedoms to the ordinary person than the right to choose how he will dispose of the earnings of his own toil. One would think that a Liberal Government would therefore bend over backwards to try to reduce the burden of personal tax.

The Government has argued that to reduce personal income tax by some $3000 million a year (by reducing the standard rate from 32 to 25 per cent.) would require increases in indirect tax which would raise prices by about 6 per cent. It rightly says that it could not contemplate such an increase. But why $3000 million? Why not $1000 million? — for a start anyway. That would boost the C.P.I. by only 2 per cent, not nearly such a frightening figure. Moreover, any reduction in personal tax — and inexplicably the Treasurer's Statement seems to place little weight on this — would certainly tend to offset the rise in the C.P.I. by improving incentives and thus productivity and, more important, by taking some of the steam out of the incessant demands for higher gross incomes emanating from all sections of the community. These demands remain the most significant immediate cause of inflation in the Australian economy.

The personal income tax issue has, for the present, been put to sleep but it is by no means dead and buried.

What Goes Up Must Come Down — Or Must It?

Wages go up but never down and prices do likewise. The bureaucracy keeps on growing. Taxes keep on increasing. Inflation is built in. A seemingly invincible ratchet effect plagues the economy. Governments appear to be at the mercy of forces against which they are impotent.

Only drastic change in the policy making environment holds out hope of a reverse ratchet.

Although few could now recall it, there was a time when this somewhat fanciful schoolboy exposition of the theory of gravity also seemed to apply to the working of national economies. There were precipitous booms and slumps. There were periods of rapidly increasing activity, bouyant markets, rising wages and prices, employment and general euphoria. There were also periods of steeply declining activity, depressed markets, falling wages and prices and general gloom. Even though there was little inflation over the long haul (that is, by present-day standards), economies nevertheless had a very bumpy ride. Governments did not recognise a responsibility for the management of their economies. That came with Keynes. The market system was largely left to its own devices.

We, that is the Western Democracies, have long since left behind those bad old days — or have we? Market forces have been stamped out by big government — or have they? Massive and increasing spending by bigger and bigger government can ensure stable prosperity — or can it?

This remarkable transition from the "tyranny" of the market place to transcendental economic bliss, from economies that went bump in the night to permanent stagflation, from robber barons to robber governments, from competitive excellence to institutional mediocrity, from the free enterprise creation to the socialistic destruction of wealth, is a twentieth century phenomenon of several stages.

Perhaps the first is marked by the belief that an economy could be rescued from a slump by infusions of public money (if there is such a thing), or pump priming as in Roosevelt's New Deal. Of course, when the pump was primed, then with the economy back to normal, Government intervention could fade away to fight another day. Then there was the belief that massive Government spending would act as a stabilising influence, a sort of economic flywheel, intended to prevent slumps, Even so, say after the Second World War, public sector spending was still small compared with it's magnitude today. However, it looks as though the step from priming the pump to turning the flywheel has in it the essence of today's problems. Government intervention in the economy changed from being small, temporary and reversible to being massive, permanent and alterable only upward. The Ratchet had arrived.

Nowadays, gravitational forces in Australia's economy, as well as in those of the Western World generally, are quite usually thought to have been stamped out. The Ratchet Effect pervades the economy. Taxes go up, as the last decade has shown, but never come down.

Admittedly, three years of this period

witnessed the economic devastation of the Labor Administration; but, for the rest, even with a Government ostensibly dedicated to free enterprise and small government, the tax bite has continued to claim, almost certainly against the collective will, a larger slice of the income dollar. The Tax Ratchet seems firmly entrenched, in spite of the increasingly pusillanimous pretences in high places that a serious attack on taxes is on the way.

The original Bureaucratic Ratchet applied to staffing and has been beautifully explained by Parkinson. True, to his credit, Malcolm Fraser has tried to buck this trend; but he has been fought every inch of the way by the bureaucrats (State as well as Federal) and, one must ruefully admit, very successfully. Nor can one be any more optimistic for the success of the so called "Razor Gang". Anyone who has seen the working of the bureaucracy from the inside will have no doubt that the public servants will have little trouble in thwarting Mr. Fraser's endeavours. Standard departmental practice, while the heat is on, requires the preparation of interminably long reports in defence of the department concerned against possible cuts (and, dare one suggest, occasionally indications of other departments which **could** be cut). These reports might, just now, be for presentation to the Razor Gang, but are more usually for estimates committees. They also have the important indirect purpose of equipping the Ministers to go in to bat for their departments. One reason for the efficacy of the bureaucrats in fighting off external attacks is that they spend a lot of their time sharpening their teeth on each other. As the heat gradually lessens, as it surely will — this has all happened before — they will feel confident enough to bring out of hiding their schemes for Parkinsonian expansion and generally get back to what (with every justification) they regard as normal — continued growth of public service staffing.

A more recent and even more scandalous phenomenon is the Public Service Remuneration Ratchet. Bureaucrats, with the support of politicians, some years ago succeeded in raising salaries in the public service to unprecedented heights in relation to those of the rest of the community, through a notorious piece of bureaucratic opportunism commonly known as the "Pacesetter Policy". They have since sought to maintain their gains, and lock them into the system, through continued pay rises and pensions indexed against inflation.

One should not, whatever one might think of the bureaucracy for pulling off these monstrous ploys, unreservedly blame the bureaucrats. For the most part they are merely exploiting to the full, and very expertly, a system which they did not invent and which, in all fairness, not all like very much.

A third and crucial gravity-defying phenomenon is of course, private-sector wages. This manifestion of the Ratchet Effect occurs especially in highly unionised areas of the economy, and is largely immune from such influences as the state of the economy, credit stringency, booms or slumps, and not least, unemployment. Perhaps the rate of increase might alter somewhat according to economic bouyancy, but that is all. It was a remarkable feature of the Great Depression in the U.S.A. that in heavily unionised industries, wages kept on going up while unemployment became enormous; yet in agriculture, virtually non-unionised, prices and incomes fell generally but there was little unemployment. In Australia, the contrast is less obvious because of the system of awards and flow-ons applying even to less union-bound industries; this does, if anything, make the Wages Ratchet more universal in this country.

Fourthly, if it is true that wages only go up, then the same must apply to prices, especially since tight profit margins so limit room for manoeuvre throughout the private sector. Furthermore, if through hysteresis effects in the economy, price rises always tend to be lagged on wage rises, this is one more reason why inflation appears to be so firmly locked in to the working of the economy.

There are, of course, numerous other examples of the "Ratchet Effect" throughout the economy. In mentioning a few of the more important of them, the intention was to bring out that they are closely linked with the scourge of our times — inflation. It now seems generally recognised that inflation, itself potentially subject to its own special Ratchet Effect, must be beaten before the economy can be restored to health and stability.

The Institute makes no apology for raising once more the subject of inflation, which it has many times discussed before. In the previous "Review", an agenda of action for the newly elected Government was set out. The principal object of this agenda was not to attack, unconstructively, economic management since 1975; but rather to suggest how the economy, could still belatedly be restored. The prescriptions set out were well within the capabilities of a moderately wise, moderately brave government.

In this, there exists a remarkable paradox. How does it come about that these prescriptions for the good economic management of this country are still so apposite, such burning issues? If the present Government is genuinely dedicated to free enterprise and keen on bringing stability to the economy, and if the policies likely to achieve these aims have been well known to it for the last five years, how does it come about that they have not been put into effect? Could it be that the problems involved in setting the economy to rights are altogether too daunting to be tackled? "Things are in the saddle and ride men".

Is the utimate Ratchet Effect one which permits governments to act destructively (whether or not with good intentions) as did Whitlam's, but never constructively? Is there, in fact, an all-embracing Degenerative Ratchet against which governments, even those which know what needs to be done, are doomed to flounder and struggle in vain?

In this context, it is not useful to say, "What do you expect? Things are never as they were in the good old days"; or to argue that maybe Western economies will indeed collapse one day, but that day is still a long way off. What is to be feared is not that the economy may collapse suddenly: the shock of that might — would have to — abrogate inhibitions and produce drastic remedies to suit drastic problems. The frightening prospect, and at present the seemingly inevitable one, is that the already ailing economy will linger on for a long time, gradually becoming less workable under an increasing load of bureaucracy, regulations and taxes. On top of that, present experience suggests that the Degenerative Ratchet affects not only the economy and possible remedies for its ills, but also the will to put such remedies into effect.

In this politically daunting climate it is perhaps not altogether reasonable to blame governments for not acting in the fashion they know to be right and necessary. Perhaps the surprising thing is not that they fail, but that they wrestle so hard, knowing that failure is inevitable.

One is led to the gloomy thought that this country (and others like it) may be doomed to slow decay and eventual collapse, possibly as a prelude to the advent of an extremist regime which would at least have the power to try to make the economy work. The only obvious alternative is to seek out ways of making the necessary political decision-making easier for democratically-elected governments, by trying to identify and diminish impediments which now quite evidently almost preclude effective action.

In plotting such a change, of course, one should recognise with clarity the heroic nature of the task. It requires the rejection of conventionally-accepted thinking that stopping the rot, preserving the economic status quo, is enough. It is a common view that a conservative government can usually be relied upon to do no more than manage, but not clear up, the mess left by its socialistic predecessor. This is not good enough. What is required is reversal of policies from which the present mess has evolved; in short a reversal of trends, already dangerously near general acceptance, towards greater taxation, regulations and bureaucratic squandering of the nation's wealth. What is required is nothing less that the genesis of the Regenerative Ratchet. It is not to be thought that such a momentous change of tack is likely to be brought into existence as a result of a blinding flash of inspired political genius. What is sought is rather the gradual evolution of a policy-making environment which permits or even encourages, policies designed to lift the burden on the economy of the giant sloth represented by Big Government.

Preventing an "Incomes Explosion"

Strong, unorthodox measures are needed to prevent a threatened "incomes explosion". Otherwise an inflation rate of well over 10% may be expected.

Among the steps needed are:—

- **A "freeze" on Parliamentary and top public service incomes.**
- **A major reduction in personal income tax.**
- **The use of the economy's capacity to pay as the principal criterion for wage fixation.**

It is not the practice of the Institute of Public Affairs to make hard-and-fast economic predictions. There are plenty of people indulging in that pastime; but their estimates of the future, in most cases, are so far wide of the mark as to render them at best useless and at worst seriously misleading.

However, we have, for once, decided to break our self-imposed rule. We are prepared to make one prediction with some confidence — but accompany it with an important proviso. Inflation in the coming two years will, in our view, be not less that 10 per cent annually and is more likely to be closer to 13 per cent, or even more. One thing, however, could change this picture — that is resolute, unorthodox action by the Federal Government.

☆ ☆ ☆

The most serious legacy of the Whitlam years was not a broken, shattered economy — disastrous and inexcusable though that was — but the public attitudes of mind to which those years gave rise — the notion that Government has a bottomless purse, out of which it can provide higher standards of living for practically all Australians; and the prevailing attitude of short-sighted, irresponsible greed manifested in the attempts by nearly all of us to seek annual increases in our incomes (and other benefits) far beyond what our combined efforts merit. These attitudes are behind the continuing rapid inflation which is causing widespread alarm and which, if not curbed, will make it impossible for us to realise the full potentialities of the massive impending energy and resource developments.

At the heart of the Australian inflation is not OPEC, but the continuing rapid rise in incomes and related benefits throughout most sections of the community — not just the incomes of modest wage and salary earners, but also those of doctors, dentists, lawyers, accountants and the like, and, not least, those of politicians and public servants. If inflation is to be beaten, or even curbed, the large annual increases in incomes, now taken for granted by almost everybody, must be drastically reduced. Nothing else will work: constraint of the money supply, balanced budgets, all the sophisticated remedies are impotent in the face of income additions of the order of 10 to 15 per cent a year, contrasted with productivity gains of 2 or 3 per cent, at best. Unless Governments face up to this inescapable fact of economics, all talk of overcoming inflation becomes a blatant exercise in hypocrisy.

In other words, all tax payers must accept cuts in living standards in order to pay for Big Government.

At present the signs are anything but promising. The impending scarcity of skilled and semi-skilled labour will put strong upward pressure on wages which, in turn, could lead to complementary increases in all other incomes. The termination of indexation by the Commonwealth Arbitration Commission, and the search for a new "workable" formula for wage adjustments, can hardly be regarded as a cause for optimism — especially in light of subsequent statements by union spokesmen, who refuse to recognize any responsibilities beyond getting a supposedly better deal for their members:

As far as inflation is concerned, indexation — as the I.P.A. insisted when it was first introducted — never had any prospect of succeeding. (It has also failed lamentably to prevent industrial stoppages on a disastrous scale.) The adoption of the principle of adjusting wages for price increases amounted to a recipe for perpetuating inflation, as the premier wage-fixing body found out as long ago as 1953 when it abandoned the system of automatic quarterly cost-of-living adjustments (which then applied not to the full wage, but only to the basic wage component). One of the main problems has been that indexation has not been confined to blue and white collar workers on comparatively modest incomes — as was no doubt originally intended — but soon began to be applied to the whole range of incomes throughout the community, from those of highly paid politicians and bureaucrats to those of senior executives in the private sector. Practically everyone now takes it as a matter of right that, no matter what the consequences for the economy, they are entitled to have their **real** incomes largely maintained intact. The only ones who have missed out in this happy procedure are some welfare beneficiaries and the elderly in retirement. In fact, those endeavouring to live on their own carefully accumulated life-time savings, lacking industrial or political power, have, to put it bluntly, been callously robbed by the rest of the community.

The system of indexation thus came to have some "South American" or "Israeli" elements, where pretty well everything, including capital assets, is hitched to price rises, needless to say at the cost of runaway inflation. Moreover, indexed wage and salaries are not the end of the matter. There have also been widespread increases outside the indexation mechanism, such as the recent spate of spurious "work value" awards, and the numerous settlements in particular industries, usually but not always arising from pressures exerted by powerful unions.

A recent deplorable example was the salary increases in December last year of senior public servants and heads of statutory authorities in Victoria — averaging close to 10 per cent — topped off, just a few weeks later, by a further 3.7 per cent rise as a "flow-on" from the January National Wage Judgement. Victorian MP's also got their cut in January in the form of $18 a day "appearance money" for attending Parliament or Government functions. If the argument used by the Remuneration Tribunal in recommending these payments is valid, namely that "an MP. should be re-imbursed for costs necessarily incurred by him in carrying out his duties" (these, presumably, are mainly travelling costs) then it would seem that a similar argument could be applied to every worker throughout Australia. This would mean that all of us would be fully compensated for our travelling expenses to and from work, and luncheon and other incidental costs arising from our attendance at the job.

The "appearance money" for Victorian MP's is, in truth, nothing more than an artful device for increasing their tax-free remuneration.

It makes one wonder whether our political leaders, at Federal as well as State levels, are not being utterly cynical when they stress in their public pronouncements, the all-important need for curbing inflation. If there is not going to be restraint at the top, to the point where it hurts, it is quite certain that there will be no restraint at lower levels. "What is sauce for the goose is sauce for the gander". The clear danger in the "break-through" recently gained by Victorian MP's and senior officials is that, like a stone cast into a pond, it may set in motion a series of ripples which will end only at the other side of the pond, that is, when comparable benefits have spread right through the economy.

These increases have been made at a time when the community is entitled to expect an example of self-sacrificing leadership from those in high places and particularly from their governments. They could be taken to suggest that Government, despite its manifest responsibility and despite its protestations to the contrary, is not really serious about restraining, let alone stopping, inflation — which could probably be unfair.

We have said many times in the past, and will now say it again, that the first step in the battle against inflation, is for the Commonwealth Government to "freeze" the incomes of all Parliamentarians and all senior officials for a period of twelve months. It should then require the States to **follow its example and do likewise.** The States, after all, are easily the front runners in the "Big Government" stakes. Between 1975 and 1980, while employment in the Commonwealth sector declined, 95,000 workers were added to the payrolls of the States.

The unexpectedly "small" increase of 2.1 per cent in the consumer price index for the December quarter has given rise to a state of euphoria about the economy among certain media commentators. One would think that inflation is already in its death-throes. The response of Commonwealth Government representatives has, wisely, been more cautious; along with the pressure on incomes likely to arise from the resource developments, the Government is clearly well aware that the intransigent attitude of the union movement, which is behind the termination of indexation, carries with it the real danger of a "wages explosion" in 1981. This would have disastrous consequences for the economy. The overriding concern of Government policy must, therefore, be to prevent the threatened "explosion" from occurring.

In a paper to the National Agricultural Conference at Canberra on January 29th, the redoubtable Secretary to the Treasury, Mr. John Stone, drew attention to some encouraging developments in the economy, particularly in the areas of consumer spending and business investments. The former, he predicts, will grow by over 3 per cent, and the latter by 15 per cent, both in real terms, in 1980/81. He also pointed out that total employment had increased by some 175,000 jobs in the twelve months to November last year. He concludes that "....the Australian economy is expanding reasonably swiftly and that the prospect is for this expansion to continue". Stone, however, makes a vital qualification to this optimistic picture. The recovery he says, could be negated by an accelerating rise in wages. (We would add to wages "and all other incomes"). Stone states, "It goes I hope without saying, that for the recovery to be maintained and faster economic growth rates pursued on a sustainable basis, inflation and inflationary expectations will have to be restored to a downward track".

We agree completely. It follows that the main thrust of Government policy must be directed at slowing, and slowing substantially, the annual growth in wages (and incomes) which most Australians have come to expect.

☆ ☆ ☆

There are a number of things the Commonwealth Government can do.

First, as we have already indicated, it should put beyond doubt its own bona fides and set an example for all to follow by imposing a "freeze" on the incomes of Commonwealth MP's and all those coming within its authority — at least at senior levels. It should then insist that the States do likewise. If any should refuse to fall into line, the Commonwealth could threaten to with-hold needed increases in their grants or specific allocations.

Second, the Government should take some of the steam out of the pressures for increased incomes by deciding for a major reduction in personal income tax. This was the course the I.P.A. urged on the Government in our December "Review". As we then pointed out, it would have additional advantages — it would reduce the incentive for, and strike a blow at, tax avoidance; it would enable and would encourage the Arbitration Commission and other tribunals concerned with wage fixation to grant smaller increases than they would otherwise have been disposed to do; it would strengthen incentives through the economy and promote more rapid growth and employment; it would help to create a healthier climate of industrial relations; and finally it would encourage public acceptance of needed economies in expenditure on Health, Education and Welfare.*

Third, the collapse of wage indexation provided the Commonwealth Government with the opportunity to propose a new method which would end the illogical absurdity of tying wages to prices. After all, over the last five years, the Government frequently urged the Arbitration Commission to ignore price movements in arriving at its judgements. Inexplicably, and inconsistently with its past attitudes, the Government has put forward a curiously complicated formula which would enshrine the price-wage link even more firmly in the methods of wage fixation. For one thing, under the Government's new proposal, the link is now to be, to some extent, automatic.

Let it be said that there is no magic formula which will at the same time appease the unions and reduce inflationary pressures. The talk of substituting collective bargaining for a centralised system of wage determination is so much nonsense, if only because Australia, historically, has had virtually no experience in these kinds of negotiations. Moreover, the present climate of industrial aggression and irresponsibility hardly provides a suitable environment for collective bargaining. Collective bargaining as a substitute for our traditional methods rears its head regularly about once in every decade, at times of mounting dissatisfaction with our traditional methods. It would cause chaos in the Australian setting and would certainly seriously aggravate inflationary pressures.

There is only one sensible formula for wage determination and that is to be found in the principles which the national wage-fixing authority itself observed, to a greater or lesser extent, throughout its

**Since this was written the Government has decided against this course of action.*

long history until prudence and common sense were thrown to the winds in the late 1960's. (The present highly inflationary increases in incomes had there genesis in these years and the whole sorry farce was then compounded by the crassly irresponsible actions of the Whitlam administration). This is to base wage and other increases, in the main, on the economy's "capacity to pay", in other words on national productivity improvements. There is no other course which makes the slightest economic sense. It is suprising, to say the least, that the Government failed to make "productivity" the central consideration of its proposal to the Commission.

Fourth, we suggest that the Government should publish regularly — perhaps at Budget time — the percentage increases in average annual incomes which can be made without inflationary consequences. It should set out at the same time its estimates of the price rises which, other things being equal, would result from various given increases in average incomes — for example 5 per cent, 10 per cent, 15 per cent. This would have several advantages. The community would at least know what consequences would follow from additions to money incomes of varying amounts. The estimates would serve as guidelines to the Arbitration Commission and other Tribunals, in arriving at their decisions. Finally, the guide-lines would help to invest the Commonwealth with greater authority over the incomes component of economic policy.

☆ ☆ ☆

The prospects before Australia in the 1980's are probably second to none — almost certainly greater than that of any other country in the Western World. They could, indeed be described, without exaggeration, as spectacular. If realised, these prospects could eventuate in substantial gains in real living standards for all Australians. But they will not be realised — as the Secretary to the Treasury, John Stone, has warned — if the present inflation-bent madness persists.

All that is needed for Australia to achieve the glittering prizes which now lie within our grasp, is the re-birth of the spirit of moderation, good sense, and fair play which, until the ugly disease of greed and envy swept across the land, was a distinctive part of our national heritage and character.

Honesty is the Worst Policy

The recent Great Debate on tax reform petered out. Personal income tax is already onerous. Yet it, and hence the incentive for tax avoidance, now seems certain to increase.

Not from our own choice, we are being turned into a nation of cheats.

The demoralising influence of excessive taxation is a potent reason for reform.

Perhaps because of election promises, or perhaps because it is not insensitive to the mood of the nation, the Federal Government itself initiated the recent debate on tax reform. For this, full credit should be given. Excessive taxation is inseparable from the threat to fundamental freedoms posed by big government, against which the Government has pledged its efforts.

For this reason, it was disappointing that all the bold proposals fizzled into nothing when it was officially decided that no material changes to the tax system were to be made. The outcome was particularly discouraging to wage and salary earners, who already bear a disproportionately heavy tax burden and whose lot will surely worsen. However, they should take heart. The debate is not dead, but sleeping. Dissatisfaction with the tax system is evidently widespread.

Possibly the most explosive feeling is that of impotence and injustice among wage and salary earners, in the face of a mounting tax grab which has emerged in recent years as an apparently inexorable threat to their freedom. Perhaps less well defined are the feelings that taxation looks suspiciously like a prime cause of inflation and unemployment; that, because a high and rising proportion of the tax dollar is just plain squandered, giving money to big government is a certain recipe for lower living standards; that the winners are the politicians, the bureaucrats, the avoiders, the evaders (taxes do not seem to soak the rich); that the losers are those dependent on fixed incomes and wage and salary earners — the harder you work the more you lose; and finally, that there is no way for ordinary people to alter the system.

On these and related questions it is perhaps understandable that, if the putative experts cannot agree, precision on difficult questions cannot be expected from ordinary folk. Yet their instinctive wisdom seems almost at times to be inversely proportional to their economic sophistication. For them, dissatisfaction with the tax system may not have reached the point of open revolt (against which democratic governments would be virtually impotent), though potent stirrings are evident. In two and possibly three ways, public disapproval of the system has already achieved massive and increasing economic significance. There is the "cash" or "underground" economy, for which the fiscal system simply does not exist. There is the avoidance industry which, with evident success, finds loopholes in the tax regulations; and finally, there are those who simply do not fill in tax returns. All three have their roots in the widespread but diffuse feeling, of which some particular aspects have been canvassed, that the tax system is seriously wrong and getting worse.

Indeed, there is by now a growing body of opinion which regards the tax system as inflationary, inefficient, inequitable and undemocratic. It is inflationary for a number of obvious reasons of which two perhaps stand out. First, it has been a major factor in facilitating the excessive growth of big government, recognized by many to be at the core of the inflation problem; and secondly, it has been a major factor in the generation of cost-push inflation. Unions, quite reasonably, try to maintain real after-tax earnings but it is pre-tax wage costs which are built into prices.

The system is inefficient (and very damaging to the economy) because it transfers excessive and increasing wealth from the productive private sector to the usually unproductive public sector (or more strictly, the non-market sector). There can now be few, apart from doctrinaire zealots, who regard tax dollars as money well spent. Many, if not most, people are convinced that giving money to vote-catching politicians and self-serving bureaucrats amounts to pouring a large proportion of it down the drain. It is undemocratic because it transfers an increasing proportion of the wealth produced by the market sector to big government without a clear mandate from the electorate.

The system is particularly inequitable to PAYE wage and salary earners, whose scope for avoidance is slight, and whose proportionate contribution to revenue has increased greatly in the last decade. It would be interesting to see how much tax could be collected from them if PAYE were abolished.

Not so long ago, it was accepted that only the rich were in a position to avoid tax, usually through schemes to exploit legal loopholes. This is certainly not so any more. Anyone with half an eye can see that a disastrous effect of excessive taxation has been the emergence of a "cash" economy of massive and growing proportions, on which the fiscal system simply does not impinge. There can be little doubt that this phenomenon is the response of taxpayers at all income levels to taxation which they regard as tyrannous in its magnitude and unacceptable in its deployment.

No doubt these factors, as well as election promises, prompted the Government to initiate the recent debate on tax reform. The Government expressed concern about the inequities of the system, and discussion centred on what indirect taxes could be introduced or expanded so that personal income tax could be reduced substantially. Then two ominous strains emerged in the discussion. First, indirect taxes tended to be judged, in part, on how effective they would be in concealing the amount of tax paid. Secondly, new or expanded indirect taxes began to be discussed not as a partial substitute for personal income tax, but to make good the predicted decline in the oil levy. A good deal of publicity was given, towards the end of the debate, to a concerted demand by the States for sufficient funds to give them a little under two per cent a year real growth, suggesting a need for higher, rather than lower, tax revenue.

The importance of tax reductions as a concomitant of smaller government, as a counter to tax avoidance, or as a fillip to the market sector, though not entirely ignored, never became central to the debate. These are the vital problems to which the debate on tax reform should have addressed itself and scarcely did.

It is reasonable to ask how this should have come about under the auspicies of a Federal Government committed to greater personal freedom, less big government and official interference, and lower taxes. What made Mr. Fraser (whose opinion quite properly dominated the Government) back off? That the increased indirect tax would have raised prices was doubtless one reason; but there were surely others. First, the electoral effect of a fairly large jump in prices would not be attractive to the Government. They got away with it on the oil levy, but might not wish to push their luck again. Secondly, there is a well-founded suspicion among electors that anything done by big government in the area of taxation will be to the detriment of the people. Thirdly, tax-induced price rises would almost certainly result in additional wage claims from unions, even if offset by comparable income tax cuts.

These reasons for not pursuing tax reform, though by no means insignificant, are scarcely persuasive, given a reasonably strong Government. More believable would be the possibility of the Government's having moved nearer the views that big government could not be prevented from becoming even bigger. This would be consistent with talk, said to be officially inspired, of personal income tax as the "growth tax of the 1980's" (for which role indirect taxes would not serve); and with the widespread reports that the efforts of the "Razor Gang" to reduce public sector spending would come to little.

As taxes increase, so too will the incentive to avoid them. Of course, the extent of the "cash" economy, though almost certainly enormous (it has been estimated at $11 billion a year), is not known with any accuracy; and knowledge of the extent of tax-avoidance schemes is little better. Nevertheless, it is clear that the moral suasion of paying taxes has been seriously eroded. For this there are salient reasons. First, personal taxation, in particular PAYE, is excessive. Secondly, it is obvious even to ordinary people with no inside knowledge that a high proportion of their tax dollar is devoted to expenditure of which they do not approve. Possibly, few would as yet argue that the tide of morality has turned, that an individual's public duty is now to try to decrease the tax grab. Yet there can be little doubt that the decline of moral force in relation to taxation is largely responsible for burgeoning avoidance.

In turning its back on any worthwhile tax reform, the Federal Government may, in retrospect, be seen to have destroyed a vital element of hope for ordinary wage and salary earners. In 1975, they had hoped that the threat of mounting taxation could be averted by the ballot box. Now they have reason to fear that both sides of the House are committed to confiscatory taxation, which not merely permits, but ensures, open-ended increases in personal taxation without specific mandate from the electors.

In this, there are frightening implications for the people of this country, suggesting that the Government may be coming, against its will and its basic philosophy, to accept as inevitable the continued growth of big government. This would require that means be sought, not to reduce, but to increase taxation (throughout the tax reform debate, there were hints that this might be the case). If the Government is now convinced of the need to increase total taxation (and one must still hope that it is not), then it would make sense greatly to extend indirect tax and reduce personal income tax, but to retain the "progressive" tax scale. This would buy time before the burden of personal tax again became as onerous as it is now; and by then the extended indirect tax might have been accepted and total taxation much increased.

In deciding against tax reform, the Government has opted for what revenue-hungry officialdom must regard as second best. However, personal income tax will still increase comfortably faster than the incomes it plunders, albeit from a higher base.

For such an increase to take place, inflation is essential. This is anyhow