

## 4 State Revenue and Taxation

### *Introduction*

The first thing to be said about State taxes is that there is no magic pudding. There are no easy solutions, and the voters must know it. The new government must deal with its fiscal inheritance, that is, the large burden of debt described in the preceding chapter. To cope effectively with this inheritance, the government has only two options: raising taxes or cutting spending. Either will involve some political pain, but it is unavoidable. The decision will be made all the more difficult by the structural bias, already noted, against taxpayers and in favour of more government spending; and its consequences will be all the more important because of the large costs imposed on the economy by the inefficiency of the tax system.

The supporters of government spending are numerous, well-organised and well-connected, and have the illusory nature of the tax system and the hand-out mentality of the political system working in their favour. Taxpayers are less well organised, and often are not even aware that they pay certain taxes. On the other hand, State taxes and charges come at a very high cost. Taxes *per se* act as a significant disincentive to firms and individuals to invest, to save, to employ people and even to remain in the State. Interstate competition, particularly from Queensland—a very low-tax State—will to some degree bring the cost of taxation into focus. Unfortunately, the cost of taxation is often invisible, or at least hard to verify; yet the benefits of government spending are obvious and often exaggerated. The result is high taxes, too few jobs, and too much spending.

The task facing the government will be to manage, fairly and effectively, its unfortunate legacy, and at least to begin the task of reforming the tax system. To achieve these tasks, the government will have to break completely from the ways and means of the past.

The first issue that needs to be addressed—because past governments have proclaimed it so vigorously to be the case—is whether

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the State suffers from a chronic and structural revenue deficiency. Then, if there is no structural deficiency, is there still a need for more revenue, or is there scope for tax cuts? If taxes are to be increased, under what conditions and from what sources?

The new government must also face the issue of the reform of tax design. The State tax system *is* a mess, and acts as a hindrance to improving the accountability of government. Tax reform is, however, a political minefield, and has a history of being used to disguise increases in tax effort. It also has a history of abject failure, in the sense of yielding a system less equitable, less efficient, more complicated and less transparent than should reasonably be the case.

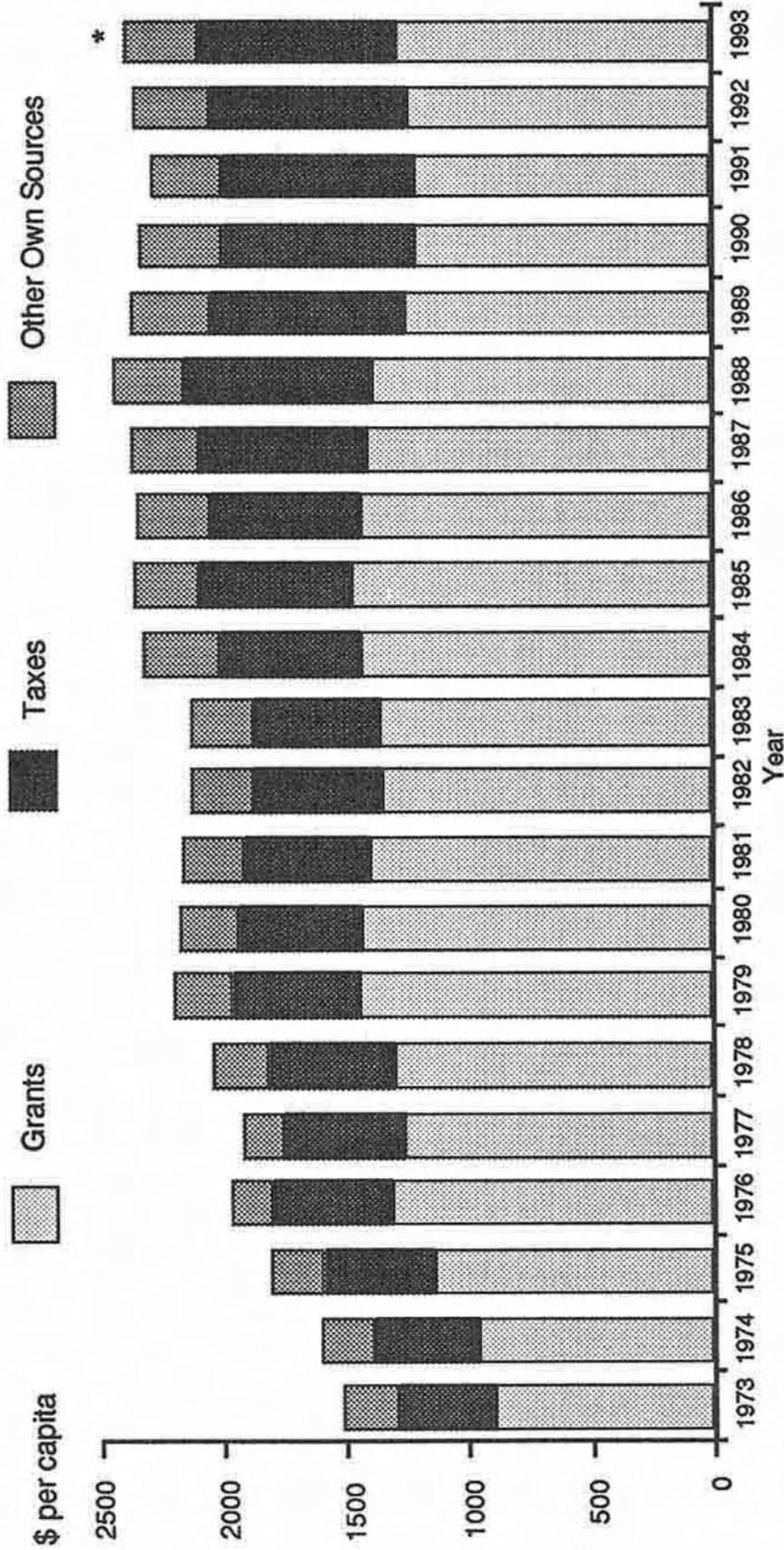
### *State Revenue: No Chronic Shortage*

Throughout the 1980s, Western Australian governments continuously claimed that the State public sector was systematically starved of revenue—mainly by the Commonwealth. Indeed, one of the principal justifications advanced for the various ill-fated WA Inc ventures was that they would overcome the 'excessive' restraint imposed on the State's funding by the Commonwealth's limiting the growth in grants and hindering access to a 'growth' tax.

Contrary to this view—one still officially promoted, and, in some quarters, looked on as received wisdom—Western Australian governments in fact enjoyed a substantial increase in revenue over the last decade. Although the State public sector has since 1986 experienced a period of comparative restraint, neither the large accumulation of debt nor the structural deficit resulted from a 'shortage' of revenue. More specifically, the State public sector is not facing a chronic deficiency in revenue. Indeed, the new government will inherit a superior revenue position relative both to other States and to this State's own recent experience.

During the 1980s, Western Australia, like most other States, experienced an unprecedented increase in State tax revenue. One of the most costly legacies of the 1980s was the squandering of these huge windfall gains, reaped during the asset boom, from stamp duties and land tax. These temporary gains were not only spent; they were, to a large degree, used to fund an increase in on-going expenditures. Moreover, when the boom collapsed and the related tax receipts declined, the government not only failed to cut back adequately on spending, but instead resorted to higher borrowings and taxes.

**Figure 4.1: WA Budget Sector Revenue, 1973-1993**  
(Real terms, \$ per capita)



\* Note: Figures for 1993 are IPA estimates.

Source: ABS and 1992-93 WA Budget Papers

### **Revenue Growth Has Been Substantial**

During the early years of the last decade (1982–86), Western Australia and other State governments experienced significant increases in revenue (Figure 4.1). In the four years between 1982 and 1986, the revenue available to the State general government subsector grew by 75 per cent in nominal terms or by 11 per cent after adjusting for population growth and inflation (Figure 4.1). The public sector as a whole experienced an even faster revenue growth.

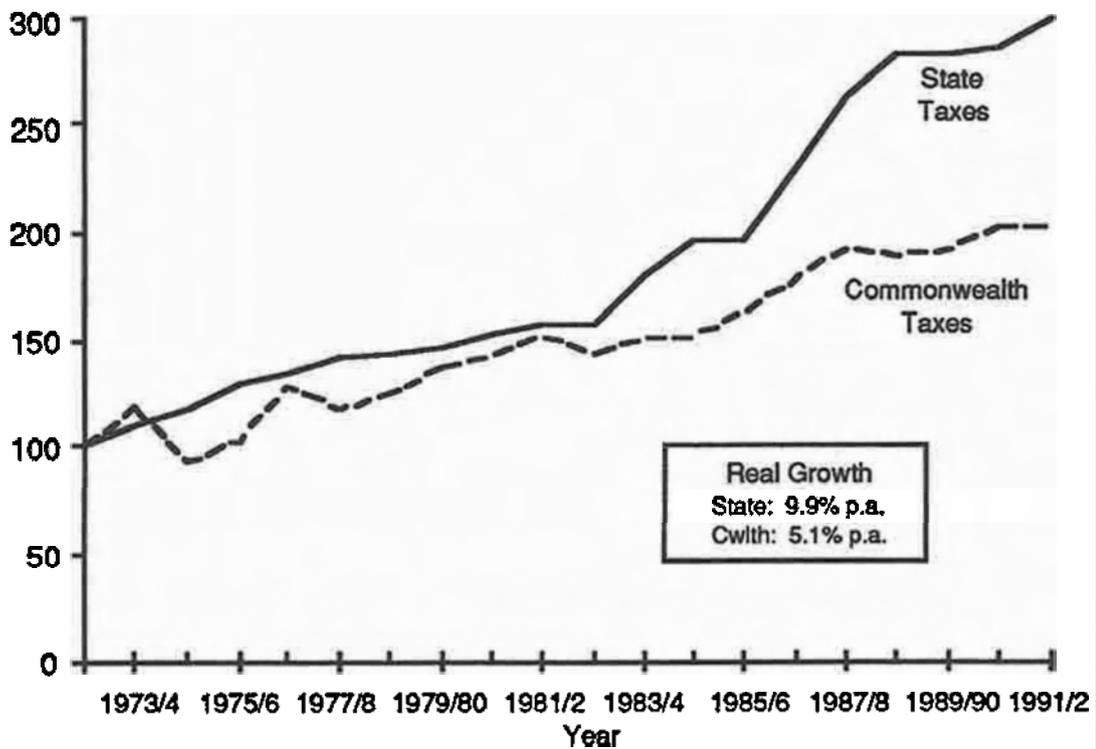
After 1986 and through to 1992, the growth in revenue available to the general government subsector slowed, and in real per capita terms declined by 0.5 per cent. This resulted from cuts in Commonwealth grants (which were reduced by 14.2 per cent in real per capita terms between 1986 and 1992) and, more recently and to a lesser extent, a recession and a policy of no increases in State taxes.

Despite the comparative restraint of recent years, the State public sector and general government subsector still ended the 1982–92 period with substantially more revenue at their disposal in real per capita terms: 20 per cent more in the case of the total public sector, and 11 per cent more in the general government subsector. Revenue in both the total public sector and in the general government subsector is expected to grow again in 1993, albeit modestly, and as a result is expected to approach, and in the case of the general government subsector exceed, the record level reached during the revenue boom of 1988.

### **Large Increase In State Taxes**

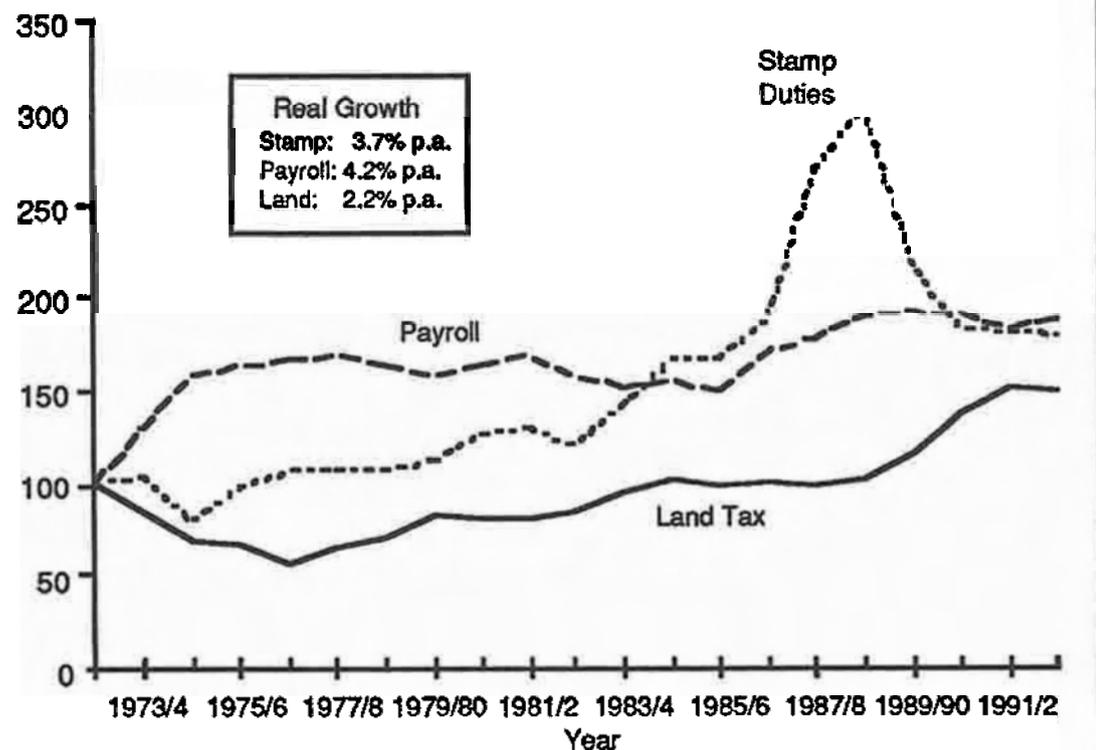
Western Australian governments, along with most other State governments, experienced a massive increase in State tax receipts over the last decade. State tax receipts in Western Australia increased by 60 per cent in real per capita terms, and by over 30 per cent as a share of Gross State Product (GSP) (from 3.7 per cent to 5.1 per cent), between 1982 and 1992. There was a marked and steady increase in tax receipts starting from 1983 (Figure 4.2). The greatest increases in tax receipts, however, took place after 1986. The main reason for the increase in receipts between 1983 and 1986 was greater taxing effort—both higher tax rates and new taxes. The post-1986 increase arose from a combination of huge windfall gains flowing from the asset boom and higher tax rates. As shown in Figure 4.3, between 1986 and 1989, stamp duty receipts more than doubled in real terms. Land tax receipts also increased, though later and more slowly,

**Figure 4.2: Growth In Total State Taxes (WA) and Commonwealth Taxes (1984/85 prices; 1972/73 = 100)**



Source: ABS National Accounts, various years.

**Figure 4.3: Growth In Selected State Taxes (WA), (per capita), (1984/85 prices; 1972/73 = 100)**



Source: ABS National Accounts, various years.

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and payroll tax also increased markedly. Stamp duty receipts fell back dramatically with the collapse in asset prices in 1990, but to a level still substantially above their pre-1986 level (Figure 4.3). Moreover, the increases in other types of taxes, particularly land tax, payroll tax and franchise fees, allowed the huge gains in tax receipts made during the asset boom to be sustained (Figure 4.2).

The growth in State tax receipts in Western Australia stands in sharp contrast to Commonwealth taxes. Until 1982, the tax receipts of the State and Commonwealth governments grew at about the same rate in real terms (Figure 4.2). After 1983, there was a sharp divergence: Commonwealth taxes continued to grow at about the same rate as in previous years, while State tax revenue shifted into near-exponential growth. Between 1983 and 1992, State tax receipts in Western Australia almost doubled in real terms, whilst Commonwealth taxes grew by a relatively modest 30 per cent.

### **Squandering Of The Tax Windfall**

Just as all the State governments received this huge tax windfall during the 1980s, all States but one consumed rather than saved this rare gift. It was the asset boom of the 1980s which gave rise to the massive increase in asset-based tax revenue such as stamp duty and land tax (see Figures 4.2 and 4.3). Despite the seductive euphoria then prevailing, it would have taken only a modest degree of wisdom or foresight to realise that this increase was to be of a temporary nature. The rational policy response should therefore have been to save the windfall by using it (or most of it) to cut the deficit. In Western Australia, a large portion of the windfall was instead used to provide the initial funding for the large increase in recurrent outlays associated with the 1989 State election (recurrent outlays grew by \$775 million or 24 per cent over 1989 and 1990).<sup>50</sup> So when the asset bubble burst, the Western Australian government had no savings to fill the revenue gap, and was forced to increase borrowings, to raise taxes and (to a lesser extent) to restrain the growth of spending.

### **WA Public Sector Is Relatively Well-Off**

Relative to other States, the Western Australian government is very well endowed with revenue. Throughout the last decade, the State's public sector, even after subtracting moneys passed on to Local gov-

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50 ABS, Cat. No. 5501.0, 1992.







































