COMMONWEALTH OF AUSTRALIA

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SENATE

SELECT COMMITTEE ON A NEW TAX SYSTEM

Reference: A new tax system

THURSDAY, 4 FEBRUARY 1999

SYDNEY

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SENATE

SELECT COMMITTEE ON A NEW TAX SYSTEM

Thursday, 4 February 1999

Members: Senator Cook *(Chair)*, Senator Ferguson *(Deputy Chair)*, Senators Conroy, Gibson, Murray, O'Chee and Sherry

Substitute members: Senators Brownhill, Chapman or Watson for Senators Ferguson, Gibson or O'Chee; Senators George Campbell, Mackay or Murphy for Senators Cook, Conroy or Sherry; Senator Lees for Senator Murray

Participating members: Senators Brown, Colston, Harradine and Margetts

Senators in attendance: Senators George Campbell, Conroy, Cook, Ferguson, Gibson, O'Chee, Murray, Sherry

Terms of reference for the inquiry:

(1) That a select committee, to be known as the Select Committee on a New Tax System, be established to inquire into and report, on or before 18 February 1999, on the economic theories, assumptions, calculations, projections, estimates and modelling which underpinned the Government's proposals for taxation reform, contained in *Tax reform: not a new tax, a new tax system*.

(2) That, in conducting its inquiry, the committee examine the following matters:

(a) the estimated levels of revenue to be generated or foregone due to the proposed changes, including the estimated level of revenue to be generated by imposing a goods and services tax (GST) on the basic necessities of life (such as food, clothing, shelter and essential services) and books;

(b) the effects of the proposed changes on:

(i) national Gross Domestic Product,
(ii) national export performance and national debt,
(iii) the national Consumer Price Index, and
(iv) the distribution of wealth in the Australian community;

(c) the effects of the package on future federal budget revenues, expenditures and surpluses, including a critical assessment of the economic assumptions underpinning the Treasury's projections in this regard;

(d) the effects of the taxation and compensation package on disposable income and household spending power for a range of ’cameo profiles’, including but not limited to those presented in the proposals, under the following scenarios:

(i) a GST extended to the necessities of life (such as food, clothing, shelter and essential services), and

(ii) a GST not extended to the necessities of life (such as food, clothing, shelter and essential services);

(e) with the aim of identifying families and groups who may be disadvantaged by the Government’s proposals, focusing on lower and fixed income individuals, families with dependent children or adult members, groups and organisations, and those with special needs, such as people with disabilities;

(f) the assumptions made as to consumption and saving patterns and the cost of living for the various ’cameo profiles’;

(g) whether the stated objectives of the package can be met by using an alternative and fairer approach; and

(h) such other matters as the committee considers fall within the scope of this inquiry.

(3) That the committee also inquire into and report, on or before 19 April 1999, on the broad economic effects of the Government’s taxation reform legislation proposals with regard to the fairness of the tax system, the living standards of Australian households (especially those on low incomes), the efficiency of the economy, and future public revenues, including:

(a) the effects on equity, efficiency and compliance costs of including, or not including, food or other necessities of life in the GST, together with any related adjustments to the package if food or other necessities of life were GST zero-rated;

(b) the effectiveness of the package in easing the poverty traps facing people on low incomes, and reforming and streamlining tax and income support for families with children, taking into account the static and life-cycle impacts on families with children;

(c) options for amending the income tax schedule to make it more equitable;

(d) the findings of the Tax Consultative Committee chaired by David Vos;

(e) options for improving the effectiveness and fairness of the tax system and reducing inequitable or unreasonable tax avoidance and minimisation, including consideration of alternative areas for tax generation, either where there are current tax concessions or where Australia’s taxation system does not address major tax potential, and without limiting the foregoing, the consideration of taxation of foreign companies operating in Australia, including the relative merits of resource rent taxes, royalties or land taxes as compared to company tax in securing a fair compensation to Australia for use of its resources, whether the 150% tax concession for research and development should be restored and whether small companies should be allowed to be taxed as partnerships.

(f) the potential for tax avoidance and evasion, including an examination of the effects on the cash economy, and the potential impact of electronic commerce on the future viability of a GST;

(g) the effects on compliance costs;

(h) the potential for reducing payroll tax, including by providing incentives to create long-term employment and by replacing payroll tax with a carbon tax;

(i) whether there are other means available for rebating or reducing the indirect taxes or excessive user charges embedded in exporters costs;

(j) excises, including those on fuel, tobacco and alcohol - identifying the industries which benefit, and to what extent, from the proposed changes to taxes on fuels;

(k) the effects on interest rates;

(l) the effects on investment, in both physical and human capital formation;

(m) the effects on small business;

(n) the effects on the non-profit sector, including the total amounts of money contributed by the sector, administrative costs, impacts on the viability of the organisations, and the consequent effects on the wellbeing of the community;

(o) the effects of the GST on particular industries, including:

- (i) key service industries such as tourism,
- (ii) the Australian automobile and related industries, having particular regard to the effects of changes to fuel excises,
- (iii) other 'invisible' export industries, such as education and financial services, and
- (iv) the international competitiveness generally of Australian industries;

(p) the implications of not requiring that the GST component of goods and services be itemised on receipts;

(q) the effects of the taxation reform legislation proposals on rural and regional stakeholders, including:

- (i) the effects on particular regions,
- (ii) the effects on rural and regional communities of different tax regimes on fuel - especially the cost of transport of goods to rural communities,
- (iii) the effects on primary industry of replacing the current sales tax exemption on agricultural machinery with a GST, and
- (iv) the effects of imposing a GST on food and other necessities of life on remote communities, including Aboriginal and Islander communities;

(r) the effects of the Government's taxation reform legislation proposals on state and local government administration, including:

- (i) the effects of the package on future federal-state financial relations and the capacities of state and local governments to adequately finance their respective responsibilities in both the short-term and the long-term, including the effects of the proposed transfer of responsibility for local government financial assistance to the states, and whether it discriminates between states,

- (ii) the implications for specific purpose programs,

(iii) mechanisms required to lock in commitments made by federal and state governments with regard to the new arrangements,

(iv) the implications for future federal-state financial relations of not extending the GST to the necessities of life (such as food, clothing, shelter and essential services) and books, and any adjustments to the proposed arrangements which would be required to federal-state financial relations,

(v) the implications of the package for the quality and affordability of public utility services and for the public utility concessions for social security recipients,

(vi) the effects of application of the GST, and of changes to tax status, on local government and its activities, particularly commercial activities,

(vii) the implications for the delivery of Commonwealth Government services, including employment services, welfare and other social and cultural services, and

(viii) the extent to which the proposed compensation arrangements are secure from change to below adequate levels;

(s) the adequacy of measures to ensure that consumers fully benefit from the abolition of existing taxes;

(t) the effects of the taxation reform legislation proposals on legal and constitutional matters, including:

(i) the constitutionality of the proposed mechanism for future changes to the GST, including whether such changes would present a significant hurdle to future increases, or reductions if deemed necessary to stimulate the economy,

(ii) the constitutionality of the proposed reorganisation of federal-state tax arrangements and whether the powers and functions of states and territories are materially affected by this reorganisation, and

(iii) the effects of the proposals on the cost of access to justice; and

(u) options for amending the proposed legislation to improve its fairness or efficiency.

(4) That, in reporting on the matters referred to in paragraph (3), the committee have regard to the reports of the references committees referred to in paragraph (17) and integrate the findings of those committees into its final report where relevant.

(5) That the committee consist of 7 senators, 3 nominated by the Leader of the Government in the Senate, 3 nominated by the Leader of the Opposition in the Senate, and 1 nominated by the Leader of the Australian Democrats.

(6) That the committee may proceed to the dispatch of business notwithstanding that not all members have been duly nominated and appointed and notwithstanding any vacancy.

(7) That:

(a) senators may be appointed to the committee as substitutes for members of the committee in respect of particular matters before the committee;

(b) on the nominations of the Greens or independent senators, participating members may be appointed to the committee; and

(c) participating members may participate in hearings of evidence and deliberations of the committee, and have all the rights of members of the committee, but may not vote on any questions before the committee.

(8) That the committee shall elect as its chair a member nominated by the Leader of the Opposition in the Senate.

(9) That the committee shall elect as its deputy chair, immediately after the election of the chair, a member nominated by the Leader of the Government in the Senate.

(10) That the deputy chair act as chair when there is no chair or the chair is not present at a meeting.

(11) That the committee have power to send for and examine persons and documents, to move from place to place, to sit in public or in private, notwithstanding any prorogation of the Parliament or dissolution of the House of Representatives, and have leave to report from time to time its proceedings and the evidence taken and such interim recommendations as it may deem fit.

(12) The quorum of the committee shall be a majority of the members of the committee.

(13) The committee set 29 January 1999 as the date for receipt of submissions.

(14) That the committee hold hearings in each state and territory as required.

(15) That the committee be provided with all necessary staff, facilities and resources and be empowered to appoint persons with specialist knowledge for the purposes of the committee with the approval of the President.

(16) That the committee be empowered to print from day to day such documents and evidence as may be ordered by it and a daily Hansard be published of such proceedings as take place in public.

(17) That the following matters be referred to references committees in accordance with the schedule below for inquiry and report by 31 March 1999, and that in undertaking these inquiries the committees have regard to the report of the Select Committee referred to in paragraph (1) and consult widely, holding hearings in each state and territory, as required. Submissions to these inquiries are to be made by 29 January 1999.

Committee	**Matters for Inquiry**
Community Affairs	The impacts of the Government's taxation reform legislation proposals on the living standards of Australian households (especially those on low incomes), including: (a) the scope and effectiveness of the proposed arrangements on charities, child care services, aged care services, welfare services, local government human services and all not-for-profit organisations in maintaining the quality and affordability of essential community services, including the implications for the public funding of these services and the implications for the commercial activities of these organisations, and whether unconditional GST-free status should apply to *bona fide* charities; (b) a detailed examination of the zero-rating of health services, including an examination of which services should be zero-rated;

	(c) the effects on community sector organisations of changes to their tax exempt status, and of the compliance costs of the proposed tax arrangements; (d) the effects of the proposed private health insurance rebate; (e) the effects on people with disabilities; (f) the effects on public, community and private housing, including the levels of rents; and (g) options for amendments to improve the fairness or efficiency of the proposed legislation.
Employment, Workplace Relations, Small Business and Education	The employment incentive and education impacts of the Government's taxation reform legislation proposals, including: (a) the scope and effectiveness of the proposed zero-rating arrangements for education in maintaining its quality, accessibility and affordability; (b) the effects on employment; (c) the effects of the proposed GST treatment on the quality, accessibility and affordability of employment services; (d) the effects on education of imposing a GST on, or zero-rating or exempting books and associated education resources; (e) the effects on education of imposing a GST on ancillary resources, services and commercial activities, including the effects on overseas students; (f) the effects of the proposed changes to the tax system on employment; (g) the effects on wage costs, particularly if the basic necessities of life are taxed; (h) the scope and effectiveness of changing the unemployment benefits, pensions and Newstart Allowance 'tapers'; (i) the effects of the proposed changes to the tax system on training and adult education; and (j) options for amendments to improve the fairness or efficiency of the proposed legislation.
Environment, Communications, Information Technology and the Arts	The broad effects of the Government's taxation reform legislation proposals on the environment, the arts and information technology, including:

(a) the environmental effects, and likely impacts of changes to fuel excises, particularly but not only diesel, and the replacement of WST with GST on vehicles and other transport services including:

  (i) possible increases in greenhouse gas emissions,
  (ii) increases by amount and type of air pollution,
  (iii) the effects on public and rail transport,
  (iv) the effects on alternative energy use in transport including, but not limited to, compressed natural gas,
  (v) the changed effects on native forests of logging or woodchipping due to the tax package, and
  (vi) the changed effects of mining in environmentally sensitive areas due to the tax package;

(b) the environmental effects of the replacement of Wholesale Sales Tax by the GST and associated changes in fuel excises on electricity and natural gas;
(c) the impacts of the proposed tax changes on the prices and existing and potential use of renewable energy particularly but not only solar energy technology and energy efficiency equipment;
(d) the environmental effects of any changes to taxes on exports;
(e) the consistency or otherwise of the proposed changes in taxation and excise arrangements with Australia's international treaty obligations, including its obligations under the Framework Convention on Climate Change;
(f) options for a tax system which better achieve environmental objectives,including incentives for fuel efficiency and alternative energy sources, such as measures which promote both environmental protection and employment generation;
(g) the extent to which environmental impacts were considered in the drafting and final copy of the Government's tax package;
(h) the scope of any consultation on environmental matters with experts in Environment Australia or any other Government departments other than the Treasury and Finance departments;
(i) the impact of a GST on ticket sales for the performing arts;
(j) the effects of a GST on the transfer of grant monies for arts projects;

(k) the effects of the tax proposals on sponsorship provided by the private sector to individual artists and arts organisations;
(l) the extent to which the package will block consideration and introduction of ’ecotaxes’;
(m) the effects of a GST on not-for-profit conservation and arts organisations; and
(n) options for improving the environmental effects of the package.

(18) That the provisions of the bills implementing the proposed new tax system stand referred to the previously mentioned committees for inquiry and report in conjunction with the terms of reference authorised by this resolution, as soon as the bills have been introduced in the House of Representatives.

(19) That when the bills referred to in paragraph (18) are first introduced in the Senate and a motion is moved for the second reading of the bills, debate on that motion shall be adjourned at the conclusion of the speech of the senator moving the motion and resumption of the debate shall be made an order of the day for 19 April 1999 without any question being put.

WITNESSES

Committee met at 9.02 a.m.

CHAIR—Today the committee continues its inquiry into the first stage of the proposed changes to the Australian taxation system. During the first stage the committee will focus on the economic theories, assumptions, calculations, projections, estimates and modelling which underpinned the government's proposals for taxation reform. In the second stage of the inquiry, the committee will examine the broad economic effects of the government's taxation reform legislation proposals. It will take regard of the fairness of the tax system, the living standards of Australian households, especially those on low incomes, the efficiency of the economy and future public revenues.

The Senate referred the inquiry to the committee on 25 November 1998. The committee expects to report on the first stage by 18 February 1999. For three related inquiries by the References Committees on Community Affairs; Employment, Workplace Relations, Small Business and Education; and Environment, Communications, Information Technology and the Arts, the scheduled reporting date is 31 March 1999. This committee will then report on the second stage of its inquiry by 19 April 1999, taking into account the findings of the references committees.

This committee has called for submissions by 29 January 1999 and so far has received well over 1,000. This is the first public hearing to be held by the committee in Sydney in the course of this inquiry. In addition to this hearing, the committee will be conducting other public hearings in capital cities and in some major regional centres.

The committee does not intend to release all submissions as yet, except for the submissions by the witnesses who are giving evidence today. Is it the wish of the committee that submissions Nos 68, 340, 383, 472 and the ABS one be made public? That being the case, I now declare that those submissions to this inquiry, together with their attachments, be released.

For the record, this is a public hearing and as such members of the public are welcome to attend. Before we commence taking evidence, let me place on record that all witnesses are protected by parliamentary privilege with respect to submissions made to the committee and evidence given before it. Parliamentary privilege means special rights and immunities attached to the parliament, or its members and others, necessary for the discharge of the functions of the parliament without obstruction and without fear of prosecution. Any act by any person that operates to the disadvantage of a witness, on account of evidence given by him or her before the Senate or any committee of the Senate, is treated as a breach of privilege.

BROWN, Mr Christopher, Chief Executive Officer, Tourism Task Force Ltd

FLOWERS, Mr Karl Stephenson, Managing Director, Decisive Tourism Consulting, Tourism Task Force Ltd

HILL, Mr Nick, Taxation Adviser, Tourism Task Force Ltd

CHAIR—Welcome. As is becoming the evolving practice of this committee, we will invite you, if you choose, to make a short opening statement giving the committee an overview of your submission that you have presented to us and then make yourselves available for questions from the committee.

Mr Brown—I would like to welcome the committee to the fair city of Sydney in its first deliberations here, and trust we can help shed some more light on this process.

The Tourism Task Force Ltd is a national lobby group representing particularly the corporate end of the tourism industry. Mr Flowers has had a career in Treasury and five years with the Department of Tourism in charge of its investment division. He now operates in his private capacity. Mr Hill is one of the senior partners in the Sydney office of Deloitte Touche Tohmatsu, an accounting practice, and is a specialist in some of the implementation areas and international comparisons of GSTs in the tourism industry.

I will make an opening statement. Certainly we would be open for questioning and no doubt rigorous interaction with the committee. The Tourism Task Force has undertaken an extensive study of the impact of the tax reform package on the tourism industry. I should point out that we strongly support comprehensive tax reform. We entered this study with an open mind on that basis. Unfortunately, our independent research shows that the package as it stands will have a significant negative impact on employment in this industry because of its impact on economic activity generated by tourists and their spending.

On government provided figures, tourism spending generates over one million full-time and part-time jobs in the Australian economy. I think it is the nation’s largest employer. Our findings are that nearly six per cent of these jobs could disappear if tax reform is passed without amendment and without transitional assistance from the government. The detailed modelling undertaken by Decisive Tourism Consulting and reviewed by the Tasman Institute, including economists, shows that 59,000 full- and part-time jobs around Australia could be lost as a result of falling spending by inbound and domestic tourists.

The impacts of the tax reform on tourism will be most heavily felt in regional Australia and particularly in states relying on long haul domestic travel, particularly such as Queensland and Tasmania. Unfortunately, here the prospects of alternative employment are much lower than they are in metropolitan areas. While I would hope and expect that this most resilient of industries would not have to shed this many jobs, this is what our modelling shows.

The impact of the package on tourism would not be as severe if the government reversed its inexplicable decision not to zero rate tourism exports. The government has rightly promised commodity and manufacturing exporters that their products sold overseas will be

GST free in the name of protecting their international competitiveness and the jobs they generate. For reasons that have not been explained properly, the tourism industry has not been treated fairly and extended the same zero rating.

This industry earns over $16 billion a year in export income, which is far more than any other single commodity or product; in fact, it is almost twice the value of coal, the number two exporter. It will be a relatively simple matter to zero rate the main component of tourism exports, namely, holiday packages bought offshore. This measure would not cover all tourism exports and is therefore nowhere near the generous treatment afforded to every other exporter. This single measure alone would alleviate much of the negative impact generated by the tax reforms, as package tourists are the most price sensitive of any in this market. They have a lot less control over their own destiny; their travel patterns are largely determined by tour wholesalers. It would be relatively inexpensive in forgone revenue, as many more tourists would come and pay GST and other taxes while they are here.

I should make it perfectly clear and place on the public record that the TTF believes that any and all discretionary spending by tourists outside the zero rated package would attract a full GST. We are not advocating that tourists wander the streets with their passport, waving it and getting 10 per cent off everything they buy. However, if the tourists do not come, they pay no tax at all. Zero rating packages would ensure that all rail travel and Bass Strait ferry services receive the same tax, and that also goes for all coach travel.

The same treatment, which is already promised for domestic flights purchased offshore, obviously will discriminate against land and sea transport operators, who would not have access to the same arrangement. It just would not be fair to penalise people like Tasmania and Queensland, which have a much greater dependence on sea travel, obviously, with the Bass Strait ferries and, particularly with Queensland, rail's contribution to getting tourists out of the gateways into the regional areas where those jobs are needed more than anywhere.

Zero rating inbound packages and providing a boost to the Australian Tourist Commission funding to ensure that other destinations do not exploit our loss of competitiveness can alleviate over half the negative employment impacts of the tax reforms on the inbound tourism industry—over half. This will be at a minimum cost, while ensuring the integrity of the government's package. We have found that, while the impact on domestic tourism is smaller in percentage terms than the impact on inbound tourism—about which I think you heard significantly from Professor Dixon yesterday—it is set to cost more jobs. In fact, it could cost up to 34,000 Australian jobs.

The GST means that the price competitiveness of destinations such as Western Australia, the Northern Territory, Tasmania and tropical North Queensland will be reduced against their overseas competitors. Australians will fly over Australian destinations heading for much cheaper South-East Asian destinations. Of course, their airline ticket will not attract a 10 per cent GST overseas but it will attract the same GST in Australia. To counter this, long haul domestic destinations should be spared some of the worst impact of the government's proposals. Long haul domestic transport should be GST free. National advertising should promote travelling within Australia and operators in remote regions should be funded to band together to improve their marketing and product.

In conclusion, I stress again that the TTF does support comprehensive tax reform and recognises that tourism has a vital role to play in ensuring Australia's economic prosperity. I should point out the admirable comments by the Treasurer to head towards four to five per cent unemployment. We want to be part of helping that, not hindering it. Without tourism, without a strongly growing domestic and inbound tourism sector, the economy will never reach four to five per cent unemployment levels.

We do not believe the government has paid enough attention to the negative impacts of the reforms on this industry or to the simple and inexpensive measures to soften those impacts. In fact, I put on record that I think it is disgraceful that so far there has been no modelling by Treasury on the job impact in the services sector, particularly in the tourism sector. We are accounting for three-fifths to two-thirds of the nation's work force and Treasury has not seen fit to produce or publish figures which show what the impact on employment would be. In fact, the Econtech submission for Treasury to this committee I believe does do some modelling even suggesting that, with everything we wanted, a zero rating of packages, it still shows a significant impact in, for example, the accommodation sector.

We make our submission in the spirit of cooperation and service to this industry, the government, the Senate and the Australian people. We hope it will stimulate further national attention on the important role that tourism plays in our national prosperity and its contribution to the national interest. We am happy to make ourselves available for questions from senators.

ACTING CHAIR (Senator Ferguson)—Thank you, Mr Brown. In the absence of the Chairman I should be as generous as him and call Senator Sherry, I think.

Senator SHERRY—Mr Brown, how would you describe the situation facing tourism. Is it glum?

Mr Brown—I suppose you can break it into an inbound and a domestic sense. Internationally, we have been knocked around a bit in the past year. Half of our inbound tourists were coming from Asia. This was predicted to grow to two-thirds within the next five years, and suddenly Asia is not as prosperous as it used to be. When suddenly half your customers go broke it forces you to sit up and take notice. Fortunately, we have been bolstered by a very strong US and European economy and by some marketing savvy of the government's agency, the ATC, in trying to tune in to those markets even more so. They have limited the fallout to probably four or five per cent reduction in tourist numbers this year.

Domestically, it is much more dire. Aussies have a passion for going overseas. There is about eight per cent growth a year. We are hopping on planes and heading off to generate jobs for other people's children instead of our own. This is particularly the case in regional Australia, which is the great beneficiary of domestic tourism. Tropical North Queensland has been hurt and Tasmania is just not getting the growth it should. A lot of these things are affected by price and by a marketing perception. It is not as if we are starting with a sparkling blue sky of wonderment. All of a sudden we have to cop a little hit on the chin where we are doing it a bit tough, and we are concerned about the impact this reform will have further.

Senator SHERRY—On page 34 you have a table 4—'Distribution of expected job losses'. Looking down that table, the areas impacted most heavily are the Northern Territory with a two per cent increase in unemployment; Tasmania, one per cent; and Queensland, one per cent. I must say I view with horror those figures for Tasmania, given the dire condition the economy is in. You have mentioned regional impact. What are the consequences of such a significant decline in regional economies, particularly where there are few options for industry growth or alternative job creation?

Mr Brown—I hate to be a doomsayer, but you are right. It actually gets worse in those places. If you are in Sydney and you are working in the Gazebo and a fall in demand means that 15 staff are laid off, a good percentage of those are likely to go and get a job behind the counter at DJs, or they can be retrained as an IT computer salesman. Quite simply, if you are running a B&B in south-west Tasmania, or you are working for somebody who is running one who only needs four staff instead of five, the situation is pretty bleak for that kid to get instant alternative employment.

We are very proud at the way this industry is contributing to regional development. If you look around Australia at the moment, they are not all correct but a lot of local government areas particularly are being polled and are saying, 'Tourism is our salvation.' There is great job hope because the farms and the mines just do not employ as many kids as they used to, but we have stepped into that breach. I am generally fearful, particularly for the impact on domestic tourism, which is where most of the regional input and regional impact is, that, particularly for the far flung markets and long haul destinations, when the source markets of Sydney and Melbourne are deciding where to go on holiday, they just do not decide between Tasmania and Queensland, they decide between 200 countries around the world which are offering a tourism product. There are probably 30 options within the equivalent time scale and travel time in our region. It is a price disincentive, and the price will decide where you go. The negative impact of that is significant. It is shown in the job figures all around the country, and particularly so in the bush.

Senator SHERRY—In the bush and in regional Australia, which you have highlighted in this survey, if we do not get investment and job creation in other industries, we are going to see a shift of industry and employment out of those regions in a net sense. One of your colleagues might like to comment as well.

Mr Brown—Yes. Without a doubt, one of the underlying ramifications of the package as it is is that this in a way becomes a tax on Queensland, a tax on Tasmania and a tax on the Northern Territory to benefit places with a bigger manufacturing base like South Australia and Victoria. New South Wales probably has a neutral impact because of its more diversified economy. It really is a tax on the regions and a tax on the outlying states, and I think the job figures are showing that. Karl might like to add to that.

ACTING CHAIR—You say that you support the package, but you are arguing the case for exemption of inbound tourist packages.

Mr Brown—We say we support tax reform in general. We are very supportive of attempts to modernise the tax system. If there is not significant change to tax, our great fear is that every state government gets in on the Sydney bed tax act and we have a raft of sector specific taxes. We are not mugs; we know we need tax reform of some nature in the country. But we are saying that you can humanise this package to protect a lot of these jobs.

Senator O'CHEE—Isn't this like St Augustine: Lord, make me pure, but not quite yet?

Mr Brown—We are not trying to get special treatment or pick winners. We are trying to protect existing winners so they can help contribute to job creation. There are not many industries that can come in and say they are predicting the job growth that normally tourism is. In fact, no industries can come in and talk of the potential development in regional Australia that tourism can. It is a mug's game to be going out and saying, 'What can we do to try to cull the job prospects in these regions?'

Senator O'CHEE—You are saying we have got to protect existing winners, but existing losers say we want to protect existing losers. Soon everybody is asking for protection.

Mr Brown—We are not asking for protection; we are just asking for equal treatment. We are asking for the same export zero rating that every other product and service for export is going to receive.

Mr Flowers—Even if you gave us, in a fit of generosity to the tourism industry, everything we asked for, the tourism industry will not get anything near the same treatment as every other sector, for two reasons. Firstly, we are not asking for zero rating for all our exports, we are only asking for those that are package tours bought overseas. Secondly, the import competition to every other sector pays GST. Ours does not, and never will. That is what is going to hurt domestic tourism.

When you are talking about jobs, as I think the Senate has a legitimate interest in, the areas that are going to benefit most from the government's package as it stands are mining and, to a lesser extent, manufacturing. Unfortunately, both modern mining and manufacturing are not great employers. They are very efficient users of capital.

The tourism industry has not as yet broken through to the same extent in our labour productivity. As a result, we are a very large employer. It is incumbent on the Treasury to explain where the jobs lost in tourism—we have estimated 59,000 and we would love to see their figures—are going to be found elsewhere in the economy. Regionally, is it the case that there will be clear winners and losers? We think there are. We would be very interested to see if Treasury agree with us.

Senator SHERRY—Can I just come to another Tasmanian specific issue. On page 27 of the submission, you refer to the Devilcat being liable for the GST. Doesn't this highlight the absurdity of the situation that Tasmania is going to face, obviously being heavily reliant on sea transport as a major part of its tourism transport to and from the state? There is not equal treatment in terms of sea transport vis-a-vis air travel, and that has serious implications for Tasmania in particular.

Mr Brown—Let there be no ambiguity: Tasmania is the loser out of this package. Tasmanian jobs are the big loser out of this package so far. Unfortunately, Tasmania does not have the capacity to adapt to some of the up sides in the package to pick up that employment slack which is going to be caused by tourism job losses. A large proportion of tourists, particularly domestic tourists, access Tasmania on a float and ride concept, putting the car on the ferry and going across and car touring around Tasmania. It does not yet receive a big enough proportion of international inbound tourism. Simply to zero rate packages does not insulate Tasmania. It does very little for Tasmania. It is more a domestic issue.

There is a much greater reliance on Aussies, particularly Victorians, driving down to Port Phillip, putting the car on the boat, going across and cruising around Tasmania, creating jobs and dropping money into the economy. We accept that the proposals we put forward are still going to have serious ramifications for Tasmania. We have not asked for a range of measures that can totally insulate it. It is too difficult to do and it would go into areas of inequity of how you treat different products within the economy. But we sure as hell want to try to do something, because we are proud of the fact that we are in some ways the economic mainstay of the Apple Isle. It would be tragic if the package, unamended, would harm that situation currently.

Senator SHERRY—I do not think you should use the term 'Apple Isle'. Its mainstay disappeared 25 years ago.

Mr Brown—It is now the Holiday Isle. You are right.

Senator SHERRY—Just two more quick points. Can I get a clarification on your recommendation 6, to amend the GST legislation to ensure that long haul domestic airfares and land and sea passenger transport are GST free. I assume you include within that the sea transport across Bass Strait as long haul.

Mr Brown—It is a difficult one. When it comes to long haul, we have assumed a kilometrage of 1,000 kilometres. That obviously would not cover the Bass Strait. It is a long sea trip, but it would not be that coming from Port Phillip Bay. I think that needs further investigation. It falls into the area of regional compensation or regional transitional assistance, more so than just that component there.

Senator SHERRY—I think we should reject the whole package, but legislatively it would be very easy to exempt Bass Strait passenger shipping from a GST, I would have thought.

Mr Brown—Depending on the final outcome, the way votes fall in the Senate, it has been jokingly referred to that people would be paid to go across on the Devilcat by the time this process is passed, particularly the way certain senators might have an influential vote on this process. But we have not asked for that yet. Quite simply, we believe that it is so important to Tasmanian tourism that it needs to be thought of outside the square. If we fail and the Senate decides that it will pass the package as is, then at least the exemption for on-carriage transport should be provided for trains, planes and buses as well as currently for domestic airfares. But at best we would also like to see part of the regional transition package consider specifically the issue of the Bass Strait ferries.

Senator SHERRY—Just one last point. I could not see anything specific on the issue of tourism railways. Do you have any comment to make about tourism railways?

Mr Brown—There is a wonderful rail renaissance in Australia. Suddenly we have tourists, both domestic and international, hopping on the train as part of their holiday experience, not only to get from point A to point B but to experience getting from point A to point B, C, D or E. The fuel exemption process quite simply does not treat train operators as generously as it does road operators. I think that has been done with freight in mind and not passenger transport, and our interest is obviously in passenger transport.

Rail users are discriminated against in comparison with the treatment that inbound passengers get on airfares, they are discriminated against in a freight sense in comparison with road users and therefore we do not want to kill the rail renaissance before it gets into full stride. Trains are a great generator of regional development. Aussies and foreign tourists going across on the *Ghan*, on the *Indian Pacific* or hopping on the *Queenslander*—or taking Peter Beattie’s new tilt train to Townsville, eventually, and to Cairns and beyond—should not be discriminated against. It is long haul travel; it is original development generation; it should be treated at least in the same way as airfares for foreign tourists are and, we would hope, treated in the way we have recommended to encourage their use in a domestic tourism sense.

Senator SHERRY—Just to understand precisely this issue, I am thinking again of the railway tourism development in Tasmania, which is not long haul. I think it is 30 to 40 kilometres, and there are similar types of operations already in existence around Australia. Tourists are not exempt, for example, if they buy the ticket as part of a package from overseas. There is quite an interest in developing that concept of tourism railways; there is significant development in packaging that sort of concept. Do you include that within your definition of an exemption?

Mr Brown—In an international sense, yes. If it is bought as part of a holiday package through a tour operator or a travel agency offshore, it would be included. Unfortunately, it would not be included under the domestic package because we tried to limit the ask within the realms of fiscal possibility. It is included internationally, though.

Senator GIBSON—I would like to follow up on the Bass Strait comment. Isn’t it true that the tax package is offering substantial savings in costs with regard to diesel excise for shipping crossing Bass Strait? My understanding is that, for the *Spirit of Tasmania*, which uses bunker C, the excise will go from about 6c or 7c a litre down to zero, and I think that is about a reduction of $1½ million a year in the costs for running the ship.

Probably more importantly, with the proposal to run one of the big Incats across the strait on a permanent basis, the manufacturer, Incat, estimates that the cost saving by going from an excise of 27c a litre down to zero will save an operator $10 million a year. Won’t that make a significant difference?

Mr Brown—One of the reasons we support the package for tax reform in essence is for some reductions in fuel. We have been fighting diesel fuel excise for passenger shipping for a long time, and we applaud the changes which are going to assist. Your comment is based on a presumption that all those costs will be passed on to the consumer, which I suppose for all of us is a leap of faith in the whole idea or, depending on how you interpret it, an enforceable activity down the track.

At the moment there are advantages in fuel for the shipping lane across Bass Strait but, having said that, we cannot sit back and assume that naturally that will all be passed on to customers and that some of the other tax differences, including the increase in the price of the trip, will lead to a price neutral effect. We have not done those specific numbers.

Senator GIBSON—I just wanted to correct the impression you gave that the total package will be deleterious to Tasmania.

Mr Flowers—I think that is a very big issue, and obviously when we look specifically at the tourism industry we cannot conclude that. We have looked at the tourism sector and what it means for Tasmania. Obviously, if tourists do not go to Tasmania because they do not want to pay up front taxes overseas when they buy packages or, indeed, if they decide that the alternative to going to Tasmania is perhaps going to New Zealand—I think Peter Dixon mentioned yesterday that, in terms of the impact on jobs in tourism in Australia, there is a real threat that New Zealand becomes a much more attractive destination, very affordable—we are concerned that, yes, there certainly will savings from the fuel change on the Tasmanian leg. But the whole cost of the trip consists of much more than the fuel savings, unfortunately, and for that reason we are still quite concerned about the Tasmanian example.

ACTING CHAIR—Did you say that people would not go to Tasmania because of the taxes they would have to pay to get there?

Mr Flowers—No, but it will certainly be an influence. We are not saying that, as a result of the government's proposal, Tasmania will never get another tourist—far from it. We are saying that Tasmanian tourism will suffer as a result of this tax change.

Mr Brown—There are alternative employment sources in Tasmania but, unfortunately, they are not quite as environmentally friendly as tourism. Damming the Gordon by Franklin or logging the south-west forests are alternatives in an employment sense, but I think the whole national debate has moved on, so that we now say, 'Yippee! Hooray! There are dollars in that natural environment. There are not in damming it, flooding it, chopping it down and shipping it out.' We see dollars in letting people enjoy it, look at it and revel in it. We would hate to see Tasmania have to go back to its otherwise more traditional forms of employment.

ACTING CHAIR—When the tax package was first released in August last year, your task force claimed that the jobs impact would be 30,000 jobs. You are quoted in last Sunday's *Sun-Herald* as saying that the impact would be 100,000 jobs.

Mr Brown—We were not quoted, Senator. The *Sun-Herald* made a figure up. It had nothing to do with us.

ACTING CHAIR—In this presentation today, you have talked about 59,000 jobs. I think today you said something about 34,000 jobs.

Mr Brown—That was just domestic. That was part of the 59,000. Last year, we had a gut reaction about what the figure would be. We did the right thing. We went and did the research. We went and paid good hard cash to get the research done—something, I would point out, that Treasury has never bothered to do. We went and did it, and we determined the figure at 59,000 jobs.

Senator SHERRY—Who did the work?

Mr Brown—Decisive Tourism Consulting, with modelling done and with the research methodology checked and approved by the Tasman Institute. The inputs were based on government provided figures of dollar depreciation and the impacts of different components. We had discussions with various eminent economists to work out price elasticity figures, including people such as Geoff Carmody of Access and Professor Dixon.

Mr Flowers—Senator, you have highlighted a difference between our first estimate and the estimate we have included in this much more comprehensive work that we have provided to the Senate today. The key difference is that—and I will take responsibility for this—we did not include in our first estimates the appreciation of the dollar that the Treasury anticipate.

The Treasury, in their PRISMOD modelling, assume an appreciation of the dollar of 3.5 per cent in response to the tax package. The impact of that on tourism, we have found, is that Australian dollar prices for many tourism products will increase as a result of the tax package, and with the inclusion of the appreciation of the dollar, the foreign currency prices increase further. We underestimated the price impact facing foreign tourists as a result of the tax package.

Econtech, in their submission to this committee—that the Treasury included as an appendix to their work—cited a 4.6 per cent appreciation of the dollar rather than 3.5 per cent. Any appreciation of the dollar does two things for tourism. It makes inbound tourism more expensive and makes outbound tourism compared with domestic tourism more attractive. More domestic travellers are going to go overseas as a result of the tax package, and fewer international tourists are going to come to Australia.

ACTING CHAIR—If you are taking notice of part of the Treasury's advice in regard to things like the impact on the dollar, did you also take into account in your estimates the predicted stronger domestic demand and growth effects created by a GST?

Mr Flowers—I appreciate that it is a very difficult technical issue. As I have mentioned, our analysis is specific to the tourism sector, so we took the assumption from the Treasury of the 3.5 per cent appreciation of the dollar. On the issue of how much household disposable income increases, we spoke to Professor Dixon, who said that household disposable income falls under the government's package.

ACTING CHAIR—Did you talk to anybody else but Professor Dixon?

Mr Flowers—We looked at the Treasury. We could not find any figures on that in the Treasury.

ACTING CHAIR—There are other modellers.

Mr Flowers—If the Treasury has a figure, we have not seen it, and we have looked. We would certainly appreciate knowing that from the Treasury because the Econtech modelling that they submitted to this committee was not based on the package. It was based on their best guess of what the package would be.

Mr Brown—I will add to that too. We have been told since day one that Aussies will have another 50 bucks in their pocket, which means an extra bit to put away for the next trip to the Gold Coast with the family. On the current travel patterns, it will either go down the gurgler of a poker machine or it will end up being tucked away for the trip to Bali.

ACTING CHAIR—We cannot do much about the poker machines.

Mr Brown—The travel patterns show Aussies going at breakneck speed to hop on a plane and fly to Bali for a holiday.

ACTING CHAIR—Isn't that happening now?

Mr Brown—I am saying that that is what is already happening. Any increase in disposable income cannot automatically be translated as an offset because Aussies will suddenly rediscover their own nation and spend money at home. They will not. They will either stay home and play the pokies, or hop on a plane and wave at the people of Surfers Paradise as they jet off to Bali.

ACTING CHAIR—So you agree that the package is going to have considerable effect on increasing disposable income for Australians?

Mr Brown—No. I said that, if it does, the current spending patterns would not necessarily translate to an increase in domestic tourism, unfortunately.

Mr Flowers—In the submission they made to the committee, the Econtech modelling showed an increase in gross domestic product of about one per cent. Obviously household disposable income is a very significant share of national income. If you assumed a one per cent growth in household disposable income, you have to have—

Senator CONROY—That is over eight to 10 years. It is a cumulative figure; it is not an annual figure.

ACTING CHAIR—Senator Conroy, perhaps we should let Mr Flowers and the witnesses answer the question. If you wish to answer questions, you should get a chair at the other table.

Mr Flowers—If you made that assumption that there would be a one per cent growth in household disposable income as a result of the package—which we haven't; we have taken a conservative assumption that there is no change and we have not been as negative as Professor Dixon on that issue—the fall in domestic tourism, instead of being 4.4 per cent, would be about 3.4 per cent. It would still be very significant.

Senator O'CHEE—When did you speak to Professor Dixon about this?

Mr Flowers—On the basis that we were doing modelling on the tourism sector—and we have some minor differences with Professor Dixon on his tourism analysis—I was interested in discovering, after seeing the December paper, that there was an economic modelling conference in which Professor Dixon identified the fall in sectors such as hotels. He made the point that the worst affected industries in Australia are those with close links to either domestic or inbound tourism or both. We were obviously interested in finding out how he did his analysis.

One of the issues we wanted to consider was the impact on household disposable income. We have the very nice scenarios at the back of the new tax package documentation, but that really does not give us an aggregate figure. If the Treasury has an aggregate figure, we would be very happy to include it in our modelling.

Senator O'CHEE—But yesterday, when asked about this issue of disposable income, Professor Dixon said that the reason why the package was stimulatory for the economy was that there was an increase in real household spending power. They were his words. You are saying to me today that he disagreed with that. He was given the opportunity. He stated very clearly that there was an increase—

Senator CONROY—That is not correct, Senator. Don't verbal Professor Dixon. That is not what he said.

ACTING CHAIR—Order! Senator Conroy.

Mr Flowers—I cannot answer with the professional competence of Professor Dixon. That is an issue between Professor Dixon, the Econtech modelling and the Treasury.

Senator O'CHEE—You were relying on a statement where you said that Professor Dixon had argued that there would be a fall.

Mr Flowers—As you will see in our submission, we did not rely on that in the modelling that we did. If we had, the fall in domestic tourism would have been greater. We took a conservative view that there would be no change in household disposable income. If Treasury can provide a figure that is different, we will gladly use it in our modelling.

Senator O'CHEE—But Professor Dixon says that it is stimulatory because household disposable income rises.

Mr Brown—My point originally was that there is no evidence to show that any increase in the state of the national economy—dollars in people's pockets—has any bearing on an increase in domestic tourism. In fact, the evidence shows the more money people have at their disposal the more inclined they are to take a holiday overseas.

Senator O'CHEE—Because you keep them all poor.

Mr Brown—As an overall, let us say, 'There is our document. We went and did the modelling. We are the only ones who have done it. We will put mine there. We will put the Treasury one next to it and we will compare them. Oh, no! The Treasury did not bother doing any.' That Treasury could not be bothered doing modelling on the job impact on tourism is an insult to the Senate, it is an insult to this committee, it is an insult to this industry and it is an insult to a million Australians who currently have a job in this industry. Either that or—and I am not one for conspiracy theories—they have done it. They know what it looks like and they are not going to publish it. The modelling should have been done. Our taxes are paying their incomes to protect and promote this economy. How dare they not do the modelling? How dare they not take the time and effort to sit down, get out the abacus and work out what a fundamental shift in the Australian tax system it is going to have and the impact it will have on two-thirds of the Australian work force?

Senator SHERRY—Tasmanians understood that at the last election.

Mr Brown—As I say, we would throw all that aside. If they can produce theirs, then you can put mine in the bin and we will work on Treasury numbers. I would quite happily work on Treasury numbers, but there are not any.

Senator FERGUSON—So the only numbers you used are those of Mr Flowers?

Mr Brown—The numbers we are using are from a modelling done by Mr Flowers, with the methodology checked by the Tasman Institute in consultation with a range of economists, including Professor Dixon, using some of the statistics we can get out of the Treasury package as the basis options. Not only is it the only modelling that we have, it is the only modelling the country has. I think that is bad for the country and I am happy to admit it.

Senator FERGUSON—Especially if there is only one model. I want to continue on with another point of Senator Sherry's because he talks about the impact of this package on Tasmania. We heard figures from Professor Dixon yesterday about the number of people who buy packages overseas and the percentage of inbound tourists, which includes people coming on business or any other matter at all, coming into Australia. I presume that somewhere in your figures you have the numbers of people who visit Tasmania and who actually buy packages overseas, percentage wise?

Mr Flowers—We would gladly take that question on notice. It is obviously a question for the Bureau of Tourism and Research. They conduct the international visitor survey. We are happy to provide the answer to that question, because in fact it is not published data. Their annual publication is the *International Visitor Survey*. It is a couple of years old, unfortunately, and that is the most current one. The data that you have asked for would be a separate data run, using their cross tabulation package, but we can certainly provide it.

Senator FERGUSON—I know that, in the case of South Australia, approximately two in every 100 international visitors visit South Australia. Of those two, only a small percentage buy packages anyway. I would suggest that for Tasmania it might not be much higher.

Mr Brown—So the answer to your question would be ‘not enough’ and ‘even less’. It is not enough currently and even less if the package gets through.

Senator FERGUSON—So it is not going to have a tremendous impact because, if it drops by the amount that you talk of—

Mr Brown—The impact it will have will hurt the opportunities given for groups like Tourism Tasmania and the government to better promote, which they are now doing. They are in the main game of trying to promote Tasmania more to the international customer. No matter what the impact is, it will all be negative. There is no positive benefit to the Tasmanian tourism industry if you do not zero rate international packages and if you do not provide the domestic regional assistance.

Mr Flowers—Just to clarify it, Senator, I am afraid you are being a bit harsh on the South Australian tourist industry.

Senator FERGUSON—The figures I have may have been from a year or two ago.

Mr Flowers—They receive, according to the data I have before me, seven per cent of international visitors.

Senator FERGUSON—Seven in every 100.

Mr Flowers—It is still not the figure they would like, but it is certainly a lot higher than two.

Senator FERGUSON—If one in six people buys a tourism package overseas, that is one person in every 100.

Mr Flowers—One in three international tourists. About 38 per cent buy packages.

Senator FERGUSON—They are not the figures that Professor Dixon gave us yesterday.

Mr Flowers—Professor Dixon was talking in terms of expenditure on the actual package rather than the total expenditure by those package tourists. It is quite a critical point. Although we would like to, we are not proposing that the whole of the expenditure by package tourists be GST free, only the component—which is the component on the package element—other than the airfare, which is currently proposed to be taxed.

Mr Brown—There is a point worth making there too. Of those current buyers of packaged holidays, the major growth sector for Australian tourism for the next 10 years, as projected by the Tourism Forecasting Council—the government body of which I am a member—is a much stronger reliance upon Asia, which is the package holiday capital of the world. The Asians come on packaged holidays. When they get their house back in order, that is the growth market for Australian tourism. It has an exponential negative impact if you do not zero rate inbound packages.

Senator FERGUSON—The reason I asked the question about employment is that I am wondering how you, as a tourism task force, can come up with employment impacts, when 19 other industry associations, including many from the tourism industry, claim that it is too difficult to estimate. I have one in front of me by Morgan that says that the tax package adds 220,000 jobs to the tourist industry, so there are a number of—

Mr Brown—What names are on top of that paper?

Senator FERGUSON—I can show you later. It is Morgan's economic strategy paper.

Mr Brown—Are they the stockbrokers, Senator?

Senator FERGUSON—I am not sure if they are stockbrokers, but I can give you the paper afterwards. Let me tell you that there already are a number of modellers—

Senator FERGUSON—There are a number of estimates. The reason those 19 other industry associations say that it is too difficult to estimate is that the data is not necessarily reliable in the first place. Mr Flowers, I understand that you are employed by the Tourism Task Force to do this work, but I would think—

Senator CONROY—He was employed by the Liberal Party.

CHAIR—Proceed, Senator Ferguson.

Senator FERGUSON—I would like to, but if you could get Senator Conroy to restrain himself a little more often, we might get further. When different estimates come up and different impacts are estimated by a variety of people, including yourself, who claim to have some expertise, it is difficult to estimate the impact.

Mr Flowers—I appreciate your question. The fact that 19 other industries have not done the employment modelling perhaps shows that they are less threatened by the package. In addition, we are very happy to put our analysis against that of Morgan's and, as Mr Brown has mentioned, against the modelling that we would like to see from Treasury.

One thing that should be said with our modelling is that, given that we used a different method from Professor Dixon from what Econtech provided for the Treasury and through the Treasury to this committee, our estimates are very much in the same surprisingly small ballpark as the estimates of Professor Dixon and the estimates of the model that the Treasury used in their Econtech analysis.

Our estimates for the impact, say, on the hotel tourist accommodation sector, which is a good indicator, is a 5.8 per cent fall in employment. Professor Dixon said it would be over five per cent in his central scenario. Econtech came up with the figure of 4.6 per cent in the accommodation sector, as one of their 303 industries. Of course, Econtech did not use the correct package that the government subsequently finalised and, as a result, the differences between our aggregate or overall impact are surprisingly small. We have a fairly small disagreement. It is a central conclusion of both Professor Dixon and of Econtech, looking through its analysis, that anything to do with the tourism sector suffers under this package.

Senator MURRAY—I want to return to the excise matter, if I may. The government's tax package includes significant cuts in the cost of diesel excise. That will translate into benefits for the tourism industry for any vehicle that uses diesel—buses, boats and ships—for supply of products. We can see the benefit of that. But in this vast country, which was one of the motivations for the government attending to the problem on diesel, aviation matters a great deal—to the Northern Territory for domestic tourism, to Tasmania for domestic tourism, to north-western Australia for domestic tourism and to Northern Queensland. One of the great impediments to the growth of domestic tourism is the high cost of air travel, and we know there are competition elements which affect that. In your view, do you think the government should have extended the principle of lowering transport costs via fuel reductions to aviation? Have you done any work which would put a cost element to that? Have you made any suggestions to government on that basis?

Mr Brown—The aviation industry has made representations to us about the cost impact on domestic airfares because of the tax package. I believe there have been discussions between the industry and Treasury. Basically, there has been a quiet acceptance by Treasury that the cost impact would be much higher than that originally projected. We think it will have a seven per cent to eight per cent impact on domestic airfares. In a perfect world, we would be having a greater tax reduction also on the cost of aviation via avgas and fuel charges.

I also do recognise and congratulate the moves that have been made on some of the fuel tax arrangements for land transport and to some extent sea transport. As I mentioned before, they have been much greater for road than they have been for rail, which is a pity. Rail continues to be treated as a second-class citizen in a transport sense by Treasury and the tax office. I am sorry we have not done more specific work on the aviation sector. We have tried to limit ourselves. In an industry like tourism which is effectively made up of about 15 different specific industries within our resources, because we had to do all the work that Treasury would not do, we could not put our resources into all the areas that we would have liked. I think there should be more work done on the cost of tax on aviation fuel because you are right: the largest single influence on travel and impact on the price of travel within Australia and to Australia is the airfare component. In fact, the figures out from ABS last week show the December quarter cost of travel within Australia is actually up six per cent and the cost of international travel out of Australia is down 1.4 per cent. That is largely influenced by the reducing price of outbound airfares and the increasing price of domestic airfares.

Mr Flowers—The other thing that perhaps should be added to that, Senator, is that fuel prices are currently very low and, as you are aware, are a surprisingly small component of the cost of airlines. I do not want this quoted, but I seem to remember it was 15 to 20 per cent of the total costs. So the impact of the GST on demand on long haul airfares we think is going to be larger than any conceivable fuel excise reduction. We can perhaps look into that question with some of our airline members for you.

Senator MURRAY—I put the question to you because the rail people indicated to the committee that $85 million would fix their problem, as they perceive it, with fuel. If it is the intention of the government to lower fuel costs for commercial use of diesel, then I just wondered why the principle was not extended to air travel, particularly when it impacts so heavily on the major industries.

Mr Brown—When it comes to principles of tax equity we are experts at it in tourism. We have never had equity and this package does not give us equity. It does not give equity for rail compared with road, it does not give equity with land transport compared with air and it does not give equity with regard to the treatment of avgas. Most importantly, it does not give equity that every other exporter will get in terms of zero rating. We have a thousand chips on our shoulder but we can only address so many at one time. We are happy now that we have Treasury's responsibility out of the way and done their work for them. We are now happy to go back, hopefully before you finish your deliberations, and possibly provide more information. I think also the Australian Air Transport Association will have addressed the situation.

Senator MURRAY—I want to see if you have another chip on your shoulder. We have had a series of business organisations before us so far and there are many more to come. Maybe I have missed it somewhere, but most of those business organisations are very voluble about the principles of taxation and will proclaim at length on whether education and health should be GST free or whether food or anything else should be GST free. One of the principal arguments in supporting the package is that it supports our export industries and makes us more competitive internationally. You would expect that principle to be applied across all sectors. I have not heard one major business organisation such as ACCI, BCA or tax accountants' organisations which have 87,000 members, one of which I presume represents many of your members as well, be voluble about the fact that you people have been hung out to dry.

Mr Brown—It is a lonely old industry I have to tell you.

Senator MURRAY—As a principle I would have thought that if you support export industries your example is a very obvious anomaly, plus a price tag has been put to it by Professor Dixon—which maybe you will comment on later—which does not seem to indicate that to correct it would be that vast in the realm of government. Why are you so lonely? Why do business organisations not speak out about it? Why do they leave you out to dry when you are the biggest and most important industry in the country?

Mr Brown—I wish I had written it; it is a great question. As a matter of interest, I trawled the Business Council of Australia library not too long ago. In five or six years worth of articles, there is yet one to appear on tourism. We are the biggest industry in the country with 15 of their 100 members also our members—tourism members. Not one article about the largest employer and the largest exporter.

They are not the only guilty party, though. We made a conscious decision in the task force not to become involved in the national business tax coalition because we recognised that many of the outcomes of this tax package will be supported by a wider group. When you say business in Australia, you really mean manufacturing and, to some extent, mining and agriculture shoved on the side. Not only tourism but a lot of the others in the services sector, such as education, suffer the same fate as we do. The two new darlings of export growth are the two lonely children of the Australian economy. Governments are pretty famous for doing it as well. As I said, it is not only business that tends to treat us as a poor, if somewhat large, relative.

As to why they have not come running to our aid, I have not given it much thought beyond that. I am sort of used to it. It is part of an ignorance. It is part of being a new industry; it is part of being only, effectively, 15 years old in this country. We are chipping away. We are making some inroads. We are the first cab off the rank this morning in Sydney to give evidence to the inquiry. Maybe this committee is leading the way and dragging us into the mainstream. But just the same way that the tax package neglects us, in a lot of ways business has.

Most importantly, young kids are not neglecting us. It is the largest, single trade education base in Australia at the moment. People are learning and they are dying to get a career in this industry; we for one do not want to dash their hopes. A lot of those kids are in the bush where, as I said before, there is not much hope for them. That is why the stakes are raised for us and why we have to run our own argument—because we did not do the deal with the devil. We did not hop into bed with manufacturing because a lot of what we are looking for would be in conflict.

We are even abandoned on payroll tax. You would have thought the nation's largest employers would be pushing hard for payroll tax cuts. Apparently, it was not part of the deal they did. They spent all their money advertising the tax package before it was even tabled. We were not part of that and maybe it is retribution.

Mr Flowers—Senator, just on the question of tax principles, one of the fundamental tax principles you learn in taxation policy is that, if you apply a tax to a product or service that is very price sensitive, you can get less tax as a result of increasing tax rates.

Perhaps the most price sensitive of our export industries—and I would welcome your questions on price elasticity, because it is a very important point—is the package tour market. Professor Dixon saw no difference in his price elasticity between the package tour market and the general tourist market—the much larger total tourism export industry. We think that is wrong. We think that, by imposing taxes on very price sensitive sectors, the government is going to lose out in a lot of revenue that tourists provide when they visit Australia and spend.

Senator MURRAY—I am not going to pursue you on the price elasticity point for this reason: Professor Dixon made it clear that his price elasticity judgments for tourism are judgments. As you know, some price elasticity comments by modellers are based on empirical fact. They have researched the actual elasticity that if you make certain cost adjustment it has a certain consequence in demand. They have not got that available research in your industry. I do not know if you have, but he certainly did not have it.

Mr Brown—One thing I can guarantee you is that there is a much greater price elasticity for package tourists than there are for what we call FIT—fully independent tourists.

Senator FERGUSON—What do you base that on?

Mr Brown—It is based on the fact that a large part of their decision is directed by a tour wholesaler, particularly in Japan, which is the main source of package tourists to Australia. There is much less discretion, say, on behalf of the traveller as to where they are going. It is much more a bulk travel market, price driven, a cultural trend which allows for group touring rather than individual touring, particularly based on language and cultural differences. So that has always had a greater sensitivity. I do not think it is a huge leap of faith for people to follow that argument that there is always going to be a greater sensitivity in a bulk market. The more money in your pocket, the more discretionary income, the less the price will have an impact, and much more in a package market.

Senator FERGUSON—The department of tourism has supplied average elasticities from all these countries overseas which are considerably less than Professor Dixon's—

Mr Flowers—Bunkum, I think we would say to that.

Senator FERGUSON—You are allowed to, but I am just saying what the department says. You are an employee of the Tourism Task Force.

Senator CONROY—You are interrupting.

CHAIR—Order! The call is with Senator Murray, but I think Senator Murray has allowed the interjection and until he pulls me up, I will allow the question.

Mr Brown—Maybe the Democrats like tourism. We do not always get treated with the respect we deserve, Senator Murray.

Senator MURRAY—I think I will return to my question.

Mr Hill—I would like to respond to Senator Murray's comment about, I suppose, the Tourism Task Force being seen to be a lone voice compared to the business community in Australia. One of the possible reasons for that is GST is not a tax on business. It is a tax on the final consumer. In that respect, GST is a very positive move in the form of tax reform for business generally.

What the Tourism Task Force is looking at is the impact of GST on the purchasers of tourism and not on the tourism sector itself, because the tourism sector will not pay GST. But GST will indirectly impact if tourist demand falls as a result.

All of the recommendations that the Tourism Task Force have made have been made with the conscious move towards keeping the compliance cost of the request for GST-free status to a minimum. There is not a high compliance cost in treating long haul domestic airfares as GST free. All the airlines operating in Australia currently have systems in place that will identify GST-free status for any designated airfare. A GST-free treatment for packages purchased overseas does not pose any compliance difficulty for business. We believe that the reforms here are both pro-business and supportive of the overall move by the Tourism Task Force to try to get a good deal for tourism, particularly the inbound package market.

CHAIR—How are you going with this one?

Senator MURRAY—I was trying to move on. I think you have misunderstood, Mr Hill. The point I was making was that businesses talk about the principles of having broad based consumption tax. They talk about the principles of export competitiveness. If one industry is left out of the principles of export competitiveness, that is why I consider you to be lonely and I do not understand why they have not raised that point.

Mr Brown—And why I would consider them to be unprincipled.

Senator MURRAY—Yes. Let us not pursue it, otherwise we will involve too much time. The other point I want to pursue with you is this. Economists and governments of any flavour fear surges in wage demands because the consequence of that is to increase costs, the consequence of increasing costs is to lower demand—a straightforward relationship.

However one looks at this package, the overall consequence is a cost increase for the tourism industry. When a cost increase for the tourism industry was not only proposed but imposed in New South Wales, quite frankly, you raised the rooftops. In contrast to the government’s package, the reaction of your industry and all services industries which are essentially seeing their taxation levels lift as an adjustment is made in society has been relatively muted. Is that because of your judgment, that although this is bad for your industry, it is good for Australia?

Mr Brown—Looking at it from the other direction, in the exalted response from New South Wales, which we were at the forefront of in regard to the bed tax, I think a lot of the passion and anger was driven by two factors. One was the discriminatory nature of it; it was only a GST on hotel accommodation. It was not on everything else, so there was absolutely no parity with other industries.

Added to that, it was really the first battlefront, the first state that bothered to hop in and try it. And I suppose we became the first theatre of war. Effectively, the message was not only to Premier Carr, it was to Premiers Kennett, Borbidge and everybody else—‘You try to bring it on and we will bring a blue on in your town also.’

Having said that, I have been personally amazed by some parts of the industry that say, ‘At least we get rid of the Sydney bed tax if the GST comes in.’ It is a strange argument. As someone who has been involved in politics as long as I have, I find that a very strange argument, but it does go to show also some of the consolidation of investment in the Sydney hotel market. Mostly everybody has an exposure there and it was leading to people doing alternative holidays, either outside the Sydney CBD or to other states and other cities. I suppose in explaining the lack of obvious moral outrage about this package, part of it is what is seen to be in the national good.

This is an industry that touches so many different components. We are not all digging up coal. Tourism is in every industry. We are part of the computer industry. We are part of the construction industry. We are part of the food industry, retailing industry and manufacturing industry. Plenty of others, the real winners out of this package—manufacturing, mining and agricultural communities—touch across tourism. What you saw with the Sydney bed tax was the accommodation division, which was probably more obvious.

Senator MURRAY—The overall conclusion of your submission is that the consequence of this package is that costs will go up and jobs and business will go down, yet you support the package. I presume you do that because you believe that, overall, the package, despite the fact that it hurts your industry, is good for Australia.

Mr Brown—We support the concept of tax reform. We do not support the package in its current form because of its deleterious impact on tourism. If you change this and give us the zero rating that we deserve and demand, give us protection for the ravages in employment in the bush, particularly, and supplement some transitional marketing assistance, then it will become much better.

In a perfect world, if we got everything we wanted, while it is not an ambit—we deliberately tried to keep the ambit out of it—if Treasury, the Democrats, Senator Colston and Senator Harradine put up their hands to say that they will humanise this and protect tourism, it would still cost about 20,000 or 30,000 jobs. No matter what we do, or no matter what we offer here, it is still going to hurt this industry and the people employed in it significantly.

Our hope is that all these wonderful winners out there that have abandoned us in the manufacturing sector are going to retrain everybody as fitters and turners. They had better get the TAFEs ready because we have a whole lot of chefs, barmen and other people in this industry who will be looking for another job. In Sydney and Melbourne they will probably get it, but in tropical North Queensland, south-west Tasmania, northern Western Australia and the Northern Territory, we had better take the tax off the long haul transport because they are all going to be coming down to Sydney to try to find a job in the manufacturing sector, a sector which over time is shedding labour.

The wonderful thing about tourism is that they have never invented a computer to make beds or smile at people. It is a wonderfully labour intensive industry—the greatest contributor that would help Peter Costello. There are two great comments he can make: one, come out of the republican closet and, two, get unemployment down to five per cent. We want to help that. It is almost with some amazement, or naivety even, that we ask: why would you be going after the only industry with a hope to help you solve the current account, the only industry with a hope to help you with regional development and the only industry with a real genuine hope to slash unemployment rates? By the way, it is also the only industry that is not going to get zero rating, and it is the only industry that is most going to be affected in its domestic consumption by a tax being applied.

I have been in politics a while, and I am still in amazement that otherwise sensible people who fill the halls of Treasury in Canberra would still be proposing a package like this. I hope it is only bravado and that they are playing tough and they are going to roll over and let you make the changes that are required.

CHAIR—Order! As loath as I am to stop this colourful stream of consciousness and evidence, we are running up against time limits. How are you with your questions?

Senator MURRAY—I had one more, but we are probably talked out.

Mr Brown—We are happy to answer it for you out of proceedings, if you wish.

CHAIR—We reserve the right, subject to your cooperation, to put questions on notice and ask you to get back to us with the answers, if you may. I understand Senator Conroy has not had the call and he has a question.

Senator CONROY—I wanted to briefly ask whether you had received a copy of a report commissioned by the Department of Tourism. They commissioned ACIL to actually look at the impact of the GST on the tourism industry. A government department has stated in one of its annual reports that it has commissioned some work. Are you aware of it at all? Has it turned up?

Mr Flowers—No, we have not seen a copy of that. We would be very interested to do so. However, we would be concerned that Professor Dixon referred in his report to departmental officials arguing that the price elasticity of demand overseas for Australian tourism is low. In 1989, the Industry Assistance Commission completely debunked that myth. The evidence on price elasticity is basically technically incompetent.

Senator CONROY—I was going to come to that. You might want to expand.

Mr Brown—On the question of the report, no, we have not seen the report. As I said before, we are used to not getting reports, which might have been done or might not have been done, which show the impact of tax on tourism. We would love to see it. We will take it up with the minister to see whether it is available. I am fully confident that, if it is there, we will receive it.

Senator CONROY—I am sure the government will continue to cooperate with this committee and provide it as well. Much hangs in the debate about making tourism packages GST free on the price elasticity of demand, which you were referring to before. Professor Dixon assumed a price elasticity of three in its base. Is this a fair assumption?

Mr Flowers—I think, overall, it is. There are a number of ways you can understand this, as a practical person. The modelling that has been done is based on visitor arrivals: how many people will come to Australia when our prices change? That is not so much the relevant issue; it is how much they will spend here. They may well still come, but they are going to change their rate of spending on a per day basis and their length of stay.

In the first six months of 1998 we found that we had a lot more visitors from the UK. In fact, we had an increase of 18 per cent in the first six months of 1998 compared with the same period in 1997. They actually spent 32 per cent more. That is official data. It highlights, as you will recall, that the Australian dollar was taking a hammering in that period.

It is a very good test in that when you model things against visitor arrivals you do not really learn much that is of use to your committee. Your committee is about price elasticity; it is about how much is spent in Australia. Visitor arrivals and the existing modelling that the departmental officials used has that problem. It also has major problems that the Industry Assistance Commission highlighted where there is massive mis-specification of their models. They do not include all the substitutes. Professor Dixon talked about this yesterday. We go into considerable length in our submission talking about price elasticities.

The key issue—and this is critical—is that your committee presumably is not going to recommend that all tourism exports be GST free. Tourists are not going to be flashing passports and getting 10 per cent off. The decisive issue is: what is the impact on tour packages of making the other components and airfare GST free? We know the package tourists are remarkably price sensitive. We know that because they choose to come by package. They elect to get a lower price—you can get a much lower price by taking a package. As well, in choosing a destination, compared with coal or wheat or wool, a customer overseas might not be choosing from 10 alternative suppliers; they are choosing from over 200 countries.

We know as well that they choose destinations, particularly as package tourists, by going up to a travel agent’s window and looking at the prices—seven nights in X, 14 nights in Y. Customers are very sensitive about the travel agent’s window. They are very sensitive about what we normally see as multicountry brochures. Australia will be four or five pages out of 35 pages in a brochure by Thomas Cook or someone in the UK, for example. So they are price sensitive. They have a lot of choices.

I think you will learn more about this tomorrow from the Inbound Tourism Organisation of Australia, which represent the tour wholesalers. Tour wholesalers themselves add a further element to price sensitivity because they get to choose how many pages in their brochures and how much marketing support they give to travel agents to push Australia. If Australia becomes less profitable, if they think fewer people are going to come to Australia, they will reduce their marketing support; they will reduce the number of pages. We know that package tourists are very price sensitive.

Professor Dixon, in his analysis, has assumed an average of three price elasticities and used that for calculating the benefits of making tour packages GST free. Those benefits are significant in terms of his overall economic impacts. He has underestimated it because he has not separately identified tour packages.

Senator CONROY—If I could just save Senator Ferguson the trouble of interjecting, there was a legitimate argument yesterday that some studies in the past have used 0.2 to 1 as in elasticity?

Senator FERGUSON—And negative three.

Senator CONROY—I was just wondering whether you might want to comment on any of those elasticities that have been used or whether they are appropriate or not.

Mr Flowers—Basically, they are rubbish, and they should not be used for this purpose. You will have the opportunity to talk to Geoff Carmody from Access Economics tomorrow, who is representing one of the other organisations. I spoke to Geoff when we were looking at setting our own price elasticity. Geoff, in Access Economics, has done a lot of work in the tourism sector, and I think would probably be the Australian expert on that issue. So take that up with him.

Senator CONROY—I look forward to his testimony tomorrow.

Senator FERGUSON—You quote Professor Dixon at length—

CHAIR—Order! We are over time now. If I take any more questions, we will not have morning tea. I am perfectly relaxed about that.

Senator FERGUSON—It is important to clarify—

CHAIR—You are all entitled to your questions.

Senator MURRAY—Put them on notice.

Senator FERGUSON—I want to clarify one thing. You quoted Professor Dixon and the findings of his report at length this morning. Have you had a chance to have a look at his report in detail?

Mr Flowers—No, Senator. Obviously we got a copy yesterday afternoon. We think that his estimate on the cost of making other elements of tour packages GST free is a gross overestimate. That $300 million is an overestimate by at least two to three times of the real cost to the revenue of making the other elements of the packages GST free. We would very much welcome the opportunity. He has basically assumed that the airfares that packaged tourists pay average $700. Unfortunately, that is not the case because so many come from Japan.

Senator FERGUSON—It is just that we have questioned some of the assumptions, and it seems as though you are also questioning some of the assumptions.

Mr Flowers—No, far from it. We think his analysis in terms of the package tour has underestimated the benefits to the economy of making the other elements of tour packages GST free and he has overestimated the cost to the revenue.

Senator FERGUSON—That is what you said. You said that he has used the wrong assumptions.

Mr Flowers—No, Senator. Obviously he had a very big job from this committee.

CHAIR—It is too soft. Is that what you are saying?

Mr Flowers—Yes.

Mr Brown—He underestimated the price elasticity and overestimated the cost to revenue—a double whammy.

Senator FERGUSON—We are questioning some other assumptions. You are questioning the basis of some of his assumptions, too.

Mr Brown—We would probably question different assumptions.

Senator FERGUSON—Yes, I am sure we would.

Senator MURRAY—My question on notice was exactly that. Could you provide the committee with your estimation of price elasticities of the cost of inbound packages to be used in the assumptions that have been made and your view as to the total cost to revenue if your sector was to be made GST free on inbound tourism packages?

Mr Flowers—Yes, we will certainly provide that to you. If three per cent fewer tourists come here, as Professor Dixon said in his central scenario, because of the GST applying to the other package elements, that will obviously have a very significant impact in terms of the other taxes that those tourists will pay. He made no adjustment for that in his calculation of $300 million.

CHAIR—The implication of that statement is that, if he had, he would have come out with a harder conclusion about the damage the package would have done, not a softer conclusion.

Mr Brown—I think that is a fair assumption.

Proceedings suspended from 10.17 a.m. to 10.30 a.m.

CARMODY, Mr Geoffrey Francis, Consultant, Australian Food and Grocery Council

HOOKE, Mr Mitchell Harry, Executive Director and Chief Executive Officer, Australian Food and Grocery Council

CHAIR—I welcome the Food and Grocery Council of Australia to the hearing—in particular, Mitch and Mr Geoff Carmody. I think you know the format. We invite you, if you wish, to make a short presentation summarising the main points of your own submission before the inquiry and then, if you would, make yourself available for what has proven inevitably to be questions from the committee on what you have got to say. For the *Hansard* record, Senator Sherry will not appear in this section of the hearing. Senator George Campbell will replace him. We now do have a quorum, and you may proceed.

Mr Hooke—By way of introduction, I am the Executive Director and Chief Executive Officer of the Australian Food and Grocery Council and Mr Geoffrey Carmody is a Director of Access Economics and a consultant on economic matters to the Australian Food and Grocery Council. We appear on behalf of that council, formerly the Australian Food Council, the peak national representative organisation of the Australian processed food, non-alcoholic beverages and grocery products industry.

Mr Chairman, as you, Senator Murray and Senator Gibson, in particular, would appreciate, the Australian Food Council became operational in June 1995, established as the peak organisation for the processed food and beverages industry. It is Australia's largest manufacturing industry, employing one in five of the manufacturing work force, with gross turnover in the order of $43 billion and exports running at about $11 billion, having grown by $5 billion—growth of some 155 per cent, about 11 per cent compound, in the eight years to 1996-97. Quite simply, it is an industry of some magnitude, an industry that makes a significant contribution to the economic and social welfare of all Australians.

On 1 January 1999—that is, this year—the new organisation, the Australian Food and Grocery Council became operational. It is a product of the merger between the Australian Food Council and the Grocery Manufacturers of Australia, which is now in the process of liquidation. The Australian Food Council's former membership represents about 80 per cent of the gross dollar value of the sector. The merger will not only increase that representative base, but will now cover suppliers of grocery products into the market.

As indicated in our submission, which I am sure you have, our representations on taxation for this inquiry, at this stage, will be confined to matters relating to the food and beverage products industry. Furthermore, as I indicated in our stage 1 submission, we have accepted the invitation to appear before the inquiry at this stage to address matters relating to the stage 1 terms of reference and particularly in relation to the research and modelling work commissioned of Access Economics by the then Australian Food Council as a basis for determining our policy on taxation reform. We have accepted your invitation to appear again before this committee on 16 March to address our stage 2 submission, which details a reconciliation of our policies with the government's package and addresses arguments in more detail about the inclusion of all foods in the base of a comprehensive goods and services tax.

I hope that the committee is impressed by the extent of the research and modelling work done by us as an industry organisation. It is indicative of the seriousness with which this industry has taken its responsibilities in this tax reform equation. Not to put too fine a point on it, few, least of all us, are oblivious to the significance of the food industry's position in the tax reform debate. Given its prominence in previous debates, particularly in the context of the Fightback package of proposed reforms, if history is any indication food was always going to figure prominently in any consideration of the adequacy of compensation to the poor and socially disadvantaged and in any arguments about the moralities of taxing the 'necessities of life'.

Equally, we are cognisant that any special plea for sectional interests that cannot be justified on economic or social grounds would ultimately only serve to undermine the integrity of any package of comprehensive taxation reforms. To do so would mean that Australians would be bound to repeat the failures of reform attempts of the past. There is simply no desire on our part to support a piecemeal approach to the reform of Australia's taxation system. Few dispute that the system is in dire need of reform; the argument is more about how it should be reformed. The case for comprehensive reform is compelling and has been made by both coalition and Labor governments.

Australia's tax system is antiquated, complex and inequitable. It puts the country and its businesses at an economic and social disadvantage. It fails the test of good taxation design principles and will not sustain Australians and the economy into the next millennium. I do not know of anybody who is not dismayed by the following features of our current system. Firstly, there is unsustainable and unfair personal income tax bracket creep to the point where high effective rates apply to many low to medium income households. Secondly, the taxation-social security interface is such that it forms a major disincentive to move from the welfare system to low wage jobs; it equates to a nation choosing high unemployment. Thirdly, the indirect tax system violates the principles of horizontal equity. It discriminates against manufacturing to the relative advantage of the services sector. It discriminates within the food manufacturing sector to the competitive disadvantage of value adding through industrial transformation. It taxes business inputs and exports. All of this significantly undermines our international competitiveness in an increasingly globalised economy. Fourthly, it promotes tax avoidance by virtue of the differential treatment of commercial activities and individuals.

Our work and our policy determinations on tax reform have been considered within the context of the broader socioeconomic objectives of tax reform and our support for fundamental reform. However, to be blunt, even at the risk of being perceived as mercenary, altruism is a fine objective provided one does not have to pay too high a price for it. The processed food and beverage products industry had to be absolutely sure that within the context of those broader socioeconomic imperatives our industry's primary interests in tax reform were accommodated—in particular, replacing the inefficient indirect taxes with more efficient indirect tax such that the taxation system was neutral in terms of its effect on resource allocation, food choices and competitiveness within and between industry sectors and internationally.

To do this it is imperative that: firstly, reform of the indirect tax system include significant offsets to business costs with the removal of existing inefficient indirect taxes, notably wholesale sales tax and payroll tax, to temper the one-off price impact of the introduction of a broad based GST; secondly, taxes on business inputs and exports are removed and new taxes apply equally to imports to significantly improve the industry's international competitiveness; and, thirdly, there is direct tax reform that delivers real improvements in disposable income and thus real increases in purchasing power of consumers, obviously for our products. Again, to achieve this requires that there is no tax mix switch using indirect taxes to fund direct tax cuts.

I am sure this select committee appreciates the basis of our industry's reform objectives, given that the current taxation treatment of processed food and non-alcoholic beverage products is a joke. All processed food and beverage products are subject to a large number of indirect taxes, but there are wide disparities between the net indirect tax burdens on different food product categories. Australian food products as a category are directly exposed to a limited extent to the wholesale sales tax but those that are are subject to double digit WST rates as well as bearing indirect tax burdens on inputs. Many food products are not directly subject to WST, but the WST burden falls on them indirectly via the taxation of inputs.

We also bear inflated costs through other indirect taxes, notably payroll tax, petroleum product excise and some of the state transaction duties, particularly FIDs and BADs—financial institutions duty and bank accounts debit. Payroll tax is a highly distorting, discriminatory tax and it causes similar problems to those caused by the wholesale sales tax. It is narrowly applied, selective and levied at different rates. It is a value added tax on labour, an additional cost in our businesses and a tax on exports.

There is little, if any, rationale for the complex, arbitrary and highly non-uniform or selective treatment of food and beverages under the wholesale sales tax. For the record, let me put a few examples on the table. Tea, coffee and cocoa are exempt from WST except when marketed in a ready to drink form. Milk products are wholesale sales tax exempt except flavoured milks, which attract a wholesale sales tax of 12 per cent or 22 per cent, depending on whether the milk content is more than or less than 90 per cent. Flavoured milk made in the home is exempt, of course. Concentrates for making drinks attract 12 per cent or 22 per cent WST, while soft drinks consisting wholly of fruit or vegetable juices attract 12 per cent and other drinks are 22 per cent.

Biscuits attract 12 per cent, unless they are manufactured and sold from retail premises or vehicles. Breakfast cereals, biscuits, rusk or crispbreads also attract 12 per cent. Confectionery and savoury snacks attract 12 per cent, but definitions throw up anomalies. For example, confectionery includes confectionery lines and confectionery ingredients, including crystallised or glace fruit, but excludes candied peel. Ice-cream goods attract 12 per cent except when manufactured in and sold from retail premises or vehicles. The list goes on. Accordingly, our modelling research work sought to determine the differential price effects on industry product categories across two possible indirect tax reform scenarios and the distribution impacts of zero rating food, albeit with a compensating increase in the GST rate to maintain revenue neutrality.

Before I ask Mr Geoff Carmody, who undertook our modelling research work, to briefly explain the process and its comparison with the modelling work of Treasury, pursuant to stage 1 of the terms of reference of this inquiry, there are a few key conclusions or take home messages from that work. We modelled a reform package of 10 per cent GST, the abolition of the wholesale sales tax, payroll tax, FIDs and BADs and a reduction in petroleum excise to price neutrality. That would, on our assumptions, generate an average increase of 3.3 per cent relative to an all industry average of one per cent in the prices of food and beverage products on the domestic market.

It resulted in the largest price increases of three per cent and six per cent for those products not currently directly subject to wholesale sales tax, including meat products, dairy products, fruit and vegetable products, oils and fats, flour and cereal foods and bakery products. It would result in a price decrease in the range from just under 0.5 per cent to five per cent on the domestic market for those products currently bearing high wholesale sales tax rates including confectionery, soft drinks, aerated waters, cordials, syrups and flavoured milks, manufactured pet foods and savoury snacks and biscuits.

Without significant business cost offsets, prices on average will increase significantly. If the outcome of tax reform were to be a 10 per cent GST, without the offsetting reductions in business costs from the removal of payroll tax and/or the other modelling scenario, the halving of petroleum excise, the price increases would be significantly greater in our food and beverage products and the reductions would be significantly less.

If payroll tax stays and all other nominated taxes are removed, the average additional price increase to the figures I gave earlier would be about two per cent, with the range somewhere in the order of 1.7 per cent to 2.5 per cent. If petroleum excise is not reduced by 50 per cent, the average additional price increase for total food would be 1.8 per cent, ranging from one per cent to 2.2 per cent.

Our modelling work also demonstrated that zero rating food—no tax on the final value added—and a rebate on the GST on inputs is neither effective nor efficient in attempting to offset domestic price increases in terms of the relative disadvantage for many food producers and the impact on the poor and socially disadvantaged. In our modelling work, bearing in mind that we factored in a higher rate of GST on the remaining tax base to maintain revenue neutrality, the distributional benefits to the poor of zero rating food were not great—they were largely illusory. We determined there to be a net gain of $1.50 per week, or 0.3 per cent of household expenditure, for the most favoured households, which was the second quintile. There was a loss of $2.50 per week, or 0.2 per cent of household expenditure, for the highest income earners.

In this vein, we contend that the critical economical objectives of efficiency, global competitiveness, investment, job creation, business and economic growth need not be in conflict with the social objectives of fairness, progressiveness and responsibility for the poor and disadvantaged. In promoting vertical equity, the essential element of the reform equation is the means. Excluding the necessities of life, including food as a compensation mechanism, will severely compromise the economic objectives of tax reform while comprehensively failing to deliver efficiently and effectively against the social objectives.

Zero rating food will, without compensating offsets, reduce anticipated GST revenue in the order of 15 to 18 per cent, undermine the principles of a soundly based tax system, and severely compromise the integrity of the government's package. Because of the financial and political implications, zero rating food—GST-free food—including restaurants and fast food, is considered highly unlikely, if not impossible, to achieve. If that is the case and the zero rating of food is to be confined to some food and beverage products only, then given the increased administrative difficulties associated with definition and compliance the GST system will be rendered substantially more complex than if a single uniform rate was applied across all goods and services.

This will create tax induced artificial anomalies in the market, providing even further scope for social engineering of dietary behaviour, to which we are vehemently opposed: increased compliance costs on both public and private sector accounts; increased administration costs as GST tax and GST-free goods would need to be continually identified, referring to gazetted schedules for the purpose of product pricing and for filing GST returns; incentives to develop products that fall within the classification of non-taxed food; and a bias against manufacturing or processing in Australia, undermining Australia's capacity for further value adding through industrial transformation.

CHAIR—Mr Hooke, I do not want to interfere with your presentation. Far be it from me to do that. But in order that I might balance the time needs, do you have much more?

Mr Hooke—No. Our council fundamentally rejects any notion of differential taxes on food and drink products. They are either all in or all out of the GST base. We advocate the former as being in the nation's and ultimately the industry's best interests, but we would accept the latter if that is to be the political consequence of parliament's consideration of the government's proposed new tax system.

However, we will not be drawn on justifying a case for the exclusion of all food or defending a decision to do so. There is little argument that excluding food from a GST will assist the poor, but there is no defensible argument that it is an efficient and an appropriate mechanism of compensation. For every dollar of compensation for the poor and disadvantaged in the lower 20 per cent of income earners, the top 80 per cent of income earners receive a benefit in excess of $5 and as high as $7.60, as estimated by the Business Coalition.

We see the proposal to exempt food as symptomatic of a lack of confidence in the adequacy of fiscal compensation measures and their political durability for lower income and socially disadvantaged people. Few argue with the intent of compensation. What is at issue is the extent of and the delivery mechanism for compensation. As I indicated at the outset, in accordance with the committee's invitation, we will reserve our recommendations and the means to remedy this apparent lack of confidence in the political durability when we appear before you in stage 2.

In summary, I have three points. We consider the package of proposed reforms meets the fundamental criteria of good tax design and will in the main deliver against the key tax reform objectives of the AFGC and is consistent with the determinations of our modelling research work, and there is scope for the package to be further enhanced in meeting economic and social objectives for tax reform. If I may, I will hand to Geoff Carmody for some brief comments.

CHAIR—I do not want to interfere with your presentation, but I am mindful that the committee will have a number of questions, and there is a time slot allocated. We are already running behind. You should not bear the responsibility for that; we must. But can you reasonably keep to a summary form?

Mr Carmody—I will be brief. The modelling database that I used for the work for the Australian Food Council, as it then was, was the ABS input-output framework. That is the same framework that drives the PRISMOD model used by Treasury. ABS data is the worst available in Australia except for all the rest. The basic assumption we made in terms of tax changes and the effects they have on cost and prices was that all tax reductions lead to price reductions and all tax increases lead to price increases. That is the same assumption that was made, for example, by the Labor government when it produced 'Reform of the Australian tax system' in 1985 with one exception, which I can expand on if you wish. It was the same assumption that was used by John Hewson when Fightback was developed. It is the same assumption that has been used by the government in the ANTS document.

I should remind the committee that the inflation one-off impact of the draft white paper reform proposal was a 6.5 per cent increase in the CPI, and that at a time when inflation was considerably higher than now. Fightback had a 4.4 per cent price increase, although they took tobacco out to get that result. Again, the inflation environment was considerably worse than it is now. We are now arguing about whether the one-off price effect is 1.9, 2.5 or whatever. But, again, it is a much lower one-off price effect in an environment which is much less conducive to not passing price reductions on.

The thing that I did not model was a tax mix switch. I modelled a revenue neutral indirect tax reform. For that reason alone, the absolute price increases for different food products will be lower than those shown in the ANTS document because, on top of the revenue neutral reform, ANTS has got a tax mix switch as well—an unfortunate ingredient, I am afraid, but it is there.

The main conclusions from the scenarios that I modelled are hardly surprising. If one removes a highly differentiated tax such as the wholesale sales tax from a range of food products, one is going to get a highly differentiated set of cost reductions associated with that. If you then replace that with a uniform, comprehensive indirect tax such as a GST, then the price increasing impact of that GST will be uniform. The net effect of those two considerations in particular will be to produce quite a differentiated set of price responses, net, on the food products that I looked at. Not surprisingly, products like confectionery and soft drinks enjoyed either small or below average price increases or even price reductions. Products that were relatively lightly directly taxed under the wholesale sales tax ended up facing higher net price increases as a result of the reform exercise.

One final point I should emphasise, however, is that the food industry that I looked at was input-output codes 2101 to 2112. It is stretching the definition a bit, I know, including tobacco, but the point I am making is that it was those food industries alone—it did not extend the analysis to the hospitality sector, for which food will be a major input. So it is a more limited definition than the one that Mitch alluded to before. I think I might leave it there, in the interest of time.

CHAIR—Thank you, Mr Carmody.

Senator GIBSON—Thank you for your opening statements, Mr Hooke and Mr Carmody. I note that in your introduction you refer to the fact that the need for tax reform has been pushed by governments of both sides of the political fence. But yesterday Professor Dixon, who appeared before this committee, made the extraordinary statement that the government has not made a case for substantial tax reform. Would you care to comment?

Mr Hooke—Geoffrey, would you like to have a go at that, given your historical involvement.

Mr Carmody—Peter Dixon is a very good economist. I thought it was disappointingly superficial for such a very good economist to make that assertion. If I can give you a potted history of my own experience going back 33 years, the case for tax reform, including indirect tax reform, was most eloquently made by John Head in the public finance lectures I attended at the ANU in 1966. The case for tax reform, including indirect tax reform, was eloquently argued in the Asprey committee report in 1975. The case for tax reform was equally eloquently argued in the Labor government's draft white paper in 1985.

CHAIR—That is option C.

Mr Carmody—But I am making the point, Senator, not about the specifics of the type of tax reform, just the articulation of the defects of the present system. That is a common thread in all of these exercises. The precise solutions to them might vary slightly but the diagnosis of the problem has been known for a long time.

CHAIR—But the present system was amended substantially by the Labor government as a consequence.

Mr Carmody—I will come to that too, Senator. It was also made quite well in the ANTS document—that is, in terms of prescriptions for reform. In terms of the real world, one thing that Peter Dixon said was that Treasury had not made a case for an indirect tax system.

I just commend the inquiry to the annual document produced by the Treasury called Budget Paper No. 1. These days the revenue estimates appear in statement No. 5. At the back of statement No. 5 there is a historical series showing how different revenue heads have moved relative to GDP. The indirect tax share of revenue relative to GDP has been falling.

In terms of budget pressures, I think it is sufficient only to remind the Senate inquiry of the 1993-94 budget. Before the 1993 election it was asserted that income tax cuts could be funded without the need for a GST. In the first budget after that election, by virtue of the fact that the revenue base was leaking, we ended up with increases in wholesale sales tax rates and increases in petrol excise in a desperate attempt to shore up the budget in the face of the looming l-a-w tax cuts.

The case for reform has recently been made by Dr Neil Warren in a little piece that you may have seen called 'GST: the long, winding road', which details at some length the need to shore up the revenue base on the indirect tax side if that part of the system is not to collapse completely. It should not be difficult to understand that, if you have a tax base that applies to a very limited part of private final consumption expenditure and that part of private final consumption expenditure is declining relative to the total, unless you continually raise the tax rates applying to that narrow base you will lose revenue.

Senator CONROY—Have you seen any Treasury figures that state that, with the current tax system, revenue growth will fall below GDP growth—the current system, not just indirect but whole?

Mr Carmody—It would be possible—this would require a fairly strong will by the governments concerned—under certain conditions, including inflation, for the overall tax take to continue to rise—

Senator CONROY—Greater than GDP?

Mr Carmody—or to hold relative to GDP even though the indirect tax take is falling. The reason that would be possible is that, if you do nothing about it, tax bracket creep will ensure that the direct tax system forces individual taxpayers into higher and higher tax brackets. In other words, you will get real increases in tax rates by stealth—without legislation, just by dint of the inflation process.

Senator CONROY—So you would support tax indexation as well as a range of the things?

Mr Carmody—Of course. That would be the honest thing for governments to do. Let us face it, most of the income tax cuts that have been given over the last decade or so have been funded by the proceeds of past accumulated tax bracket creep—nothing more.

Senator CONROY—I would agree. You seem to think it is an important issue that they have changed the base of indirect taxation, that wholesale sales tax, which has also been modelled on Treasury figures, is growing faster than GDP. WST is growing faster than GDP: the usual definition of a growth tax. Your argument is that they have changed the base: they have widened it; they have upped the rates. Would you accept that the fall in indirect taxation that you are referring to is because the government equally made a decision to reduce tariffs which has cost $4 billion within that tax base?

Mr Carmody—There is no doubt that the reduction in tariffs has a revenue negative effect.

Senator CONROY—Substantial?

Mr Carmody—Your assertion that wholesale sales tax has risen as a proportion of gross domestic product is not borne out by the Treasury papers.

Senator CONROY—Unfortunately, a week ago they produced a paper to the committee that bore it out.

Mr Carmody—From 1995-96 to 1998-99 the estimate is 2.6 per cent of GDP, and that is by virtue of the fact that the Dawkins budget in 1993-94 assisted the process.

Senator CONROY—But that is a discretionary decision.

Mr Carmody—Yes, and that is all I said.

Senator CONROY—WST is growing faster than GDP. Treasury figures bear that out.

Mr Carmody—For those last four years it is growing in line with GDP and only because of what I said before: discretionary decisions to jack up the rates.

Senator CONROY—You are prepared to say that there is a problem with the existing tax base when a discretionary decision to lower tariffs is there, but you are not allowed to have an argument that says, 'We made a discretionary decision to increase over here.' That does not count, but a discretionary decision on this side of the ledger that reduces it, which supports the argument that there is a falling revenue base in this area, is okay. Both of them were discretionary decisions.

Mr Carmody—Indeed so, and the point is that the base that you are taxing under the wholesale sales tax is suffering more and more distortions relative to the rest of the base as those rates go up.

At least the virtue of the tariff reduction is that you are getting out from under the more efficient industries and allowing them to have a fair go. The point I am making is that, whichever way you cut it, the indirect tax system is declining as a proportion of GDP. The only way you can make that up—and you are going to have to make up more than that to fund the demands of the Australian economy as the population ages—is by increasing the direct tax take.

Senator CONROY—That is an assertion not borne out by the modelling yesterday. If I could put in context Senator Gibson's comment to you which you then referred to about Professor Dixon. Professor Dixon was referring to the fact that his model, under the assumptions—and we can have an argument about the assumptions—shows that the current revenue produced by the current system, with no discretionary changes of any sort right now, grows at slightly more or equal to the existing GDP. The point he was making is that continual assertions that the existing revenue base is ramshackle, is falling apart and is not going to produce what you describe as the needs for the Australian community are not substantiated. Treasury have not produced a single figure, not to this committee and not in the ANTS document, that supports that.

Mr Carmody—I would trade Neil Warren's judgments on indirect tax and on the indirect tax system, and combined with history, against assertions made by Peter Dixon on his modelling, any day of the week. I would like to see the basis on which he made the assertions that you have just mentioned.

CHAIR—Have you had a chance to look at the work done by Professor Dixon?

Mr Carmody—No, I have not.

CHAIR—So you are making that judgment about Professor Dixon's work without actually having looked at it.

Mr Carmody—I would like to see the basis on which he reaches that conclusion, given—

CHAIR—You just damned Professor Dixon.

Mr Carmody—No, I didn't.

CHAIR—Yes, you did. You said he was disturbingly superficial. That is what you said in an answer to Senator Gibson, but you have not read the study that Professor Dixon makes his statements on.

Mr Carmody—The comment I made was based on the comment put to me that the Treasury and the government had not made a case for tax reform. The point I was trying to make in relation to that aspect—not this point about what happens to the indirect tax revenue take over time—was that the case for tax reform has been made time and time again, in all sorts of fora, by both sides of politics—in government and out of government—over the last 33 years.

In relation to the forecast for indirect tax revenue as a proportion of GDP, I might say that the budget monitor forecast that we routinely produce every six months always shows that at some stage or another, unless there is a discretionary change in wholesale sales tax rates, in trend terms the revenue from wholesale sales tax tends to decline simply because of the fact that the base, relative to private consumption expenditure, is shrinking. That is the same point that Neil Warren has made.

CHAIR—I just have to disagree with you, respectfully, Mr Carmody. In 1985, the government brought forward a paper which canvassed several options for tax reform and set out voluminously the detail about that. It then engaged in a structured public debate, peaking in a national summit on tax reform. No such presentation comprehensively has preceded this package. In evidence to the Senate Economics Committee, the chairman of the Treasury's tax task force said it was secret, there were no records and they were not going to release publicly any of the papers that Treasury had commissioned and that all the records and conclusions were 'in his head'. I do not regard that as being of equal stature or public exposure of a case for reform. However, we may disagree on that.

Mr Carmody—I certainly disagree. My argument has all been on the diagnosis of the problems. I suspect what you are talking about there is the modelling that was done of particular proposed solutions.

CHAIR—We have not seen it.

Mr Carmody—But I am assuming that is what you are talking about—the distributional effects, et cetera, associated with particular proposed solutions.

Senator O'CHEE—Just for the slow witted on the committee, can I just put the question to you again. Are you saying that without any changes in the tax rate it is not possible for wholesale sales tax to keep pace with GDP growth?

Mr Carmody—That is correct.

Senator O'CHEE—And the only way it can happen is to keep on jacking up the wholesale sales tax rate.

Mr Carmody—The only way to maintain the revenue buoyancy of the wholesale sales tax is either to broaden the base or to raise the rates on what is remaining.

Senator CONROY—What is your definition of buoyancy?

Mr Carmody—Growing in line with GDP.

Senator O'CHEE—The next question I have for you is this: if you keep increasing rates or if you change categories, bring in another category of food product or whatever into the wholesale sales tax, what effect does that have on compliance costs and what effect does it have on efforts by businesses to evade the wholesale sales tax?

Mr Carmody—Obviously, as recent governments have known only too well, efforts to try to streamline the wholesale sales tax by reducing the number of rates have been at best temporary. We had an attempt at that in September 1985, when the number of rates were reduced to three. We are now back to six. But the more rates you have, the more borders you have between different rate categories, the more interminable argument you will have about whether a particular product falls inside or outside a category and the more effort you will make to try to make sure that your product qualifies for the lower tax rather than the higher tax.

The other point is to do with the case when all of these rates move up—a la the Dawkins budget, for example. All taxes have some distorting effect; that is well understood. The higher the tax rates that apply to particular goods or particular activities, the more likely it is that the distortion costs in terms of efficient allocation of resources will be higher as well. It is better to have a very broad base for a tax regime to which is applied a low, reasonably uniform rate. That way you reduce the compliance cost and you reduce these ridiculous and interminable arguments about whether, for example, yoghurt is taxed or not taxed. That went on for two years, didn't it, Mitch?

Mr Hooke—Two years and a court case.

Mr Carmody—If you have low rates, there is less incentive to try to change your behaviour in a way that evades or avoids the tax. A broad based low rate is a more sensible way to raise tax revenue.

Senator O'CHEE—You would be aware that Professor Dixon said that there was no case for tax reform. He reckoned he had done the modelling and it showed no case for tax reform. What would be your response to that?

Mr Carmody—I had better be very careful because, mindful of Senator Cook's comment, to be fair to Peter I should carefully read his paper. I would make the point that I have seen little of it. For example, there is a little bit in the *Financial Review* today which talked about employment scenarios as a result of various alternative scenarios that he modelled. I just draw the committee's attention to what that graph on page 2 showed. The first point to note is that the range of outcomes ranges from a positive effect to a significant negative effect. How do you get the negative effect? You get the negative effect by assuming that workers are going to do something stupid. Even though they are fully compensated by income tax for the ANTS package, they are going to embark on a round of wage demands to compensate for the one-off price effect. Garbage in, garbage out. If there is a wage explosion as a result of a tax package which is fully compensated for anyway, of course you are going to get adverse effects on employment, and that drives through the wage mechanism.

The other point to note is that you should be aware of the model outcomes—and I am only going on this one graph now, Senator, so I am mindful of your earlier comment. Those graphs show percentage deviations from a baseline; that is, the model is being solved in terms of rates of change. If you look at the graph quickly, you might reach the conclusion that after a certain period of time there is no net benefit as a result of this change—everything has gone back to baseline. The point to note is that those percentage changes, whether above or below baseline, produce permanent changes in the level of employment, GDP, exports or whatever, relative to baseline. So, even when rates of growth go back to baseline, at that point the cake is going to be that much bigger. That is what you would expect from structural reform. Structural reform by and large is going to give you a lift in performance which in terms of levels will be sustained permanently. But you should not be expecting a permanent lift in the rate of growth. I want to make that point.

CHAIR—I do think you should read the full study, in fairness to you, Mr Carmody. I think the point that Professor Dixon also made was that changing the tax mix to a GST was not going to stimulate the economy. What was going to stimulate the economy was tax cuts coming out of the surplus, and that is just good old-fashioned Keynesian stimulus in that sense. That would produce the jobs, not the tax mix switch.

Mr Carmody—I must say I agree with you on the tax mix switch. I do not think it was a sensible element of the tax package. Everyone knows that. Senator Gibson knows that. I have made no secret of that. The two sources of stimulus to the economy that one could imagine coming from the ANTS package, apart from the tax mix switch, are, as you say, the net fiscal stimulus associated with using the surplus to generate a real income tax cut. The other, more subtle benefit—and I do not think it should be overclaimed—is associated with the efficiency gains of moving from a raft of inefficient indirect taxes to a less inefficient indirect tax such as the GST. They are much more tricky to model. They are not going to be as large, arguably, as a substantial fiscal stimulus; nevertheless, they are worth while having. I do not know whether Peter has been able accurately to model those particular efficiency gains.

Senator O'CHEE—He did not. He did not attempt to.

Senator GIBSON—I asked him yesterday and he said he was not able to put in those nuances of changes in marginal tax rates, for instance, with regard to the labour market, or the increases in efficiency within business, with regard to changing the taxes, getting rid of nine taxes out of 10 taxes.

Mr Carmody—That is an area where modelling work that we have done for state governments, for example, suggests that some of the deadweight losses associated particularly with some of those state taxes are quite high proportions of the revenue raised. If they were removed and replaced with a GST on a comprehensive base at a uniform rate, there would be net efficiency gains for the economy. As I say, that is not the sort of thing that you can easily pick out of some sort of Keynesian dynamic model, or even maybe Peter Dixon's model. It is the more subtle efficiency gains that are of a piece with the sorts of gains you get from reducing tariffs or making structural reforms elsewhere.

Senator O'CHEE—Mr Carmody, the point is that those efficiency gains, for example taking costs off business in terms of worrying about compliance, making the whole system more efficient and the more efficient allocation of resources, are ongoing. They are not one-offs, are they?

Mr Carmody—In terms of the level, you would get permanent benefits from that. But, as I said earlier, you should not expect to be getting permanent increases in rates of growth. You will get an increase in the cake as a result of this change, permanently.

Senator O'CHEE—Can I just take you back to the question of assumptions. You talked about the possibility of people asking for wage rises, notwithstanding the fact that they have a package where they are fully compensated. Professor Dixon yesterday said that households had a real increase in their spending power. He also said that it would be an economically irrational decision to ask for a wage increase to compensate for a package that is already compensated. Would you agree that it would be economically irrational to do that?

Mr Carmody—Provided—this is a proviso that I think we need to come to in more detail, either later today or in March—it can be established that the compensation package associated with the tax reform is both adequate and, more importantly, permanent, then it would be irrational. Basically, those extra wage increases would themselves be, and they should be sheeted home as, the source of the increased unemployment that might flow from some simulation of a model. It is those wage increases that cause that unemployment. Provided the compensation package is adequate and durable, wage increases that are sought as compensation for the price effect would be irrational.

Senator O'CHEE—So you would not be out there advocating that people should ask for wage increases?

Mr Carmody—Of course not, Senator. The point is anyway that we are talking about the introduction of a tax reform package in an economic environment this time which is worlds apart from that which existed in 1985, or even the early 1990s. It is a much lower inflation environment, it is a much more competitive environment and it is an environment where the labour market, I think, is much more conscious of the need to make sure that wage increases can be financed, either out of productivity or otherwise. I think that, again with that proviso, provided the compensation package is adequate and durable, there is just no reason for wage increases, because what really interests people is their after tax purchasing power.

Senator CONROY—Do you believe it to be adequate and believable? You are in here supporting the package, so presumably you do.

Mr Hooke—We are going to address that in stage 2.

Mr Carmody—Let me just foreshadow: I do think that there is an excellent case for looking very carefully at particularly the durability of the compensation package, particularly at the low end, as part of the ANTS package. Let me just say that.

Senator MURRAY—Just following on from that, Mr Carmody, you would be aware, as a very eminent economist yourself, that intangibles often have as great economic effects as do the tangibles, such as confidence measures and how people react to feelings about the future. To add to your compensation list of adequate, permanent and durable—you can interchange permanent and durable—probably should be that the people themselves have to believe that the compensation is adequate, permanent and durable. I think one of the great problems we have—why so much focus has been on the estimates the government have made of the level of inflation, on the common assumptions they have made across all income cameos and on the difficulty of translating disaggregated HES figures into particular categories of Australians—has been that there are many categories of Australians who believe, and this is what the welfare groups are saying, that they are not adequately compensated yet, and so on. I would guess within the range of your responses you would not be averse to cranking up compensation measures where there is a likely and reasonable belief that the cushion is too thin, that the margin for error is too great. Would that be a correct summation?

Mr Carmody—Let me respond in a couple of ways. Firstly, whatever the defects of the household expenditure survey and regardless of the fact that pension increases are automatically indexed to some average notion of the CPI, I have no difficulty with the proposition that different people have different consumption bundles and therefore different people will be affected differently by this particular tax package. I would add the point that the differentiation between people is precisely because the price effects of the tax package will themselves be differentiated across products because a differentiated tax is being taken off. So I have no difficulty with the notion that you should look at families in different circumstances. That was done, for example, in *Reform of the Australian tax system*, although the state of modelling then was way less adequate than it is now. It was done explicitly in Fightback, where we used Neil Warren and we used his STATEX model, a private sector version of PRISMOD, and it can certainly be done by Treasury with PRISMOD. I think at the end of the day they have actually provided some information to that effect. I agree that you need to look at those sorts of differentiated circumstances. I agree that people have to have confidence that the compensation will be adequate and durable as well. Later on we will propose a mechanism that we hope might produce that outcome.

Mr Hooke—That is a central tenet of our policy.

Senator MURRAY—Yes, I understand that.

Mr Hooke—Because, as I said in my opening remarks, we do not see the zero rating of food as doing it effectively and efficiently; therefore, we are looking at the fiscal measures to do it.

Senator MURRAY—In other words, you are not saying the package has to be accepted on an all or nothing basis. If a case was reasonably made that the compensation area is inadequate at present then you would support its adjustment.

Mr Hooke—Yes.

Senator MURRAY—My next question really concerns a judgment you have made about the basis on which you would support the tax package, yet it seems to contradict two basic criteria, and I want to know why you still support it. The first is a long campaign by yourselves for the abolition of payroll tax, yet this package does not deal with that issue. The second is your comment, strongly reinforced by Mr Carmody, concerning tax mix switches. The effect of the tax change is around $8 billion in terms of tax mix. Those two things breach your criteria for tax reform. I wonder, in the light of that, why you still support the overall package.

Mr Hooke—The abolition of payroll tax and halving petroleum excise came out roughly ballpark in terms of our modelling scenarios, but we modelled that on the industry, not just on our members. Our membership is skewed more to those who are actually paying payroll tax. So my membership, as you might expect, put a priority on getting rid of payroll tax ahead of the removal of other inefficient indirect taxes. The reason why they have held to supporting the package, notwithstanding that one of the fundamental conditions is the removal of payroll tax, is that the radical changes to the state-federal financial relations provide the states with, firstly, the revenue—certainty—conditions that they were looking for to remove payroll tax; secondly, the GST is a growth tax, particularly relative to the WST—and you have just been through that debate.

Therefore, provided they can restrain their expenditures, they will have the revenue to remove payroll tax down the line and the market is already putting pressure on state governments to compete payroll tax away. So competitive federalism is likely to be the issue. Therefore, while it will not do anything in terms of one-off price impact, which is what we are after, the ultimate goal is achievable in the marketplace.

In terms of the tax mix switch, I guess it is a case of not getting all that you wanted. Our primary interest in the tax mix switch was to make sure that there was sufficient revenue to get rid of as many inefficient indirect taxes as we possibly could. We did not get that, but on the other side you could say there are two sides to the coin in increasing the real purchasing power of consumers but you have the price inflation impact offsetting that.

Mr Carmody—Reducing the tax mix switch brings me back to the compensation issue. I do not think I would go as far as Senator Meg Lees's press release a couple of days ago which suggests that the compensation package is being driven solely by the one-off CPI effect, which seems to be an implication in that press release. The more you can reduce the extent of the tax mix switch, the lower the net price effect will be. The lower the net price effect, the lower the cost of the package overall. I do not think that is in dispute. You will still need some compensation at the bottom end, I think, but it does seem to me that the more you reduce that tax mix switch, the more that problem goes away. That is not an argument, in my opinion, for taking food out of the GST base. It is an argument for either putting more indirect taxes into the bucket for abolition, such as payroll tax for example, or, if you want to keep the base broad, which is desirable, lowering the rate of the GST. It seems to me that they are the more sensible ways of reducing the extent of the tax mix switch, thereby reducing the need for compensation.

On payroll tax, pointy heads will tell you that, if you had a properly designed, comprehensive, uniform rate payroll tax, it would be nearly as good as a GST, and that is probably right. The trouble with the payroll tax in Australia is that it is not comprehensively based. There is a payroll tax free threshold, which is growing inexorably over time. There is a slight differential in rates between different states and all states are adept at giving special payroll tax holidays to companies which set up in their state rather than somewhere else. It is that threshold where the payroll tax cuts in that does a lot of the distorting damage. Besides, even if you could get a fully comprehensive, uniform rate across everything, you basically have two value added tax systems operating in tandem rather than one.

Mr Hooke—Which goes to Senator O'Chee's point.

Senator MURRAY—On the payroll tax issue, one way with which it could be dealt within this package is to reduce two concessions which are currently proposed. One of those is income tax cuts, and that would have to affect the higher income people, and the other one is to halve the diesel excise cuts so that they only apply to heavy road transport and off-road transport and rail; in other words, that non-commercial use would continue to pay a higher rate. That would release moneys to either erode or largely abolish payroll tax. How would you react to that kind of shift in policy judgments within the package?

Mr Hooke—The analysis shows that there is not a heck of a lot of difference in terms of the impact across the industry as a whole. As I think I said earlier, in terms of the up-front first-round impact on my member companies, payroll tax is likely to have more of an impact than halving the petroleum excise.

Mr Carmody—Could I just understand that question? Were you suggesting actually raising more revenue than proposed under the ANTS document from existing indirect taxes?

Senator MURRAY—No. I am suggesting that there is an amount of money, probably half, of excise cuts in fuel which are going to go to non-commercial use; and there is an excess of direct tax cuts to higher income earners, which notionally could be attacked.

Mr Hooke—Are you proposing to use part of the tax mix switch or the majority of the income tax cuts going to the higher income earners to remove half of the petroleum excise?

Senator MURRAY—Typically, what happens in these committees is that the two majors have an argument about what they want to pursue and I am left with a short portion at the end. Let me put this question on notice to you: can you have a look at what I have said and, in your next response, give consideration as to whether you would like payroll tax partially or totally abolished by redirection of policy decisions within the existing ANTS package? It is as simple as that.

Mr Hooke—Sure.

Senator MURRAY—There is a second question I would like to put to you on notice. You are the Food and Grocery Council and you also deal with beverages. One of the issues which is bound to come before this committee is the question of whether alcohol should be taxed by volume, or on its existing basis. You deal entirely with the non-alcohol approach?

Mr Hooke—Correct; that is not in my charter.

Senator MURRAY—I will leave that one alone. This question you can answer shortly: in view of your belief that an indirect tax system should be as simple and comprehensive as possible, ideally would you have preferred education and health to be GST imposed?

Mr Hooke—That is starting to get into the broader economics again, and I will defer to my colleague.

Mr Carmody—Again, I think a case can be made for that broader base. If one made that case, it seems to me that you would require, for lower income groups at least, compensation for the cost associated with that.

But it certainly will be the case that, if health and education are zero rated, there will be arguments at the borderline in defining what is health and what is education. A comprehensive, easy to comply with and efficient revenue raising system, including health and education within the base would have been easier. That would have required, however, more compensation, particularly for lower income groups.

Mr Hooke—But, in principle, the bottom line is—and, again, the reason why we cannot get into it is that you are getting into some other territory—that the broader the base, the lower the rate, the lower are the one-off price impacts on our products and the more revenue that is available to offset more of those indirect taxes we were talking about earlier.

Senator MURRAY—Three major business organisations that I have asked that question of have all said that they want it as broad as possible and, ideally, they would have preferred education and health to have been taxed. I can see that that is consistent with a view. But, if you argue that it is okay to exempt them, the argument opens up as to what else it is valid to exempt.

Mr Hooke—It goes to my earlier points. Unless you can justify it all on economic or social grounds—and with a pretty strong case—then all you will do is start to sponsor a chorus of 'me too' bids, and food is in that category as well. If you cannot sustain a case on either of those—and, as I said earlier, we do not see that they necessarily are in conflict—all that will happen is that you are going to start to have everybody lining up for a 'me too', you will start to unravel the package, you will start to unravel the base, and those who are left in there will be getting belted, and you will be back to all of the problems we had in terms of the discrimination, distortions and complexities of the existing wholesale sales tax system.

Senator MURRAY—My last question is on notice, if you could again respond to that. Explicit in the case that there is the potential for wage demands to radically erode the benefits of this tax package is the belief that the pass-through effects will not be in the same time frame and also will not be complete—in other words, the price impacts will be immediate; the benefits will be medium term and will not be total. I would appreciate, as I guess the committee would, your professional view as to the likely time frame in which the pass-through effects will happen and when both cost impacts and the benefits will occur.

Mr Hooke—Are you giving that to us on notice?

Senator MURRAY—Yes.

Mr Hooke—Okay.

CHAIR—I have one question related to what is being pursued about how broad the base should be and the arbitrary decision the government has made to exclude particular sectors from the base. Your policy, as I understand it, is that in a perfect world the base would be as broad as it could be, everything would be in and, thus, the level of tax would be lower. Does that mean that, if the bills pass in their current form, you will be lobbying the government to include education, health and financial services in a further tranche of 'tax reform'?

Mr Carmody—Just to backtrack a little, there are parts of the private final consumption expenditure base which it is impracticable to include in the GST base because it is a transactions based tax. The biggest and easiest example to illustrate that is imputed rent on owner-occupied dwellings. That is a big chunk of private final consumption expenditure but, if you like, it is a notional entry that the ABS calculates in producing its estimates of private final consumption expenditure. The reason that is not in there is that it is impractical. Because that is not in, the proposal is not to tax market rent for investors who have rental properties because you are trying to treat those two the same. So, effectively, you input tax there. Similarly with financial services, in some cases at least, there is a practical issue valuing the service, and so input taxing is a solution there as well.

I think, to be honest, Senator Murray is quite right: in a sense, for the rest, the door has been opened by education and health. There is concern about whether we are talking about publicly provided education and health versus private, or both. So it is a difficult judgment call. Ideally, we would still like, all those practical considerations aside, to have the broadest base possible. Given that education and health have been left out, we are not going to end up being the most consistent advocates of our side either. We are accepting implicitly, I guess, that education and health can be zero rated. But, if that is the judgment call that allows us to get an indirect tax system which produces a reasonably buoyant revenue stream over time which can be used to fund what will be growing government expenditures as the population ages, that is better than the alternative. So we are pushing it as far as we can.

CHAIR—Yes, I understand that you are pushing it as far as you can. But my question is: assuming that the package is legislated in its current form, does that mean in a perfect conservative world in three years time we will be back here inquiring into why you want education and health excluded; that you have an ongoing agenda to broaden the base of the GST?

Mr Hooke—I have to tell you that we have not got a position on that within the AFGC. Given that I am here on behalf of my council, that is not a question we have put up; in other words, is my council prepared—to go to your point—to tackle education and health within the context of the broad base and that we did not get the elements that we were looking for? No, it has not made that call. It certainly has made the call about all food in and all food out, which I stated in my opening remarks.

Senator CONROY—Mr Carmody, your organisation modelled Fightback for the Liberal Party?

Mr Carmody—The accurate answer to that is that we employed Neil Warren using his STATEX model to analyse the price effects and the distributional consequences of Fightback and we used one of our own employees at the time, Chris Murphy, to use his dynamic macro-model to do some of the longer run simulations. So it was a mixture of contracting out and internal. But, on the importance of price distributional stuff, we relied on Neil.

Senator CONROY—Do you have a macro-model that you use now?

Mr Carmody—Yes, we do.

Senator CONROY—Have you modelled the ANTS package?

Mr Carmody—Not explicitly at this stage, no. No, we have not.

Senator CONROY—I guess this will be a harder question to answer then. At the moment the committee is aware of three models with three estimates of GDP growth over and above. Do you believe that the ANTS package creates jobs; do you believe that it will lead to more jobs?

Mr Carmody—Let me break that down into three components, and this is going back a bit to what Senator Cook said before. To the extent that the ANTS package generates a fiscal stimulus in the environment within which it is being introduced, I think it is likely to produce some boost to jobs. To the extent that we are talking about a tax mix switch, I am not sure what that will do—cause a lot of aggravation, probably.

In terms of reforming the indirect tax system on a revenue neutral basis, I do believe that replacing that raft of existing inefficient indirect taxes with a less inefficient GST over time will produce efficiency gains which, in turn, will help to produce jobs. In terms of magnitudes, I think the fiscal stimulus will be the most obvious and easy to model. In terms of longer term benefits, the efficiency gains from the indirect tax reform will be more subtle and harder to capture. If you are talking about magnitudes of maybe one per cent of GDP or thereabouts, it is hard to pick that stuff up in some of these models—but that does not mean that it is not worth while.

Senator CONROY—We heard yesterday from the Business Coalition for Tax Reform about the ‘dynamic benefits’; that I think was the way they described what you have referred to. We asked its representatives whether anyone had done any modelling to try to capture the dynamic benefits, and we were told that there is no empirical evidence on dynamic benefits because you cannot empirically model the future. So I am just wondering: were you planning to try to capture a figure on that at any stage, or an estimate, a guesstimate? Treasury come before us and say, ‘We are the best guessers.’ Do you have a best guess?

Mr Carmody—If someone commissions us to do the work, we would be happy to do it. But at the moment we are flat out.

Senator CONROY—The three models that we have received so far, over the long run, have come up with figures of 1.7 per cent extra GDP growth, two per cent, around zero and, depending on various assumptions, minus 0.2 or plus 0.2—and I will split the difference and say around zero—and this equates annually at best to 0.2 per cent of extra GDP growth annually. Are you familiar with any or all of those? I think they are the Melbourne Institute’s model, Murphy’s model itself and Dixon’s model.

All of those models consistently argue that there is not a significant increase—and I think yesterday Professor Dixon defined ‘significant’ in economic modelling terms as one per cent plus. None of those models has produced a significant increase in GDP, either in the short term or over the longer term. Is that an unfair characterisation? Would you agree with that?

Mr Carmody—In my view, the efficiency gains associated with this indirect tax reform part of the package will be those sorts of marginal gains. But in level terms, if GDP is $500 million, one per cent is quite a lot; it might appear small in percentage terms.

Senator CONROY—This is an important point. Professor Dixon said that a one per cent gain was significant and that that was, he implied, a sort of consensus among modellers. You are a modeller.

Mr Carmody—I’m not personally.

Senator CONROY—Okay, sorry; but you are very familiar with a lot of modelling work. He also said that, when you went below one and you got towards the zero aspect, it was insignificant; even though you might define it in dollar terms as significant, in terms of boost to the entire macro-situation, it was insignificant.

Mr Carmody—I wonder whether Peter is making a statistical point about standard errors around forecasts rather than a comment about the magnitude of a particular change. I wonder whether he is not making that point.

Senator CONROY—No, it was not a statistical question; it was on the magnitude. It was a magnitude issue that we were trying to get to the heart of.

Mr Carmody—If I could get half a percent of GDP, if it were lying on the path in front of me, I would pick it up. That is a lot of money.

Senator MURRAY—And you would hand it in at the police station.

CHAIR—I think we have come to the end of questions. I am mindful that we will have you back again in the next phase of our inquiry. Thank you very much for making yourselves available today.

Mr Hooke—Thank you.

[11.41 a.m.]

BELCHAMBER, Mr Grant Douglas, Senior Research Officer and Advocate, Australian Council of Trade Unions

GEORGE, Ms Jennie, President, Australian Council of Trade Unions.

CHAIR—I welcome the ACTU to the witness table. The procedure is that we invite you to make a short opening statement on your submission if you choose to, and then to make yourself available to the committee for questions.

Ms George—Thank you very much for the opportunity to come and speak to you on behalf of over two million workers who belong to trade unions, and their families. Obviously the issue of taxation is a very fundamentally important one for working people, and it has always been our objective to ensure that we have systems of tax that are fair to ordinary working people.

Philosophically, we have not been supporters of indirect taxes or consumption taxes. But what we have done on this occasion, as we did in 1985 and 1993, is to assess the package on its merits. Essentially, there are four criteria we have looked at: what is the overall economic gain of this package in terms of GDP; what is the employment impact; what is the inflation impact; and, very importantly for our constituency, what is the distributional effect?

Having applied those tests on previous occasions, we have come to these conclusions about this package. On each previous occasion, as in this case—and as your discussion that has just terminated indicates—the overall gain to GDP in growth, even on the most optimistic estimates, will be small: in the order of a few dollars a week at most per family. But the price to be paid for this is a massive change to tax arrangements with the huge switch in the tax mix.

Secondly, on the issue of jobs, as on previous occasions when we have examined packages that have been before us, the jobs dividend has either been small or negative. We believe that this is true again on this occasion. Certainly the government papers do not quantify the employment impacts. But the assumption somehow is peddled out there in the community that the introduction of a GST, ipso facto, leads to employment growth.

When one looks at international evidence, there is no such correlation. In fact, some of the countries with the highest rates of unemployment are countries that have introduced consumption taxes; and some of the countries in the OECD that have among the highest economic growth figures and outcomes are, in fact, countries like Australia and the United States which currently are without a consumption tax.

In the estimate of the ACTU, because the GST hits labour intensive sectors the hardest—for example, tourism, and you have had an indication of that this morning—the net jobs dividend impact, in our judgment, is likely to be negative. Those analysts who have argued that there might be a small positive jobs impact, I think, obscure from where that comes. In our judgment, in those analyses, the job gains rest primarily on the fiscal stimulus from the income tax cuts and, in some instances, from replacement of more distortionary taxes with less distortionary taxes. We would argue that a GST is not required in either instance.

An income tax cut for our people is warranted, particularly to compensate for bracket creep. In the modelling exercises, if the alleged distortionary and inefficient state taxes were replaced with equivalent income tax revenue, the same employment boost, we argue, would result. So, on the jobs dividend, we do not see any pluses in this package.

The third and very important issue for our constituency is the inflation impact of the package. On the night it was released, we ventured our opinion then that the 1.9 impact was a severe underestimation—and I am pleased to say that we can rely on people more eminent now than even the ACTU's judgments on that issue. Allowing for differences in consumption and savings patterns across households rather than suppressing them, and also for the timing of the introduction of the separate elements of the package, and being realistic about the prospects for pass-on of indirect tax cuts proposed, the ACTU believes that the average inflation impact of four per cent on ordinary Australian households is, in fact, likely to err on the side of underestimation. So the inflationary impact is a serious issue not just in economic terms but also because of the impact it has on the wellbeing of the people whom we represent.

The fourth issue is the distributional impact. Our philosophical position of opposition to indirect taxes has always been premised on the notion that they are, of themselves, inherently regressive. So the focus in assessment of the distributional impact that we have made falls on the compensation offered to different family types. From the government's own cameos and in the charts that we have in our submission, it is clear that income will be transferred from workers on less than average weekly earnings to high income earners; they are the greatest beneficiaries. The income tax cuts offered are central to assessing any compensation proposed.

The simplest case that we offer to you to point out the inadequacy of this package is to take the case of single unemployed persons without dependants. The official government papers show that there are some 3.723 million such income units in the economy. We will show in the table that we have before you that the real tax cuts proposed—and I say 'real' because you must make allowance for bracket creep—are negative for workers earning between $450 and $550 per week before, and I stress 'before', any GST price impact is considered.

Every single income earner on a pre-tax wage between $380 a week, which is the federal minimum wage, and $860 a week receives a real income tax cut in this package of less than 1.9 per cent. This is insufficient to compensate for even the 1.9 per cent inflation impact of the package claimed during the campaign and well short, as I am sure you are now convinced, of what would be required as compensation on any realistic appraisal of the inflation impact. Distributionally, this package leaves all but the highest-earning single income units worse off. The tax cuts, in our opinion, offered as compensation are clearly and utterly inadequate.

Finally, let me say that the ultimate inflation impact of the package will depend on whatever is finally passed into law. The ACTU will have regard to these issues in seeking, as is our obligation, to protect the real living standards of ordinary working people. Clearly, the inflation consequences of any package will affect the purchasing power of ordinary workers' wages. Hardest hit under the current proposals are full-time low-paid workers, those who rely on the living wage increase as their only means of adjusting living standards. But beyond these, let me say that any worker receiving income of up to $50,000 a year, in our judgment, would have to take into account the outcome of any package carried by parliament in terms of the wage outcomes they would seek. I would ask Grant just to explain in more detail the table we have put there for you.

Mr Belchamber—We have provided a copy of a table. It is just one page, and it is headed 'Illustration—Adjusting Tax Scales for Inflation'. The purpose of this is just to enlarge a little on table 1, which is at page 14 of attachment B to our submission to this inquiry. To make the point about the effect of bracket creep and the necessity to allow for it in working out the real net tax effect of the package, we have provided in this table handed up this morning income levels which move by $1,000 increments, whereas the table in the attachment to the submission increases over the critical range by $5,000 per time.

CHAIR—This is headed 'Table 1: Illustration of Distribution of Winners and Losers'.

Mr Belchamber—Yes, 'Single Person'. We focus on the single person income unit at this point because it is the simplest example and, in terms of absolute numbers, it has by far the greatest weight in all the cameos which are included in the official tax papers. The official papers show, at page 178, that there are 3.723 million income units covered by this single person cameo, many more than apply in any of the other cameos included. For these people, changes to social security arrangements have very little effect on the net position.

But, to assess the compensation offered in the package for the price effects of the GST, it is necessary first to adjust for bracket creep which has occurred since the tax scales were last adjusted and through to the time that the new tax scales will be introduced. We have done this in a very simple way. In the box at the top of the table handed up today, the first three columns set out the current personal income tax thresholds. Then in the second column these are indexed by a factor of 20 per cent. Then the current marginal income tax rates are set out in the third column. In the fourth and fifth columns are set out, respectively, the proposed marginal tax rates under the government's package and the proposed income tax thresholds.

The relevant comparison, before looking at what is required to compensate for the price effects of inflation, is to see how much is left for workers at different income levels when allowance is made for the effect of fiscal drag or bracket creep; the effect of inflation of raising the average tax burden by people at all income levels. In the bottom half of the table we set out, in the first column, income levels rising by $1,000 a year and translate that into dollars per week. The middle two columns set out the tax which is due on the old scales, as indexed. The fourth column sets out the tax which is due on the proposed new rates and thresholds in the tax package. Then the final two columns show us the difference, firstly in terms of dollars per week and then, secondly, as a percentage of the old after tax income.

What this table shows is that, throughout the range from $20,000 to $45,000 a year, the real tax cuts are less than 1.9 per cent of previous after tax income. For the critical range,

$450 to $550 a week, these proposed tax scales do not even compensate for bracket creep before there is any allowance at all for the price effects of the GST.

The rates of pay for single persons in full-time employment at the bottom end of this scale, in the range from $20,000 to $30,000 a year, or from $400 to around $600 a week, are earned by people who benefit from living wage increases. In the previous living wage case, the government proposed $8 payable to anyone who earned less than $450 a week. These scales show that the proposed income tax cuts in the new tax system package leave workers earning between $450 and $550 a week behind, shouldering an increased real tax burden before there is any introduction of a comprehensive goods and services tax.

We then come to the tax cuts available to compensate for the price effects of a GST. Would you turn your attention back to the table attached to our submission—Table 1, ‘Illustration of Distribution of Winners and Losers under GST Package—Single Person’. We have set out three different adjustments for the cost of living under the package. Cost of living 1 is the official estimate at 1.9 per cent, which is now widely accepted to be a significant underestimate of the real impact price effect of the package. The second column takes a factor of four per cent, and the third column has a factor of five per cent for people earning less than $40,000 and three per cent for those earning above that. Then we conduct an exercise which asks, ‘What is the package worth to me?’ Clearly, over the range where most ordinary workers lie, this package leaves them worse off.

There are 3.7 million single income units. The rule of thumb is that around two-thirds of workers earn less than average earnings. That suggests that some two million single income earners are worse off under this package as proposed when allowance is made for the inflationary impact and the real tax cuts that the package promises.

Senator FERGUSON—I will use the table that you have just quoted from. In your submission, as well as using the 1.9 per cent, which is the figure that was used by the government in its package, you have also chosen four and five per cent. How are those figures calculated? What statistics or what basis did you use for determining four or five per cent? The modelling has all been done on statistical analysis or by using a basis, so what did you use to choose four or five per cent?

Mr Belchamber—We chose a range of plausible inflation effects deriving from the package to show the sensitivity of the claim that ‘everyone is a winner’ to small variations in the price effect of the package. In the official documents it is clearly acknowledged that in the first year the price effect is more in the order of 2½ per cent, and that is after excluding a price impact for housing and tobacco. It is also assuming full pass through of the price reductions deriving from abolition of indirect taxes and excises. Relaxing each of those assumptions suggested to us on 20 August last year—one week after this package was out—that 1.9 per cent was a gross underestimate of the likely real price effect of the package and that four per cent was a plausible ballpark estimate.

These figures of four per cent and five per cent do not derive from a detailed modelling exercise. They are in the nature of a sensitivity analysis to be applied to the claims about the distributional properties of the package. Subsequently, these points have been substantially borne out by a range of analyses that have appeared, and I understand that they have been put to this inquiry.

Senator FERGUSON—I am not sure that four per cent or five per cent has been borne out by a range of analyses. I cannot remember that any of the modellers we have used or that we have had submissions from have suggested that it was four per cent or five per cent. Some have said that it is higher than 1.9 per cent, which the government does not accept, but it is a fact that there is a range of options. I concede that it may be higher than 1.9 per cent—that it may be 2.5 per cent in the first year—but you say it is plausible to choose four per cent or five per cent. I think that is quite debatable.

Mr Belchamber—I will say two things about that. Firstly, even if the price effect were 1.9 per cent, after bracket creep everyone on average earnings or less is worse off.

Senator O'CHEE—That is not answering Senator Ferguson's question.

Mr Belchamber—Excuse me, Senator. I am trying to answer the question that Senator Ferguson put to me. If I can complete the answer, I would be obliged. My understanding is that work conducted by the Melbourne Institute has found that an average price impact for low income groups is in the order of 3.6 per cent, taking into account all these considerations—but not full pass through of the price reductions from wholesale sales tax and diesel—and having regard to different savings, consumption patterns and so on, which is not a long way short of four per cent. There is plenty of room to make up that ground, having regard to the full flow through of the price reductions. Secondly, if 3.6 per cent is an average, then there are a great number of households that are going to have much more than that, and there will be some with less. The point of this exercise is to provide a sensitivity analysis, or a sensitivity gauge, on the claim that everyone is a winner.

Senator FERGUSON—The committee will be getting distributional modelling done which will test the accuracy of some of the assumptions that have been used in other models and some of the figures that you have put here, but nowhere has anyone suggested, to my knowledge, five per cent. You have used 1.9 per cent, four per cent and five per cent. I think we should treat them as a range of possibilities—you say 'plausible' results.

On page 5 of your submission you list a whole range of goods and services that go up in price. In the same document with the list of things where prices went up, there was also another list of things like education, down 0.3 per cent; health services, down 1.3 per cent; community services, down 2.7 per cent; soaps and detergents, down 1.5 per cent; and medicines, down 2.8 per cent. You do not quote anything that has gone down, only those things that have gone up.

Mr Belchamber—In this analysis, we have considered the situation most likely to be confronted by low income households. The point is that low income households consume intensively in things like public transport, clothing, and food in particular. To the extent that that is the case, that is suppressed in the official documents, where it is assumed that savings and consumption patterns are the same across household types. We are drawing attention here to the fact that any household whose consumption bundle is intensive in the sorts of items noted at page 5 will be facing price increases of that order. These numbers do come from the official document.

Senator FERGUSON—I am not quite sure where you draw the line for low income earners. Low income earners are going to use all those things, but do you suggest that they are not going to use education, which goes down by 0.3 per cent, or health services, which go down by 1.3 per cent, or community services, which those same groups of figures show to go down? You chose to include the ones that are going up but not to mention anything that might go down.

Mr Belchamber—We have mentioned a number of aspects of the package. This section of our analysis deals with inflation and with the claims that the inflationary impact of the package would be 1.9 per cent. That is the basis for measuring the adequacy of the compensation on offer. We draw attention here to a range of considerations which show why that claim is not sustainable, particularly for low income households.

Senator FERGUSON—If you are going to show the things from the official document that will go up, you should also, in fairness, put some weighting on the things that the official document shows will go down.

Mr Belchamber—The price falls are in the papers for all ACTU Executive members to see, and they have seen them. It is a question of whether low income families spend intensively on items and commodities whose prices fall significantly. There is a limit to how intensively you can spend on detergent or soap powder, particularly when you are buying Home Brand items from the supermarkets in order to make ends meet. There is certainly not likely to be—

Senator FERGUSON—You are being selective, though. You are again being selective by pursuing soap and detergents. Community services are used a lot by low income earners and health services are used a lot. I am trying to put things into perspective.

Ms George—You have to understand that for a lot of those low income families they are in fact dissavers. In the submissions we have made to the commission that look at the consumption and expenditure patterns of low income households—things like food, rent and travel by public transport—they consume a large proportion of their disposable income.

Senator FERGUSON—I know my time will be reasonably limited so I will move onto the subject of bracket creep. You have mentioned it quite a lot in your submission. In your submission you are suggesting to us that income tax rates should be indexed to take account of bracket creep. Have they ever been?

Ms George—There have been different periods where there have been compensatory adjustments for the impact of bracket creep, but it has always been longstanding ACTU policy that, in ensuring fairness in the system and having less of a burden on those with least capacity to pay, the tax scales should be adjusted regularly. So tax indexation has been a longstanding policy.

Each time that we have assessed different ‘reform proposals’ for the tax system, we have always factored in the bracket creep factor in making the judgments about the impact on the people that we represent. In other words, before we start looking at the compensation, let us look at what they should have got back if indexation had properly applied.

Senator FERGUSON—There has been only one period of time when income tax was indexed for bracket creep, and that was during the Fraser government, I think, for one year.

Ms George—I thought it was a couple of times.

Senator FERGUSON—I think it was only once, and never under a Labor government has there ever been an indexation for bracket creep.

Ms George—That does not excuse Labor governments. That is our policy.

Senator FERGUSON—I understand. I am not blaming you for that. I hope you complained just as bitterly to them at the time.

Ms George—We did when Mr Hawke and Mr Keating wanted to introduce the consumption tax. We applied exactly the same criteria in judging the efficacy of that package as we are applying to this. That was found wanting, as is this one.

Senator FERGUSON—One of the best ways of eliminating bracket creep to the best extent possible, if you are not going to have indexation, is to have a large majority of Australian taxpayers paying no more than 30 cents in the dollar. Eighty per cent of Australians will never be subject to bracket creep because, in fact, their tax rate will never go higher than 30 cents in the dollar.

Mr Belchamber—With respect, Senator, that is not correct.

Senator FERGUSON—Are you saying that 80 per cent is not correct?

Mr Belchamber—No, that your assertion that they will never be subject to bracket creep is not correct. In fact, as long as you have a progressive income tax scale, anyone within the range, for example, $20,000 to $50,000, who has a wage increase pays a higher average tax bill due to the effect of fiscal drag or bracket creep.

The point in these papers is that bracket creep over the period of the 1990s, since the end of 1993, hits hardest the real battlers, people in the mid-$20,000 area, people earning between $450 and $550 a week. They are the hardest hit by the effects of bracket creep, not the high-flyers up the top end. The real adverse consequences of failure to adjust the tax scales for the effects of inflation with the present scales are concentrated on low income earners.

Senator FERGUSON—Let me say that I will concede the point that it does not eliminate bracket creep, but the best way to minimise bracket creep is not to have an extra progression in that lower income group, which in fact we have at present. Up to $50,000 we have the three tax rates, which accentuates bracket creep. Under our proposals, from $20,000 to $30,000 people pay no more than 30 cents in the dollar. That is the biggest movement towards the elimination of bracket creep that we have had in a long time for low income earners.

Mr Belchamber—With respect, Senator, I disagree with that too. The cuts to the bottom marginal rates of tax during the 1980s delivered substantial benefits to low income families. The cuts and the juggling of the thresholds, the reduction of the $20,700 threshold down to $20,000 and the failure to index, mean that the problems generated by bracket creep are not fixed by this package for low income earners.

Senator FERGUSON—They are fixed far more than when you have three different ranges of taxes.

Mr Belchamber—Not for low income earners.

Senator FERGUSON—I know we should not debate this; we may finish up agreeing to differ. I think the other point about bracket creep is that the income tax cuts this government has proposed in fact not only fully compensate for any bracket creep that we may have had occur under this government but in fact partly compensate for the bracket creep that occurred under previous governments. That is one of the reasons for the income tax cuts that we have put forward.

Ms George—Could I just say in response to that that the actual table we have presented, the objective data, disproves your assertion. It does not compensate for bracket creep, let alone provide any compensation for the impact of a GST.

Senator FERGUSON—This is the first time I have seen your figures. I would want to have them tested because they have come using figures from 1993.

Ms George—Yes, certainly, but all the assumptions are there.

Senator FERGUSON—I would like to have a look at them, as they have just been put in front of us. Under food, I am talking about your press release of 13 August 1998, which you have included in this submission. You state that the tax mix switch will hit low income earners the hardest while the wealthy will benefit. Isn't it true that, if food were to be exempt from the package, the benefits have been calculated by reputable modellers and others—and I do not think they have been disputed—as up to $5 billion? There have been various figures given as to the amount of tax that the exemption of food would be in forgone revenue to the government, but in the most commonsense a figure has been accepted of around 4.4. Dixon said 2.3, but he was using—

Senator MURRAY—It was 2.5.

Senator FERGUSON—Okay, 2.5, but we think that may be a narrower definition than what is generally accepted. Between $4 billion and $5 billion is generally the accepted figure. Isn't it a fact that of that $4 billion to $5 billion only about $660 million is GST that would be paid on food consumed by people considered to have low incomes and the other nearly $4 billion would be paid by the wealthy? So isn't it true that if you exempt food you are in fact overwhelmingly benefiting the rich?

Mr Belchamber—I do not believe that is the case. You have quoted a large number of figures here this morning and I am not familiar with all of the details of those figures or the sources of them. Some of them I think have only been put before the committee recently. We will be looking very carefully at any specific proposals for amending the package and, when there are some concrete proposals for amending the package and excluding some items or others, we will be looking at the effect of those and the distributional effect of those on ordinary working families.

Senator FERGUSON—I think it is fair to say that some people might question the volume or the significant amount of money, but it would be a fact that the wealthy do spend a lot more on food consumption than those on lower incomes in total dollars, although they are a much smaller percentage of the population.

It has been argued not only by us but by some modellers that it is far better to overcompensate people at the lower end—to still collect the GST on food from the rich but give extra compensation to those at the lower end. It would be fairer. Professor Dixon said the same thing yesterday. For every dollar that it costs the low income earner, it benefits someone on a higher income by $7.60. I think these were the figures he quoted yesterday.

Mr Belchamber—Unfortunately, the package as it stands does not overcompensate anyone for the price effects of the package, and it undercompensates full-time earners earning less than average earnings.

Senator FERGUSON—We accept that that is your submission and that is why you are here. Let us face it.

Senator GEORGE CAMPBELL—Mr Belchamber, you said that you have used the inflationary figure of 1.9 per cent when doing the calculations in the document you presented this morning. Are you aware that the 1.9 per cent is the impact in the second year and that Treasury has estimated the impact as 3.1 per cent in the first year?

Mr Belchamber—Yes, indeed, Senator.

Senator GEORGE CAMPBELL—Have you taken that into account in these calculations?

Mr Belchamber—In the calculation that we have put up this morning, we have not taken any price impact into account. This is simply bracket creep. This is where you stand before there is any price effect at all. What it shows is that, over the range of $20,000 up to $45,000 a year, the maximum real tax cut is 1.9 per cent. The point is that that does not even meet the 1.9 per cent that was widely referred to over the past five months or so. We do note, and point out in the briefing for executive that is attached here, that the inflation impact is 3.1 per cent in the first year in the official papers, and 1.9 per cent is the second-year effect. The second-year effect is based on many quite restrictive assumptions.

Senator GEORGE CAMPBELL—In the submissions that the committee had before it yesterday, Professor Quiggin, apart from arguing support for a GST, demonstrated in his submission that the tax on food—and his argument was to exempt food from the GST package—would operate as a poll tax. He presents a table in his submission—and I recommend that you have a look at it—which shows the distributional effect across all households on a per capita basis. The expenditure on food is about the same, irrespective of the household income level. If that were proven to be correct, what is your view of the impact of that in terms of the distributional effects?

Mr Belchamber—The regressive nature of the package would be reduced by the exclusion of food. That is the clear consequence of that proposition.

Senator GEORGE CAMPBELL—We also had submissions yesterday from Professor Dixon. Are you aware of the scenarios that he presented in terms of the likely impact of the package on jobs, given the various wage responses that might occur?

Mr Belchamber—I have had a quick look at some of the scenarios that Professor Dixon has produced.

Senator GEORGE CAMPBELL—Which of those scenarios do you think is the most likely wages response from the trade union movement if this package is introduced in its current form?

Mr Belchamber—Firstly, Professor Dixon's modelling has a high degree of academic excellence attached to it but, like all modelling, it rests on some specific assumptions. Its long run effects and short run effects depend on some of the specific assumptions that underpin the results that he generates. The key result is that the overall gain of the package in terms of growth and welfare is negligible. It is not very much.

CHAIR—By welfare, do you mean standard of living?

Mr Belchamber—Yes. That has been the central result from our consideration of the consumption tax packages on each of the three occasions. On each of the previous two occasions we have considered the packages, the result was that, at the end of the day, there is not much in it. There are some results in Professor Dixon's work which have to do with before tax and after tax wage bargaining. He says that, in the central simulation, he has adopted the favourable assumption that workers make their wage bargains in real after tax terms. This means that workers accept the income tax cuts in the government's tax package as compensation for the increase in the CPI associated with the imposition of the GST package. That is his assumption. The favourable assumption is that this package is accepted as compensation for the CPI effects associated with the GST.

You cannot spend the same dollar twice. If you are getting a dollar in compensation for bracket creep so that your real tax position does not fall away over time through the effects of inflation, you cannot spend the same dollar as compensation for the particular price effects coming from a GST package. It is not there to be spent twice. The critical questions for us down the track are: what is the CPI increase associated with, whatever package finally transpires and passes into law, and how does that and its CPI effect measure up in real terms in terms of the taxes paid by workers?

Our principal duty as a union movement is to protect the living standards of union members and their families and low paid workers and their families. So there are two aspects. One is what may happen in a living wage context with a claim made in the normal way to the Industrial Relations Commission and argued out on the merits. The second aspect is what unions will have regard to in collective bargaining. The favourable assumption in the professor's modelling work is that workers will accept the income tax package as adequate compensation for the GST. But, clearly, they will not.

Ms George—In follow-up to that, with the package before us that has been outlined, it is clearly the view of the ACTU and the union movement that the compensation offered is inadequate. It is barely adequate to meet the bracket creep for some elements of the people that we represent, and that would be taken account in their round of wage claims. What might emerge as a result of your inquiry, and what becomes law, will be then assessed as to its adequacy, taking into account bracket creep and the inflationary impact. But what we have before us is clearly and unequivocally unacceptable in terms of the supposed compensation it offers.

Senator GEORGE CAMPBELL—If I can sum up, what you are saying is that, if the current package that you have looked at and done your analysis on is passed into law, then the likely response from a significant section of the trade union movement will be to seek compensation through the wages system for what they believe the impact will be on their membership.

Ms George—Our primary responsibility is to protect real wage levels and living standards of working people. To the extent that I have already outlined that this is clearly inadequate, we would seek to redress that inadequacy either through arbitral proceedings for those who have no capacity to bargain or through the bargaining mechanism. But that is very hypothetical. All we are saying is that clearly what the government has put to the ACTU and to working people is rejected on the grounds that for those earning under $45,000 the compensation offered is clearly inadequate in that it does not fully compensate all working people for bracket creep, let alone compensate for the 1.9 assumption, which, in everybody's judgment now, is far below the real CPI impact that the introduction of a GST would have.

CHAIR—The direct answer to Senator Campbell's question is yes, is it not?

Ms George—The maintenance of real wage levels has to be the guiding principle for the union movement and will continue to be.

Senator SHERRY—To come back to the issue of the CPI, after a great deal of questioning, we finally got out of Treasury that 3.1 per cent figure, average. Obviously, some people will be above or below the average, but there are two other critical assumptions that I put to you will add to that 3.1 figure. One is that the Treasury has assumed a full and immediate flow through of price reductions as a result of the elimination of wholesale sales tax and other factors. Numerous witnesses have questioned that assumption—that there will be an immediate flow through. Secondly there is another factor, that is, the issue of compliance costs to business which are estimated to be $2 billion dollar. Again, there is an assumption that business will not flow through those additional compliance costs of $2 billion. I put to you that the average inflationary figure, certainly in the first few years, is likely to be higher than 3.1 per cent.

Mr Belchamber—I certainly would agree with that, Senator. It is in line with the points I was making earlier with Senator Ferguson. We think four per cent is a realistic and plausible ballpark estimate—even an under-estimate—of the likely inflation impact associated with this package. Of course, if the flow-through of the price reductions occasioned by abolition of wholesale sales tax and the diesel excise and related matters is not passed through in full in the first year, there is some evidence to suggest that the overall effect of the package will be negative on employment and negative on growth.

Senator SHERRY—But at the end of the day, if the inflation figure—we know it will certainly be higher than 1.9 per cent. That is a ridiculous figure. Even Senator Ferguson conceded that there were some doubts about that.

Senator FERGUSON—Are you sure I did that?

Senator SHERRY—I think you did. We can check *Hansard* later. As a duty, you have to respond to the quite legitimate concerns of your members, particularly those lower middle income earners—$20,000, $30,000, $35,000, in that sort of range.

Mr Belchamber—That is why people belong to unions. Yes, it is a central concern.

Senator SHERRY—And the issue raised by Professor Dixon yesterday—if there was a response because of the government, in my view, deliberately underestimating inflation and the impact, what was likely to be minimal if any change to employment as a result of this package, in fact, will be a significant impact on employment levels.

Mr Belchamber—Certainly there is a significant risk that the package will see employment levels fall in labour-intensive sectors, and that includes a lot of small business. If we were not to have regard to bracket creep in assessing the adequacy of the compensation on offer here, it would be saying that it is fair that low income earners pay for the tax cuts to be delivered to high income earners.

Senator SHERRY—I also draw your attention to I think it was the Victorian Council of Social Service that provided us with a breakdown of categories across income. It showed that, for lower middle income earners, there was a range of impact from five to seven per cent in terms of the total cost of living and decline in their standard of living, as a consequence of this package. We have had figures that are higher than four per cent. From memory, I think the numbers in relation to Victoria were that there were some 330,000 families in the category of five to seven per cent. Again, many of those would be trade union members. Would that put additional pressure on the ACTU to have to respond to that sort of impact?

Ms George—It really relates to an issue which I think Senator Murray raised about perception. Let me make it quite clear that the general perception of the pay-as-you-earn taxpayer is that they are the only honest taxpayers in this country and that there is nothing particularly wrong with the system which we have currently in terms of the principle of progressivity other than those at the top end having the means to avoid, to minimise and get away with it, and our people do not. So the government is asking these same people at the lower end of the income scale to cop the additional impost of a GST. Even in the cameos presented and the charts we have given there is a massive redistribution of income from those below AWE to those at the top end of the scale.

The biggest beneficiaries will be the $75,000-plus single income earners with children. We do not have too many of those in our ranks. The losers are the people we represent. Their argument is, 'Get the system to make sure that those who avoid their obligations pay their fair share. Stop the haemorrhaging that is occurring. Stop the incentives that are given for various forms of tax minimisation rather than putting on an additional impost.'

I have told our people that 1.9 is a severe underestimation. They know that it is not real. The more that this inquiry goes on, the more the ordinary person is hearing not just from the ACTU but from eminent economists talking about the under-estimation. So public perception is a very important element in this equation.

Senator GEORGE CAMPBELL—On that question of perception, what impact is the fact that the business tax reform package is being done separately from this package having on people's perception of this equity issue?

CHAIR—You mean the Ralph inquiry?

Senator GEORGE CAMPBELL—The Ralph inquiry, yes. Is the ACTU concerned that it is happening separately from this?

Mr Belchamber—There are some concerns with the issues identified in the tax reform papers and to be referred to the Ralph inquiry about the different taxation between trusts and companies. It is a concern to us that that aspect of change to the tax system which goes directly to the revenue base available to government to deliver services is off in a separate arena for separate consideration. The proposition that companies are to be taxed more like trusts is one which does ring some alarm bells, given that the trust vehicle has been a major vehicle for tax minimisation schemes and for the development of them in Australia over the last couple of decades.

Senator GEORGE CAMPBELL—And is there a perception amongst your membership that business is likely to be treated more favourably in the tax outcomes than the PAYE taxpayer?

Ms George—Without a doubt.

Mr Belchamber—That is explicit and overt in these papers. The GST package is not a tax on business. It says so in as many words here: 'Business costs fall by 3.2 per cent.' There is undoubtedly a shift involved in the package in the tax burden from consumers and from workers to business.

Senator MURRAY—Ms George, there are three standard measures that influence real wage increases: the first is supply and demand of labour in a particular sector or industry; the second is the cost-push pressure which arises when workers' disposable income deteriorates, say, if the CPI goes up; and the third is productivity. There used to be a fourth in this country, which was the wage tax social contract that the workers movement had entered into with the government, but that is no longer an option. I understand that, overall, as a generalisation, there have been real wage increases over the last three or four years. If that is true, what is driving that? Is it the supply and demand factor, the CPI factor, the productivity factor or a mix of them?

Ms George—There have been real wage increases for those who bargain, but nothing like the pace of real wage increases for directors, for executives or for senior public servants. A lot of that is driven by the enormous sustained growth that we have seen in productivity. It is workers saying, 'We've contributed, and we want our fair share of the productivity gain.' The low income workers have not been getting real wage increases. Our vehicle for predicting their living standards is through the living wage case, and there is a new application before the commission at the moment.

In terms of the overall wages scenario, it is this government that walked away from any understanding with the union movement. It was the government that put an end to the accord, so any wage-tax trade-offs that might have occurred over the period of the Labor government are no longer a consideration. From the point of view of our constituency, the protection of living standards has largely been fought out and bargained over in the marketplace in terms of the productivity growth that has been sustained or by the kind of argument we have put forward at the level of the commission for decent living standards for the low paid.

Senator MURRAY—I want to put my question into this context. Business groups, a number of economists, and the government in particular have argued that the net effect of the total new tax system will be to improve our economy in a number of ways—which is particularly driven by perception, I might say. Professor Dixon said yesterday that, even if that were true, if the result of the change was that workers and worker organisations felt that they had been dudded and drove for significant wage demands, there would be job losses, investment losses and much of the economic benefits would therefore dissipate. The issues of how working people feel about the package therefore become very important, particularly their perceptions, their confidence levels and the issues of when the price impacts and benefits occur, which is the whole argument about pass through. You, as a leader of the workers organisations will pay a pivotal role in that.

One last thing I would add before you comment is that there might be a perception amongst some—which I do not share—that, anyway, you would drive to promote that perception, even if it were not true, simply because you do represent workers and are on their labour side of things. How do you react to all that?

Ms George—As President of the ACTU, obviously my priority is concern and consideration for those who are members of the union movement, but I do not do that blindly or foolishly without consideration of the impact of what we do on macro-economic outcomes, be it inflation, employment or whatever else. So it is not as if we charge off without considering, 'Well, if we go for a 10 per cent increase, what impact will that have on employment levels?' All of those factors are taken into account.

But I think you ought to appreciate that, for my constituency, there are obvious and growing wage inequalities that are occurring in this society. It clearly is the case that there is one law for the rich and another for the poor. We are told that wages have to be restrained, when some people are battling on less than $20,000 per year. Employers are saying that you cannot have a wage increase for those people, yet the government can offer senior federal public servants another $400 extra per day. People see that. Those kinds of unequal outcomes—the unfairness and the inequalities—are so rampant.

They know about the high fliers who do not pay a zack in tax, and yet they are being slugged. They know that the pay-as-you-earn people are the only honest taxpayers. I think you need to look at this new withholding arrangement because not only will it provide a ruse for people to avoid their employment obligations but, as we have seen with the PPS system in the construction industry, it moves more people out of the pay-as-you-earn system, which erodes the tax base.

Apart from being a union leader, I am a concerned Australian. I want this country to be fair and just. I do not want the people who have the least capacity to bear the burden to continue to do it. As this package is showing, single income earners under $45,000 per year are going to be decidedly worse. In the absence of any social framework with this current government—where you can sit around a table and discuss those issues—we will do what the government has encouraged, and that is that you seek wage increases out in the field. While we have a commission, we will seek to protect the living standards of the low paid, those under $20,000 and $25,000, through the arbitral mechanism.

Senator MURRAY—So, in summary, you are saying that the sense of injustice, unfairness and inequality in our society is going to massively influence the way in which workers will regard the final package that comes through. I want to follow on from that, because the psychological intangible dimension is absolutely critical to the acceptance of any government package or policy. Have you ever surveyed your members as to how they feel about politicians and the political process?

Ms George—No, but I guess they would feel like a cross-section of the Australian community. I will just give you an illustration. When I am battling to argue on behalf of low paid workers a minimum wage of $400 per week before tax and super and you can give federal public servants—I am not saying they do not deserve a wage increase—that amount by way of extra payment in a day, and when politicians can get in their overnight allowances, for one night, what families are taking home after tax for a week's work, then people do ask: where is this country heading?

Senator MURRAY—You know me well, and you know I ask a question seriously. The Roy Morgan Research Organisation has done such a survey of Australian attitudes since the 1970s, and the trust in politicians, according to that organisation, has fallen from 20 per cent in the 1970s to seven per cent. In other words, most people do not trust politicians and possibly, by extension, do not trust the political process.

As a consequence, regardless of the good economic and efficiency arguments for putting a broad base consumption tax into the community—we all understand those efficiency arguments—people may not trust the government of the day or the next government to retain the compensation levels. They will, however, understand that if food is made GST free, that is it—it is GST free. How do you build in, for instance, the competing argument of giving more compensation and saying 'Trust us, folks, we won't take it away' against the argument 'We'll make food GST free and you'll get the immediate seen benefit'?

Ms George—From the overall perspective, I have given the reasons on economic grounds where I do not believe the shift to a GST and the huge tax mix that is involved is warranted. So it is a bit hard for me to move away from that fundamental position. The average person does not believe the compensation will last because there are no other countries, I think—if there are, there are very few—that have introduced a GST that has remained at the same level.

They look around the world and they know. They say, 'Yeah, that is what they say but, next time around, what will the GST be?' If you surveyed average opinion out there, I think there would be a high degree of scepticism. First of all, they know that the impact is going to be more than 1.9 per cent on prices and, secondly, I think the average punter does not believe that the compensation will be permanent or will be sufficient to offset the price increases. But they do know, quite clearly, and my constituency know because I have told them, that the highest beneficiaries are those that are at the top end of the income scale. They know that very clearly.

Senator MURRAY—My last question is this. Would you agree with me that this package should make lots of people worse off—for instance, people who are not paying their fair share, people who are avoiding or minimising tax, people for whom the burdens of taxation fall on others such as PAYE earners and some organisations, companies and industries that pay more than others? I believe that the other side of that coin is that we should look at making some people better off, which is the argument of the social services people, for instance, the poor—and I distinguish between these—and low income people. Would it be your view that that is a desirable social policy goal for this government to pursue, namely the redistribution of real disposable income to the poor and lower income earners, and that, because they tend to spend everything they get anyway, the economic benefits of doing so will be immediately apparent because that money will flow back into the economy?

Ms George—There are a number of issues that you have traversed there. Let me just say that, in terms of the alleged benefits of reaping the windfall from the black economy, our paper points out—and Grant can bring examples to bear—that these so-called gains that you get have not been obvious in countries that have introduced the GST. In fact, it is often an incentive to the black economy rather than the reverse.

I cannot talk on behalf of the welfare sector, but ACOSS will. In terms of redistributional issues, I think you need to bear in mind too the sentiment among a lot of my low income members about their predicament with the amount of disposable income when they are working. I do not begrudge social security recipients having a decent standard of living, but a lot of the people I represent argue that, at the lower end of the income scale, there is sometimes an incentive for them not to work—rightly or wrongly. That is the argument that is put. The adjustments have to be targeted to those who are finding it very hard to make ends meet, and I do not think this package does that in any way.

It does not compensate properly for all working people. Within its confines, the greatest beneficiaries are those at the top of the end of the income scale and not at the bottom. I think the solution to the problems you have raised philosophically is to retain a progressive tax system which taxes all income, whether it be through the pay-as-you-earn system or through other means of deriving income fairly, a tax system which has a minimum company tax that is above board so that all companies pay their fair share, and a system where tax minimisation, evasion and concessions to the wealthy are closed, with that money distributed back for the common good of all citizens.

Mr Belchamber—I can add to that. Senator Murray, your question goes to the heart of the issue of whether a tax package should be progressive or regressive in redistributional terms. Our answer is that it unequivocally should be progressive in its effect, delivering benefits to low income and poor members of the community and ensuring that those who are evading or avoiding their proper responsibilities pay more. The essence of this package is that it is regressive. The benefits go to the top end particularly, and the costs to low paid workers.

During the election campaign, a Treasury analysis of the package—claiming to show that the tax package is progressive—was given prominent coverage in at least one national newspaper. The analysis divided families into five groups of 20 per cent—five quintiles—and it compared the share of total tax paid by each of those quintiles in the population. It compared the share of tax currently paid and the share of tax that would be paid under the proposed new tax scales.

It claimed to show that the bottom 80 per cent paid a smaller share of the total tax take under the new package than they do at present and that the top 20 per cent pays a higher share of the total tax take under the new package than under the old. This was claimed to show that the package is progressive. But the issue of bracket creep is important here too. The relevant comparison to see whether the package is progressive is the share of tax paid by those quintiles under the current tax scales indexed. That should be compared with the share of tax to be paid under the proposed scales.

Getting hold of the unit record data to do this analysis on a family income unit basis proved beyond me, at least, during the last two weeks of the campaign but, looking at individuals, the picture is clear. When you adjust for bracket creep the picture is reversed. The share of tax to be paid under the new scales is higher for the bottom 80 per cent than would apply under tax indexation. The share for the top 20 per cent is lower under the proposed scales than would apply under the present scales, indexed. It is certainly within Treasury's capacity to do that analysis and that comparison but I have not seen it done.

Senator O'CHEE—Ms George, I probably agree with the sentiment in your last comment, that for low income workers it does not seem very fair that you can end up with less money than being on welfare. I think everybody would agree that that is something we have to eliminate. The reason for that, I think you would probably agree, is that frequently when you start to earn money you drop off some of the income support measures, don’t you?

Ms George—I think it is tied up with the whole issue of poverty traps. We need to get rid of the disincentives to employment that are so obvious in our current system, and I am not sure that the package goes far enough to do that. Yes, that is an issue, and I think it is the interaction between social security and the wage system. But what I am asking you to consider is that the federal minimum wage is now $373—that is $19,500. So between that and $25,000 there are probably about one million individuals or families that are trying to survive—in some cases, raising families on a single income—and they are the category of people who are going to be severely hit by the introduction of a regressive consumption tax. They are the ones who are struggling to make ends meet and they are the ones who will suffer the additional impost if this package goes through. They are the people I am trying to represent in the submissions I have made to you.

Senator O’CHEE—If we are going to deal with the interaction between the welfare system and earnings—you just said that is very important and I agree with you—then surely changing the taper rate is quite significant, isn’t it?

Mr Belchamber—The issue gets a sharp focus in the official papers on pages 42 and 52, where there is a cameo example given of Richard and Fiona. On page 42, in the break-out box, the example says that the return from additional work is not sufficient. Richard and Fiona have two children, Julie and Jack, aged seven and four. Richard is unemployed and works casual shifts at the local pub earning $120 a week. The pub owner has offered Richard a full-time position but, if he accepts, the family’s disposable income will increase by less than $47 a week, because they will lose some social security.

On page 52, we are invited to recall Richard and Fiona to see how much better off they are under the proposed package than under the current system. Under the proposed package, Richard is to work an extra 28 hours at an effective hourly wage rate of $2.50 an hour. The effective marginal tax rate is reduced from 85 per cent to 77 per cent in this particular cameo. At the bottom end of the scale, this particular package has a very small effect on changing the effective marginal tax rate that applies to people on low incomes who are presently working part time.

In terms of the transition from not working into working, it is not a very effective package. It has perverse effects on work incentives, on the other hand, for one of a couple contemplating a return to work after a period away, perhaps on child rearing. That is a point that was made, I believe, by Professor Dawkins.

Senator O’CHEE—It follows from all this that frequently a family has a principal income earner and another income earner who works part time. Because many of the benefits or allowances for having a family are based on the family’s income—we are talking about people with a just below average or round about average total family income—would you accept that, for those people, the effective marginal rate goes from 85.5 per cent down to 61.5 per cent?

Mr Belchamber—I am not going to comment on those particular figures without seeing the basis for them.

Senator O'CHEE—If it could be demonstrated to you that, for those people, the effective marginal rate goes from 85.5 per cent to 61.5 per cent, you would have to say that that is a big step forward, wouldn't you?

Mr Belchamber—I think the issue of effective marginal tax rates and work disincentives is most important in the movement from out of work to into work. The work incentive issue that you referred to may have some relevance to someone offered increased overtime. There may be some effective tax rate incentive issue there for someone contemplating working more overtime, but then there are the related issues of the adequacy of the income in total as a package and the additional stress on family life by having a principal income earner out of the home for extra additional longer hours each week.

Senator O'CHEE—We are also talking about a decision that somebody would make, for example, to go back into part-time work rather than not. That is a real issue many families face.

Mr Belchamber—With the issue of going back into part-time work, there is an example given by Professor Dawkins. According to his sums, a family with one child under five, whose gross earnings increase from $30,000 to $35,000 as a result of a second person entering work, ends up with about $3,900 in their pocket under the current regime. But, under the Howard-Costello plan, this family would receive only an extra $2,900 in extra net income. So, for the family such as you have described, the movement in effective marginal tax rates is perverse. It goes the other way.

Senator O'CHEE—Would you accept that a change in the effective marginal rate, from 85½ per cent to 61½ per cent is a good thing?

Mr Belchamber—Effective marginal tax rates are one consideration amongst a whole range of considerations affecting the decision—if it is available—to work or to work longer, to work more hours a week. It is one consideration.

Senator O'CHEE—You would not advocate a higher effective marginal rate, would you?

Mr Belchamber—I would advocate a consideration of the effect of the package over the range of incomes. When we look at the effect on low income families, reliant on social security or benefits, and the decision to move into work, this package is ineffective in reducing effective marginal tax rates. On the example I just referred to that Professor Dawkins had identified, the effective marginal tax rate under the package increases where one party is contemplating a return to work. It is the case, as you have mentioned, that, in some instances, particularly above $38,000 a year, which is above average weekly earnings—

Senator O'CHEE—Family income.

Mr Belchamber—Above that level, there is a greater reduction in the effective marginal tax rate because of the slashing to the top marginal tax rates that is included in the package.

CHAIR—Order! I have to call you to a conclusion, Senator O'Chee.

Senator O'CHEE—Mr Chairman, I have had less than five minutes of questions.

CHAIR—We divided the time between the parties. Before I called you, your side had used up all of its time. How your side divides its time is a matter for it. Because I have allowed extra time, I am now asked to provide extra time at the other end of the table. Unless we want to sit through lunch, I have to get some sort of rigour into this.

Senator MURRAY—I do not need extra time, Mr Chairman.

CHAIR—No, but I had a request from Senator Sherry and Senator Campbell for one extra question. I understood you had only two extra questions and I think you have had six extra questions.

Senator O'CHEE—Mr Chairman, I have had five minutes of questioning. If you want to cut the questioning short, well, that is your decision.

CHAIR—It is my decision.

Senator O'CHEE—If we have to cut it short, then just cut it short. Cut it off.

CHAIR—That would be unfair in terms of the balance of questioning each side of this table has had. I call Senator Sherry.

Senator SHERRY—There was some discussion earlier about the very brief period of tax indexation that this country enjoyed. I think at least some of us remember when the current Prime Minister, Mr Howard, was Treasurer prior to the 1977 election and the 'fistful of dollars' and what happened to that nine months later.

I would like to put this scenario to you in that context. Let us assume—from my point of view, unfortunately—that this package goes through the Senate. With or without food, let us assume it goes through. The tax cuts that are delivered are delivered substantially because the budget is in surplus, not because of the GST. At some future date the economy either goes into recession or at least growth rates decline significantly, the budget goes into deficit, and the government is required to make a combination of decisions involving tax increases or cuts in expenditure. Let us assume that scenario, which I think is at least a reasonable scenario at some time in the next three, five or 10 years. Who do you think will suffer most as a consequence of decisions having to be made to put the budget back into surplus when that happens?

Mr Belchamber—Can I say, firstly, that the downside, if I can call it that, on the deficit is magnified when one considers the alleged black economy savings that are included and the so-called efficiency dividends which are claimed for the package. When one allows for those, the effect of the promised tax cuts on the deficit is much greater and the rate at which the surplus is run down or the deficit is run up is much faster.

Who loses in that circumstance? It depends on what policy measures are taken. If growth slows, job opportunities slow. If services are cut, it is essentially the people who rely on provision of services from the government who have their living standards reduced directly through the reduced availability of services.

Senator SHERRY—Would that be low and middle income earners?

Mr Belchamber—Overwhelmingly.

Senator SHERRY—You cannot see the prospect of taxes being increased for higher income earners?

Mr Belchamber—Not by the present team.

Senator SHERRY—I will leave it at that.

Senator O'CHEE—In this document, and in table 1, you talk about indexation and compensation for bracket creep at a notional rate of 20 per cent for a period from, say, 1993 to 2000. But the bracket creep itself is measured by increases in wage rates, isn't it?

Mr Belchamber—No, it is the increase in average earnings.

Senator O'CHEE—The consequence is that, if you argue for a wage increase to compensate for the effect of bracket creep, you are asking for a wage increase to compensate for the effect of previous wage increases, aren't you?

Mr Belchamber—We are asking for a wage increase to ensure that people do not go backwards in their rightful entitlements and do not suffer increasing tax burdens by virtue of a failure to index the tax scales.

Senator O'CHEE—But, as soon as you increase the wage rate, you take a whole heap of people who might be below a given margin and carry them above the margin.

Mr Belchamber—As I mentioned before to Senator Ferguson, the effect of bracket creep does not arise only when a worker moves from one tax bracket into another. So long as you have a progressive rate scale, it affects everyone in terms of the average tax payable at any given income level.

Senator O'CHEE—If you are going to talk about adjustment for bracket creep, isn't it a bit unreasonable to say to a government, 'We expect you to compensate for all bracket creep over the last seven years, all of a sudden and in one go,' when that was not a demand on the previous government?

Mr Belchamber—We are talking about the proposed new tax package. The claim has been repeatedly made that everyone is a winner. It is simply not the case.

Senator O'CHEE—Why don't we talk about bracket creep over the last 18 months to two years?

CHAIR—Let us not debate it. You have asked the question. Let us hear the answer. I wish then to conclude this section of the hearing.

Ms George—It is our view that we ought to put hard data to you on objective grounds to show that the claim that everyone is a winner is fallacious, and that, secondly, the 1.9 per cent, which is a conservative assumption, is not properly compensated because, as we show in these figures, the compensation offered currently is not even adequate to make up for bracket creep since the early 1990s, let alone even look like covering the 1.9 per cent assumption. It is well short of what it would require on any general assumption that the CPI impact might be between three per cent and four per cent.

From the point of view of the ACTU, we have looked at the package against general economic criteria and found it wanting in terms of employment, in terms of the overall impact on GDP and in terms of inflation. This alleged claim that the compensation makes everybody a winner is absolute nonsense. The people I represent will be losers under this claim and, to the extent that I and other unionists have a responsibility to protect the real living standards and real wage rates of those people, that will continue to be a primary objective that is pursued. Clearly, the case that will be put to the membership of unions is that, under this package, they are the losers if they are earning $45,000 or less.

CHAIR—I remind members of the inquiry that they can put questions on notice. I ask the ACTU that, if questions are placed on notice, they be kind enough to answer them. I also observe that this is phase 1 of our inquiry into the macro-economic effects. After we report on this, we go into phase 2 of our inquiry. I ask—I am not soliciting—whether the ACTU would be available for that part of the inquiry if senators felt they wish to pursue this matter further?

Ms George—Certainly.

CHAIR—The committee will now adjourn for lunch.

Proceedings suspended from 1.10 p.m. to 2.08 p.m.

DAVIDSON, Mr Peter, Senior Policy Officer, Australian Council of Social Service

RAPER, Mr Michael William, President, Australian Council of Social Service

ACTING CHAIR (Senator Ferguson)—I welcome Mr Michael Raper and Mr Peter Davidson. We have your submission, Mr Raper, and I invite you to speak to the committee on your submission and afterwards we will have questions.

Mr Raper—Thank you very much. We appreciate the opportunity to address this Senate committee on the basis of our submission. Could I just clarify that my colleague here on my left, Peter Davidson, is not the Social Policy Adviser as shown on your list but Senior Policy Adviser at ACOSS and is thankfully a bit of our corporate memory on these issues, having been around since the 1985 tax reviews through to 1993 and onwards.

From the outset—and I will come back to this issue—I wish to assure this committee that the story in the Melbourne *Age* earlier this week was based on a leaked copy of the document—or parts of it; I do not know. I just wish to assure the Senate that we are well aware of the limitations on Senate submissions and we certainly did not leak that submission. I do not know who did. I do not know where it came from, but I wish to assure you that that certainly was not leaked by us. You might understand that because the *Age* drew different conclusions to our conclusions, and I am sure you would see that. I will come back to that point.

We also, by way of opening, note that we understand the scope of today's submission goes to the questions of modelling. In our view it does not go to all the other issues around this whole complex and comprehensive package. We have put in a submission to the business tax inquiry. We are putting in a submission to the community affairs committee dealing with the issue of the impact on charities. We are putting in a comprehensive submission, for which we have been given a week's extension, dealing with the whole package—the income tax cuts, the federal-state financial relations, the GST and how it all fits together. Therefore our comments today we are addressing particularly to the first part of this inquiry, part A relating to the questions of modelling.

I also need to stress that we do not come here with any unique piece of original research or some sort of comprehensive model that provides a knockout proof or a knockout disproof of anything. We come only with our analysis; with our experience; and with our best endeavours to genuinely unpack this, to genuinely assess the likely impact of the proposed GST on low income earners and whether or not the proposed compensation is, firstly, structured properly and, secondly, adequate. That is what we have come here to try to address in a genuine and objective way, based on our real life experience and on the real life experience of low income earners, pensioners, sole parents and unemployed people. They are the ones we endeavour to give voice to.

The government, as you know, have proposed a package of tax reform. They have claimed in that package that everyone will be better off. That assurance is based on a compensation package and on a number of cameos of different effects for different people all saying that they will be better off. As you know, the compensation and the cameos are based on Treasury modelling of the effects of the changes that are likely to come about from the

GST on household living costs. Modelling, therefore, is very important in our view: it is very important that it be accurate; it is very important that it be objective and not designed to reach some preordained conclusion.

In our view the modelling must pass two key tests. One is that it should overestimate the impact—not underestimate it, not guess it, not average it but overestimate the impact. There are two reasons for that. One is trust. The government have given assurances here. They have given assurances to low income earners for whom $2, $3 and $4 a week mean a lot. Those amounts make a big difference to their budget which they determine on a daily or weekly basis. So there is that trust question. Trust in government, trust in the assurances is very important. It behoves us all to get it right. Secondly, it has to be an overestimate because modelling, as you know, is unreliable. It is based on a number of assumptions—best guesses, best estimates—nevertheless, it is modelling. It is that. It has in-built unreliability.

The second test it should pass is that it should take account of differences, real life experiences: differences between people, different family sizes, different compositions, different types of households, different income levels, different expenditure and savings patterns, and the fact that low income earners spend more than they earn very often. I will come back to that.

On those two tests the Treasury model fails. In the summary on pages 2 and 3 of our submission—and I invite you to turn to those—it is very clear in what way the Treasury model fails. It underestimates the effect of consumption tax changes on the living costs of low income households by comparison with other households, it overestimates the effects on high income households by comparison with other households and it underestimates the average effects overall.

I will come briefly to the *Age* article to which I said I would return, because perhaps it sharpens the focus of the issue before you and the issue as we present it. It goes to the heart of a number of issues. I would have to score the *Age* high on numeracy but very low on literacy. They have taken the table on page 8 of our submission—to which I draw your attention—and looked at the last column. They have simply said, 'All those figures are under four per cent. The government said four per cent. Whacko, everybody is okay. ACOSS has not proved anything. They have not proved that anyone is worse off.'

For a start, the onus is not on us to prove that. I put it to you that the onus is on the government to satisfy the population generally and low income earners who live on the edge financially from day to day. First up, the onus is on the government to satisfy. Secondly, we would put it to you that these figures show a number of very significant things and prove the points that we have said from one week out from the time that the government brought down its package, when we queried the Treasury modelling and the assumptions that it made.

This chart shows a number of things. One, the Melbourne Institute uses a different CPI figure—2.5 not 1.9. Somebody else is saying that the 1.9 is at least conservative. Secondly, it shows that if you look at the different households and different types of household you get a different effect, and that effect ranges from 2.8 up to 3.6. That is a long way from 1.9. That is very different from 1.9, a significant percentage difference from 1.9—30-odd per cent variation at least in places.

Thirdly, that figure is still an average. If it is an average, then it is conceivable that the effect ranges from somewhere about one per cent to possibly up to five per cent. A three per cent average could have 50 per cent on one and 50 per cent on five. The fact that it is an average must be taken into account, and averages will always suffer. Therefore, you have to make sure that your compensation goes way up to the top end of the likely effect and is not satisfied by sitting on the average.

Fourthly, the government itself acknowledges the need for a buffer zone because of the fact that there are averages, because of the fact that modelling is in itself unreliable. The government's buffer zone is 1.5 per cent. If you put 1.5 per cent on those figures or on that range, you are way out of the area of 1.9 per cent. We cannot put a figure on it. We have not put a figure on it. We have not come before you with a series of cameos and individual files, although our file back at the office is this big with individuals writing in to us giving us their budgets and showing us what they believe the effect is going to be. I do not think that is the issue.

This is a much more serious issue than whether or not somebody can roll out 13 or 50 cameos, or 16, 60, 100 or 600 different individual budgets. We can do that. That is not the issue. The question here is: what is the overall effect? How is this going to affect people—especially low income earners? The Melbourne Institute obviously uses different assumptions and shows, I think, the validity of so doing and the need to do so.

So what do we say needs to be done about this problem? The Treasury model is inadequate, the figures therefore are highly questionable and the government cannot honestly assure low income earners that they are definitely okay. The first thing we believe must be done is to fix the structural flaw at the core of the package, to remove the heavy reliance on compensation that this package demands—that is, to remove food from the GST. There is no justification for food at the heart of this package when this package raises some $6 billion more in GST revenue than the consumption taxes that it replaces. It is that tax mix switch, that massive increase in consumption tax, that is actually at the core of the flaw in this package and is why, under this package, low income earners would need to rely far too heavily on compensation in the first place.

We have only to look across the Tasman to New Zealand. As you know, the New Zealand government introduced a 10 per cent GST in 1986 which included food, and compensation was provided to low income households through both the tax and the social security systems. Two years later, during a severe downturn, as I understand, the GST was raised to 12.5 per cent with no increase in compensation. Two years later, with the economy then in recession, social security payments were cut by between five and 30 per cent.

How could any low income earner rely so heavily upon, or be required to take the risks involved with, a compensation package that is based on questionable modelling and assurances that it will remain there forever, when the example across the Tasman—as close as that, and there is a pattern internationally to that effect—shows that that cannot be relied upon? Our first and primary conclusion is that food has to come out of the package.

The second goes to our recommendations on pages 4 and where we call on this Senate select committee to commission its own modelling. We do not believe that we should rely on any one model or any one set of modellings. You need to have before you a range of models that examine a range of different assumptions and possibilities, as we do. We are in the same position as you. We do not have the evidence before us to be certain. We cannot say to people who ring ACOSS week in, week out that we can be certain that this compensation is adequate, that the package is going to be okay. We cannot give them that assurance, and I put it to you that neither can you and nor can the government.

We need independent modelling. We therefore call on this select committee to undertake that, as per our recommendation 1. Recommendations 2 and 3, which I will not go into, elaborate on that, and call for Treasury to undertake a sensitivity analysis and for the Australian Bureau of Statistics to undertake research and analysis to improve the HES.

We acknowledge the HES has problems, but it seems as though Treasury is saying to us, 'We know that our model has problems.' All the experts know that that model has problems, and Treasury is saying, 'We would rather rely on that modelling which we know has problems rather than on other modelling which may have some problems, which is not 100 per cent, which is not as good as we would like it.' We would rather rely at least on other modelling which is a lot better, in our view, than the current Treasury modelling.

ACTING CHAIR—Senator Murray and Senator Gibson have to attend another committee meeting briefly for about half an hour and may or may not be able to ask questions. If they are not back in time, Senator Murray has requested that he put some questions on notice to you.

Mr Raper—That is fine, thank you. Senator Gibson explained that this would be happening.

Senator O'CHEE—Mr Raper, when you first saw the package, you raised certain queries about the way Treasury were going to model this. One of the things you asked was that Treasury release the HES data set that was used, didn't you?

Mr Raper—Yes.

Senator O'CHEE—That has been done. That has been used by the Melbourne Institute in the modelling that is included in your submission. Is that correct?

Mr Davidson—I believe the Melbourne Institute used the HES directly rather than relying on Treasury work. That is my understanding.

Senator O'CHEE—One of your concerns was that you thought that HES was more useful. That has been used by the Melbourne Institute in this modelling. On page 8, a table offers four assumptions across the page. Assumption A is a Treasury assumption of 1.9 per cent. Then you say,'Let's take the Treasury approach but let's say inflation is another half a per cent higher—2.44.' Then you say in assumption C, 'Maybe that is not enough. Maybe we need to go further. Let's assume that inflation is higher than what Treasury forecast and we will run it through the HES data set as well.' Is that correct?

Mr Raper—Essentially, yes.

Senator O'CHEE—Your final assumption is, 'Maybe that is not enough either. Maybe we need to go further. We will assume a higher inflation rate. We will run it through the HES data set and then we will adjust it because we believe that somehow solves dissaving. That is basically what assumption D is. Is that correct?

Mr Raper—Yes.

Senator O'CHEE—On table 8, we have a range of possibilities. Would you say that assumption A—1.9 per cent—is conservative?

Mr Raper—Yes, based on the expert opinions.

Senator O'CHEE—You would accept that the other end of the range is assumption D. It gets progressively worse all the way through. So A is at one end and D is at the other end of a range of assumptions. Is that correct?

Mr Raper—Yes.

Senator O'CHEE—And then what you have done is you have gone through and said, 'Let's accept the other extreme, not the Treasury view. Let's accept the most dismal possible projection,' which is D. Then in the fifth column, you have analysed the change in terms of percentage of disposable income, accepting the most dismal set of projections. Is that correct?

Mr Raper—In this range, yes. There are more dismal projections possible.

Senator O'CHEE—Let us go through this, because this is the modelling that you people decided to use. A single age pensioner, under the most dismal range of projections that your modelling could come up with, has a 3.3 per cent increase in disposable income. Is that correct?

Mr Raper—In this table, you are reading the correct figure, yes.

Senator O'CHEE—So that is less than the four per cent compensation?

Mr Raper—Correct.

Senator O'CHEE—An age pensioner couple, similarly at 3.3 per cent, is less than the four per cent compensation.

Mr Raper—To save you the trouble, all of the figures in that right-hand column are less than four per cent.

Senator O'CHEE—So every one of the groups that you have constructed under the most dismal circumstances in your range of projections—you have four ranges here—is less than four per cent?

Mr Raper—Correct. Without agreeing with your premises necessarily—but I will come back to that—essentially, yes, all those figures are under four per cent.

Senator O'CHEE—And that is using the modelling that you put together, or you had put together for you.

Mr Raper—No, let us correct that point: this is Melbourne Institute modelling; it is not our modelling. We do not have the capacity to do modelling. We have the capacity to do analysis.

Senator O'CHEE—You are relying on Melbourne Institute.

Mr Raper—This is Melbourne Institute. Melbourne Institute did the modelling and published the modelling. It did not publish everything in their modelling, but we asked them to provide to us other bits of their modelling that were not published initially, and that constitutes assumptions B, C and D. It is Melbourne Institute modelling, yes.

Senator O'CHEE—It is Melbourne Institute modelling, with assumptions that were not previously published which you have added in, because you accept the fact that that is going to give you the biggest margin of error.

Mr Raper—Certainly not to achieve a preconceived end.

Senator O'CHEE—No, I am not saying that. I am saying that, to give you the biggest margin of error, you have added in all of those factors.

Mr Davidson—That is not correct. The only difference between this data and that which was previously published by the Melbourne Institute is that we asked them to extract the numbers for pensioner and beneficiary groups. This is based on the same data set using Melbourne Institute assumptions—not our assumptions. A, B, C and D are all Melbourne Institute assumptions. It is simply extracting some additional figures relating to particular groups, because their previously published data had income ranges for different family types. So that is all we have done. We did not commission that research. We did not have any input into the assumptions made. We did not rely exclusively on a single piece of research. As Michael indicated earlier, and as we say right up the front of this submission, you cannot rely on a single piece of research.

Senator O'CHEE—So what we have here—

Mr Davidson—Is a piece of research.

Senator O'CHEE—A piece of research, where you have asked them to extrapolate it for given income groups who are predominantly in receipt of government benefits.

Mr Raper—That is right.

Senator O'CHEE—So they put it together for the groups that you asked them to put it together for.

Mr Raper—Yes.

Senator O'CHEE—And in every one of these groups the change is less than four per cent.

Mr Raper—The average change—

Senator O'CHEE—Is less than four per cent.

Mr Raper—Yes, but I stress that it is the average.

Senator O'CHEE—But when we talk about modelling, the whole point is to get a data set which is objective. You have said, 'We've got to use something which is objective,' and you have used the word 'objective' over and over. Surely, you have asked them to do this because you believe that would give an objective measurement of the impact on these household groups. Is that correct?

Mr Raper—It would give another modelling measurement, yes.

Senator O'CHEE—An objective measurement?

Mr Raper—To the extent that any of these figures are objective.

Senator O'CHEE—This is objective.

Mr Raper—I do not see the particular point but, yes. Nobody is subjectively analysing these figures, if that is what you mean.

Senator O'CHEE—So, if a lobby group were to come to me and say, 'Look, we've run the figures by the groups of people that we represent, and here they are,' you could understand why I would say, 'Yes, the government is over-compensating these groups of people,' because the compensation is more than the range of impacts that you have been able to model.

Mr Raper—Senator, how do you address the average question that I have raised? This is a range by definition. Intuitively, you must be able to work out that, if it is three per cent, that could be a range from one per cent to five per cent. That is the point about an average. How can you be satisfied with an average if somebody perhaps were on five per cent? And how do you then address the question that the government itself acknowledges the need for a buffer zone in the order of 1.5 per cent? If the figure, therefore, is out at the extreme end of the average, then the 1.5 per cent buffer zone is not there, so this would be inadequate.

Senator O'CHEE—Mr Raper, the 1.5 per cent buffer zone is 1.5 per cent above CPI. You have assumed that CPI is 2.44.

Mr Raper—The Melbourne Institute has come at that figure.

Senator O'CHEE—Okay, the Melbourne Institute. If the assumption is that CPI is 2.44, 1½ per cent over that still does not come to four per cent. We are still over-compensating. The simple question I ask you is this: if a lobby group comes to me and says, 'Here is the modelling that we are using, and for every one of these household groups the result is less than the amount of compensation,' then it is perfectly reasonable for me to say, 'Well, I do not understand why that lobby group would ask for more, given every assumption that they have made falls less than the compensation range.'

Mr Raper—I will give you a number of reasons. A low income earner cannot afford to be $3 out in their weekly budget. They are right to the extreme already. There is already $23 million provided by the Commonwealth government each year in emergency financial assistance. That is estimated to be some 10 per cent of what is given out by St Vincent de Paul, the Salvation Army and other charities throughout the year. That is some $230 million at least just on emergency financial assistance that is going out each year. That is $230 million of dissaving. That shows that low income earners—and our emergency relief survey data shows that these are primarily unemployed people, sole parents—have to live beyond their means, and we already know that age pensioners live beyond their means or, at least, that they dissave because they are drawing down their savings.

Senator O'CHEE—Which is already taken into consideration in assumption D.

Mr Raper—If you take all of that into account, and you come up with averages of 3.6, let me put it back to you: a lobby group could come to me, as the government, and say, 'We are extremely concerned on behalf of low income people, pensioners and the unemployed'—that is, those who actually will get the compensation, and I will come back to the point about the large and increasing number of people who do not even get the compensation, like newly arrived residents in their first two years, unemployed people in their waiting periods, the increasing number of waiting periods. We do not take into account special atypical expenditure patterns here of people with disabilities and the need to cover off those things.

But if I came along to you as a government member and said, 'I am very, very worried about the fact that there are figures here that show up to 3.6 as an average, and you are trying to tell me that your 1.9 per cent is okay, that that is safe for the people that I represent,' I, as the government, would want to be sure that we pitched the compensation at the top end of that scale—not at some average, not at the bottom—to make sure that low income earners, who cannot afford to be even a couple of dollars a week out, were fully compensated and not running the risks that these figures would indicate that they are being invited to take.

Senator O'CHEE—You have put the proposition to me. All I observe is that you have come here with a range of figures. The most dismal figure in every group, in the range that you have, is less than the compensation that we have put on offer.

Mr Davidson—The point about the 1.5 per cent buffer picks up on Mr Raper's point and expands it a little. In every major consumption tax package over the last 15 years or so—there have been two of them—it has been accepted by those putting it forward, and widely accepted amongst expert opinion, that you have to over-compensate low income people. Compensation should not operate at the edge of the average price increases faced by different groups of low income people. There has to be an adequate buffer. One of the main reasons for that is the average problem to which we referred. The government has, in principle, accepted that proposition in putting forward a 1.5 per cent CPI buffer, but that is inadequate because it is based upon the average CPI rise and not the increase faced by particular groups.

With assumption D, for a single age pensioner to have that 1.5 per cent buffer, the compensation would have to be to the order of 4.8 per cent; for an age pensioner couple, to the order of 4.8 per cent; and single, work force age or unemployed to the order of 5.1 per cent—all of which are well above the four per cent figure and also well above 2.4 per cent plus 1.5 per cent. There is not enough margin for error. There is not enough of a comfort zone between those 2.8 per cent to 3.6 per cent numbers and what is being offered by the government in compensation.

It is a compensation package that, on these numbers, runs very close to the wire. If these numbers in assumption D were correct, then it would be inevitable that large numbers of people would be worse off. It would be inevitable because large numbers of people will have above average effects within each of those groups.

That is precisely why in 1985 and 1992 it was taken for granted that compensation should be adequate to provide that buffer. In fact, the word ‘over-compensated’ was repeatedly used in the debate. This is not over-compensation; this is very close to the wire on those numbers, which is one set of research we have taken for consideration, and not the final word, by any means.

Senator FERGUSON—Going on from Senator O’Chee’s question, when the package came out it was based on the Treasury’s model with the 1.9 CPI, which you did not accept. You asked for the release of the household expenditure data, which Treasury did, which you still did not accept. You then commissioned your own modelling, using work from the Melbourne Institute. I remind you, Mr Raper, we are talking about modelling today so we have to be looking objectively at what is in front of us. In the modelling that you have put forward in this submission to us, in none of those scenarios is there a greater than four per cent increase. In other words, in relation to the compensation under your own modelling—three sets of modelling: two that you have rejected and one that you have commissioned yourself as an additional modelling—none of those come to over four per cent.

While I acknowledge the concerns you quite rightly raised about people on the margins of these figures, you must logically accept that, under the modelling that has been put to you, which you requested—modelling done by the Treasury, by the household expenditure survey data and by your own modelling—according to these figures, your own figures in this submission, in general poorer people will be better off under this tax package than they are today.

Mr Raper—Senator, I have to repeat: we do not accept that conclusion.

Senator FERGUSON—But these are your figures.

Mr Raper—They are not our figures.

Senator FERGUSON—They are figures that you have put in your submission.

Mr Raper—Certainly. They are the Melbourne Institute figures, and it is the Melbourne Institute modelling. I repeat: it is not ours and it is not commissioned by us. However, that aside, we cannot draw that conclusion, we do not draw that conclusion and we do not believe it is open to you to draw that conclusion from these figures.

Senator FERGUSON—If you are using modelling, we can only go on what you have put in your submission.

Mr Raper—That is correct. There would be little point, it seems to me, in repeating either my answer to Senator O'Chee or Peter Davidson's further clarification. It would seem to me that you are ignoring the fact that these are averages. You cannot ignore the fact. It is not honest. It is not open to ignore the fact that these are averages and that, by definition, means that there is a range. Those at the top end of that range, by definition, will be worse off, and low income earners cannot afford to have that risk. They cannot afford to take that risk, nor should any government require them to take that risk. It means that they are out of pocket and down the tube at the end of the week. It is food on the table.

Senator O'CHEE—I think we are letting emotion get a little carried away. By definition, a person is not necessarily outside the range. You said, 'We are here today to talk about modelling.' On modelling, you have to accept the fact that this modelling means that the average low income earner is better off with this package in place than they are at the moment. The choice is whether they are better off after the package comes in than they are now. I do not think, being intellectually honest, that you would say to me that these groups of people will be worse off after the change than they are now, because their real disposable income does go up.

Mr Raper—I repeat: I do not accept that conclusion, for the reasons I have given.

Senator O'CHEE—So you would say that we should not bring in the package, and these people will not get a four per cent increase in income even, though their increase in spending is only 3.3 per cent?

Mr Raper—Those are not the conclusions that we have reached. We will put the whole package together and give you our comprehensive conclusions about the overall package, what needs to be done to it and what should be done. I run the risk of repeating myself. Peter would like to have another go at that explanation.

Mr Davidson—On this 'average' point, we can agree or disagree that, on average, low income people are better or worse off, but I do not think that is very helpful or informative. Low income people, on average, could be better off while one-third of them are worse off. This 'age pensioner, single' category, includes over one million people. To say, on average, that those one million people are better off does not go far enough, in our view. We did not publish this data to provide a final word on the effects of the package on low income people; it was to demonstrate the difference that different assumptions can make to the outcomes.

We are urging this committee to commission modelling which goes into a great deal more detail than this. I would like to know how the bottom 20 per cent of single age pensioners are affected, the second 20 per cent and so on, and similarly with unemployed people, sole parents and so on. I do not think you can use this data and nor did we intend to. I apologise if the impression was given it is the final word on the effect of the package on low income people.

Senator O'CHEE—Do you agree on average that poorer people are better off according to your results?

Mr Raper—I go back to the word 'average'. You ask us to agree on average, and we say that average is not helpful because if it means a million people or whatever number of people are worse off, then it is incumbent on the government to ensure that that does not happen. So you can ask the question about averages, but that is not the issue.

Senator O'CHEE—So you are saying that we should just throw it all out.

Mr Raper—No; get it right. Do not throw it out. Get it right.

Senator O'CHEE—You admitted that this is the most dismal range of assumptions you could come up with.

Mr Raper—No, in your words they were the most dismal, Senator. I am sure there are much more dismal scenarios that could be put together. We have said that you should not be relying on one set of figures, that we need to actually commission others. We need to have a range. We need to look in a much more comprehensive and sophisticated way. What we have before us is one set of inadequate figures which certainly demonstrates a big difference from the other set of inadequate figures, and we need to get a much more comprehensive set of figures. As Peter says, it does demonstrate that there are differences, but I urge you to take account of the points that we have been making about averages and that it does not help us if we simply continue to argue around that when an average demonstrates that there is a range. If you fail to take account of that, it is not helpful.

Senator O'CHEE—If you have a whole heap of poor people and you have the opportunity on average to make every group within that range of poor people better off, are you suggesting we should turn our back on that opportunity?

Mr Raper—No, I say we should take the opportunity to make sure that everybody in that group—not just that group on average, but everybody—is better off. This tax reform is not there to simply reward high income earners—and we are certain about that. It is there, presumably—I would have thought, primarily, first up—to address the problems of low income earners first and foremost—and all the others, yes, fine. To expect low income earners to be the ones that are at risk is inconceivable.

CHAIR—I am back in the chair. I apologise for my absence earlier, Mr Raper. Before I ask Senators Conroy or Sherry to put questions to you, I will ask a couple of fairly straightforward questions. Yesterday we heard from the Business Coalition for Tax Reform. We have heard other people from time to time—I do not mean this pejoratively—including

VCOSS, speak for your organisation or refer to your organisation and its position. Indeed, even this week, such an elevated figure as the Treasurer, I think, did so. Can you tell us straightforwardly and plainly where you actually stand in terms of this package? Do you support it or not? Do you support it with significant amendments or minor amendments? Exactly, what is your position?

Mr Raper—I will do that in summary, but note at the outset that the full position will be very clearly set out in our comprehensive submission next week.

CHAIR—I just note that there is a titanic struggle going on to put words in your mouth. I would like to hear them from your mouth.

Mr Raper—I am very pleased to have the opportunity to do so. Subject to finalising the details in the next day in our large submission, it is clearly this: we believe that there is a need for tax reform. We believe that revenue is at risk—in fact, revenue has declined. We believe that that tax reform needs to be comprehensive on the income tax side, on the consumption tax side, on the business tax side and in federal-state financial relations. We believe strongly that, in all of that, we also need to address the situation of families and the poverty traps that have been addressed. The package that the government has put forward addresses a number of those things, but there are substantial problems with the package and substantial modifications that need to be made to this package in order to get a balance between equity and efficiency.

In the past, we have published our views, our benchmarks and what we believe tax reform needs to be. We have published our own agenda. We have measured the government's package against our agenda. It comes up deficient in a number of ways. We believe it needs to be modified. We have published those modifications. We will repeat a list of those modifications in our submission next week, but it should be evident from the evidence I have given to date that at the core of this package is an increase of some $6 billion in consumption tax. There is a reliance on food, which you could identify as at least $5 billion of that $6 billion. Food in the package creates enormous difficulties because it is 25 per cent. It constitutes 25 per cent of the expenditure of low income earners each week. Food needs to come out of the GST. The tax mix switch or the extra reliance on consumption tax of some $6 billion needs to be removed. If you need to fill that gap, we need to examine ways and we will put forward a number of ways that that can be done such as to demonstrate that the package does not unravel if you take food out.

CHAIR—We are senators who, at the end of this process, will have to vote and shift our bodies from one side of the chamber to the other according to the proposition before the chair. We have to make a decision. If the changes that you seek to the package are not agreed by the government—bearing in mind what the government has said about changing its package—do you support the package or don't you?

Mr Raper—If there are no changes?

CHAIR—If the changes that you seek are not made—you might have gradations of them, of course; but if the principal changes, the core changes, that you seek—these are my words; I am not trying to put words into your mouth—to bring fairness, equity and justice to this package are not agreed, where do you stand—for it or against it?

Mr Raper—If we do not make substantial progress, if there are not substantial changes, then we could not assure low income earners that they are better off under this package.

CHAIR—Therefore, if you were in my shoes and had to shift your body from one side of the Senate chamber to the other on a question of whether you vote for this bill or not, what would you do?

Mr Raper—I would be urging that you put the interests of low income earners foremost in your mind—not only, but foremost at least—because they are the ones who can least afford to be damaged by this package. That is not to say that we do not need tax reform—I think our interest in the subject, our preparedness to embrace tax reform and our record on that should be clear—but not at any price.

CHAIR—Not at any price?

Mr Raper—No.

CHAIR—I just want to be careful about this because it is, to me, an important point. Does that mean yes or no when it comes to the question? I mean we have to answer the question at the end of the day and, with no disrespect, would you mind answering it for your organisation? If the amendments are not there, would you vote for it or wouldn't you?

Mr Raper—It is a hypothetical, as you know, given that—

Senator FERGUSON—You do not get a vote.

Mr Raper—We do not get a vote, that is for certain. In two or three months time, who knows what further modelling might be able to give us—what evidence we may be able to base it on—and I hope there will be much better evidence so we can actually make that decision.

In many respects, there is great progress in this package. Certainly we have identified the proposals in relation to poverty traps, which are well overdue, and the move towards bringing services into the tax base but, unless there are substantial progress and substantial changes to this package, low income earners have far too much risk and we would not support the package under those circumstances. I hope, however, that there are changes that can be made so that we have sensible tax reform, so that we do ensure our tax revenue base for the future, which we believe strongly that we need, in a way that does not put at risk low income earners, pensioners, unemployed people and sole parents.

CHAIR—I will try to make a statement to see if you agree with it. Please correct it if you do not, because I think there is a lot of mangled language out there, and people looking for headlines or short grabs sometimes get it wrong. I do not reflect blame or guilt on anyone, but this is a public debate fiercely contested over a serious issue. If I were in a position of talking to you on behalf of the government, would I regard those remarks as meaning that you would want the core of your package but that you are not going to die in the ditch if you do not get every damned part of it?

Mr Raper—Sorry, I need to clarify that.

CHAIR—I understood you to have said that, firstly, you hope it changes. Let us all agree with that. The proposition I am putting is that the government has said that, at the end of the day, it is not going to change. We can be cynical about that or not, but that is what is before us and that is what we have to deal with. You want to make the changes that you are seeking—that there is some sort of cut-off where you might make acceptable progress. As far as that is concerned, you would buy the outcome, but there is a point beyond which you would not go to buy the outcome. Is that what you are saying?

Mr Raper—Possibly. That is substantially correct. We do not have to face that just yet, thankfully, because there is a long way to go. This is the beginning of what we consider to be the debate process around tax reform. It is by no means the end. We think the process was very regrettable—that there was no public debate during the time when the package was put together. This is the beginning of the debate, so we hope that much more will come out, that there will be much more evidence on which we can base that final decision, but there are some fundamentals that we are seeking.

Senator FERGUSON—Mr Chairman, can I clarify one point of Mr Raper's answer to you?

CHAIR—Yes.

Senator FERGUSON—Senator Cook asked you a question about the existing package. Can I take it from what you said in your answer—and I think I am right—when you said that you support the taxation of some services, that you have no objection to the principle of a goods and services tax replacing the wholesale sales tax system provided the people that you represent are better off?

Mr Raper—That has been our position, yes. That is fairly accurately put. We have never been opposed to a GST, per se. There is no such thing as a GST anyway. It depends on the rate, it depends on what is in it, it depends on the base, it depends on what is out—all of those issues. It depends on the compensation and a whole range of those issues. We have never advocated a GST either.

We have been prepared, however, to examine the need for tax reform because of our concerns about revenue—I have already said that that included income tax and all the others—and that includes the examination of a consumption tax. We acknowledge the evidence that we have before us that the consumption tax base is at risk because of the shift in consumption towards services and the decline in consumption of goods. Historically, that trend is there. It has been pumped up over the years because of increases—for instance, the increase in the rates of the wholesale sales tax in 1993, which had a very serious effect on low income earners. We are anxious to avoid that happening again, because there was no compensation in the hiking of the wholesale sales tax rates in 1993.

We do understand the need to embrace services, but we do not understand the need for a goods and services tax to have a negative impact on low income earners—that if you structure it correctly and build compensation after you have structured it correctly with adequate and appropriate compensation based on a good range of models, then, yes, we have never been opposed to that need. In fact, we believe it is part of overall comprehensive tax reform.

I will add to that—I know the way these statements get used. We have always argued for comprehensive tax reform. Let me stress that that means closing down loopholes and shelters on the income tax side. That is our primary concern, in fact—to close down those loopholes and shelters to restore the integrity of our income tax base, which is still our primary source of revenue. One of our biggest concerns with this package is that the government has not gone anywhere near far enough towards closing down loopholes and shelters and restoring the integrity of the income tax base. It is hard for anyone to really believe in the overall package when they have not been prepared to do that and to firstly restore the base there.

Secondly, we have argued for business tax reform in the context of all of the other reforms—that is, income tax, consumption tax and federal-state financial relations—yet we fear that that is now drifting out to a report date of 30 June. We are asking for business tax to be reviewed and for the government to acknowledge that these things should be brought back together and kept together.

Senator FERGUSON—You have clarified the position. It was really a clarification that you do not oppose the GST in principle. Senator Cook is talking about people moving from one side of the chamber to the other, when in fact the position of the opposition is opposition in principle to the goods and services tax. I wanted to make it clear that that was not your position.

CHAIR—I will speak for myself, thank you very much.

Senator FERGUSON—The Labor Party's public position is that they are opposing in principle.

CHAIR—The Treasurer says that he does not give a damn what this inquiry finds. If you want to trade in absolutes, we can trade in each other's absolutes.

Mr Raper—We certainly do give a damn about what this inquiry finds.

CHAIR—I think you give several damns.

Mr Raper—Yes.

CHAIR—After the statement that was just put to you by Senator Ferguson about the goods and services tax, you said that you made a proviso. So that you are not misquoted, it seems to me that the proviso stands out in as sharp relief as the Manhattan skyline at twilight. This is not an insubstantial proviso. It is a substantial proviso, and you cannot take the first part of the sentence without taking the whole of the sentence.

Senator FERGUSON—Does this mean that you might change your position, Senator Cook?

Senator O'CHEE—One of the things that we have said consistently all along and that, if others are putting words in my mouth, the Business Coalition for Tax Reform has agreed with us on and public stated, is that whatever you do with the GST, whatever you do with your consumption tax base, you should only raise sufficient revenue to replace other consumption taxes. You should not raise more revenue from your consumption tax than the taxes you are prepared to replace. At the core of this package is a $6 billion increase in the amount of revenue that is being raised from consumption tax. That is a fundamental flaw. We have said that all along. It is part of the reason why we had to state a week after the government's package was tabled that we believed it was unfair.

CHAIR—You said that your primary concern is about the loopholes. I do not want to gloss over that, because if it is a primary concern it is fundamental to everything else. We have not got to talking about trusts and how they are treated and so forth—that will come in a later part of our inquiry—but I just want to clarify whether those words are right on consideration. Is it your primary concern?

Mr Raper—I think I said 'a primary concern'. We have a number of primary concerns—they are all pretty high on the list—but we have always advocated the need to get that income tax base right.

CHAIR—Okay. ACOSS has always struck me as an organisation that is intellectually tough enough so that, if there is new evidence that was not available before that changes the circumstances, it would have the moral courage to change its conclusions. I think that is right.

Mr Raper—I hope that is correct.

CHAIR—As a committee, we commissioned research by Professor Dixon, and he emphasised the point that in his research commissioned by us the revenue generated from the existing system will more parallel GDP growth than will the changes being made. As I comprehend it, your support is for comprehensive tax reform in order to develop the pool of funding to meet the needs of the welfare bill that governments should, in equity and conscience, meet and your primary concern has been based on believing there is not sufficient money out there, as the system stands, to do that. Professor Dixon said yesterday that that is not true, that under the present system it is there and he cannot understand why Treasury has not done that modelling and presented it to the community.

I do not expect you to know whether I have accurately described Professor Dixon's work. I do not expect you to have studied Professor Dixon's work. In public life there is a belief that as soon as you hear a comment you understand comprehensively every last detail of it. I am one who does not believe that is true. People should be given sufficient time to acquaint themselves and make considered judgments rather than make the immediate media grab. But if you were satisfied that my description of it was right, on reflection and study you would change your position, wouldn't you?

Mr Raper—We would put forward fearlessly our assessment and analysis based on what we believe is best for low income earners—for pensioners, for unemployed people, et cetera.

We review all the evidence. We cannot undertake primary research, so we rely on reviewing other people's research and making an analysis of that. That is largely what we have to do most of the time. You are quite right, I have not had the chance to see that. We are prepared to revise our position if it is necessary, but that is of course one piece of evidence and we need to take into account all of the evidence, and we will certainly be doing that.

CHAIR—Okay, that is fine. It is now a public document and we will make it available to you. Can I suggest, respectfully, that ACOSS look at the work that Professor Dixon has undertaken and, if necessary, talk to Professor Dixon. In the context of your general position, when you come back to talk to us again, maybe we could talk about whether you feel that one of the reasons you have adopted the position is as sound as it has up until now been assumed.

Mr Raper—Fair enough. We shall do that when I come back. I believe it is probably appropriate to stress that the criteria that we would use in making those assessments do not just go to revenue alone—as in whether there are enough dollars. There are two other factors at least in all this. Efficiency is one—in a tax system, of course, you have to take that into account—and equity and fairness is another. Our assessments are based on all of that. Is it efficient? Is it effective? Is it equitable and does it derive the right revenue?

CHAIR—We have heard a fair bit about efficiency, and efficiency is doubtless a fundamental principle of tax law.

Mr Raper—Yes, but it needs to be balanced.

CHAIR—But in the balancing of efficiency and fairness—I am just flagging that I am in the fairness corner—if someone has to take the pain, let it be a little less efficient but a little more fair. There is the bias.

Senator CONROY—You were expressing your concern and disappointment about the manner in which some of the debate took place over the last few months in terms of there not being enough public information. ACOSS co-hosted a seminar on tax, which was closed and invitation only. I know because I actually wrote to your organisation and to the president and sought an invitation and was specifically excluded on the basis of my—

Mr Raper—Was this some years ago?

Senator CONROY—Yes.

Mr Raper—In 1996?

Senator CONROY—In 1996 or 1997. That was closed to—

Mr Raper—To politicians.

Senator CONROY—To me on the basis of my occupation.

Mr Raper—That is right, so I am informed.

Senator CONROY—So I probably have a little bit of a problem in terms of the question of public debate when you actually close your own seminars to interested members of the public, which I define myself as despite my occupation. You said that you assess your position—because you are not a primary source of modelling and things like that—on the information available to you. What information have you been provided so far by any source that shows the existing revenue base is declining or not keeping pace with GDP?

Mr Raper—Can I answer the first part and get Peter to elaborate? Just to clarify the point: we do not have the resources. There are very few full-time staff at ACOSS. There are a few policy officers. As you probably know, most of the people on the board, et cetera, are honorary. We do not have resources to commission modelling except occasionally when we rounded up some money to commission modelling about the impact of food in the GST, prior to the announcement of this package. But that is a separate issue. But you are coming to the question, broadly, of on what basis did we come to this view that we needed tax reform because of a declining revenue base or that that was at risk.

Senator CONROY—A potential threat.

Mr Raper—Peter will summarise that for us. We have documentation if you would like us to provide it to you.

Mr Davidson—To begin with, reflecting our primary concern with the income base, we focused most of our research on the erosion of that base, but we have concerns about the consumption base as well. In overall terms, between 1985-86—the last big tax reform package—and 1995-96, 10 years later, federal revenues declined by roughly two per cent of GDP, which is around $10 billion in current numbers. In our view, that has led directly to a series of rather nasty expenditure cuts, both in the late 1980s and again in the 1996-97 federal budget. There were a lot of factors that led to that decline.

Senator CONROY—What is your source document on that?

Mr Davidson—Federal budget papers. I refer you also to a document we released in September 1998, entitled 'But it is Broke. Comprehensive Tax Reform is Essential to Restore Public Revenue', copies of which I have here.

Senator CONROY—Could you supply it to the committee?

Mr Raper—The sources are noted throughout that document, including ABS sources and government budget sources.

Mr Davidson—On the income tax side, we believe that the primary reason for revenue erosion is the growth in tax avoidance and evasion and the increasing use of a range of tax shelters and avoidance opportunities. Some were closed off by the 1985 measures, but others remain. The only reason that federal revenues have held up as well as they have is that governments have retained the proceeds of tax bracket creep.

On the consumption tax side, we believe the underlying problem is the relative increase in household consumption on non-taxed items, especially services, and the relative reduction in growth in household expenditure on taxed goods. We provide some evidence from last year's taxation statistics, namely a graph which plots growth in household consumption in respect of items to which sales tax applies and items to which it does not apply. That is all in this document.

The story is a lot more complex than that, and there are a series of swings and roundabouts but, fundamentally, it is the weakness of the income and consumption tax basis. The income base has been propped up by bracket creep and the consumption base by increases in tax rates such as the 1993 federal budget and the action by state governments to ramp up tobacco excise and so on.

Senator CONROY—You mentioned earlier a figure of 25 per cent for low income earners for consumption of food.

Mr Raper—Yes.

Senator CONROY—What is your source for that?

Mr Davidson—The Melbourne Institute publication. I think it is sourced in these.

Senator CONROY—You did not arrive at that yourselves, you have just taken it from them?

Mr Davidson—They derived it from the household expenditure survey.

Senator CONROY—The St Vincent de Paul organisation appeared before us last week and argued very strongly that all the measures so far did not reflect their own survey. Admittedly, it was relatively small compared with, say, the HES data, but it was exclusively of low income earners and it was much beyond 25 per cent. Would you agree with them, in terms of real world examples? They were not drawing cameos from anywhere, they were not generating a computer model picture of people, they went out and interviewed real people.

Mr Raper—I can give you the benefit of my experience in my day job at the Welfare Rights Legal Centre. We find many of our clients are having to repay debts to Centrelink—to the Department of Family and Community Services as it is now called. In order to justify having a reduction in the amount of repayment of that debt, we have to draw up with them, or get them to draw up, statements of income and expenditure. Invariably, I find that their expenditure on food is higher than 25 per cent but there is a range. With some single individuals it does not seem to get there but, intuitively, to me the 25 per cent is at the lower end of the range. Peter, can you add to this?

Mr Davidson—The household expenditure survey itself suggests that certain low income groups spend a relatively high proportion of their budget on food because of the particular expenditure mix that they have—they are age pensioners and low income families with children—but it would not surprise me in the least that those at the very bottom of the income range who are approaching organisations like St. Vinnies would have much higher proportions of their budget devoted to essentials such as housing and food.

Senator CONROY—Given your own real world experience, and now St Vinnies, why wouldn't you ask the Melbourne Institute to factor in a figure higher than 25 per cent in their modelling?

Mr Davidson—One of the deficiencies of the data they have produced thus far—and we mentioned it earlier—is that it is not disaggregated enough. You have got all single pensioners, for example. As I understand it, they are not, at this stage, able to break those numbers down further into smaller subgroups of age pensioners, sole parent pensioners and so on.

Senator CONROY—But, given your own argument that you need to be pitched at the top of an average range, you are not going to be able to solve that problem in the next three or four weeks before we have vote on it in parliament. Shouldn't you be asking for some modelling based on the higher end of that?

Mr Raper—Perhaps I could put that back to the committee. Couldn't the committee ask for modelling along that basis? We have no capacity—

Senator CONROY—It would have been nice if Treasury had done it.

Mr Raper—Yes. It would have been nice.

Senator CONROY—It would add some integrity to what they have done.

Mr Raper—Absolutely. It would have been nice. I would have thought it was essential, in fact.

CHAIR—We are commissioning some distributional modelling, but, at the end of the day, it surely is incumbent on the government to provide this information.

Senator CONROY—They will be held accountable if they will not.

Mr Raper—I could not agree more. We said from the outset that the onus here is on the government to demonstrate that low income earners will not be adversely affected by this. It is not on us to prove that they will be.

Senator CONROY—Is the Melbourne Institute modelling based on a first year or on a second year inflation figure?

Mr Davidson—I believe it is based on a first year figure, but I am not certain of that. As we indicated earlier, we did not give them those parameters. They conducted their own modelling and we got some figures from them. It is higher in the first year.

Senator CONROY—Before you start questioning some of their assumptions, Treasury have admitted that their figure is 3.1 per cent. Following discussions with Professor Harding, she was willing to concede that the figure is over four per cent in the first year for the income groups that you and we are the most concerned about. I was surprised to see your modelling. Although I appreciate that you have attempted to say that there were deficiencies and have explained that you have not been party to the assumptions, attaching your name to a document has given it a great deal of credibility, as you have seen from the *Age* and from the Treasurer, who today has again endorsed your report.

Before a range of assumptions are questioned, the first-year inflation rate is over four per cent. I am surprised that, given your relationship—whether you are paying them or they are doing it voluntarily—you have not sought to press them on some of these issues in terms of more realistic real world assumptions on the inflation rate. What is the Melbourne Institute's pass through effect? Is it a 100 per cent pass through rate?

Mr Davidson—I believe so.

Senator CONROY—Do you think it is credible to believe that business will pass on a 100 per cent of all indirect tax cut savings in the first year?

Mr Davidson—It is not going to happen in all cases. The problem you face in modelling these things, though, is coming up with a realistic assumption.

Senator CONROY—One hundred per cent is unrealistic?

Mr Davidson—Anything other than that is a stab in the dark. But one has to view these numbers with scepticism, given that all those factors are at play and in force.

CHAIR—That is an intellectually slothful position, Mr Davidson, I have to say. You are saying 100 per cent is not realistic but, therefore, you cannot look at other variations, because it is a stab in the dark, and so you accept the unrealistic one. Surely that is intellectually slothful?

Mr Davidson—No. You could undertake a sensitivity analysis, but I am not aware of any distributional analysis—either in this phase of tax reform or in previous debates—which has attempted to slot other assumptions into distributional modelling.

CHAIR—But you agree it should be done?

Mr Davidson—For the purpose of sensitivity analysis, it should, yes.

Senator SHERRY—But we are not wrong: your members are worse off.

Senator CONROY—The Farmers Federation is concerned about the pass through; VECCI is concerned about the pass through; St Vinnies is concerned about the pass through. Every other organisation has sat here and unequivocally said, 'We don't believe—

CHAIR—Business organisations tell us it is unrealistic.

Senator CONROY—Business says 100 per cent pass through is not going to happen. You have to believe in the tooth fairy to believe in 100 per cent pass through.

Mr Raper—Senator, there can be no doubt that we absolutely share that concern, but we are not in a position to commission our own modelling. That, simply, is the point. They did this study well before we came anywhere near them, and we have to take what they have put in there and make the most of what we can. But let there be no doubt, please, that we share those concerns.

We also feel that we always need to put forward a conservative position. We do not have a reputation for taking things out to the extreme and maximising any position or advantage that we might get out of figures, because we have only our research integrity to rely on. We, therefore, always put forward a conservative position, and we warn people about reading too much into the figures.

So, with all those caveats, we are in a difficult position. Again, it seems to me, to come back to you, the Senate and the committee, that you are the only ones, if the government and the Treasury refuse. I do not know what your capacities are, but it seems to me that the onus rests on this committee to get that modelling in some form, to get whatever is available, before the—

CHAIR—Ultimately, the government funds the Department of the Senate, which enables us to conduct these sorts of surveys.

Mr Raper—It is essential that it be done, so that the Senate is in a position to make the decision, as you have said, Senator.

Senator CONROY—You have been in partnership with some of the business organisations in this country for the last couple of years, looking at this issue. They have got you to a certain point, based, presumably, on indications of support and commitment about a broad package. You are standing at the altar. They are behind closed doors, talking about dudding the entity tax, trusts and capital gains tax. Are you beginning to work out that you have been had yet?

Mr Raper—I do not know if this is the appropriate place to deal with those sorts of allegations or suspicions.

Senator CONROY—They are in the newspapers. They are saying they are not going to come before this committee to talk to us about their concerns on entities, which are in this package.

Mr Raper—Let me address the issues you raised, objectively. Whether or not we have been dudded is another issue. What is at stake here is whether or not low income earners are going to be dudded by this overall package. We share that concern. We do share the concerns you have raised about the business tax review, and we have said so in our submission to the business tax review. Much of that has been published today, and I am happy to give you a copy of the submission we made to the business tax review.

We do share those concerns about the implications for that business tax review, particularly on personal income tax. We share concerns about trusts and what happens with them. We share the concerns about whether the capital gains tax rate might come down to 30 per cent. We share the concerns about the company tax rate perhaps being reduced to 30 per cent, in the absence of mechanisms being introduced now to prevent high income earners from exploiting private companies to reduce their tax rate to 30 per cent, with anything above that being optional.

That is absolutely right, and the Business Coalition for Tax Reform agreed—and agrees—with us that this should be a comprehensive approach and that those things should not be dealt with out there on a limb, separated from this overall package. We have argued today, in other documents—and I am happy to argue this before you—that the Senate, in our view, should not be called on to look at GST legislation and income tax legislation before and unless and until they know what is going to come out of the business tax review.

CHAIR—You are asking us to return the legislation?

Mr Raper—No, I am asking the business tax review to get a wriggle on. And we have clearly called on the government today to rule out the possibility of a 30 per cent company rate without mechanisms to close down the opportunity for high income earners to exploit private companies, and to rule out a capital gains tax of 30 per cent.

CHAIR—And if they do not?

Senator CONROY—How long are you going to wait at the altar for them?

Senator FERGUSON—Four people are asking questions at once.

CHAIR—Quite right.

Senator SHERRY—Can I bring you back to something you said earlier: that we are at the beginning of this process. I must have missed something in the last 15 years. We have had a 15-year debate, we have the government's package in front of this Senate committee, we have to hand down a report one way or the other in just over a week: that is the bottom line.

The Treasurer is saying, 'I am not going to remove food from this package.' You are saying, 'We want food removed from the package.' The Business Coalition for Tax Reform, who you have had a working relationship with, has said, 'Don't remove food from the package. It is not worth proceeding, if food is removed from the package.'

If, as the Treasurer and the Business Coalition for Tax Reform keep saying, food is not removed from the package, what is the bottom line? There is one week before the Senate report, and people like the Democrats and Senator Harradine and Senator Colston have to declare their hands. If food is not removed from the package, what should they do? Should they vote for or against it?

Mr Raper—I was not aware of this one-week timetable.

Senator SHERRY—We have to report in a week.

Mr Raper—I was not sure that the Senate was voting in a week.

Senator FERGUSON—That is not true. According to my advice, 19 April is the reporting date.

CHAIR—We have to report on the macro-economic elements of these proposals.

Mr Raper—We have been given an extension until the end of this week to put in our submission in broad. I understood that we were to be invited back to address the senators, as Senator Cook indicated earlier, perhaps in March. I do not understand the one-week timetable.

CHAIR—The procedure is that we have to report by the end of next week on the macro-economic effects of the tax package. Following that report, the other committees will take the macro-economic parameters that we report on and review particular areas. We will pay heed to their reports and bring down a final report. But food does touch on the macro-economic elements, I think.

Mr Raper—So there is some urgency.

Senator SHERRY—Yes, there is some urgency. It seems to me that you have outlined a whole range of concerns. One of your bottom lines is, 'Get food out of the tax package.' The Treasurer is saying, 'No, I will not take food out of the package.' The Treasurer is saying that you support this package and the government's position. What is your position, if food is not removed from this package?

Mr Raper—Obviously, ACOSS is not responsible for the timetable, nor do I necessarily think the Senate has to accept that timetable. The Senate has to make a decision on this issue, taking everything into account. I understood the Senate ultimately was in charge of its own timetable there.

I am not responsible for what the Treasurer says nor for his views. Ultimately, the question the Senate has to deal with is whether this package is fair overall for low income earners and whether food should be in or out. If you are not in a position to make a decision, because you have not got the modelling, then I am not sure that the decision should be made.

However, we certainly would not be supporting the package without that tax mix switch of $6 billion being addressed without food coming out of the package. We have been very clear on that. We would say that the hole can be filled by adjusting the income tax cuts, as proposed, and by looking at many of the other loopholes and shelters on the income tax side that would easily fill the hole that would come from taking food out. I do not see the difficulty for the Senate in doing so.

Senator MURRAY—On page 8 of your submission, there is a remark that the Melbourne Institute's estimate of the average CPI increase is 2.44 per cent, compared with

Treasury’s estimate of 1.9 per cent. I understand that you have had extensive questioning on this area already, but I want to check whether that 2.44 refers to the first year, the second year or the average of both years?

Mr Raper—We have dealt with this already, but I will have to ask Peter to clarify what he understands the position to be.

Mr Davidson—We will have to take that on notice. We would have to have another look at the Melbourne Institute material because, as has been pointed out, if it is the second year effect, then it is likely to be higher in the first year.

Senator MURRAY—I presume you are arguing that any compensation calculations should be based on the first year effect?

Mr Davidson—That is correct.

Senator MURRAY—Thank you, I thought so.

Mr Raper—This submission, as you would appreciate, was put in before Christmas, and that was probably the last time that we looked in detail at the Melbourne Institute figures, so we will take that on board and get back very shortly with a quick answer.

Senator MURRAY—Stop me if this point has been raised earlier: the Vinnies people made the remark that the cost of food, particularly fruit, vegetables and that fresh area, has been growing at a faster rate than the average CPI for the last four years. I have checked the CPI figures, and this seems to be accurate. None of us can predict the future but, if that were to continue, food would continue to become a larger percentage of the overall basket of goods. Is that not so?

Mr Raper—Precisely. That is certainly our understanding of the fact that the CPI in relation to food has been increasing faster than the actual CPI rate.

Senator MURRAY—Given that the statistics are quite clear that food makes up a greater percentage of a low income, poor household’s basket than of a rich person’s basket, that is going to increase.

Mr Raper—It is 25 per cent versus 12.5 per cent.

Senator MURRAY—Yes. Which reinforces the point made by the Labor senators that we—or you or somebody—therefore must ensure, if possible, that the modelling puts some sensitivities in on the percentage that food is.

Mr Raper—Correct. And, in your absence, there was some talk about that 25 per cent being at the bottom end of the range.

Senator MURRAY—Which reinforces that point. I have been fascinated by ACOSS’s approach to this whole thing, because I believe you have been exceptionally conservative. But, in my view, you share a characteristic with Vinnies and other people concerned with the welfare of ordinary Australians, particularly less well-off Australians: there is very little politics in your approach. It is very much trying to make sure people are better treated by the system.

I really want you to address a concern I have that the language employed by people such as yourselves is in fact too cautious and too conservative. My reading of all the data over the last decade is that, in relative terms, the relationship of the poor and of low income people to high income people has deteriorated. In other words, the gap has widened.

Mr Raper—Absolutely.

Senator MURRAY—My reading is also that, in absolute terms—in real disposable income terms, in real expenditure terms—the poor and low income people are actually worse off than they were some years back.

Mr Raper—I think it is more accurate to say that they are more numerous. They are not necessarily poorer, but there are more poor people. The number of poor people in Australia has increased. The number of people below the poverty line has increased. Some mechanisms which have been introduced—for instance, the increase in the aged pension over the last decade or the decade before, bringing it up to 25 per cent of average weekly earnings—have held the line until recently. In the last three, four or five years there was also some slight decline not in the number of people who are in poverty, because that certainly is increasing, but in the levels of poverty as well.

Senator FERGUSON—You were talking about a decline: is that as a percentage of the population or in real numbers?

Mr Raper—The percentage of our population living below the Henderson poverty line has virtually doubled since the Henderson poverty line was first measured.

Senator FERGUSON—Which was when?

Mr Raper—In the mid-1970s. It has gone from about six per cent to about 11 per cent or 11½ per cent.

Senator MURRAY—My understanding of the evidence put to this committee is that at the highly disaggregated level and with regard to particular sectors of society—such as rural and regional Australia, and the unemployed and poor people—the ability to model the actual impacts of this change is limited, simply because the database is poor.

I do not want to misrepresent the government's position, but my understanding of it is as follows: they have chosen an inflation figure, which is in dispute, as you know. Then they have said, 'But, over and above that, to cope with the margin for error and to make sure that people are not going to be damaged materially, we are going to add 1½ per cent.' What I am putting to you with this line of questioning is that I believe that people like yourselves should actually be advocating that, through tax changes of this sort—and this is an instrument of social policy—we should be attempting to make poorer and lower income Australians better off.

Mr Raper—Absolutely. I have argued that here today.

Senator MURRAY—Good. Now, to achieve that, you need to indicate, I think, in our terms, what percentage might possibly deliver that and restore people, perhaps, to the position they were at a decade or so back, depending on what point you choose. Because our society has become less egalitarian, less fair, we need to be doing something about addressing that problem.

Mr Raper—That is absolutely correct. However, that is a separate question from GST compensation, as you would appreciate. It is certainly the subject of our entire budget submission, which we will be presenting to the government shortly and making public. It goes to a much wider question than simply GST compensation, but I take your point.

Senator MURRAY—It does, but it is within the same ability to address the policy position, because the other point I would put to you is that it should be the intention of this package to make substantial numbers of Australians worse off: those who are not paying their way.

Mr Raper—Sorry, it should be the intention to make substantial numbers of Australians worse off?

Senator MURRAY—Yes: those who are not paying their way, those who are avoiding tax—tax dodgers and tax evaders. Do you get the picture?

Mr Raper—Yes, precisely.

Senator MURRAY—On the other side of the coin, you want to make people better off. I do not think this tax policy can be addressed solely in terms of compensation, because compensation implies a balancing out. My question to you is: why have you not overtly campaigned on that basis? Why have you, as an organisation, just looked at what would happen if certain things are done, at how will we be no worse off? That is the feeling I have from your submissions.

Mr Raper—I am sorry; I got a little distracted by a byplay over here about—

Senator FERGUSON—We are trying to manage the time.

Mr Raper—No, it is the withdrawals debate that distracted me, and I missed that. I do apologise.

Senator MURRAY—I will leave that on notice.

Senator SHERRY—Don't repeat the question!

Mr Raper—I shall happily take it on notice. I do apologise.

Senator MURRAY—As a former socialist, you should surely like this.

Senator SHERRY—The evidence is obvious to us, I can tell you.

Senator MURRAY—Let me summarise, if I may. I suggest you take this on notice, and when you address the committee next, I would like the committee to hear your views as to how you believe inequalities in our society could be addressed through using a package which has a fiscal impact, which are income tax cuts, and has a tax mix change, which are the indirect tax cuts.

Mr Raper—Thank you, we shall do that.

Senator FERGUSON—Mr Raper, when you commenced your presentation, you said we should be concentrating on modelling today, because that is what the first part of this inquiry is about and what your submission was about. Although emotions have run a bit high on my right in regard to some of your answers, we ought to get back to one or two questions which I want to clarify about the modelling.

In asking one of his questions, Senator Conroy said you should have used some 'real world' figures or assumptions when you were asking the Melbourne University to do some research, or when they were using their research. In fact, if you are going to use anecdotal evidence or disaggregated statistics, it becomes very difficult, because if you are looking at modelling, you have to do a statistical analysis, and it can only be done on statistics. If you are going to accept the use of modelling, which we are talking about today, you can only accept that modelling is important if you use averages: is that a fact?

Mr Raper—Surely, noting the fact that they are averages, you adjust. You do not ignore the fact that they are averages. Sure, it comes out as an average, but you do not ignore the fact. You accept the fact that an average is a range.

Senator FERGUSON—If you are talking about statistical modelling, which we are—we are using statistics and using modelling—you can only accept the use of modelling if you are prepared to accept the averages that they come up with. Because that is the only way they can arrive at any outcomes with any predictability.

Mr Davidson—It depends on the level of detail that you are prepared to go to in arriving at those averages. As I suggested earlier, an average of all low income people is a fairly meaningless figure, but we believe the HES and other data is capable of providing reasonably reliable data on the basis of, for example, quintiles of aged pensioners and not all aged pensioners, as appears in the table in our submission.

Senator FERGUSON—Do you accept the fact that the more you disaggregate information, the more unreliable the results can be?

Mr Davidson—It is a matter of judgement. I suggest you pose that question to the ABS this afternoon.

Senator FERGUSON—I am quite sure we will. When the government set out to put this package into place, it did take into account that there would be a one-off effect on low income earners and the general CPI. It accepted that fact and agreed to put in place some compensation. Senator Cook previously said that he would like low income earners to be compensated and to make sure that, if anything, they were over compensated.

CHAIR—No, I did not say that. I said that, in the trade-off between efficiency as a tax principle and equity, I err in favour of equity. If it means that we have got a slightly less efficient but a fairer system, that is a good outcome for Australia. That is what I was saying.

Senator FERGUSON—I am not sure whether that has been a principle that has always been applied by the Labor Party in government. As I understand it, when they raised indirect taxes by two per cent in 1993, there was no compensation whatsoever for low income earners or for those on fixed incomes or for social welfare recipients. Is this the first time in your knowledge that, when indirect taxes have been raised, a package of compensation has been put in place? Whether or not you judge that package to be adequate or not is open to debate later on, but is it the first time that a compensation package has been put in place to account for an increase in indirect taxes?

Mr Davidson—In both the 1985 package and the 1992 Fightback package, there were compensation packages proposed. Indeed, we believe the compensation package proposed in *Fightback!* is much more robust and adequate than the one that is being advanced by the government today. It is also true that there was very little in the way of compensation in the 1993 budget change, and we were just as loud in our objections to that as we are to the risks that we believe this package imposes on lower income people today.

Senator FERGUSON—In that case, there was no compensation offered; in this case, your complaint is about the adequacy or the level of the compensation?

Mr Davidson—Yes.

Senator FERGUSON—You have stated quite categorically your position in relation to food and the GST. Senator Murray has said on a number of occasions that he does not want the low income and poorer people in Australia just to be not worse off; he actually wants them to be better off. It was with that in mind that the government put this 1.5 per cent above CPI cushion in place.

If you could be satisfied that low income people would actually be better off with a compensation package that was put before you, and if the alternative was to have no tax reform at all and to leave people as they are today, would you still advocate the rejection of this package because the government said it would not move on the exemption of food?

Mr Raper—The first point I need to repeat is that we would want food taken out, in order to make this structurally a package that does not require anywhere near the amount of compensation first up. That is a fundamental point that you come back to.

Secondly, I do not understand, to be perfectly honest, why some think—and some advocate this—that if food were taken out the whole package would unravel. There is no justification for having that extra $6 billion in revenue in there. It is $6 billion more than what is being replaced. The whole rationale for a GST was to round up a number of taxes and replace them with one smooth, easy, clean, efficient tax.

Senator CONROY—Do you really believe that?

Mr Raper—That is the public rationale. So there is no justification for raising the extra $6 billion in the first place. Taking food out addresses both of those problems, and it largely addresses the amount of risk that low income earners are being exposed to.

Senator FERGUSON—Except that we have had a lot of witnesses before us saying that, by taking food out of the package, you significantly increase compliance costs.

Mr Raper—Yes.

Senator FERGUSON—You make it more complex: you then have to decide what is food and what is not, for example. A lot of other countries have had difficulties in that area. We have had a lot of witnesses say to us, 'Make sure that you provide adequate compensation, but leave food in, because it only adds to the complexity if you exempt it.' I know you come from an alternate point of view but this is one of the reasons why it is in.

Mr Raper—I understand all those reasons, and mostly that is true. It does make it more complex, it does make it less efficient. But that is the price you have to pay. Most countries, in fact, do not include food. And the government has already accepted the need to exempt or zero rate a number of things, including health, education, child care and community welfare services. So food is just another thing. It is no different, in the sense of adding complexities or difficulties. Those conclusions are true, but that is the price you pay for getting tax reform that is balanced between efficiency and equity. It is the fundamental flaw in that balance, in our view.

Senator FERGUSON—But most of the countries that have either a zero rate for food or a lower rate for food also have value added taxes of somewhere between 15 and 25 per cent, and those would also impact on low income earners.

Mr Davidson—That is probably largely because they rely less on excises than we do in Australia. Most OECD countries have a pretty similar balance between consumption taxation and income taxation to the balance we have in Australia.

Senator FERGUSON—The figures show that the United Kingdom's 17½ per cent VAT supplies about 8.7 per cent of revenue, whereas New Zealand's 12½ per cent, broad based, provides only 6.7 per cent—or the other way around, I am not sure.

Senator CONROY—VCOSS appeared before us earlier in the week. They have devised something referred to as the RPI: is either of you familiar with that? It is a way of calculating a CPI for low income earners.

Mr Davidson—Yes.

Senator CONROY—Are you incorporating that in your modelling or your calculations for your submission next week? We have agreed that there is a specific expenditure pattern, and it is perhaps higher than the 25 per cent that is acknowledged at the moment. Equally, there is a CPI figure that is not relevant to low income earners as well.

Mr Davidson—We are submitting that this committee should commission modelling which examines, in a disaggregated way, the effect of the package on the expenditure bundles of different income groups, because we do not accept that a single CPI measure, as used by the Treasury, is accurate. However, we do not have the capacity to undertake that modelling ourselves.

Senator CONROY—VCOSS appears to have done a fairly substantial amount of modelling.

Mr Davidson—Yes.

Senator CONROY—Is that a reasonable guide? They put to us very strongly that, if it did not use the sort of weighting that they refer to as an RPI, any modelling, whether it be one we commissioned, the Treasury's or anybody else's, was poor modelling which had not been well-researched.

Mr Davidson—I think their main point is that you have to separate out the likely effects on the CPI for each group. The CPIs for different groups move differently over time, that is the whole point. So it is essentially an argument for disaggregated modelling of the kind that is undertaken by some independent modellers but, apparently, not by the Treasury any longer.

CHAIR—I think that brings us to a conclusion for today. As you have pointed out, this is evidence in progress, and we expect to hear from you again. I thank ACOSS, Mr Raper and Mr Davidson.

[4.03 p.m.]

EDWARDS, Mr Robert William, First Assistant Statistician, Economic Accounts Division, Australian Bureau of Statistics

KROON, Mr Harry, Director, Household Income and Expenditure Section, Australian Bureau of Statistics

SKINNER, Mr Tim, Deputy Australian Statistician, Australian Bureau of Statistics

WOOLFORD, Mr Keith Victor, Director, Prices Development Section, Australian Bureau of Statistics

CHAIR—We now have a quorum, so I will open the final stanza of proceedings today. I welcome the witnesses from the Australian Bureau of Statistics and apologise for keeping you waiting. We thank you for indulging us in that.

Before I ask you to proceed, can I say that I have consulted with members of the committee—not with all members of the committee but with a representative sample—and I want to put on the record that ACOSS approached me in the break to indicate that on Monday they anticipate lodging a supplementary submission to the submission they have lodged with the committee. This committee has given privilege to submissions as it has heard them. Is there agreement on the committee that, upon lodgment of the supplementary ACOSS submission and a sighting by the committee of that submission, that submission be released and given privilege? There being no objection, it is so ordered.

Let me now turn to the Australian Bureau of Statistics. I thank you, as I was saying before, for your preparedness to show us a bit of indulgence in putting up with the delay. I invite you, if you wish, to make a short overview oral presentation to the committee on your submission and then would you be kind enough to make yourselves available to answer questions from the committee. According to my list, Mr Tim Skinner, Deputy Australian Statistician, is the senior person here. I will go to you, Mr Skinner, to introduce your colleagues and to take charge of the proceedings from your end.

Mr Skinner—Thank you, Chairman. I would like to make just a few brief comments, if I may. Before doing so, could I introduce my colleagues. We were unsure of the level of detail we might get into in the questions and we have brought some real experts along on particular aspects. On my right is Rob Edwards, who is First Assistant Statistician of the Economics Accounts Division. Rob is responsible for the CPI, as well as a number of other economic accounts activities in the ABS. On my left is Harry Kroon, who is the Director of the Household Income and Expenditure Section. He is directly responsible for the conduct of the household expenditure survey. And on my extreme right is Keith Woolford, the Director of our Prices Development Section, who is an expert on the CPI itself.

I understand the invitation to the ABS to attend arose from a number of statistical issues that came up in the earlier discussions. In its written submission, the ABS has attempted to pick up some of those issues and respond to them as we can. But there were just two issues I thought I would highlight from our submission in the way of introductory comments.

First, there has been a great deal of comment about the accuracy of the data coming from the household expenditure survey. The data limitations on that survey I think are well known and understood by most expert users. The committee should realise that it is just not possible to compile perfect statistics in this area. The collection of income and expenditure statistics is, at best, sensitive to most people; the provision of the required data is quite onerous, involving a long interview and the maintenance of a diary recording all expenditures for a two-week period; and adequate records are not always available.

But, having said that, the ABS does consider that statistical data from the household expenditure survey can be used at a suitable disaggregated level and, after appropriate adjustments are made to the reported expenditure, to describe the expenditure patterns of the population and its various subgroups. ABS itself uses the data in this way. We use it in the calculation of the CPI—the weights within the CPI—we use it in what is called our fiscal incidence study, and we use it in the compilation of a number of national accounting estimates. However, ABS takes the view that users must exercise their own judgment on the fitness of those statistics for the purpose for which they want to use it. We cannot come here and provide an imprimatur on the way in which our statistics are used.

Second, I want to make it clear that the ABS makes no claims to any particular expertise in economic modelling, whether that is at the macro level or the micro level. We see our main role being to support such work with the provision of data and advice on its quality—the underlying concepts and the definitions and so on. Thank you, Chair.

CHAIR—Thank you, Mr Skinner. I will ask Senator Gibson to ask questions to begin with. But, if I may, I will just ask one from the chair. Yesterday I thought we were given a piece of cautionary advice from a professor of economics who is producing modelling figures for this committee—Professor Dixon. To use my description of what he said—I do not have the quote before us—he cautioned us to not look too narrowly at the figure but, more importantly, to understand the reasons for how that figure had been calculated and the assumptions upon which it was based, to understand what its significance was—the tolerances within which it might be accurate. Is that a piece of cautionary advice that the bureau might also offer to this committee?

Mr Skinner—It is indeed. I noted an earlier witness to this inquiry, Professor Warren, made the observation that you do not just use the data without becoming extremely familiar with it and without knowing its limitations. We would see the household expenditure survey as a very valuable data set if it is used with care. We know there are a number of difficulties with it. Any use of it must be cautious.

CHAIR—I think, at some stage, Mr Harry Kroon may have been thought of as responsible for the HES as been—

Senator CONROY—Evil incarnate!

CHAIR—Well, I shall stop my sentence there. HES came in for a bit of critical comment. But I am sure, during the course of this session, we will hear from Mr Kroon as well. Senator Gibson.

Senator GIBSON—I think it would be useful for the committee for you to re-emphasise a point which I think you made quite clearly on the relationship between sample size and error. In paragraph 20 you give examples of expenditure for staple items of bread where you need 20 households for a 25 per cent standard error. For clothes driers we are talking 2,000 to 3,000 minimum sample, but for some relatively infrequent items like a trailer or a lawnmower you need the whole 8,400. Would you care to expand on that a bit, because I think it is very important that everyone on this committee, and the public, understands these concepts well. Otherwise, it is easy to run off with the wrong conclusions.

Mr Skinner—We could spend a lot of time on this. Let me jump in and try to give a quick response to that, if I may, and then take it further if you wish. I think I have to start with the concept of what a sampling error is. Because the household expenditure survey is that—a survey of a population of about 8,400 households in total, and not the entire population—depending on what sample you would draw from the population, we would get a different answer or a series of answers. The sampling error, which is something we calculate in all of our surveys, is an attempt to put a confidence interval about the estimates that we would obtain. Having obtained an answer within the survey itself, we provide that answer with some level of confidence, and you can assure yourselves that the correct answer is somewhere within that range.

The sampling error is a function of two things. One is the size of the sample—the number of observations that contribute to it—and the second is the variability of the variable itself. I will come back to the example which you are quoting in there. For some items in the household expenditure survey, like bread, butter or milk, every household in Australia would be purchasing it—whether they are low income or high income and whether they are a one-parent family or a two-parent family or whatever. The variability often, within those expenditures, is very low and that will have the tendency to bring the size of the sampling variance down. The other element is the size of the sample itself. As it reduces, the errors themselves will increase and the less confidence you can have within that particular estimate.

Senator GIBSON—Running on from there, you also point out some of the difficulties with regard to estimation of income, and point out that income from employees on salaries and wages and from government—pensions, et cetera—are relatively well defined, whereas those who are self-employed and on an outside income are poorly defined. You went through similar comments on the side of expenditure. Hence, can I conclude out of that that, because an estimate of savings would be the difference between the two, it is extremely difficult to use this HES information to get an estimate of savings.

Mr Skinner—We include in all of our publications in our household expenditure series a caution for our users not to use the difference between income and expenditure through the survey as a measure of dissaving. There are a lot of reasons why it is not a measure of dissaving. I could go into those reasons. We have tried in our submission to explain some of them. The survey is not designed, even at the household level, to produce a balanced budget. The way in which we collect the income, and the way in which we collect the expenditure data, even if done perfectly, would not end up necessarily with a balanced account for every household. It is certainly not true as we aggregate our survey.

Senator GIBSON—I have a couple of quick questions on the CPI. In paragraph 58 on the last page, you make reference to your publication in 1990 and 1992 about the experimental indices for age pensioner households, how there is little difference between the index for age pensioner households over 11 years compared with the normal CPI, and how that work was repeated in both 1993 and 1995. Would you care to comment further on that?

Mr Edwards—I will take that question. As the paragraph says, in response to a parliamentary inquiry in the early 1990s, the ABS was encouraged to do some work in measuring changes in the CPI for population subgroups.

In 1992, we did such a study for pensioner households and constructed waiting patterns applicable to pensioner households. On the basis of that we then calculated what the CPI changes would be for that population subgroup. As the paragraph says, the results were that over the 11-year period to 1992 there was only a very small difference between the CPI result and the result for the pensioner households. That is not to say that within that 11-year period there were not some changes, but they tended to average themselves out over that longer period.

Senator GIBSON—Just running on from there, you point out in the last paragraph that the ABS is in the process of constructing indices on an outlays basis for subgroups using the HES data. What groups are you considering or is that still being finalised?

Mr Edwards—It is still being finalised. During the course of our most recent CPI review, we had representations from the ACTU that they would like to see us construct an index for wage and salary earner households. We also had representations from ACOSS that they would be keen on us constructing an index for social welfare beneficiaries.

Our intention is that we hope to be in a position to publish such indexes later this year. I think probably as a minimum we will construct indexes for those two subgroups, but we may possibly go further. We would want to do some more consultation with our users on this before we finalise our plans.

Senator FERGUSON—Can I just follow up from Senator Cook. I asked this question of ACOSS and some other people who have come before us—about economic modelling. In simple terms, is it fair to say that the more you disaggregate statistics the more unreliable they become?

Mr Edwards—It is certainly true with the household expenditure survey that the further you go down into smaller and smaller subgroups the higher the sampling errors that pertain there. That is true.

Senator FERGUSON—And so you could not rely on some of the information from very dissagregated statistics or surveys for the purposes of devising what is the average over that group of people that you were surveying?

Mr Skinner—I think the real answer to that one is that it would depend on how and for what purposes you were going to use that. For some purposes, that might be quite an acceptable thing to do but for others it may not be. That is a judgment you as a user would have to make.

Senator FERGUSON—I wonder whether you could explain a bit a bit more about the known under-reporting—this is to do with the household expenditure survey. You talk about an under-reporting of alcohol and tobacco expenditure, which is assumed to be part of the statistics for household expenditure. It probably is in the case of my kids, too. The other thing is that you might have under-reporting of income from some self-employed people.

Mr Skinner—If I can make just a couple of observations. If we look at alcohol, tobacco and gambling on the expenditure side—and they are the items which are well known to be under-reported—from our own comparisons of the estimates we get from household expenditure surveys, say, to the national accounts estimates, we would estimate that alcohol and tobacco were under-reported by about 40 per cent.

Senator FERGUSON—Forty per cent?

Mr Skinner—Forty per cent, whereas gambling expenditures we would estimate are under-reported by about 75 per cent. Those three items are way ahead of any other item, as you might expect.

On the income side, our comparisons on wage and salary earners and various beneficiaries show that the income data is reasonably robust. But as we go into self-employed and investment income, we know that those estimates do not line up with external benchmarks which we can get from other places.

Senator FERGUSON—Do you try and compensate for that in your household expenditure surveys?

Mr Skinner—No. We publish them as is and then we provide a lot of advice to people about those deficiencies, so, depending on how they want to use it, they could take that into account.

Senator FERGUSON—The point I am trying to make is this. We have heard talk about, for instance, St Vincent de Paul, who did a survey—came to us with the results of a survey—where in fact they made an instance of the consumption of fresh fruit and vegetables and how the price had gone up by 29 per cent. I think you have statistics that show that in low-income families, only two per cent of their income is spent on fresh food and vegetables. Their sample in some states was three households. Would you suggest that a survey that is done like that could provide, perhaps, some anecdotal evidence but not very reliable statistics?

Mr Skinner—I would view it as a case study at work which have their own value when you look at them in isolation, but you really would need to have a reference point to come back to. My own judgment is that the household expenditure survey with 8,400 respondents—and we spend a great deal of time and money getting that information—would provide a much sounder base.

Perhaps I could just add to an answer I gave you—to extend it more than correct it. You asked me if we make any adjustments to our own household expenditure surveys, and I said no. As we publish it in that form, the answer is no. Internally, when we are using it, though, we make a number of adjustments to the household expenditure survey as we calculate the weights for the CPI. So we take account of the deficiencies that we find in these data, make judgments about them and adjust for it as we calculate CPI weights. On occasions we do for our purposes, but as we release it we do not.

Senator FERGUSON—I am really concerned about this under-reporting, because we have had surveys brought before us where, for instance, it is said that low income earners spend 25 per cent of their income on food, some may spend up to 40 per cent—I think that was one of the figures that was quoted. It is just possible, and I am not saying it is probable, that because of under-reporting some of those low income earners may be spending some extra money on food, alcohol or gambling and, in fact, in reporting, may say that it is being spent on other items.

Mr Skinner—That is entirely possible.

CHAIR—Perhaps I should just ask you one follow-on question from that about something which has always intrigued me. We are told that there is a major drug problem in Australia. I am not aware of any statistics collected as to the extent of that. It is asking to measure an illegal activity that no-one is going own up to, so it is very hard to do that, so it is always estimates. But in terms of the socioeconomic distribution of that problem, it seems to concentrate itself—not exclusively, but obviously—in middle and lower income areas. To the extent that that was a problem, that would also be a further cost to households, wouldn't it?

Mr Skinner—I would assume so.

CHAIR—Do you know of any way of saying anything that is useful to anyone on this subject?

Mr Edwards—Senator, I might come in there. There was a recent study that was done in the United Kingdom trying to put an estimate on the size of the so-called underground economy in this particular area. I cannot recall the detail now, but I could certainly provide to the committee a copy of an article that was published on that. The work was done by the Office for National Statistics in the UK.

CHAIR—But that would be Britain. In relation to what applies in Australia, at best, you could say, 'Well, that is in a like country', but population densities, porousness of national borders—all those things go to this. You could just say, 'Well that is true of Britain.' Maybe there is a bigger problem than we thought of as a problem in Australia.

Mr Skinner—I am not aware of any information in Australia of that sort. I do not think we have ever collected information in that domain.

CHAIR—In terms of the black economy, I know the tax office tried to make assessments of that. Are you aware of any work that might be done to try and assess the size of the black economy in Australia?

Mr Edwards—Yes, I am, Senator. In fact, the ABS and the Australian Taxation Office are currently involved in a joint study on this, but focusing particularly on the cash economy. The work is at a very preliminary stage at this point, and no useful results have come out as yet. We are hoping to complete that study by about the middle of this year.

CHAIR—One of the areas that concentrates the mind of this committee at various times is whether the cash economy will increase or diminish and what its value is, given certain types of tax settings. Clearly that is an issue in this debate. Are you aware of any work overseas that might have made comparative studies—before and after type studies—in switching the tax mix?

Mr Edwards—I believe some work has been done but I would need to check that. I cannot say definitively here, but I will get back to the committee on that.

CHAIR—It seems to me, in the absence of information, that everyone is an expert on this issue. The information may be sufficiently bland as to enable every subjective interpretation to stand—I do not know.

Could I turn to you, Mr Kroon. Treasury made some remarks to us about the reliability of the household expenditure survey for making assessments about distributional impacts and so forth which were not flattering—at least, that was my interpretation of what they said. Professor Warren also said that he relies on it but he makes judgment calls about what he includes in and what he includes out and regards it as a pretty fair broad guide if you make sensible—which is the most subjective thing you can ever do—judgments about it. Since you have been given the inevitable reputation of being responsible for it, what do you say about these things?

Mr Skinner—We would view the household expenditure survey as a very valuable data set which, if used with caution, as I said at the start, if used sensibly, is very valuable. Indeed, that is signalled by our own use of it. We use it in the compilation of our CPI and we use it in the so-called fiscal incidence study.

CHAIR—Could I get it clear. The consumer price index is based on your HES work?

Mr Skinner—Yes. In paragraph 51 of the submission it takes you through the steps that we would take, starting off with information we would get from the household expenditure survey and what processes we go through to derive the weights. The HES is the starting point and the CPI weights obviously differ by the adjustments and corrections that are made in the process.

Coming back to my answer on how good these estimates are, and the Treasury's own view of it, we think it is a good data set. We know a lot of people use for that purpose and we are encouraged by that. We use it ourselves. My own view is that some of the criticisms I have seen of the household expenditure survey by Treasury are overstated. But I have to accept, at the end of the day, that they are the user. They need to understand what the problems are, how they are going to use it and make their own judgment as to whether they think it is up to scratch or not. I know people make different judgments and I am certainly not going to give an imprimatur to one or the other.

CHAIR—No. Could I pause you at that point. When you said that you think certain of the Treasury criticisms of the HES are overstated, which particular criticisms do you think fit that category?

Mr Skinner—I think the Treasury has taken the view that the HES does not support the analysis of various sub-population groups, by its nature. Hence, they rely on a general CPI weighting to then provide the weights for their own analysis. My own view would be that the HES, used wisely and cautiously with due consideration and so on, is sufficiently accurate to allow you to do it for various other population groups.

When Mr Edwards gave the response to Senator Gibson that we would be looking to produce a CPI for, say, beneficiary households, we again will start with household expenditure survey data and make a series of adjustments to go through to some weights for pensioner households. That, again, is a use of HES for some sub-population group. I think they have overstated it, to that extent.

CHAIR—Do you keep it under constant review and refinement, in order to try to meet the needs of the users so its accuracy is—

Mr Skinner—We actually are in the field at this very moment, over the course of the financial year 1998-99, running another household expenditure survey. Leading up to that one—we tend to run them each five years for a whole variety of reasons, one purpose of which is to update the CPI—within that five-year period, we obviously learn each time we run it of some continuing difficulties with the way in which we collect that information.

In the last round, we have been very conscious of the desire of a number of our users to look at income and expenditure and subtract the two and come up with some measure of saving or dissaving. We will never be able to resolve that issue and we have not set that as a goal. Some of the things were able to do will aid that process, but it will not solve that process.

CHAIR—In my experience, you statisticians are cunning people in that you are prone to ask the same question in different ways in order to see whether we give different answers or the same answer and before you conclude as to what you think the facts are. Is there some check you run on HES that reassures you that you have got it right?

Mr Skinner—We do a number of checks. Some of our users, and perhaps critics, in this respect would look at the timeliness within we will release data. It takes us many, many months—nine to 12 months—from the moment we finish collecting until we start publishing our information. One of the things we are doing throughout that period is editing that data, investigating it and analysing it to see how internally consistent the information is in ways it should have been and then trying to work towards resolving those things. That is certainly one way we go about that process.

Once we get the aggregate information, we will then take it and, from our sample estimates, start comparing it with known external estimates. I mentioned earlier, on gambling, alcohol and tobacco, that we do those comparisons and realise those estimates are well short. We then share this information with various people—our expert users in this area—so that they are aware of those difficulties. We would look at the income distributions against other income surveys that we have run. We would look at the estimates coming out on pensioner beneficiaries against social security data. So there are a lot of external checks done as well, trying to ensure that that data set is as good as we can make it—but not just as good as we can make it: having released it, we can then advise users about the deficiencies and strengths of that data set.

Senator SHERRY—Can I just ask a question about the tobacco and gambling?

CHAIR—Yes. If you have to go, I defer to you.

Senator SHERRY—On tobacco and gambling, I think tobacco as a weight was 0.3 for the CPI?

Mr Skinner—People will check that as we are talking.

Senator SHERRY—Okay. I think you said that tobacco is under-reported by 40 per cent, which is quite a massive figure.

Mr Skinner—The calculation of the weight in the CPI will have made the adjustment to take it to 100 per cent.

Senator SHERRY—Right. I was going to ask you that. I assume it did the same for gambling as well?

Mr Skinner—Indeed. That is one of the adjustments that we do: taking HES data through to the CPI. But gambling is not included in the CPI.

Senator SHERRY—What is gambling?

Mr Skinner—Buying raffle tickets.

Senator SHERRY—Sorry, what is it if it was included in the CPI? I know what gambling is. My first job in my working life was working in a casino for four years, so I know what gambling is.

Mr Skinner—Ask a statistician and he will give you a definition.

Mr Edwards—Raffle tickets, poker machines, a bet on the races—all of those sorts of things. One of the conceptual difficulties you have got with gambling in a CPI measure is what actually is the price. Technically, that is quite a difficult issue to work through.

Senator SHERRY—But it is taxed.

Mr Edwards—Yes.

Senator SHERRY—The tax issue is pretty critical to the inquiry. Have you been able to resolve that difficulty?

Mr Edwards—No, gambling is excluded from the CPI.

Senator SHERRY—Have you done any surveys of gambling—its total expenditure and what it represents? Mr Kroon was going to hazard a guess.

Mr Kroon—No. I said only in the household expenditure survey. That is the only direct attempt that we have. We know that, by making comparisons against other estimates, such as taxation information and the like, it is under-reported to a significant extent.

Mr Edwards—We do have some other data sources, though. Our public finance statistics include information on government revenues on gambling. Also, a couple of years ago we did a survey of casinos in Australia and there has been some published information on that.

Mr Skinner—They will give you aggregate numbers, but no distributions. So you cannot see who it is that is gambling or what part it plays in motives.

Senator CONROY—Would you be aware of Dr Carnahan's paper?

Mr Skinner—Yes.

Senator CONROY—Were you, or anyone else from the ABS, involved in discussions with Treasury over their decision to use or not use? I ask this because we have seen some minutes of a conference that appeared—I am not sure if 'conference' is the right word, but some sort of discussion group. Was ABS involved in that?

Mr Skinner—I think we attended that particular discussion group but we were also invited at one stage to comment on the Carnahan paper when it was in its penultimate draft.

Senator CONROY—Are your comments a document that is available?

Mr Skinner—I would presume so.

Senator CONROY—Would we be able to get a copy?

Mr Skinner—Yes.

Senator CONROY—I guess, without having seen it, you would not have agreed with the Carnahan paper. Professor Warren described it as a courageous decision to toss the baby out with the bathwater, to quote somebody else.

Mr Skinner—I think our comments fell into three categories. Firstly, we signalled that we saw it as not appropriate for us to comment on the methodology or approach they were using to taxation modelling. That was beyond our expertise. We made a second observation that we thought that the statistical data from HES could be used for various sub-population groups beyond what they had assumed and stated, along the lines of my earlier question. A third observation was that we indicated that we did not think the analysis that we had done—which was in the early 1990s; it was the piece of analysis that Senator Gibson referred to earlier—did indeed show that the weights for various households converge over time. So we cast some doubt on that particular conclusion of theirs within the paper.

Senator CONROY—That is one of the arguments that we have been having on the committee. A question that has been kicked around is whether or not a pensioner expenditure pattern converged to the norm. It has been consistently quoted that that is the case.

Mr Skinner—I think it is a misunderstanding of the research that we have done. What our research shows—

Senator CONROY—I am pleased to hear you say that because intuitively it just seems an absurdity.

Mr Skinner—What our research shows is that the price behaviours themselves converge over time. That diminishes any effect on the calculation of a CPI, depending on what the various expenditure patters were to start with. What it does not show is that the expenditure patterns themselves converge over time. I can use as an example that over time there is no reason to suggest that a pensioner household will suddenly start buying houses, because they have done that earlier in their life and at any point in time that would be the case, and over time there is no reason why they would converge.

Senator CONROY—There was an attachment to one of our other submissions today. It is an old paper by Dolan and Wright, which was also casting doubt on it. Are you familiar with that one as well?

Mr Skinner—Vaguely.

Senator CONROY—I think it was 1992.

Mr Skinner—I am aware of it but I do not know it in detail.

Senator CONROY—The budget papers classify the GST revenue as a state tax. Were you consulted about that decision?

Mr Edwards—No classification decision has been taken by the ABS on this matter at all.

Senator CONROY—Are you aware that Treasury has classified it in the budget papers as a—

Mr Edwards—I have seen reference in various documents to the GST being described as a state tax, but the statistician has not made that decision at this stage.

Senator CONROY—Has Treasury contacted—

Mr Edwards—I think there have been some discussions at various stages with Treasury people foreshadowing that they will require a decision by the statistician on this matter, but that is about as far as it got.

Senator CONROY—Given it is a piece of Commonwealth legislation and it can be varied by only the Commonwealth—

Mr Skinner—The statistician will make that judgment independently.

CHAIR—He is a statutory independent.

Mr Skinner—That is correct, for these sorts of reasons.

Mr Edwards—Could I just make one elaboration on that. In making a decision in this regard, the statistician will be strongly influenced by any international standards that are around in this area. In this particular regard, the International Monetary Fund has promulgated statistical standards with regard to government finance statistics. So we will be looking at the detail of the GST in the context of those standards and any particular aspects that might be unique to the Australian circumstances.

CHAIR—That is a transparent process.

Mr Skinner—That is correct.

CHAIR—While the statistician is a statutory independent authority, the statistician, in considering how things are classified, has regard to a transparent set of proclaimed data and seeks to apply that in a reasonably transparent way so that we all know where it is coming from.

Mr Skinner—Yes.

Senator CONROY—Treasury draw on your HES data a lot, I would imagine. Are you able to give us an indication of how many different uses Treasury—and you can take this on notice—have for your data? Are you able to calculate that?

Mr Skinner—I think the short answer is that we would not; and I am not sure that we would know unless we asked Treasury themselves, in which case the question might be better directed to them.

CHAIR—From time to time you review your workload and invite organisations to put views to you as to whether you should change your focus, or better focus, or whatever else. In doing that, has Treasury ever put to you what they regard as your key statistics: things that they have regard to most, things that they would like to see you do?

Mr Skinner—I am not aware of any single submission where there is a ranking of various statistics. But, from the very extensive discussions we have with Treasury as a key user and a number of other key users, we have, I think, a pretty good understanding of some of the things that they would see in that top basket. The CPI would be one and the national accounts would be another—that is population estimates, labour force statistics, and so on. Whenever we are reviewing our program, we do consult quite widely to get that understanding of quite different judgments that are made about priorities. The statistician's role then really is to weigh those and come up with a program.

CHAIR—I just wonder whether, for the sake of our committee, if you have something—and I do not want to put you to undue and extensive diversions—handy about what Treasury regard as the important issues for the ABS, you could let us have that.

Mr Skinner—I am trying to reflect on what document there might be. It would be a question which would be more easily answered, I think, by Treasury, unless there is a document that exists—and I am fairly sure that it does not exist. To go to a major government agency and ask them to rank their statistics in particular priorities is not the sort of thing that we do; we tend to look at them in various groupings.

Senator CONROY—The reason for my question before is that I am aware that Treasury does make use of your data in something as important as a retirement income model, which is within Treasury. We do have apologise for coming to you with this. We have asked Treasury about this issue and been unable to get any answer. But on the one hand they are willing to support the use of your data to find information for retirement incomes, pension changes, all those sorts of things; yet all of a sudden this seems to be the only time they have dismissed its use. Are you aware of any other instances where they have just said, 'We will not use your data'?

Mr Skinner—I think, on a whole lot of decisions Treasury would make, our data is one of the many pieces of information they get in forming a decision. On occasions some of our data, my guess is, will not line up with other pieces, and they will choose to ignore some of our data for that purpose. It is obviously a judgment they have to make in the context of the advice that they are giving. I think, fortunately perhaps, it is not the lot of statisticians to have to make those judgments—where they are providing those data sets to aid those decisions, not to make them.

Senator CONROY—Are you aware of any work that was done in Canada on the black economy, what impacts interaction with a GST had on the economy?

Mr Edwards—This came up in some earlier questioning, and I indicated a vague awareness of some work that was done overseas. One of the examples that I had at the back of my mind was some work that I thought had been done in Canada. We would certainly be able to chase that up.

Senator CONROY—I think the Fraser Institute is one that I am aware of which has looked at this issue, and it has been able to identify which areas in an economy have suddenly shrunk after a GST being introduced. If you can chase up anything without putting yourself to a great deal of trouble, that would be appreciated.

Senator MURRAY—I would let Senator Conroy know that, whilst he was out of the room, Senator Cook explored that. Mr Skinner, have you seen the *Hansard* record of the committee's discussions with the Treasury on this inquiry and on the HES data?

Mr Skinner—Yes.

Senator MURRAY—My summary of Dr Henry's evidence and of the Treasury's approach is that they regard the HES data as lacking integrity and, therefore, have not used it in this exercise. My summary of your submission, having read it, is that you violently disagree with the Treasury—as violently as persons in the public sector can express themselves, that is. Is it correct for me to say, you having read the *Hansard* record, that you disagree with the Treasury as to the matter of HES?

Mr Skinner—I think I said earlier that I thought some of the Treasury criticism was overstated. But, as a statistician, I really must step back from the decisions, the ways in which those data will be used; people make those judgments themselves. I have not read all the *Hansard* of this committee. In that which I have read, I have seen some quite different opinions being expressed from people who have started with household expenditure surveys as a base data set—or CPI.

I can form no judgment on those. They are not exercises we get involved in, other than to provide data. We do not become involved in the econometric modelling of the macro or micro side; we are not experts in that area. We really have to leave those decisions for the treasuries to make, their knowing what it is they will do with it and how it will be used.

Senator MURRAY—I searched in your submission for instances where the Treasury does use your data, and I am aware of areas where they do. In item 4 of Mr McLennan's letter, he indicated the places in which the ABS use the data. If you turn to your submission, item 9, you itemise where the Treasury uses the data. You say:

The weighting patterns used in constructing the 12th series CPI (the series used by Treasury in its modelling of new taxation arrangements) were based on results from the 1988-89 HES.

So we know that the CPI is built up on the back of HES and we know that Treasury use the CPI, and yet Treasury say that the HES lacks integrity. I am afraid, logically, that does not follow for me. I would ask whether you, being in a profession of people who specialise with logic, agree with me.

Mr Skinner—In my reading of the evidence that was given earlier, I thought there were occasions where some of the logical flows did not exist. There was one given, I think, which I did jot down which was: if HES is irredeemably flawed, it automatically correlates that the CPI has to be flawed—and I am quoting from what you have said. I disagree with that. I think it was Dr Johnson who was here at the time, and he agreed with the statement.

There is a non sequitur in there for the very good reason that we know that HES does have some flaws. Whether it is irredeemably flawed is, again, a value judgment, I think, depending on the purpose. It certainly is a value to be used in certain types of analysis. But we do not unthinkingly take our HES data and merely calculate the weights of the CPI. We put a lot of effort and analysis into ourselves examining the accuracy of that HES data, and we compile the CPI weights accordingly.

Later in the submission, we go through those steps. There are some quite significant steps in there where we are making value judgments of our own, based on our own analysis and comparisons with external benchmarks as to how good the data is, and we will make adjustments as we move through to the CPI weights.

Senator MURRAY—What I think the committee would accept—and my colleagues will correct me if I am wrong—is that the current HES is outdated; you have a new HES which you are about to bring on, as I understand it.

Mr Skinner—We conduct the HES every five years, so there is a 1993-94—

Senator MURRAY—It is five years old, essentially.

Mr Skinner—It is now five years old; that is correct.

Senator MURRAY—The latest one, I understand, will be released this year.

Mr Skinner—Not quite. We will finish collecting it in June-July this year, and it will take us about nine or 10 months to start releasing it.

Senator MURRAY—It is too early to get any indications out of it.

Mr Skinner—Indeed.

CHAIR—Can I just say that I am not sure I would necessarily accept the phrase that it 'is outdated'.

Senator MURRAY—But it is five years old; would you agree with that?

CHAIR—I accept that it is undergoing current renovation to update it. But it is the current measure; that is the point.

Mr Skinner—If I may say, the 1993-94 HES is the survey that we have used in the latest reweighting of our CPI. So it is current and being actively used by us in that way.

Senator MURRAY—Perhaps I should explain that there are areas within that which I think have changed in five years. One such area in particular is that of gambling, which we were discussing earlier, where there is great difficulty in using it. We know from the state results that there has been a massive increase in the percentage of money spent on gambling. Am I correct in saying that the CPI figures used in ANTS are based on the 12th series?

Mr Skinner—That is correct.

Senator MURRAY—You have stated in section 49 that you have now, since ANTS, moved on to the 13th series. You have said something which for me has significance, but maybe I am overstating it. You have said:

The two most noticeable changes introduced in the 13th series CPI—

that is, compared to the 12th series—

were:

extension of the population coverage of the CPI from wage and salary earner households to all private households—

so that is a huge jump—

in the eight capital cities.

So it still excludes rural and regional Australia. You then said:

This has resulted in the population coverage increasing from 29% to 64% of Australian private households . . .

As a non-statistician but as a plain person, as Senator Cook would say, I would assume that a CPI which covers 64 per cent of Australian households is a far better guide to the likely situation in the community than one which covers 29 per cent. Is that a reasonable assumption?

Mr Edwards—Yes, it is a reasonable assumption, depending on what you are trying to measure with your consumer price index. Historically, the CPI was geared around the highly centralised wage and salary setting arrangements in Australia, hence its limitation to the wage and salary earner household sub-population. The principal purpose of the 13th series CPI has been quite explicitly redefined to be a measure of household price inflation. Therefore, in the context of that redefined objective for the CPI, it is entirely appropriate to broaden out the reference population group the way we did.

Senator MURRAY—As you are aware, the figure of inflation being used by the government and, therefore, the compensation consequences of that figure go to make up a particularly central issue with this package. What the government have said is that their 1.9 per cent figure is drawn on the 29 per cent of Australian households, which is based on wage and salary earners, excluding rural and regional Australia and excluding non-wage and salary earners. There are rather a high number of exclusions. The government have also then gone further and said, ‘We will apply the same percentage across all income and expenditure cameos.’

Non-government observers are saying that those are dangerous assumptions to make. You have indicated, through the quality of this submission alone, your independence, if I may pass you a compliment. As professional statisticians—not as persons judging any actions of the Treasurer or anybody else—is that a wise set of assumptions to make?

Mr Skinner—The difficulty I have in answering is that you are putting us back into the role of ‘fitness for purpose’. The way I would view the Treasury position is that they have looked at the household expenditure data and its soundness for a particular analysis and they have looked at the so-called CPI based analysis. So presumably—and publicly, I think now—they have made a judgment that, in terms of 'accuracy/fitness for their purpose', one is better than the other.

Senator MURRAY—As a statistician, let me put the question to you in a precise fashion. If you took a representative sample of self-funded retirees living in rural and regional northern Queensland and you compared them with a two-income, two-kids wage and salary earner household in Perth—at, say, the third quintile of earnings—is it reasonable to assume that their basket of goods, and therefore the effects on them of any change in prices, is the same—1.9 per cent—for the two representative samples of those two rather large groups?

Mr Skinner—I want to recast your question because I think you have made it more difficult for us to answer. The two population groups that you have identified are very tiny groups.

Senator MURRAY—Well, give me two big groups.

Mr Skinner—I could give them as large as a pensioner household and a wage and salary earner household. Your question could easily be: is the distribution of expenditures, the pattern of expenditures, between those two household groups the same or different?

Senator MURRAY—Give me northern Queensland, rural and regional pensioner household versus a Perth—

Mr Skinner—My difficulty with the northern Queensland, third quintile, whatever, is that when I go to my household expenditure survey and look at it I will have very few observations. The estimates of the patterns of expenditure we will come out with will have very high standard errors. The two populations I have just given you—pensioner households and wage and salary households—have got very large populations and so I would have more confidence that the patterns that came out could be compared reasonably.

Senator MURRAY—And would they be the same?

Mr Skinner—I think the analysis is on the table already; they are not the same. Now what effect that difference has on the judgments and decisions that are made from it is not a question for me. That is for others to make and they have made that judgment.

Senator MURRAY—If I may pursue this, it may be reasonable for the government to say, 'Look, we'll put 1.9 per cent across, but we're now going to add this cushion, and that accounts for a standard error.' That is one way of dealing with it. Of course, the government has not said that all people will get is 1.9 per cent, so let us be fair in this argument. They have said it is 1.9 per cent plus something else. But what I merely wanted to know from you is that it is highly unlikely—as a statistician—that in large groups of dissimilar Australians the percentage will be the same. I understand your answer to be 'no'.

Mr Edwards—Yes. As statisticians we can say that the expenditure weighting patterns would be different. Obviously, if you are living in northern Australia your expenditure on heating, for example, is quite low, relative to households in Tasmania. So, yes, we can say the expenditure weights would be different. Then if you are asking us to say, 'What does that mean in terms of price change?' we could only speculate on that in terms of what the relative price changes are going to be for those various spending patterns.

Senator MURRAY—I will ask you one last question and then move the questioning back to Senator Conroy. My last question is this: you are probably familiar with your December quarter publication—I hope so!

Mr Skinner—It is not the first time we have seen it!

Senator MURRAY—I would be disappointed if you were not! There is a section marked '3' which has 'CPI groups—weighted average of eight capital cities' and has in there the major categories of food, clothing, housing, et cetera, all the way through to all groups. That runs back for four years. What that shows me is that over the past four years, food has been growing at nearly twice the CPI rate overall as a generalisation. It has certainly been growing faster. It moves from 110.9 per cent in 1994—sorry, not twice—to 126.0 per cent in 1998. The all groups is 112.8 per cent to 121.9 per cent. So it is a faster rate. That is correct, isn't it?

Mr Edwards—Looking at table 3, which I gather is the one you have got in front of you—

Senator MURRAY—I will show it to you. That is correct?

Mr Edwards—Yes. In 1994-95, on an index base of 1989-90 equals 100, the level of the CPI index for food was 112.1.

Senator MURRAY—Why does mine say 110.9? Sorry, 112.1, yes I have found the figure.

Mr Edwards—In 1994-95 the all groups CPI was 113.9—that is the right-hand column. At the December quarter 1998, which is the bottom row, there is 126.0 for food, and 121.9 for—

Senator MURRAY—That to me means food price grew greater than did the all groups price: that is correct isn't it?

Mr Edwards—Yes.

Senator MURRAY—My question to you again—as a statistician—is this: is this a trend that goes back to way back when you started, or is this a recent trend?

Mr Edwards—No. In fact, it is reasonably recent. If I could draw you to the March quarter 1997 in that same table, you will see the index number for food of 120.2, and for the all groups CPI 120.5. So at the March quarter 1997 the index number for food and the index number for all groups CPI—

Senator MURRAY—Were nearly equivalent.

Mr Edwards—Were pretty close, whereas, in the periods since then, food has deviated quite a deal more than the all groups.

Senator MURRAY—All right. The relevance of my remarks, you would understand, relates to the fact that food is, again, a central issue in this debate. My question then is as follows: would a household with higher food expenditure within its basket of goods, which is growing faster than the all groups—anyway generally—so who is higher within their particular basket of goods? Would they have a higher CPI, therefore? Let me give you a statistical example of it. If it was 35 per cent in one and 20 per cent in somebody else's, their CPI would be greater, wouldn't it, as a gross thing?

Mr Skinner—That is correct.

Senator MURRAY—So if this trend in food continued—that it continued to grow faster than the all groups area—people with high fruit components within their basket of goods would, on the government's formula, need greater compensation? That is the logical progression, isn't it?

Mr Skinner—I think logically progressive, but others can form that final step, I think. I will go beyond the statistician at that point.

Senator MURRAY—Thank you, I will leave it there.

Mr Edwards—I should point out, Senator, coming back to some earlier questioning about fruit and vegetables, that over the last 12 months the price of fresh fruit and vegetables has increased quite considerably—from memory, 22.4 per cent over the 12-month period.

Senator FERGUSON—It actually went higher than that—26 per cent and 29 per cent. But it does also show that the lowest quintile spend 2.2 per cent of their income that they spend on food on fresh vegetables and for the second quintile 2.02, I think, is the percentage of income that is spent on fresh food and vegetables as part of the food budget.

Mr Skinner—I think I will to take your word for it without checking.

Senator FERGUSON—I do not always study the ABS documents as they come out, but I was particularly noticing this one.

Senator CONROY—I just have a very quick question. The CPI excludes the non-metro?

Mr Skinner—Basically yes.

Senator CONROY—The assumption everyone makes from that is, therefore, it is a little bit more expensive outside. Do you have any data that would support that—that it is more expensive in that area? Do you have enough data to make that assumption? Do you have any data?

Mr Edwards—There are two points that I would like to make there, and they relate to whether we are trying to measure price levels or price changes. It is certainly clear that price levels outside the metropolitan areas are quite likely to be different from price levels within the eight capital cities. Whether prices change at a different rate ex-met compared with the metropolitan areas, is another matter. We do not have much evidence one way or the other on the second point. What I can say is that up until 1990, the ABS collected statistics on food prices for 200 country towns in Australia. The data show that over a 30-year period food prices did not change very differently in those country towns from the capital cities. That is a general comment. There were some exceptions to that, though. For example, where there was a significant structural change like a branch railway closing down to a particular country town, then that could have impacted the prices. But in the absence of that sort of change the data we have—which only covers food and only covers the 200 country towns that were covered—showed that price change was about the same.

Senator CONROY—I am just trying to think that through intuitively. Your price level is higher in the country. No-one argues that.

Senator FERGUSON—Not for everything.

Senator CONROY—You are saying the percentage change is the same. I guess there is no way to either prove or disprove it but if head office decides to increase the price of a loaf of bread by 50c then it is 50c everywhere, presumably.

Senator MURRAY—Fifty and 110 is more—

Mr Skinner—If I can put it a different way, on a basket of goods it may well be that in a capital city the total cost of that is $100 and in a country area it is $120. Over a 10-year period the prices may go up 10 per cent in each. So the prices rise at exactly the same amount.

Senator CONROY—That is what I was just trying to—

Mr Skinner—You have the same differential of level at the end.

CHAIR—People migrating from the city to the country are likely to be hit with a higher bill.

Mr Skinner—Yes, because the levels are different. People migrating the other way may be hit with a lower one.

CHAIR—That is correct.

Senator FERGUSON—I think there is also a converse of that. As I live in the country I know that in most cases the number of people who move into the country are single parents with children and pensioners. They move there because in fact it costs them less to live in the country than it does in the city.

Senator MURRAY—Is it housing?

Senator FERGUSON—Housing is part of it. But they actually move to the country because they find that they can afford to live in a country town much more easily than they can afford to live in the metropolitan area. So I think it probably balances out.

Mr Skinner—What we are saying is that over a period of time the prices tend to move in the same way but the levels will stay the way they were. If they were a certain distance apart to start with they will end up about the same distance apart after a long period.

Senator GEORGE CAMPBELL—If you apply tax—

Mr Skinner—If it is equally provided then it will just continue to move relative to one another in the same way. It is the same tax rate.

Senator GEORGE CAMPBELL—But if you are paying $100 for a parcel of goods, and you apply a 10 per cent tax on that, it is $110. If you are on $120, at 10 per cent you are paying $132. So the gap in fact has widened.

Mr Skinner—In absolute terms, yes.

CHAIR—When we started this there was some suggestion that we may not take the full hour but we have taken over 70 minutes. This does indicate that there is considerable interest in the work that you do and the weightings and meanings that we should assign to it. I thank you very much, Mr Skinner, and your colleagues Mr Kroon, Mr Edwards and Mr Woolford, for giving us the evidence that you have. I note there are several takeaways that have been offered to you, some of which you have accepted. We look forward to receiving your advice on that. Thank you very much. This hearing is now adjourned.

Committee adjourned at 5.09 p.m.