How Australia Got a VAT

By Susan C. Morse

Australians, like Canadians and New Zealanders, call their VAT a goods and services tax, or GST, but their GST fits the VAT mold: it is a credit-invoice method, destination-based consumption tax with fairly limited tax base exclusions.1 Although all OECD countries aside from the United States have value-added taxes, external pressures like those resulting from preconditions for European Union membership2 or for financial support from organizations such as the World Bank or International Monetary Fund3 have played a role in many countries’ VAT enactment

1See Liam Ebrill, Michael Keen, Jean-Paul Bodin & Victoria Summers, The Modern VAT 2 (2001) (defining a VAT). This paper uses the term tax base “exclusion” to mean “a situation in which the rate of tax applied to sales is zero, though credit is still given for taxes paid on inputs” which is called “GST-free” in Australia and “zero-rated” elsewhere. This contrasts with “exemption” or, in Australia, “input-taxed” treatment, which means a situation in which “tax is . . . not charged on outputs, [but] tax paid on inputs cannot be reclaimed.” Id. at 3.

2See European Economic Community First VAT Directive (Apr. 11, 1967) (“Member States shall replace their present system of turnover taxes by the common system of value added tax . . . ”).

stories. In other cases, an unusual exercise of executive authority\textsuperscript{4} or extreme fiscal crisis\textsuperscript{5} helped make it happen.

Australia is interesting because its GST came about through a more conventional political process.\textsuperscript{6} John Howard, the conservative Liberal National Party coalition (LNP Coalition) Australian prime minister from 1996 to 2007, made the GST a central plank in his policy platform in the 1998 national election and oversaw its enactment in 2000. Its implementation is the most recent in the OECD and included a federal solution. And the GST-enacting LNP Coalition government retained power for seven years after the legislation passed.\textsuperscript{7}

(In Australia, two major political blocs dominate politics at the national level. The Liberal and National parties in practice are a permanent center-right coalition between the Liberal Party, which focuses more on urban interests, and the National Party,


\textsuperscript{7}See David Adams, Staying On, in Howard’s Fourth Government 263, 282 (Chris Aulich & Roger Wettenhall, eds., 2008) (noting Howard’s mostly superior performance in public opinion polls until he “met his electoral match” in Labor’s Kevin Rudd in 2007). By some measures, the GST is popular too. In an informal online poll conducted by the Sydney Morning Herald in June 2010, 84 percent of the 3432 recipients responded to the question “Do you think the GST has been beneficial to Australia’s economy?” with the answer “Yes, it simplified the tax system across the country” rather than “No, it made the cost of many goods and services prohibitive.” See Poll, available at http://www.smh.com.au/opinion/politics/if-its-tax-reform-you-want-try-the-gst-20100622-yvq.html#comments (last visited June 25, 2010). However, the Australian Democrats, some of whom supported a GST with improved distributive qualities, thus permitting the reform package to pass the Senate, were “decimated” in subsequent elections. See Kathryn James, An Examination of Convergence and Resistance in Global Tax Reform Trends, 11 Comp. Tax L. & Culture 475, 479 (2010).
which draws its base from rural regions. The LNP Coalition maps most closely onto the Republican Party in the United States, and the Labor Party corresponds most closely to the U.S. Democratic Party.

This paper discusses four components of the Australian story: (1) framing the GST as a relatively efficient tax; (2) building an interest group coalition; (3) emphasizing efficiency while addressing regressivity in the political and legislative process; and (4) the use of a side payment to solve the challenge of coordination with the six states and two territories, or, collectively, the states.

A Relatively Efficient Tax

In 1972, LNP Coalition Prime Minister William McMahon called for a study of Australia’s tax system. The 1975 Asprey Report resulted. In its early sections the report considered the ideal tax system without reference to existing particulars of the Australian tax law. Based on the principles of “equity, simplicity and efficiency” it compared the two extremes of “a single broad-based tax on goods and services” and an income and capital tax system. It called the consumption tax alternative superior on simplicity and efficiency grounds, but inferior on equity grounds. This draws on the empirical consensus that consumers bear the burden of a well-designed VAT, and the

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9 See Judith Brett, Australian Liberals and the Moral Middle Class From Alfred Deakin to John Howard 176-77 (2003) (noting Liberal’s relative commitment to “individualism” and Labor’s relative commitment to “collectivism”).
10 See James, supra note 6, at 327 (noting that the Asprey Report was the first official consumption tax recommendation in Australia).
12 See, e.g., Charles E. McLure, The Value-Added Tax: Key to Deficit Reduction? 45-46 (1987) (noting that in Denmark and Norway, where a VAT did not replace other taxes and where therefore data were cleaner, consumer prices rose upon enactment); Michael Smart & Richard M. Bird, The Economic Incidence of Replacing a Retail Sales Tax by a Value-Added Tax: Evidence from Canadian Experience 35 Can. Pub. Pol’y 85, 95 (2009) (concluding based on event study following some Canadian provinces’ replacement of retail sales taxes with value-added taxes, that changes in taxes related to the transition were fully shifted (and perhaps in some cases over shifted) to consumers).
related view that a VAT is relatively efficient in a global economy if the location of consumption is relatively inelastic.\footnote{See, e.g., James R. Hines Jr. & Lawrence H. Summers, How Globalization Affects Tax Design, 23 Tax Pol'y & Econ. 123, 126 (2009) ("In a globalizing world, expenditures have relatively clear geographic associations, reducing the potential for international tax avoidance and generally reducing the mobility of the tax base compared to alternatives such as personal income taxes or source-based business taxes such as the corporate income tax."). The point about globalization is distinguishable from, but not inconsistent with, the optimal taxation idea that a consumption tax is preferable to an income tax because it avoids taxing capital income and thus avoids distorting taxpayers' choice between present and future consumption. See, e.g., Joseph Bankman & David A. Weisbach, "The Superiority of an Ideal Consumption Tax Over an Ideal Income Tax," 58 Stan. L. Rev. 1413, 1422-30 (2006) (discussing double distortion argument and possibility of addressing redistributive concerns through the consumption tax structure). There are also political economy considerations relevant to the use of a VAT in addition to an income tax base. See, e.g., Neil Brooks, An Overview of the Role of the VAT, Fundamental Tax Reform, and a Defence of the Income Tax 597, 607-08, in GST in Retrospect and Prospect, supra note 5 (raising the possibility that the "[h]aving lower rates of tax and two tax bases will lead to less political pressure for special treatment").}

The report recommended starting with a consumption tax and solving the problem of regressivity with "an income tax and a capital tax with high minimum exemption limits that effectively confined their impact to the upper end of the scales of income and wealth" plus "grants . . . to deal with vertical and horizontal equity at the other end."\footnote{See Asprey & Parsons, supra note 11, at ¶¶ 5.2-5.7.} In particular, it expressed a strong preference for a VAT relative to the existing cascading and differential Wholesale Sales Tax (WST), a multirate consumption tax paid by businesses through the wholesale level on sales of most goods, but not services.\footnote{See id. at ¶¶ 27.27 & 27.28 (identifying WST disadvantages of favoring goods with a relatively large "proportion of . . . value . . . added at the retail level" and impracticality of taxing services at the wholesale level); ¶¶ 27.31, 27.38 & 27.39 (recommending a VAT as the best broad-based consumption tax option); Neil Warren, Tax Facts Fiction and Reform 32, 35 tbl. 2.2 (2004) (describing narrow base and multiple rate structure of WST).} The suggested approach reflects a certain throw-up-the-hands approach to distributive justice;\footnote{Cf. Eccleston, supra note 6, at 59 (noting that the Asprey committee did not receive political input relating to the "normative objectives of tax reform").} the authors conceded the persuasiveness of the distributive case at either end of the wealth or income spectrum, but considered that in the "middle band" covering most Australians, the population "will accept as fair and convenient an approximately proportional taxation system."\footnote{Asprey & Parsons, supra note 11, at ¶¶ 4.37 & 4.38.}
The Asprey Report received support from both the LNP Coalition and Labor. The Labor government in office in 1975 when the report was released did little with it, but an unsuccessful consumption tax proposal surfaced in 1980-1981 under the LNP Coalition Fraser government, in which Howard was the Treasurer. Then, the reformist Hawke Labor government presented a retail sales tax proposal as the leading option in a comprehensive tax reform package draft prepared for a prominent tax summit with stakeholder groups in 1985. But base-broadening fundamental income tax reform prevailed instead.

In 1991 the LNP Coalition attempted to win leadership of the government from the Labor party with a comprehensive economic reform platform called “Fightback!”, which advocated a 15 percent “food in” GST and outlined a comprehensive package of offsetting personal income tax cuts and compensation measures including family allowance and pension and welfare increases. Fightback! had business support, but the LNP Coalition faced significant political pressure from “politically savvy yet fiscally irresponsible” promises made by Paul Keating, the Labor Prime Minister, to match Fightback!’s income tax cuts without imposing a GST. In 1992, the LNP Coalition revised Fightback! by removing food from the base and proposing smaller reductions to the

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19See Eccleston, supra note 6, at 69 (describing Howard’s “open commitment to broadening Australia’s consumption tax base in order to provide income tax relief”); James, supra note 6, at 330 (recounting several Howard efforts to push consumption tax reform in the Fraser government).

20The Hawke government’s proposal for a 12.5 percent retail sales tax was aired at a stakeholder summit promised in the 1984 election and was championed by Paul Keating, then the Treasurer. At the summit, a central business group refused to support it reportedly in part because of accompanying proposals to tax fringe benefits, while union and welfare groups refused to accept it based on regressivity and inflation problems. See Eccleston, supra note 6, at 90-91; James, supra note 6, at 334-35 (noting business support for a consumption tax but opposition to any direct tax increases and welfare group opposition to consumption tax). The 1980s tax reform materially changed the Australian income tax, including by enacting a capital gains tax and fringe benefits tax, thus significantly expanding the range of income subject to tax. See Richard Vann, Australia, 3, 7 in Comparative Income Taxation: A Structural Analysis (Hugh J. Ault and Brian J. Arnold, eds.) (3d ed. 2010).

21See Eccleston, supra note 6, at 104 (describing Fightback! I).

22See James, supra note 6, at 337.
top income tax rates to make up lost revenue. But the LNP Coalition still lost — a surprising result given the serious economic recession presided over by the Keating government.

After the election, the Keating government’s 1993-1994 budget quickly made it clear that the promised income tax cuts would be rolled back and a budget deficit offset by “a $3 billion increase in the WST tax and alcohol, fuel and tobacco excises” — taxes which were more regressive and less efficient than the GST proposed by the LNP Coalition in the election. Welfare groups’ realization, in the aftermath of the 1993-1994 budget, of the possibility of even higher, less efficient taxes or inadequate funding for social welfare programs in the absence of consumption tax reform has been called an example of “active learning by key interest groups in the Australian tax policy process.”

Even though neither party mustered a successful consumption policy proposal in the 20 years following the release of the Asprey Report, a common analytical framework had taken root. The VAT option was understood as a better tax from an efficiency perspective, certainly compared to the WST and in some views compared to the personal income tax, but a worse tax from a regressivity perspective. “Efficiency” meant at least two different things: nondistortionary to trade and economic productivity, and therefore better for business competitiveness; and also less susceptible to tax planning and politically motivated base erosion, and therefore better for ensuring revenue stability for social

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23 See Eccleston, supra note 6, at 115-16 (describing Fightback! II).
24 Sources refer to an “unloseable election” given “a Prime Minister who was responsible for the worst recession since the war.” Brett, supra note 9, at 182; see also Eccleston, supra note 4, at 78 (noting Labor’s “superior political strategy and leadership”); James, supra note 6, at 336 (noting 17 percent interest rates, 11 percent unemployment and “record levels of foreign debt”).
25 See Eccleston, supra note 6, at 123-24 (describing Keating tax increases once in office). The failure of the 1985 reforms to achieve revenue neutrality contributed to the deficit situation. See James, supra note 6, at 335.
27 See Eccleston, supra note 6, at 48 (noting WST’s narrow base, its exclusion of services, its taxation of business inputs, its multiple rate structure and its complex exemption rules); Warren, supra note 15, at 35 tbl. 2.2 (showing different rates under WST); 37-38 & fig. 2.1 (showing that the GST’s replacement of the WST reversed the trend of declining consumption tax contribution to tax revenue).
welfare programs.28 This idea of the GST as an efficient tax with a regressivity problem would frame the ultimately successful effort, powered by interest groups as well as politicians, to enact a GST over the five years from 1996 to 2000.

Forging an Interest Group Coalition

In 1996, under Howard’s leadership, the LNP Coalition re-claimed the Australian government on a platform that did not include any reference to the GST. Howard emphatically distanced his party from the issue. He replied as follows to a reporter who asked him if he would propose a GST:

Howard: “No, there’s no way that a GST will ever be part of our policy.”

Journalist: “Never ever?”

Howard: “Never ever. It’s dead. It was killed by the voters in the last election.”29

Yet in 1998 Howard led his party to victory in a parliamentary election presented as a referendum on the GST.30

In the intervening two years, there developed a fascinating interest group discussion about the GST quite independent from government. One main player was the Australian Council of Social Service (ACOSS), the “peak” council of Australia’s “community services and welfare sector.”31 Another was the Australian Chamber of Commerce and Industry (ACCI), which has “more than a century of history serving the interests of business.”32 Business groups such as the ACCI supported the GST,

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28See Warren, supra note 15, at 81 (2004) (“The economic case for a GST rests on two main attributes: revenue raising ability and its neutrality properties. Having a broad base, the GST has significant revenue raising potential at relatively low rates and secondly, it has the ability to ensure cross-border trade is free of tax based distortions.”).


30See id., at 273 (“Well, here it is...here’s the new policy. If you don’t like it you can throw us out,’ and they almost did.”) (quoting treasurer Peter Costello’s recollection of the 1998 election).


32See http://www.acci.asn.au (last visited June 21, 2010). ACCI collects and disseminates data on business activity, develops and distributes issue papers and various other (Footnote continued on next page.)
and the discussion convinced ACOSS to accept the idea of a GST, subject to appropriate compensation to address regressivity and inflation.33

ACCI appears to have devoted substantial energy to this issue in large part because, consistent with business groups’ support of Fightback!, it believed in the GST as a better tax policy alternative for business, particularly compared to the WST. ACCI’s view, like the LNP Coalition’s, highlighted the competitive economic efficiency of a GST for a small global economy. ACCI argued that the GST would affect business decisions and resource allocation less than other alternatives, including the WST.34

Why did ACOSS come to the table? Social welfare leaders recognized that the excise and WST increases adopted by the Keating Labor government in 1993-94 were even more regressive than a GST.35 And concerns about revenue security for social welfare programs, developed over years of observing budget policy and communicating with Labor and LNP Coalition governments, also appear to have motivated ACOSS participation.36

Personal willingness to engage in genuine discussion of the issues must also provide part of the answer. One commentator writes simply that “Graeme Samuel, president of [ACCI], expressed support for the introduction of the GST and persuaded

publications, and lobbies on behalf of business interests. Its members include the chambers of commerce and industry such as the Australian Federation of Employers and Industries, state and territorial business groups, and numerous industry groups (the Australian Food and Grocery Council, for example).

ACOSS proposals also advocated for substantial broadening of the income tax base in order to shut down strategies used by the relatively wealthy to reduce their taxes and suggested the transfer of GST revenue to the states. See Peter Davidson, “Tax Reform: A Retrospective,” 23 Univ. N.S. Wales L.J. 36 (2000) (noting that these proposals were largely not adopted as part of the GST reform).

See, e.g., Aus. Chamber of Commerce & Industry, Tax Reform: The Need to Push Ahead 3 (2007) (citing goals of “improv[ing] the overall competitiveness of Australian goods and services . . . and ensur[ing] that the tax system encourages employment, savings and productive investment”). The ACCI document also considers the goals of simplicity and administrability and the advisability of achieving revenue security “for all levels of government.” Id.

See Eccleston, supra note 18, at 298.

Robert Fitzgerald, president of [ACOSS], to support it.”\textsuperscript{37} Another observes that “key business and welfare leaders such as Graeme Samuel and Michael Raper [later president of ACOSS] actively played the role of policy entrepreneurs mobilizing a cross-class coalition for tax reform.”\textsuperscript{38}

On October 3-5, 1996, ACOSS and ACCI held a Tax Reform Summit. “Parliamentarians and public servants were not invited.”\textsuperscript{39} Following the summit, a Tax Reform Forum that the two groups formed went on to hold tax reform roundtables in the subsequent year. These efforts provided opportunities for both the business interests and the welfare interests to articulate their concerns and priorities. The joint press release that emerged from the summit, for example, articulated seven tax reform criteria.\textsuperscript{40} It implicitly expressed support for a broad-based consumption tax by recommending “[b]roadening the tax base by removing unjustifiable gaps, biases and distortions . . . in each of the following areas: income, assets and consumption” and “[t]he integration, extension or abolition of existing narrowly-based taxes.”\textsuperscript{41} It also called for increased progressivity, simplification and integration of national and state taxes, as well as a sustainable plan to raise adequate government revenue.\textsuperscript{42} The discussions reportedly generated policy benchmarks including the belief that a 15 percent rate was too high to permit adequate compensation.\textsuperscript{43}

ACCI and ACOSS continued to articulate different agendas following their cooperative meetings. ACCI emphasized the ways in which the 1996 summit and roundtable discussions supported consumption tax reform. In a policy paper released about a year after the 1996 summit it said that “productive

\textsuperscript{37}Id. at 149.
\textsuperscript{38}Eccleston, supra note 4, at 83.
\textsuperscript{40}These were equity, efficiency, adequacy, simplicity, transparency, cost minimization and minimal incentive for tax avoidance. See Joint Statement from Graeme Samuel, President, ACCI and Robert Fitzgerald, President, ACOSS (Oct. 5, 1996) (hereinafter Joint ACCI-ACOSS statement)
\textsuperscript{41}Id.
\textsuperscript{42}See id.
\textsuperscript{43}See Harrison & Stretten, supra note 39.
business plays a vital role in creating wealth, tax revenue and employment, and that the tax system [particularly the WST and high individual income tax rates] is limiting productivity." It wrote that ACOSS “recognise[d]” the productivity issue.

Perhaps so, but ACOSS had not conceded its concerns over the regressivity of a consumption tax, including the regressivity of inflationary effects and the importance of income tax reform. In a contemporaneous paper ACOSS stated that it had “neither advocated nor rejected a GST. . . . The impact of any GST proposal would be determined not only by its precise nature (such as the rate and coverage) but also by the total package of which it is part.” ACOSS expected part of that package to consist of fully offsetting cuts in other consumption taxes, in addition to inflation-offsetting increases in social security payments. Its position was that any income tax cuts should be funded by base-broadening measures applicable to wealthy individuals and businesses.

Addressing Regressivity
Despite a continued divergence of views after the 1996 summit, interest group agreement on a policy framework provided Howard with a substantive starting point and political cover for making GST reform his issue again. Economic growth and a

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45 See id.
46ACOSS, Tax Reform Pack (September 1997).
47Davidson, supra note 33 (noting ACOSS’s emphasis on income tax base broadening as part of the package, which was not in ANTS, though ANTS did include a few items such as taxing trusts like corporations).
48Howard’s earlier support for consumption tax reform provides one explanation for his support of the GST as good policy, see supra note 19, but the story does not appear to be that of a strong executive spending his political capital. Howard may have had little to lose in choosing the GST as the centerpiece of his platform. According to one account his popularity rating was 20 percent in 1997 while the GST’s was 59 percent. See Eccleston, supra note 18, at 299. See also James, supra note 6, at 341 (“Sensing the mood for change, Howard hoped to use his career-long commitment to broad-based consumption tax reform to salvage his declining credibility on a range of economic, political and social issues.”).
strong fiscal position also helped pave the way to reform. In August 1998, Treasury released the white paper titled “A New Tax System” and generally known as ANTS, which included the 10 percent GST that was largely enacted in 1999. Tax reform was the central policy question in the October 1998 parliamentary election, a narrow LNP Coalition success. After the election, the LNP Coalition controlled the House of Representatives but not the Senate, where it was a few votes short of the number necessary to pass the tax legislation.

ANTS emphasized the capacity of the GST to stimulate economic growth. In particular, ANTS noted Australia’s status as a relatively small open economy and the discriminatory pricing problems presented by the cascading and unevenly applied WST to Australian exporters and producers of goods for domestic markets in which importers also competed. The public relations and advertising efforts mounted by the LNP Coalition and

49 See James, supra note 6, at 342 (noting the relatively good state of the Australian economy).

50 ANTS also included other items such as an overhaul of the business tax payment system which instituted uniform taxpayer numbers, monthly or quarterly payments and a single tax return used for different taxes owed regularly by businesses. See Tax Reform, Not a New Tax a New Tax System: the Howard Government’s Plan for a New Tax System 133-46 (Aug. 1998) (hereinafter “ANTS”); Warren, supra note 15, at 17 (describing tax administration reforms).

51 See Tom Allard, Democrat Deal Clears Way of Tax Inquiry, Sydney Morning Herald, Nov. 25, 1998, at 5 (reporting the necessity of either Democrat or independent support for the GST measure in the Senate).

52 For example, of the 14 reasons offered as to “[w]hy a new tax system is a clear national priority for Australia” in ANTS, 8 are best described as economic reasons. The document argues, for example, that the tax system should “reward growth and employment” and “avoid exemptions and loopholes that distort investment decisions and consumer choice.” Three of the 14 statements make general assertions about the outdated state of the Australian tax system, one mentions the federalism problem of “revenue security” for the states and territories, and two focus on simplicity and/or administrability. In addition, two statements mentioned the goal of fairness in connection with other stated priorities. ANTS, supra note 50, at 4-5. A large literature considers GST administration and compliance. See, e.g., Cedric Sandford, Minimising the Compliance Costs of a GST, in Tax Administration: Facing the Challenges of the Future (Chris Evans & Abe Greenbaum eds. 1998). For a view challenging the assertion that the GST achieved massive simplification and tax administration improvements, see Stewart Karlinsky, Dale Pinto & Jeff Pope, “Top 10 Myths of a Consumption Tax System,” Tax Notes, July 25, 2005, at 453.

53 See ANTS, supra note 50, at 7-8 (“Australia’s exports and import-competing goods and services have to bear the burden of wholesale sales taxes which cascade throughout the production and value-adding processes, while no such burden is applied to the traded goods and services sectors of our competitors. . . . The choice of business

(Footnote continued on next page.)
Howard’s government also reflected its belief in the competitive efficiency of the GST, though at least some communications also permitted the interpretation that ANTS would provide the benefit of greater efficiency as social welfare groups saw it — in other words, greater revenue-raising efficiency through a broader, more secure and better administered tax base.

Almost two years elapsed between the release of ANTS in August 1998 and the entry into force of the negotiated GST tax package on July 1, 2000. That time saw three successive public relations challenges: to win the October 1998 parliamentary election on a platform dominated by the GST issue; to support a legislative compromise resulting in GST enactment in June 1999;54 and to smooth the public acceptance of the GST in advance of its implementation in 2000.55 The legislative negotiations certainly involved considerable detail, and the outreach and educational programs designed to enable taxpayers to comply with the new law deployed familiar tax administration tactics, including public rulings, fact sheets, Web-based advice and in-person “advisory visits.”56

But perhaps the most striking aspect of the public relations effort was the Howard government’s ability to package its complex tax reform plan in a simple, aspirational, and somewhat ambiguous efficiency concept. Of the September 1998 “launch” of the LNP Coalition election platform, one commentator writes:

Howard led with the tax package, asking voters to see the national interest ahead of personal doubts and fears. This reflected a recognition that the detail of the package was

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54 See Ross Peake, Senate Approves GST, Finally, Canberra Times, June 29, 1999, at A3 (reporting passage of GST on June 28, 1999).
55 One commentator put the total cost of education and advertising in connection with the GST at about AUD 350 million and the cost of the “chains” campaign at AUD 46 million. See Ross Gittins, Beware the Chain Reaction, Sydney Morning Herald, June 21, 2000, at 21.
56 Michael D’Ascenzo, Commissioner of Taxation, Australian Taxation Office, Australia’s Approach to GST Administration, Speech Before Twenty Years of GST: The Best Path Forward Conference (Nov. 16-18, 2006). See also, e.g., Benjamin Haslem, Tax Office Draws GST Line Through Food, The Australian, June 15, 2000, at 1 (reporting release of “500-item” “definitive GST food guide”).
now damaged goods. The policy was now being sold as a test of political courage and forward thinking.\textsuperscript{57}

Another commentator writes that \"[s]ensing the mood for change, Howard hoped to use his career-long commitment to broad-based consumption tax reform to salvage his declining credibility on a range of economic, political and social issues.\"\textsuperscript{58}

The 2000 \"Chains\" advertising campaign also managed to transcend detail. It had a slogan: \"Tax Reform: Because We Shouldn’t Hold Australia Back\”; a song, the licensed Joe Cocker number, \"Unchain my Heart\”; and \"emotive image[s]\"\textsuperscript{59} of \"people being freed from hefty chains.\"\textsuperscript{60} The campaign \"sold the concept rather than the details about the tax,\"\textsuperscript{61} leaving out regressivity and inflation and emphasizing efficiency and simplicity.\textsuperscript{62} It received criticism as \"feel-good\” advertising lacking \"hard information,\"\textsuperscript{63} and the opposition Labor Party objected that taxpayers had inappropriately funded political propaganda.\textsuperscript{64} Nevertheless, it appears at least that the campaign was an effective \"attention grabbing strategy\”\textsuperscript{65} — a compliment which few tax administration communication efforts can claim. And it captured the key idea of GST efficiency, however the audience chose to understand the point.

ANTS paid some notice to concerns about regressivity. It proposed to raise approximately AUD 42 billion annually through the 10 percent GST (which contributed the lion’s share, AUD 32 billion), an increase in tobacco excise taxes, some income

\textsuperscript{58}James, supra note 6, at 343.
\textsuperscript{59}See Sally Young, A History of Government Advertising in Australia, in Government Communication in Australia (Sally Young, ed. 2007).
\textsuperscript{60}Sid Marris, GST Ad Unchains Public of $270,000, The Australian, May 30, 2000, at 1.
\textsuperscript{61}Andrew McKenzie, Kiwi Tax Lesson Lost in Telling, The Australian, June 20, 2000, at 22.
\textsuperscript{62}Cf. Gittins, supra note 55 (stating that the Chains campaign \“describe[d] all the nice bits and ignore[d] all the nasty bits\”).
\textsuperscript{63}Andrew Hornery, GST Ads Panned as Fluffy Failures, Sydney Morning Herald, May 25, 2000, at 35 (quoting advertising professional Warren Brown).
\textsuperscript{64}Benjamin Haslen, Labor’s Reaction is Legal Warning, The Australian, May 29, 2000, at 8.
\textsuperscript{65}Michael D’Ascenzo speech, supra note 56.
tax base broadening, and administrative improvements. It planned to spend most of the revenue on replacing other indirect taxes: AUD 18 billion on WST repeal; AUD 7 billion for the repeal of state-level business franchise fees functionally similar to excise taxes; and AUD 5 billion on the repeal of inefficient state-level business taxes such as stamp duties, financial transaction taxes and accommodation or “bed” taxes. But it also allocated AUD 12.5 billion to personal income tax cuts, more heavily weighted toward the upper end of the income spectrum than social welfare groups preferred; AUD 2.5 billion to increased and better-designed family welfare payments; and AUD 2 billion to increased payments to pensioners. Government revenue reductions were anticipated at about AUD 5 billion annually.66

The opposition Labor Party adamantly opposed ANTS. But ACOSS — typically Labor’s political ally — instead chose to seek additional offsets to regressivity.67 And the pivotal debate in the Senate with the Australian Democrats featured a similar exercise.68 The Democrats,69 led by Meg Lees, had nine Senators after the 1998 election (though two eventually declined to support the GST measure).70 Lees was willing to negotiate. Her strategy, like the ACOSS approach, was to accept the GST and extract distributive improvements to offset the regressivity of the package, including the regressive impact of the inflation expected to result

66See ANTS, supra note 50, at 34-35, 67, 86-89, 100-04. Figures are given for 2001-2002 and usually rounded to the nearest AUD 1 billion. Various changes to excise taxes other than tobacco were undertaken to maintain the price of taxed goods (such as beer, wine and luxury cars) at the same level. See Warren, supra note 15, at 88-89.


68Cf. James, supra note 6, at 322 (noting that the Australian Senate had “evolved to become a powerful house of review”).

69The Australian Democratic Party has been described as a breakaway party from the LNP Coalition following a 1977 split and professes a “social liberal” philosophy of “free enterprise, justice and compassion governed by independent democratic institutions.” See Åron Paul & Luke Miller, The Third Team: A Brief History of the Australian Democrats After 30 Years 5 (2007) (paraphrasing speech by founder Don Chipp).

70See Ross Peake, Lees Puts Down Party Revolt on GST, Canberra Times, June 21, 1999, at A3 (reporting that the GST had split the Democrats and that two Democratic Senators would vote against the bill).
from enactment.\textsuperscript{71} The Democrats’ achievements in this respect included excluding basic food from the GST base, increasing the compensation paid to pensioners, and decreasing the reduction in personal income tax rates for upper-income taxpayers, as well as reducing certain fuel rebates on environmental grounds.\textsuperscript{72}

A Senate Select Committee played a key part in the effort to evaluate the distributive justice of the tax package.\textsuperscript{73} Composed of seven members — three from Labor, three from the LNP Coalition, and one Democrat\textsuperscript{74} — it undertook to evaluate the economic efficiency, inflation and wealth distribution results of the proposed GST reforms. ANTS already included GST-free treatment for health and medical care and services, education, childcare, charitable activities and religious services,\textsuperscript{75} and, consistent with Democrat priorities, the committee received explicit instructions to consider excluding from the tax base “the necessities of life (such as food, clothing, shelter and essential services).”\textsuperscript{76}

The committee’s work included a modeling exercise led by academic economists, which considered ten different variations
of the plan. One key finding explained that if the tax plan
excluded food from the taxable base, “the estimated [inflation]
impact of [the tax package] (2.7 percent) would be cut to 1.6
percent.” The report concluded that “low income households
would be the main beneficiaries from the exclusion of food from
the GST.” The report also stated a preference for a “the food
in/compensation up approach” rather than a “food out/tax up
approach” — in other words, for a plan that included food in
the GST base and compensated by increasing transfer payments.
Targeted grants beat tax base exceptions because they cost less, as
no benefits are extended to higher-income taxpayers and admin-
istrative costs are lower.

Yet the food exclusion approach prevailed, instead of a more
Michael Graetz-style plan that might have traded increased
income tax progressivity and transfer payments. There appear
to be at least two reasons for this. First, the food exclusion issue
had high political salience. One pair of poll questions circulated
in May 1999 revealed 40 percent support and 51 percent oppo-
sition for a GST without a food exclusion and 52 percent support
and 39 percent opposition for a GST with a food exclusion.

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77 See Select Committee Main Report, supra note 74, at §§ 2.22, 2.25. The report was
published as Neil Warren, Ann Harding, Martin Robinson, Simon Lambert & Gillian
Beer, Distributional Impact of Possible Tax Reform Packages, in Select Committee Main
Report, supra note 50, Appendix IV 445-508.
78 The inflation adjustment was less than the anticipated GST rate of 10 percent in part
because offsetting reductions in prices resulting from WST repeal were also expected.
79 See Select Committee Main Report, supra note 74, at § 2.48.
80 Id. at §§ 2.56, 2.61.
81 See Warren, supra note 15, at 93 (noting that upper-income households benefited
considerably more in absolute dollar terms from the food exemption than lower-income
households); see also Hearings of Senate Select Committee on a New Tax System, April
8, 1999, at 2382-83 (“There is enormous consistency from economists that food should be
kept in and that compensation is the way to handle that. It is neater. It is more efficient
in economic terms in that sense. . . . [B]ut it is just not fair. We say the price you have to
pay is a little unneatness, a little less of that so-called efficiency around the fringe.”)
(testimony of Michael William Raper, President of ACOS). Cf. Louis Kaplow, The
Theory of Taxation and Public Economics 122-148 (2008) (criticizing differential com-
modity taxation).
82 Michael Graetz, 100 Million Unnecessary Returns (2008) (proposing to offset the
regressivity of a VAT by eliminating the personal income tax for families below a high
exemption threshold such as annual income of $100,000, subject to developing a
different EITC delivery mechanism).
(2001) (reporting Newspoll results in Table I).
Second, social welfare interests believed that a food exclusion would endure, while compensatory measures in the form of higher transfer payments or personal income tax relief would be more vulnerable to erosion for political economy reasons in the future\textsuperscript{84} — as had happened in New Zealand.\textsuperscript{85}

As a result of compromises struck with the Senate Democrats, the exclusion of basic food and other smaller additional exclusions from the GST base cost about AUD 3.8 billion annually. Increased compensation payments cost about AUD 500 million annually and various environmental provisions, GST administration costs and other miscellaneous provisions cost about AUD 400 million. These were paid for by an approximately AUD 1.2 billion reduction in personal income tax cuts,\textsuperscript{86} by increases in fuel levies of about AUD 700 million, and by a postponement of plans to repeal certain state levies in the amount of about AUD

\textsuperscript{84}See Hearings of Senate Select Committee on a New Tax System, supra note 81, at 2369 ("We have always argued that no government can guarantee the security of the compensation package."); 2379 ("[T]here should not be a central flaw in the package which relies heavily on fragile compensation. Take out the flaw in the first place and compensate the other necessities of life in an adequate way. That is our position.") (statements of ACOSS president Raper). See also Select Committee Main Report, supra note 74, at § 2.62 (quoting Ann Harding as saying that if the "compensation package will be eroded over time," "that does call into question the whole food in food out issue, because option 7 was predicated on the assumption that you would try to buttress the compensation package at the bottom end with more generous compensation and that that compensation would be maintained through time").

\textsuperscript{85}See Davidson, supra note 33 (noting ACOSS concern with the durability of compensation given the rollback of regressivity offsets in New Zealand); Hearings of Senate Select Committee on a New Tax System, supra note 81, at 2359 (statement of ACOSS president Raper that after the initial enactment of the GST in New Zealand, GST rates went up and transfer payments were cut).

\textsuperscript{86}The lower income tax brackets were enacted as proposed — 17 percent for income AUD 6001 — AUD 20,000, and 30 percent for income AUD 20,001 — AUD 50,000, which represented a reduction from 20 percent applicable to a rough equivalent of the first bracket and 34 percent (up to AUD 38,000) and 43 percent (thereafter) applicable to a rough equivalent of the second bracket. The higher brackets showed less relief for upper-middle and upper-income taxpayers than ANTS. In particular, the rate applicable to the bracket of income between AUD 50,001 and AUD 60,000 increased from 40 percent to 42 percent, and the highest rate of 47 percent applied starting at AUD 60,001 rather than AUD 75,001. See Anne Daly, Unfinished Business: Reform of the Tax System 209, 213, in Howard’s Second and Third Governments (Chris Aulich & Roger Wettenhall, eds., 2005).
2.3 billion annually, although others were abolished on schedule.87 Government forecasts showed that the net result of the tax package would be an additional revenue loss of about AUD 500 million annually.88

According to one analysis, the final legislative package gave material benefits to low-income taxpayers (for example, a 3 percent gain in disposable income for a single taxpayer at the AUD 10,000 annual income level) and upper-middle-income taxpayers (a 5 percent disposable income gain for a single taxpayer at the AUD 55,000 annual income level), but extended few benefits to lower-middle-income taxpayers (AUD 20,000-25,000) and only modest gains to upper-income taxpayers (for example, a 1 percent disposable income gain for taxpayers with about AUD 140,000 in annual income).89 The overall distributive impact of the GST reform is, however, a subject of some debate. Because the GST was partly deficit-financed, the question of who bears the burden of post-enactment changes in the tax and transfer system is connected to the adoption of the GST.90 In addition, the experience of certain groups of taxpayers is affected by the particulars of applicable transfer and tax changes.91

87See D.J. Collins, The Impact of the GST Package on Commonwealth-State Financial Relations 26-27 (2000) (noting that accommodation and gambling taxes were abolished as of July 1, 2000; financial institutions duty and stamp duties on quoted marketable securities as of July 1, 2001, and debits tax as of July 1 2005; others including stamp duties on credit, installment purchase, rental, lease agreements and mortgage and other loan agreements were postponed).
89See Ann Harding, Neil Warren, Martin Robinson & Simon Lambert, The Distribu-
tional Impact of Year 2000 Tax Reforms in Australia, 7 Agenda 17, 25-26 (2000). Other reports also suggest that the distributive impact of the reforms is somewhat lumpy. See Daly, supra note 86, at 217 (describing Treasury research results that “show considerable variation between different family types”).
90See, e.g., Davidson, supra note 33 (noting deficit financing of the GST and the possibility of future cuts in transfer programs); James, supra note 6, at 345 (arguing that higher GST revenue than expected has permitted income tax cuts under subsequent Howard governments which favored high income taxpayers).
91One question is whether compensation for pensioners was adequate. See Harding et al., supra note 89 (noting that a flaw in ANTS that would have “rendered meaningless” increased compensation for pensioners was fixed in the final package); Davidson, supra note 33 (arguing that “some households with non-average savings and expenditure patterns will be worse off”). Another question is whether the transfer (Footnote continued on next page.)
Paying Off the States

In Australia, constitutional law limits the taxing jurisdiction of the six states and two territories. Commonwealth policy with roots in a 1942 law effectively removed the power to levy an income tax from the Australian states by conditioning federal grants on states’ agreement not to impose income tax, and a specific constitutional provision prohibits state imposition of customs and excise duties. This custom and excise prohibition was interpreted in 1997 to block franchise fees, structured as ad valorem charges on alcohol, tobacco or fuel sales, that approximated consumption taxes and raised about AUD 5 billion annually for the states. After this decision, states’ and localities’ tax jurisdiction was limited to payroll, property, capital transfer and a few other miscellaneous categories of taxes.

Yet states are responsible for significant spending commitments. The result is “vertical fiscal imbalance”: the states spend more than they collect, while the Commonwealth collects more than it spends. In 1997-1998, the states relied on the federal government to fund about 40 percent of their spending. This system increases effective marginal tax rates at certain critical points for low-income families. See Daly, supra note 86, at 218. There are also horizontal equity issues. See Harding et al., supra note 89, at 30 (noting disparities including that “families with children generally do better than those without” and that “age pensioners with substantial non-pension income make larger gains than those fully dependent on social security”).

See Warren, supra note 15, at 32-33 (noting that the states and territories have lost “more and more of their taxing powers’’); Vann, supra note 20, at 5 (noting broad High Court interpretations).

See Ha v. New South Wales, 189 C.L.R. 465, *49-61 (Austl. 1997) (rejecting argument that excise should be more narrowly interpreted in the context of a concern about uniform tariffs as a tax that discriminated between domestically produced goods and imports); see also Cheryl Saunders, The High Court: Section 90 and the Australian Federation, in Reshaping Fiscal Federalism in Australia (Neil A. Warren ed. 1997) 31, 32-37 (describing the tax at issue in Ha, “set at 100 percent of the value of [tobacco] sales in the relevant period” and explaining the constitutional issue of the definition of excise tax).

See Warren, supra note 15, at 56-57 (outlining state taxing jurisdiction).

See Owen E. Hughes, Australian Politics 279 (3d ed. 1998) (noting states’ status as employers and their capital investment); see also id. at 281 (noting political accountability problem with vertical fiscal imbalance).

See Collins, supra note 87, at 36-37 (providing figures for vertical fiscal imbalance ratios for national, state and local governments).
gave the national government a strong negotiating position in its
effort to persuade the states to sign onto the federal GST plan.

The Commonwealth secured the support of the states with a
side payment. In particular, it agreed to transfer all of the revenue
from the GST to the states in exchange for their agreement to
forgo almost AUD 20 billion annually in federal grants that had
previously closed vertical fiscal imbalance gaps.97 The 1999 GST
law incorporates by reference an agreement reached by Howard
and the eight leaders of the states in September 1998 and signed
in June 1999.98 That agreement, in turn, provides for the transfer
of all GST revenue to the states, the elimination of other sources
of Commonwealth support, and the guarantee of revenue com-
mensurate with earlier revenue streams; and for the repeal of
certain state taxes, together with the commitment of the states
and territories to not “reintroduce similar taxes in the future.”99
Revenues are divided among the states annually according to
certain “horizontal fiscal equalization” principles, which natu-
really prompt significant ongoing debate.100

Under the same agreement, variations from the 10 percent GST
rate and some GST base changes require unanimous consent of
the state governments.101 But the national government still
appears to hold the upper hand. In 2010, for example, Kevin
Rudd’s Labor government developed a plan to transfer 30

97See ANTS, supra note 50, at 84-85, 104.
98See A New Tax System (Goods and Services) Tax Act 1999 § 1.3 (providing
Parliament’s “acknowledgment” that legislation would be introduced to provide the
GST revenue to the states and administer the GST consistent with the agreement reached
between the commonwealth and the states and territories).
99See Intergovernmental Agreement on the Reform of Commonwealth-State Rela-
tions ¶¶ 5, 10 (1999) (hereinafter “Intergovernmental Agreement”). Appendix B of the
agreement provides that the division of revenue will be based in part on population and
on “health care grant” needs. Appendix C addresses minimum revenue commitments
for an initial transition period. See supra note ?? for a summary of the state tax repeal
agreements.
100See Collins, supra note 87, at 42-54 (describing multifactor analysis used by the
Commonwealth Grants Commission); James, supra note 6 at 345 (arguing that the GST
did not give the states needed tax jurisdiction). See, e.g., Rick Wallace, Boom States
Accused of Waste, The Australian (Oct. 5, 2009) (reporting that officials of Victoria and
New South Wales accused resource-rich Western Australia and Queensland of “squan-
der[ing]” mining revenue and then expecting GST revenue from consumption in other
states to balance their budgets).
changes to the GST base require majority approval under the agreement.
percent of GST revenue and 60 percent of the responsibility for public hospital funding to the Commonwealth. Seven of eight states went along, after receiving the persuasion of some extra grant funds. The path to resolution of Western Australia’s objections was not clear, even as it agreed to continued discussion with the national government.102

* * *

Australia’s path to GST enactment rested on an analytical framework that cast the GST as an efficient tax with regressivity problems. Business groups like ACCI articulated their interest in efficiency from a global competitiveness perspective, while at least some social welfare groups, through ACOSS representation, showed more interest in revenue-raising efficiency. But there was enough common ground to support an interest group coalition, which permitted Prime Minister John Howard to return consumption tax adoption to the center of the LNP Coalition party platform.

In the political and legislative process, ACOSS and the minority Democrats focused attention on offsetting the regressivity of a GST. The final package included increased transfers to pensioners, adjusted personal income tax rate schedules and the exclusion of basic food from the GST base. The food exclusion was thought to have the advantages of political salience and durability relative to personal income tax cuts or increased transfer payments. Finally, the reform included an agreement that transferred all GST revenue to the states in exchange for their repeal of certain taxes and in lieu of previously extended Commonwealth financial support — a fiscal federalism development facilitated by the Australian constitutional framework, which reserves most taxing jurisdiction to the national government. ■

102 See Peter Hartcher, Anatomy of the Rudd Health Deal, Sydney Morning Herald (Apr. 24, 2010) (describing Kevin Rudd’s persuasion of the state leaders, with the exception of the Liberal leader of Western Australia, with whom he was still in discussions); Malcolm Farr, Kevin Rudd to Hold Plebiscite If Premiers Reject Health Reforms, The Australian, Apr. 19, 2010 (reporting that the government would respond to sustained resistance from state leaders by holding a popular plebiscite like that used to select a national anthem, though such a plebiscite would apparently not have the binding force of law).