

Calls for tax reform heightened by Australia’s deepening debt projections

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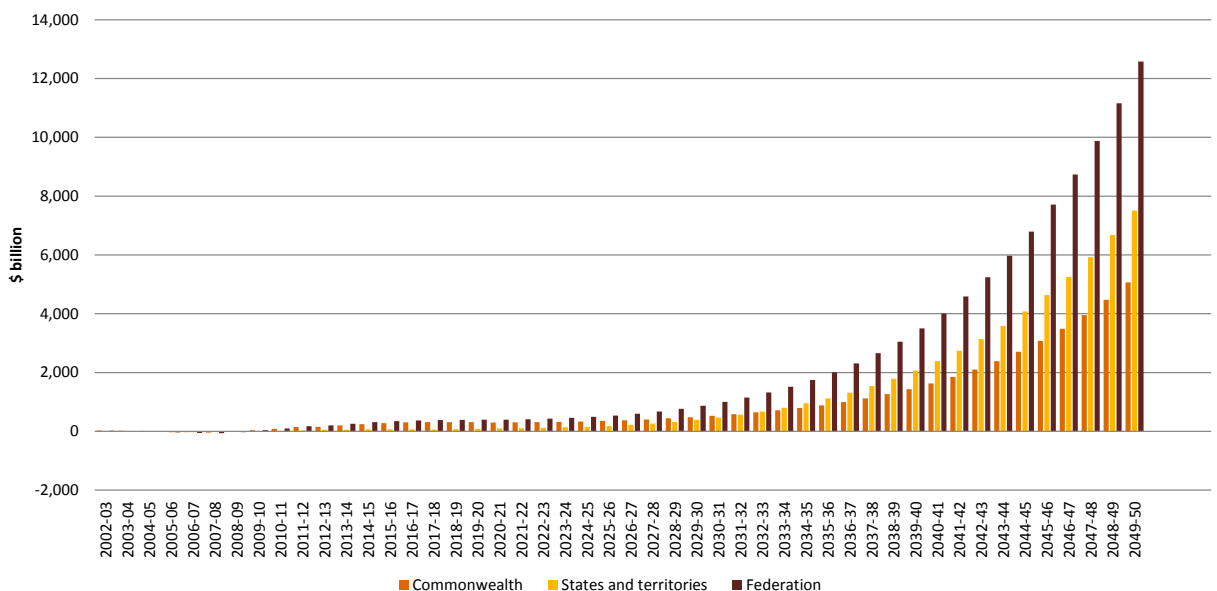
With our governments – at the Commonwealth, and state and territory levels – facing a growing fiscal challenge, the need for major tax reform is reaching critical stages.

Australia’s net debt is currently estimated at \$345 billion (or around 21 per cent of GDP). While this may not raise any alarms for some; it sits within a context of rapidly increasing expenditure on health, education and infrastructure and no measures for addressing weak government revenues.

Taking into consideration projections regarding population growth, along with rising expenditure on critical services such as health, education and welfare, PwC forecasts total net debt across all Australian governments will exceed \$1 trillion within the next 15 years (equating to almost 28 per cent of GDP). By 2037-38, the Commonwealth Government’s net debt levels alone are expected to exceed \$1 trillion.

Looking further ahead, PwC forecasts Australia’s net debts levels will reach over \$12 trillion by 2049-50 – which equates to over 138 per cent of GDP.

Figure 1: Australia’s net debt levels, \$ billion



Attempts by the Commonwealth Government to introduce savings measures in the 2014 Budget have not been successful to date. Measures such as changes to the indexation of welfare, including pensions and family payments, the Medicare co-payment and changes to higher education FEE-HELP arrangements have not passed through the Senate.

At the same time, Australia's economic growth rate has eased and real incomes per person have begun to decline. There has also been larger than expected declines in Australia's terms of trade, driven by decreases in the price of commodities such as iron ore and coal. This will further weaken Australia's key economic fundamentals, and adversely affect Commonwealth revenues.

The debt projections presented above are based on the assumption that Australia's economic growth will move back to trend and the international economy will remain relatively stable. Such assumptions are highly optimistic and underline the vulnerability of the Australian economy.

Tackling real reform

It is clear that economic growth alone will not be sufficient to repair the budgets of Australian governments. But it is also clear that economic growth will not come without reforms, including tax reform.

Even if the proposed savings measures being pursued by the Commonwealth Government are eventually passed through the Senate, they will not be enough on their own to address the broader fiscal challenge facing Australian governments. Indeed, the fiscal position of states and territories will remain in a precarious position as they seek to fund the increasing costs of education and health services.

Governments need to act now to ensure that measures are in place to maintain the living standards that Australians expect. To do this, a broad reform agenda will be required which looks at cutting waste, driving efficiency in the delivery of key services and promoting productivity growth. And a key part of any agenda must be comprehensive reform of Australia's tax system.

Effective tax reform must consider the need to improve efficiency, reduce distortions, promote investment and increase participation incentives in the workforce, all while maintaining a progressive and fair system that generates sufficient revenues for governments.

While this may not be easy, it needs to be addressed sooner rather than later. The Commonwealth Government should proceed with its proposed White Paper on the Reform of Australia's Tax System, including a genuine consultation process across all sectors of the community, including business and community leaders.

PwC is front and centre in the debate on tax reform. Nearly two years ago we formed an Advisory Panel representing charities, unions, the business community, academia and other parts of society. The Panel, along with our Tax Experts Group, has informed two papers on tax reform which can be accessed at: <http://www.pwc.com.au/tax/tax-reform/>.

Let's talk

For a deeper discussion of how these issues might affect your business, please contact:

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