

Queensland the low tax state: The birth and death of an idea, and how to bring it back to life

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Executive summary

- Queensland once prided herself on maintaining the lowest taxes in Australia, which fuelled migration from other states, providing impetus for substantial growth in investment, and unleashing the entrepreneurial potential of the business community.
- However, on most available indicators of relative tax competitiveness Queensland has lost its mantle as the low tax state to the likes of Tasmania, Western Australia and, on some indicators, Victoria.
 - This means that Queensland has become a less favourable destination for business development and economic growth.
- While politicians since colonial times have never been hesitant to announce tax reductions, the modern origins of Queensland the low tax state emerged under the conservative administrations of former Premier Sir Joh Bjelke-Petersen.
 - The abolition of death duties in the late 1970s, and progressive reductions in business taxes since that period until the late 1980s, signalled that Queensland was open for business and led to the emergence of a modern, sophisticated state in Australia's north.
- The Labor government under Wayne Goss continued the low tax state policy, although there were emerging pressures within the government and amongst vested interests to increase government spending to levels found in the southern states.
- While the first Beattie government maintained the rhetoric of Queensland as a low taxer, it diluted Queensland's tax position by engaging in a program of substantial public spending.
 - This stance was largely justified on the need to reverse previous spending 'neglect' by conservative governments, even though Queensland's public sector was arguably the most efficient in the country delivering services to those who needed it.
 - The 'Smart State' strategy gave new momentum for government spending, even though the effectiveness of the program remains clouded.
- The loss of Queensland's low tax position coincided with an erosion of fiscal best practices by the Beattie and Bligh governments, eventuating into the worst set of fiscal books amongst the eight states and territories.
- The first priority of the Queensland government must be to restore sustainable public finances based on asset sales and reductions to recurrent spending.
- Even so, the government should publicly announce a medium-term objective of reinstating Queensland as Australia's low tax state.

The virtues of low state taxation¹

State governments in Australia compulsorily acquire revenues from a number of sources to fund the production and provision of certain goods and services - such as justice and policing, education, health care and transportation. Taxation represents a key component of the revenue-taking armoury of the states, accounting for 28 per cent of general government sector revenue in 2009-10.²

While taxes are utilised by government for the purposes mentioned above, they have significant implications for economic performance including if high levels of taxation are employed for purposes, such as income redistribution or macroeconomic stabilisation, in addition to defraying the cost of public services.

It is well known that the cost of taxation on the community is much greater than that implied by the forcible transfer of funds from businesses and individuals to governments for subsequent public expenditure.

As explained by the conventional public economics literature, taxes either raise the cost or lower the return to the taxed activity and thus distort choices in the market as economic agents seek to minimise their tax liability, by substituting away from activities taxed at higher rates to those taxed at lower, or no, rates.

These economic costs are known as the 'deadweight cost' or 'excess burden' of taxation. Indeed, as the public sector expands the increased taxes induce additional distortions to economic decision making.

Consider, for example, the impact of taxes on capital. Taxation can affect the cost of capital, or the hurdle rate of return that a project must meet in order for an entrepreneur to undertake it. When returns from a project are taxed then the project must earn an even higher return for it to be considered a worthwhile investment. A tax on investment thereby reduces the number of viable projects that would proceed in a competitive market.

In addition, the imposition of a tax may reduce the cash flow of an entrepreneur which may affect investment decisions. Specifically, to the extent that liquidity constraints exist in financial markets, a tax on capital could lead to a reduction in the demand for capital. Further, Sobel and Hall state that taxes can restrict the cash flow rights associated with property and thereby weaken private property rights more generally.³

In recent years numerous empirical studies have been undertaken in Australia in an effort to quantify the efficiency losses associated with state taxes. For example, a commissioned study by

¹ Unless otherwise specified, information in this section is drawn from Julie Novak, 2010, *Business Bearing the Burden 2010: The Size and Impact of State and Territory Government Business Taxes*, Institute of Public Affairs Occasional Paper.

² Australian Bureau of Statistics (ABS), *Government Finance Statistics*, Australia, 2009-10, cat. no. 5512.0.

³ Russell S Sobel and Joshua C Hall, 2009, 'The Sources of Economic Growth', in Peter T Calcagno, ed., *Unleashing Capitalism: A Prescription for Economic Prosperity in South Carolina*, South Carolina Policy Council Education Foundation, Columbia.

KPMG/Econtech for the Henry Tax Review found that the marginal excess burdens of state taxation upon economic activities ranged from eight cents in the dollar (for land tax) to 67 cents in the dollar (for taxes on insurance).⁴

The excess burden of taxation is not the only additional cost rendered by the taxation system. Other costs include administrative costs, compliance costs, enforcement costs and 'rent-seeking' costs associated with resources spent by individuals and businesses lobbying politicians and bureaucrats to avoid tax (both in an *ex-ante* and *ex-post* sense).

More fundamentally, most comparative static analyses of the efficiency consequences of taxation tend to overlook the dynamic, long run implications of this element of government intervention.

The market economy can be properly understood as a decentralised, spontaneously ordered process through which economic inputs are converted into value-added economic outputs. The entrepreneur is at the centre of this process as they discover and capture, through trial and error, profitable opportunities that improve the coordination of individuals' economic plans. To the extent that the level and structure of taxation reduces pure profits it detrimentally affects entrepreneurial activity and the coordinative properties of the market.⁵

It is on these efficiency grounds that state governments should remain cognisant of the need to minimise their taxation burdens on individuals and businesses, including through seeking efficiencies in public sector expenditure financed by such revenue takings.

An assessment of Queensland's tax policy performance over time

While it is generally agreed that low levels of taxation are indispensable for the promotion of desirable economic outcomes, such as economic growth, investment generation and job creation, there remains a debate amongst economists and public policymakers concerning appropriate measures of taxation policy performance.

One aspect of taxation performance, which is the focus of this paper, is the concept of tax competitiveness. This concept could be generally described as a situation in which tax burdens are lowered, relative to comparator jurisdictions, in an effort to encourage the inflow of productive resources or prevent the exodus of those resources.⁶ Other things being equal the lower the level of taxation imposed by a jurisdiction, the greater its taxation competitiveness relative to other jurisdictions.

⁴ KPMG-Econtech, 2010, CGE 'Analysis of the Current Australian Tax System', http://taxreview.treasury.gov.au/content/html/commissioned_work/downloads/KPMG_Econtech_Efficiency%20of%20Taxes_Final_Report.pdf.

⁵ Frédéric Sautet, 2002, 'Economic Transformation, the Pretence of Knowledge and the Process of Entrepreneurial Competition', New Zealand Treasury Economic Transformation Project, Preliminary draft paper.

⁶ Wikipedia, 'Tax competition', http://en.wikipedia.org/wiki/Tax_competition.

In the sections that follow a range of indicators are presented to estimate the tax competitiveness of Australian state governments.⁷

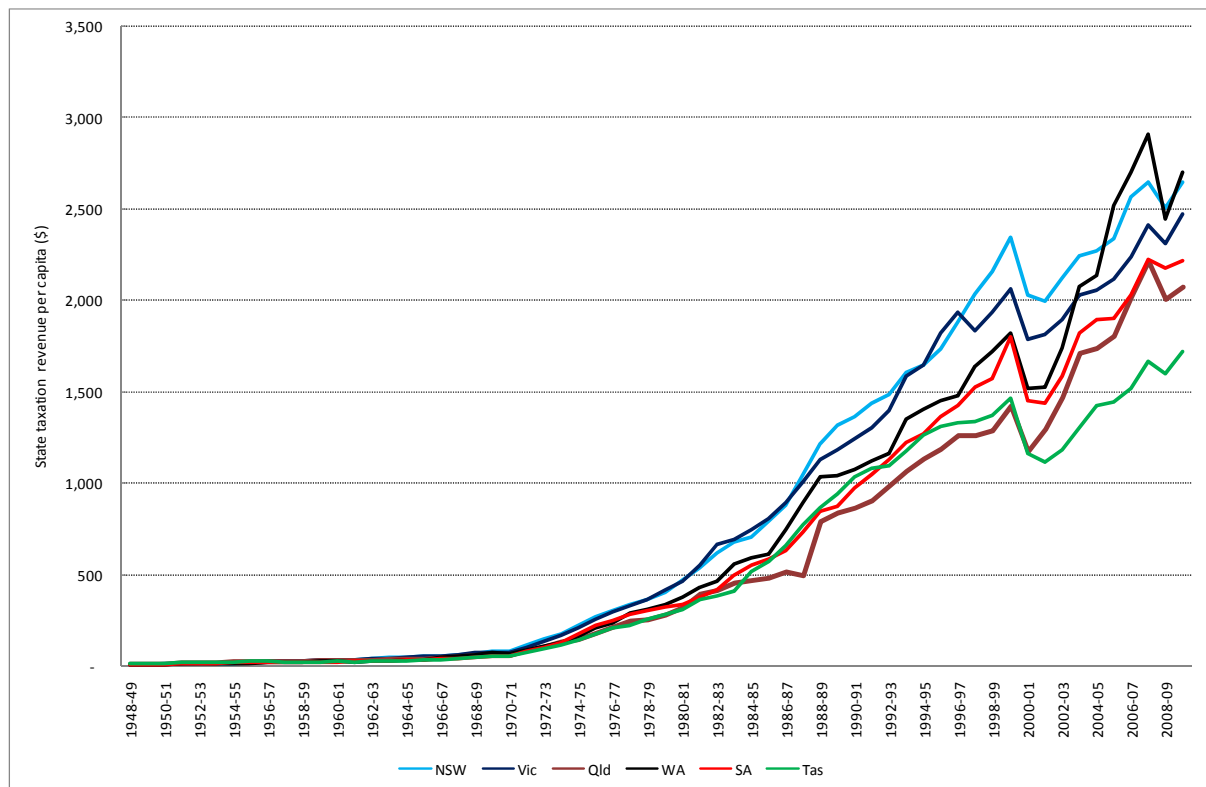
Taxation per capita

A commonly used indicator of taxation competitiveness is the level of taxation revenue collected relative to the size of the population within a given jurisdiction (Figure 1).

During the 1950s and early 1960s Queensland's level of state taxation per capita was generally slightly above the average of the six states' from 1951-52 to 1955-56, from 1959-60 to 1960-61 and 1962-63.

Since that period the level of taxation per capita in Queensland has been consistently below the average of the six states. The discrepancy between Queensland's tax per capita level and that of the six states progressively widened, to such an extent that the state's tax per capita was some 41 per cent below average by the late 1980s. However, strong growth in taxation per capita in Queensland since that period had substantially closed the gap with the six states' average.

Figure 1: Level of state taxation per capita



Source: ABS, Commonwealth, State and Territory Tax Collections; ABS, Public Authority Finance, Taxation; ABS, Taxation Revenue, Australia; ABS, Australian Historical Population Statistics; ABS, Australian Demographic Statistics.

The most notable trend in this data series is that the level of taxation per capita in Queensland was the lowest of all states from 1982-83 to 2000-01. Since 2000-01 Queensland's relative tax

⁷ Unless otherwise specified, this section excludes the Australian Capital Territory and the Northern Territory.

competitiveness has diminished with Tasmania now assuming the position as Australia's most competitive tax state on a taxation per capita basis.

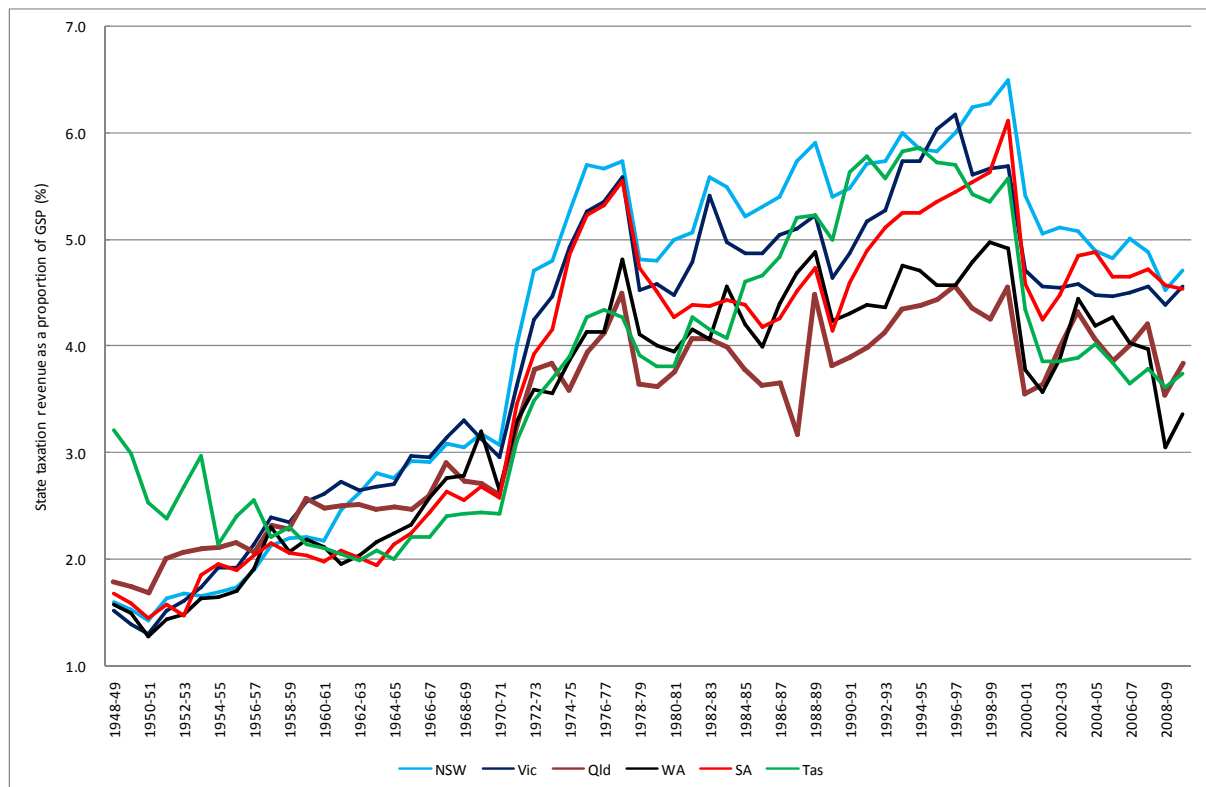
Taxation as a proportion of gross state product

Taxation as a proportion of GSP is another indicator used by state policymakers to gauge the competitiveness of their tax systems (Figure 2).

During the 1950s and 1960s Queensland's level of taxation, as a proportion of GSP, was generally above that of the average of the six states in Australia. In 1951-52 the level of Queensland taxation was about 14 per cent above the average.

From the 1970s this trend was reversed with Queensland significantly improving its tax competitiveness. In 1986-87 Queensland's tax as a proportion of GSP was about 21 per cent below the average of all states, and this gap widened through a year later to become 33 per cent below average. By the end of the 1990s Queensland was still some over 20 per cent below the tax-to-GSP average of the six states.

Figure 2: Level of state taxation as a proportion of GSP



Source: ABS, Commonwealth, State and Territory Tax Collections; ABS, Public Authority Finance, Taxation; ABS, Taxation Revenue, Australia; ABS, Australian National Accounts: State Accounts; W A Sinclair, 'Annual estimates of gross domestic product: Australian colonies/states 1861-1976/77'.

In a similar fashion to taxation per capita trends, Queensland progressively improved its tax competitiveness to eventually become the lowest taxing jurisdiction in Australia from 1978-79 until

2001-02. By the end of the last decade Queensland's status as the low tax state had been supplanted by Western Australia and Tasmania.

Taxation effort ratios

The Commonwealth Grants Commission publishes on an annual basis taxation revenue effort ratios for the Australian states and territories.

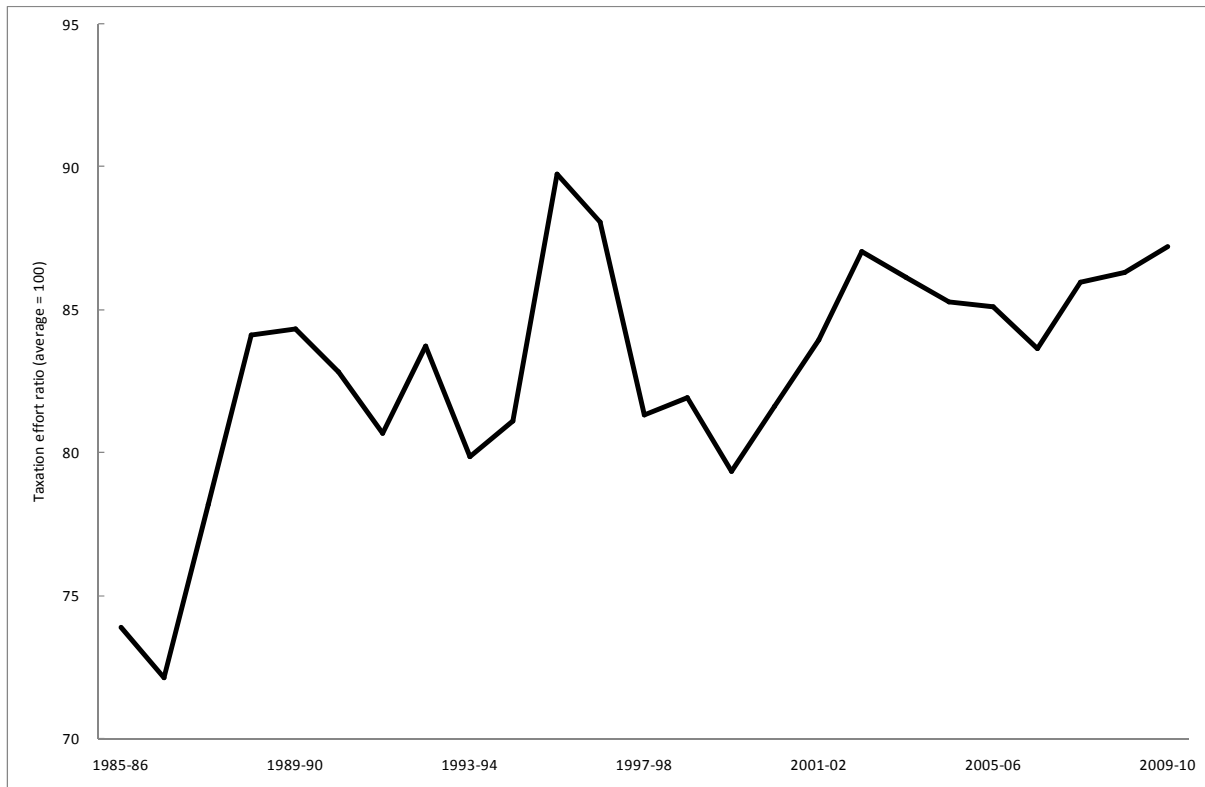
This ratio indicates the actual effort by a jurisdiction in raising tax revenue relative to the average effort of all states (including the ACT and NT). It is a measure of what a jurisdiction actually raises compared to what it would raise if it applied average tax imposts to its taxation revenue bases.⁸ A ratio higher than 100.0 indicates a tax raising effort above the Australian average, whereas a ratio of less than 100.0 indicate an effort of raising taxes less than the average.

While changes in the fiscal equalisation methodology ensure that caveats must be applied when comparing ratios over time, it is clear that Queensland has generally maintained a taxation effort ratio at less than the Australian average since the mid-1980s (Figure 3).

In the latter years of National Party administration in the state, the taxation revenue effort ratio significantly increased from under 75 per cent to less than 85 per cent. Apart from a temporary upswing in the tax effort ratio during the mid-1990s, the last decade of the twentieth century saw the ratio fluctuate between 80 per cent 85 per cent.

Since 2000-01 the general trend has been for Queensland to increase its effort in exploiting a narrower revenue base, with the latest data showing a ten-year high taxation revenue effort ratio of 87 per cent. Tasmania, by contrast, has undertaken concerted action over the past decade to reduce its tax revenue effort to now closely rival Queensland as the lowest taxing state against this indicator.

⁸ Catherine Hull and Bob Searle, 'The Impact of Equalization on Service Delivery', http://aysps.gsu.edu/isp/files/ISP_CONFERENCEDESIGNCHALLENGES_HULL_AND_SEARLE_PAPER.pdf.

Figure 3: Queensland taxation revenue effort ratio

Source: Commonwealth Grants Commission, Reports on State Revenue Sharing Relativities.

Taxation under 'reference business' scenarios

Another method to calculate the relative taxation competitiveness of jurisdictions is to estimate the tax liability upon a, real or hypothetical, case study business. Assuming that similar operational and financial characteristics pertain to the business when comparing its tax liability across jurisdictions provides a 'like with like' basis for the estimation of tax competitiveness.

The Institute of Public Affairs has published for the past three years rankings of business tax competitiveness for Australian states (and territories from 2010). The IPA analysis is based upon a hypothetical medium sized 'reference' business, based on World Bank analysis, which grows in size proportionally to changes to national GDP per capita.

Excluding the two territories from the 2010 data, Table 1 reveals that the tax competitiveness of Queensland has steadily eroded in recent years with Western Australia, and more recently Victoria, offering more hospitable tax environments for business.

Table 1: State taxation liability on 'reference' business

	2008		2009		2010	
	Tax liability (\$)	State tax ranking (no.)	Tax liability (\$)	State tax ranking (no.)	Tax liability (\$)	State tax ranking (no.)
NSW	220,156	6	240,277	5	270,129	5
Vic	202,421	3	222,485	3	256,830	2
Qld	197,388	2	221,963	2	264,630	3
WA	195,622	1	219,010	1	256,195	1
SA	219,068	5	240,783	6	281,744	6
Tas	210,180	4	236,549	4	265,248	4

Level of business taxation liability as at December of each year. Includes payroll tax, land tax, land transfer duty, insurance duty and motor vehicle duty. Vehicle registration fees and workers' compensation premiums excluded from the data presented in this table. State taxation rankings are scaled from 1 (lowest tax liability) to 6 (highest tax liability).

Source: Institute of Public Affairs, *Business Bearing the Burden*, various years.

While general caveats exist in terms of each of these indicators, the conclusion to be made on the basis of the available information is that Queensland's taxation competitiveness has deteriorated significantly over time. On any reasonable assessment Queensland is no longer the low tax state of the Australian Federation, with significant implications for its long term capacity to sustain economic growth and improve living standards.

From 'Cinderella state' to economic powerhouse: Queensland as the low tax state

A number of economic historians and political scientists have characterised Queensland prior to the 1970s as possessing a 'Cinderella economy,' an outpost in northern Australia just waiting to fulfil her potential.

Queensland was home to 14 per cent of the nation's population,⁹ with an industrial structure perceived to be largely dominated by pastoral activities, sugar and other crops, and mining.¹⁰ Further, just 12 per cent of Queenslanders completed at least nine years of schooling, with a tendency by the most highly skilled labour to leave the state for lucrative opportunities in the financial and legal centres of Sydney and Melbourne and the public policy citadel of Canberra.¹¹

Over the next two decades the economic and social structure of Queensland was substantially altered in a number of respects. The agricultural and mining sectors provided a significant impetus for technical innovation while business investment soared, particularly in the Sunshine Coast-Brisbane-Gold Coast conurbation as attested by former Premier Sir Joh Bjelke-Petersen's references to the 'crane-o-meter' gauge of construction activity.

While it is commonly observed that Queensland has undergone significant social change since the 1970s, with Brisbane and major regional centres developing a cosmopolitan arts and café culture not unlike those found in the population centres of southern Australia, insufficient recognition has been

⁹ Australian Bureau of Statistics, Australian Historical Population Statistics, cat. no. 3105.0.65.001, data for June 1970.

¹⁰ Roger Scott, Peter Coaldrake, Brian Head and Paul Reynolds, 1986, 'Queensland', in Brian Galligan, ed., *Australian State Politics*, Longman Cheshire, Melbourne.

¹¹ Julianne Schultz, 2008, 'Disruptive Influences', *Griffith Review*, http://www.griffithreview.com/images/stories/edition_articles/ed21_pdfs/schultz_ed21.pdf.

accorded to the important role of economic growth and change in driving the observed changes in Queensland's cultural outlook.

As stated above the role of low and stable taxation is a central aspect of the institutional framework conducive to economic development. The following sections provide an account of state tax policies pursued by successive Queensland governments during the low tax state era of the 1970s to late 1990s.

Low tax state policy under Bjelke-Petersen

While previous Queensland state governments have highlighted policy decisions reducing tax burdens upon individuals, households and businesses within the state, it could be reasonably argued that the formalisation of a consistent policy stance in favour of low state taxation emerged under the Country (later National) administrations under Premier Sir Joh Bjelke-Petersen.¹²

During the 1970s the government designed tax policies intended to attract business investment into Queensland: 'major cuts in stamp duties, yearly increases in the exemption levels on payroll tax, and decreasing land taxes were examples of the emphasis on low taxation to induce foreign and interstate capital to invest in Queensland's economic 'progress' and 'development.' Such policies were also indicative also of the National Party's underlying strategy of stealing the 'free enterprise' mantle from its coalition partner, the Liberal Party.'¹³

A pivotal moment in the positioning of Queensland as the low tax state of Australia was the Bjelke-Petersen government's decision to abolish death duties, or more formally known as succession or probate and gift duties.

In the early 1970s a probate (administration) duty of \$2 for every \$200 (or part thereof) applied where the net value of an estate amounted to \$600 or more. The succession duty was payable as a percentage of the estate succession, with a progressive rate structure applicable (maximum rates ranging from 20 per cent to 30 per cent). A duty on gifts exceeding \$4,000 was imposed with rates ranging from three per cent to a maximum of 20 per cent. Certain exemptions applied under each of these duties.¹⁴

While death duties had been long opposed by farmers and small business owners on the basis of the tax impediment on the succession of their estates and businesses respectively, a push to abolish death duties gained political momentum with the early 1970s through the election of one-term independent WA Senator Sydney Negus who won election on the platform of abolishing death taxes.

¹² The Country (National) Party maintained a coalition agreement with the Liberal Party until 1983, with the dissolution of the Coalition incited in part by the National Party's refusal to introduce a parliamentary Expenditure Review Committee.

¹³ Denis Murphy, Roger Joyce, Margaret Cribb and Rae Wear, 2003, *The Premiers of Queensland*, University of Queensland Press, St. Lucia, p. 312.

¹⁴ Australian Bureau of Statistics, 1974, *Queensland Year Book 1974*, AGPS, Canberra.

As early as 1973 the Queensland government repealed probate duties.¹⁵ In September 1975 the government abolished succession duty on estates transferred to a spouse, and in November of that year gift duty was repealed on any gift made by a person to his or her spouse.¹⁶

This was followed on 10 March 1976 by an announcement by Bjelke-Petersen in the state Cabinet that all death taxes would be unilaterally abolished.¹⁷ As Bjelke-Petersen described his decision in his political autobiography, '[a]fter considering the matter for some time, I walked into Cabinet and announced I was going to abolish death duties and gift duties.'¹⁸ This caused considerable consternation within Cabinet, particularly for Liberal Party Treasurer Sir Gordon Chalk, not least for the fact that the decision was presented without an accompanying formal Cabinet submission.

Chalk was reported to have criticised the tax abolition proposal by stating '[i]t's easy enough for anyone to sire a child. But someone had to be experienced if he is going to father and nurse it.'¹⁹ In subsequent analysis by the Queensland Treasury it was estimated that abolition of the taxes would lead to \$30 million in lost consolidated revenue.²⁰

Despite introducing a tax on soccer pools in 1976 as a concession to Chalk's concerns about potential revenue losses,²¹ Bjelke-Petersen won close to unanimous approval from the joint Coalition party room for the measure. All remaining Queensland death duties were abolished in 1977 in circumstances where the tax liability arose as a result of death, and in respect of gifts made in Queensland, on or after 1 January 1977.²²

Fearing the loss of productive human capital and financial investments to Queensland, the other states were obliged to follow suit. Within twelve months of Queensland's complete abolition of death taxes, New South Wales and Victoria announced timetables to abolish their taxes. Western Australia abolished its death duties in 1978, while South Australia a year later announced a timetable for repealing similar taxes from 1980.

Tasmania was most reluctant to abolish her death duties on revenue sufficiency grounds, with a government-commissioned study showing that in 1977 alone some \$11 million in capital was being transferred from that state to Queensland.²³ However a year later Tasmania bowed to the pressures of competitive federalism exerted by Queensland and other tax-cutting jurisdictions, and also announced the abolition of its estate and gift duty regimes.

¹⁵ Australian Bureau of Statistics, 1975, *Queensland Year Book 1975*, AGPS, Canberra.

¹⁶ Australian Bureau of Statistics, 1976, *Queensland Year Book 1976*, AGPS, Canberra.

¹⁷ Denver Beanland, 2004, 'From cottage industries to the low tax state: Economic growth and migration of Queensland, 1945 to 1990', *University of Queensland Historical Proceedings* 15 (1): 51-62.

¹⁸ Sir Joh Bjelke-Petersen, 1990, *Don't You Worry About That! The Joh Bjelke-Petersen Memoirs*, Angus & Robertson, Sydney, p. 182.

¹⁹ William H Pendrick, 1981, 'Oh, to Die Down Under! Abolition of Death and Gift Duties in Australia', *Tax Lawyer* 35 (1): 113-141, p. 115.

²⁰ John Wanna and Tracey Arklay, 2010, *The Ayes Have It: The History of the Queensland Parliament, 1957-1989*, ANU ePress, Canberra.

²¹ Tomas J F Riha, 1987, 'Public Finance in Queensland (1859-1987)', University of Queensland, Queensland Economic Policy Research Unit, Research Report; Rae Wear, Johannes Bjelke-Petersen: The Lord's Premier, University of Queensland Press, St. Lucia.

²² Riha, *Ibid.*

²³ Pendrick, *op cit*, p. 115.

Citing the 'distress and hardship to thousands of Australian families, to small business, to farmers,'²⁴ Prime Minister Malcolm Fraser also followed Queensland's lead and announced the abolition of its estate and gift duties in 1978, ensuring that by 1984 Australia was one of the few advanced economies with no explicit wealth taxation system.

During the late 1970s the Queensland government also abolished road permit fees and maintenance charges, which were personally opposed by Bjelke-Petersen on the basis that they 'increased prices for people in the bush.'²⁵

The government widely promoted its taxation policy record in the public domain. In a speech during the 1977 state election campaign, Bjelke-Petersen stated that:

*'[t]he hallmark of good government is its performance, not its promises. ... Performance is measured by achievement. This is your government's record - The lowest state taxes and charges in Australia. ... Another balanced budget with no tax increases. The only government in Australia to eliminate three major taxes - death duties, gift duties and road permit fees. The only government actively cutting payroll tax and workers compensation premiums'*²⁶

In addition the government took opportunities to extol its low taxation policies in Budget speeches from the late 1970s:

- In the 1982-83 Budget the Treasurer Llewellyn Edwards stated that 'the Government has been able to formulate its Budget without having to resort to increases in the rates of taxation or introducing new forms of tax such as business franchise fees for tobacco and petrol. At the same time, very significant concessions have been provided in death duties, pay-roll tax, land tax, stamp duty, road maintenance charges, road transport permit fees and so on. The overall effect has been to maintain Queensland's enviable position of being the lowest tax State in Australia. Recent studies by my Department suggest that Queensland has significant capacity to very substantially increase revenues by simply bringing Queensland up to the taxing standards of the other States. I hasten to add that the Government does not see this as desirable or necessary.'²⁷
- Premier and Treasurer Bjelke-Petersen stated in the 1986-87 Budget speech that '[t]he Government is committed to keeping Queensland as the low tax State. It is essential for long term economic growth that the private sector not be burdened with unnecessary taxes.'²⁸

While the low tax strategy appealed to the general community, there existed various strands of opposition against the Bjelke-Petersen policy framework.

²⁴ Pendrick, *Ibid*, p. 116.

²⁵ Hugh Lunn, 1984, *Johannes Bjelke-Petersen: A Political Biography*, University of Queensland Press, St. Lucia, p. 62.

²⁶ Margaret Cribb and P J Boyce, 1980, *Politics in Queensland: 1977 and Beyond*, University of Queensland Press, St. Lucia, p. 291.

²⁷ Hon Dr L R Edwards MLA, 1982, 1982-83 Budget Speech and Financial Statement of the Treasurer, 23 September.

²⁸ Hon Sir Joh Bjelke-Petersen MLA, 1986, Budget Speech 1986-87, 26 August.

The Labor Opposition challenged the low tax state thesis on the basis that government tax revenues increased in absolute terms, or on a per capita basis, over time, and reference was often made to a growing reliance on fees and charges as a means of supplementing revenue.

Intriguingly, in her maiden speech to the Queensland Parliament in 1983 Anne Warner, a future government minister who subsequently emerged as something of a mentor for Premier Anna Bligh, offered a more strident critique of the state's taxation framework:

*'[National Party] members said that they were proud to live in a low-tax State. I ask: low taxes for whom? For shareholders in New York, London, Paris, and even Johannesburg! These low taxes are produced by a combination of especially generous taxation concessions for the mining industry, low rail freight, low electricity charges, low royalties and what could only be charitably referred to as clever financial arrangements such as transfer pricing, the use of tax havens and financing which takes the form of loans rather than shares'*²⁹

Public sector and other trade unions, and some economists, contended that the price of maintaining Queensland's status as a low tax state was a low level of governmental services, if not low wages, compared with other states. As early as 1975 a commonwealth Commission of Inquiry into Poverty reported that Queensland had the highest share of 'very poor' adults in Australia yet the state's per capita expenditure on welfare services was considerably less than that of other jurisdictions.³⁰

As will be suggested below, these and other critical views of low Queensland taxation became more influential in policy terms over the course of the next ten years.

Low tax state policy under Ahern, Cooper, Goss and Borbidge

The short term National Party successors to Bjelke-Petersen, Premiers Mike Ahern and Russell Cooper, maintained Queensland's low tax position with the important exception of the introduction of a state tobacco business franchise fee for the first time in 1988. The funds collected under the tax were hypothecated to the Queensland Institute for Medical Research.³¹

A year later the Labor Party, led by Wayne Goss, was returned to power after 32 years in opposition with the public's distaste for corruption scandals under previous conservative governments outweighing warnings that Queensland Labor would emulate the fiscal recklessness of other state Labor administrations around the country.³²

While many Labor supporters were hopeful that the Goss government would eschew the low tax policy of the previous conservative administrations, and transform Queensland's fiscal profile into a pale imitation of Victoria's, Premier Goss and Treasurer Keith de Lacy were eager to fashion a state Labor brand of economic responsibility and fiscal rectitude.

²⁹ <http://www.parliament.qld.gov.au/view/historical/documents/memberBio/documents/Warner.pdf>.

³⁰ Wear, op cit, p. 189.

³¹ Julianne Schultz, op cit.

³² Prior to the 1989 state election the National and Liberal Parties sought to capitalise on a statement by Goss made on 25 October 1988 that 'just as business has prospered under the economic stewardship of John Cain in Victoria ... so too will business prosper under a Goss Labor Government in Queensland.' Murphy, Joyce, Cribb and Wear, op cit, p. 365.

A representative portrayal of the Goss government's economic framework was described in an economic strategy released in 1992 entitled *Queensland Leading State*.

Stating that '[t]he contribution of State governments will be greatest when they clearly understand the limits on their economic influence and make best use of that influence in those areas where the State government's economic strategy can have a demonstrable impact,'³³ the strategy commended a 'market enhancement' approach to policy whereby 'government creates an environment in which markets can operate efficiently, with minimal government interference with prices and commercial decision-making, and concentrates its own efforts on areas ... in which markets prove inadequate.'³⁴

On this basis, the government indicated that '[s]ound financial management and a low tax regime are the foundation of the Queensland Government's economic policy. More than anything else, they ensure a stable framework for business decision-making.' These principles in turn were encapsulated in a 'fiscal trilogy' approach to budgetary management during the first term of the Goss government:

- no new taxes, no increases in existing tax rates, and no increases in charges on average by more than the increase in the CPI
- full actuarial funding of the state's long term liability (such as superannuation and workers' compensation)
- fully funding through the budget of social infrastructure such as hospitals and schools, and borrowing only for economic infrastructure which generates a commercial return adequate to meet debt service charges.³⁵

Despite the lingering effects of a national recession and onset of a severe drought from 1991 Queensland was able to maintain its low tax state status during the first term of the Goss government.

Based on 1991-92 data, for example, Queensland would have raised an additional \$800 million if it imposed a range and level of taxes and charges comparable to those of the other states. During the Goss government's first term, the maximum payroll tax rate was some 40 per cent below the rates applying in other states and territories and it was the only jurisdiction at the time to apply a stamp duty concession upon all purchases of principal places of residence. In addition, it did not impose a state petroleum business franchise fee or financial institutions duty.³⁶

The government undertook a number of initiatives to maintain the state's low taxing position. Apart from increasing exemption threshold levels and selective rates for a number of taxes, Queensland halved the rate of stamp duties on marketable securities in 1995 in its effort to position itself as an

³³ Hon Wayne Goss MLA, 1992, *Queensland Leading State: State Economic Development Policy*, Government Printer, Brisbane, p. 23.

³⁴ *Ibid*, p. 28.

³⁵ *Ibid*, p. 31.

³⁶ Queensland Government, 1993, Budget Overview and Statements of Receipts and Expenditure, State Budget 1993-94 Paper No. 2, p. 4.

active participant in regional financial markets. The other states reacted quickly to this measure by also reducing their duties.³⁷

On the other hand, the Goss Labor government increased a number of taxes while still maintaining Queensland's relative position on the tax competitiveness front. Putting aside the transfer of the commonwealth bank account debits tax to the states in 1991, Premier Goss proposed during the 1992 election campaign to increase the state tobacco franchise fee by 150 per cent to fund 28,000 public sector jobs and finance a hospital reconstruction program.³⁸ A tax on poker machines based on three per cent of turnover was introduced in the 1991-92 financial year.

However, there were growing pressures for the government to fundamentally alter its budgetary management stance. Trade unions and social welfare advocates were demanding that the Goss government ease the low taxation fiscal constraint in order to fund additional social expenditures. There was also increasing internal pressure from within the government to explore additional opportunities to raise revenues.

For example, in a speech to the Queensland Parliament in June 1993 influential backbencher, and future Premier, Peter Beattie canvassed the possibility of a state fuel tax regime:

*'we do need to look in a more rational but at the same time compassionate sense at the economic policies which dominate Government. We need to look at the funding issue. There are those who argue, for example, that in Queensland we need to broaden the tax base, that in fact our tax base is too low. We have been in an advantageous position because of our low-tax nature and because that has been one of the things that have attracted people here. I am not a high-tax person in any sense, but I do think that there will be a time, somewhere along the road, when we will need to look at widening the tax base and maybe issues such as the petrol tax need to be put on the agenda and discussed, looking at it from the position of equity. ... if we are looking at quality of life for Queenslanders, and we are looking at where we are when it comes to education, particularly, and health, which were ignored for so long under the National and Liberal Party Governments in this State, we do need to look at it very seriously.'*³⁹

From 1996 to 1998 the National and Liberal Party Coalition government, led by Rob Borbidge, maintained a stance to retain Queensland's low taxation status in the Australian Federation. Premier Borbidge and Treasurer Joan Sheldon released a State Economic Development Strategy outlining a case for maintaining low taxation in the state as a means of holding down costs in an increasingly competitive economy.⁴⁰

To signal its low taxing credentials to the general public, the Coalition during the 1995 election campaign committed to phase out land taxation over a ten year period. As part of this strategy the government increased exemption thresholds, and changed for basis for calculating land tax liability by introducing a three year average valuation process. Additional relief was also provided for businesses paying payroll taxes to the state government.

³⁷ Owen Gabbitas and Damien Eldridge, 1998, *Directions for State Tax Reform*, Productivity Commission, Staff Research Paper, AusInfo, Canberra.

³⁸ Jamie Walker, 1995, *Goss: A Political Biography*, University of Queensland Press, St. Lucia.

³⁹ Peter Beattie MLA, 1993, Record of Proceedings, 13 July.

⁴⁰ Queensland Government, 1997, *State Strategic Plan 1997-2007: State Economic Development Strategy*, Government Printer, Brisbane.

On the other hand, the Borbidge government's first Budget enacted an increase in the license fee payable on tobacco products (to fund an increase in the health budget) as well as an increase in the debits tax rate to that in New South Wales, Victoria and South Australia. These measures, however, did not endanger Queensland's ranking as the lowest taxing state in the Australian Federation.

The spending surge: How Queensland lost its low tax state status

While both major parties in Queensland maintained a business friendly low taxing environment, it could be argued that the seeds of destruction of the low tax state policy were sown during the 1990s if not earlier.

As described above both Labor and conservative governments increased taxes largely to meet explicit social objectives, such as redirecting tobacco and gambling tax revenues towards health and problem gambling measures respectively. Governments also relied upon non-taxation revenues, for example freight charges for coal haulage on railways or fines for traffic violations on roads, for the purposes of meeting growing demands for public expenditures.

However concessions made by government to substantially lift social services spending played the major part in diluting Queensland's historical tax advantages.

As noted above unions, welfare advocates and academics for a number of years painted a Galbraithian 'private splendour, public squalor' narrative of the Queensland economy, whereby the maintenance of low taxation was accompanied by parsimonious government expenditure on public services particularly in the areas of education, health and welfare.

According to Commonwealth Grants Commission data in 1991-92 Queensland spent \$1,589 per capita on social services, the lowest of any state and ten per cent below the national average. Low levels of state expenditure on services were evident in education (\$670 per capita compared with a national average of \$710), health (\$574 per capita compared with national average of \$639) and welfare services (\$78 per capita compared with a national average of \$137).⁴¹

A Public Sector Management Commission review of expenditure by the state Department of Family Services and Aboriginal and Islander Affairs in 1991 appeared to confirm the CGC analysis when it noted that '[t]he department's ability to achieve its key welfare and social justice objectives is significantly compromised by its poor resource base. In fact the Department of Family Services and Aboriginal and Islander Affairs is the most under-resourced and under-capitalised department which the PSMC has reviewed.'⁴²

⁴¹ Peter Walsh, 1993, 'Welfare Policy', in Bron Stevens and John Wanna, eds., *The Goss Government: Promise and Performance of Labor in Queensland*, Macmillan Education, South Melbourne.

⁴² Ibid, p. 222.

The relatively low levels of government expenditure in this and other selective areas, compared against the southern states, were conceived by some big-spending advocates to represent a significant problem founded upon a 'neo-liberal' conception of the role of the state:

*'Consistent with the Bjelke-Petersen government's ethos is a formulation of welfare based on the premise that there are two natural channels through which an individual's needs are met: the private markets, and the family. Only when these break down should social welfare institutions come into play, and then only temporarily. This is a model of welfare described as residual. An alternative model sees social welfare as a positive force for social development operating outside the market system.'*⁴³

Implicitly endorsing these modes of thinking, the Goss Labor government committed itself to overcome the alleged 'neglect' of government services by previous conservative administrations, including to substantially raising Queensland expenditure on education:

*'The Goss Government inherited an education and training system based on unacceptably low funding and standards. ... When the Goss Government came to office State funding for schools was only 90% of the national per capita average. In line with its pre-election commitment, in its first two Budgets it has increased funding through the Department of Education by more than \$250m in real terms and brought per capita funding into line with the average of the States'*⁴⁴

In its 1995-96 Budget the government announced an expansion of recurrent funding for health and welfare, education, law and order and the environment by 10 per cent, as well as an \$800 million program for the development of social infrastructure over a three year period. Treasurer de Lacy noted in his Budget Speech that 'the critics will label this a "big spending" budget, and they will be right. I make no apologies for that. It is aimed at meeting the expanding needs of our rapidly growing community.'⁴⁵

From 1992-93 to 1995-96 Queensland experienced the largest increase in expenditure per capita of all the six states of 12.3 per cent over the period. By contrast, Victoria, Western Australia and South Australia had in fact reduced the amount of government spending on a per capita basis.

A year later, in 1996-97, Queensland was overtaken as the lowest spending jurisdiction per capita by Victoria. As a proportion of gross state product, Queensland's expenditure (13 per cent of GSP) was greater than Victoria (11 per cent), Western Australia (12 per cent) and NSW (12.5 per cent).

Based on CGC data the assessed level of service provision for Queensland increased from 84 per cent in the mid-1980s to about 100 per cent by 1996-97, while the service provision levels in Victoria and New South Wales declined over the same period.

Returning to office in 1998 the Labor government, led by Peter Beattie, again denounced the expenditure 'neglect' committed by the previous National-Liberal Coalition government and

⁴³ Patricia Smith, 1985, 'Queensland's Political Culture', in Allan Patience, ed., *The Bjelke-Petersen Premiership 1968-1983: Issues in Public Policy*, Longman Cheshire, Melbourne, p.99.

⁴⁴ Hon Wayne Goss, *Queensland Leading State*, op cit, p. 58.

⁴⁵ Hon Keith de Lacy MLA, 1995, Budget Speech 1995-96, 23 May.

committed to significant increases in government spending. As acknowledged in the 2000-01 Queensland Budget Overview statement:

'[e]nhancements to service delivery to meet the growing demand for Government services, and to move towards levels in other States, are reflected in Queensland spending more than previously in key social service delivery areas.

In recent years, Queensland's recurrent expenditure effort has been moving towards the average of the other States in key service delivery areas such as health and education. ... over the past 10 years, the expenditure effort on these key areas has risen from around 80% of the average of the other States to variously between 90-100%.⁴⁶

To some extent increasing budget allocations were targeted in an effort to resolve specific policy problems as they arose. In response to a Commission of Inquiry into Queensland's Public Hospitals and a review into state health systems, which exposed endemic dysfunction within Queensland public hospitals, the government announced additional health funding of \$6.4 billion over five years.⁴⁷

The Beattie government also justified additional expenditure in the guise of a 'Smart State' strategy.

Referring to the importance of a 'low cost tax' environment for economic development only once, the Smart State strategy document emphasised the importance of greater public investments in education and skills development, science and technology and innovation for growth and productivity.⁴⁸ A particular area of attention for the government was in biotechnology, described as 'the heart of the Queensland Government's Smart State strategy.'⁴⁹

Expending \$3.6 billion on selective human capital, industry incentives infrastructure and R&D initiatives from 1998 to 2007,⁵⁰ Beattie claimed that the Smart State policy 'succeeded in turning around the perception of Queensland from just a 'rocks and crops economy' to a modern, high-tech state with value adding at every opportunity.'⁵¹ However, as discussed in Box 1, the very basis for pursuing an activist approach towards industry development is highly questionable.

⁴⁶ Queensland Government, 2000, *Budget Overview*, 2000-01 Budget Paper No. 2, p. 73.

⁴⁷ Hon Peter Beattie MLA and Hon Terry Mackenroth MLA, 2005, 'Beattie government injects \$6.4 billion into health', Joint statement, 25 October.

⁴⁸ Queensland Government, 2005, *Smart Queensland: Smart State Strategy 2005-2015*, Queensland Government, Brisbane.

⁴⁹ Ross Fitzgerald, Lyndon Megarrity and David Symons, 2009, *Made in Queensland: A New History*, University of Queensland Press, St. Lucia.

⁵⁰ <http://www.science.qld.gov.au/dsdweb/v4/apps/web/content.cfm?id=15120> (accessed 24 May 2011).

⁵¹ Hon Peter Beattie MLA, 2004, Ministerial Statement, Weekly Hansard, 18 August.

Box 1: Queensland's Smart State policy: A critique

In a market economy innovation can best be understood as a process guided by entrepreneurs who seek to discover new sources of economic value by 'combining resources in a new way by using prior (tacit and explicit) knowledge in connection with knowledge of the current market situation (i.e. knowledge of time and place)' (Sautet 2002).

As the economist Joseph Schumpeter reminds us innovation is multi-faceted by its nature, and can encompass more than simply technology uptake and R&D to include new forms of organisation or the formation of new markets. The prospect is available to all firms, industries and sectors of the economy to demonstrate innovative behaviour.

Innovation can also engender structural changes in the economy as competition between firms that seek to add value redirects resources towards profitable firms. This dynamic process cannot be replicated or replaced by 'catalytic' intervention or 'economic leadership' by governments through the guise of industrial policies.

A major problem with the Smart State strategy is that it biases scarce public funding – through R&D subsidies, funding for research institutes and investment attraction incentives - towards politically perceived emergent industries, such as alternative fuels, aviation, biotechnology, 'creative' industries, nanotechnology and therapeutic industries, which each contribute modest amounts of value added to the Queensland economy at best.

By contrast, business expenditure on R&D (BERD) in Queensland reflects its prevailing industry structure. The services industries accounted for about 51 per cent of BERD in 2008-09, with construction alone representing about 30 per cent of total services BERD. This was followed by mining which accounted for 28 per cent of Queensland's BERD (within this, coal mining represented some 54 per cent of total mining BERD). Manufacturing accounted for about 21 per cent of BERD in the state, with food processing and metal product manufacturing businesses playing key roles in overall BERD in this sector.

It is difficult to attain a clear picture of a sectoral breakdown for government expenditure on R&D (GERD) by the Queensland government, with the state Office of Chief Scientist annual R&D expenditure report demarcating GERD into exotically named policy categories such as 'environmentally sustainable Queensland,' 'safeguarding Queensland' and 'Tropical Opportunities' which tend to overlap with each other.

The 'smart industries' R&D category, with funds directed towards mining, manufacturing, food and fibre and biotechnology activities, accounted for 15 per cent of Queensland GERD in 2008-09. It is conceivable that much of the R&D funding under this category, in turn, was directed towards the state government's much-favoured biotech ventures.

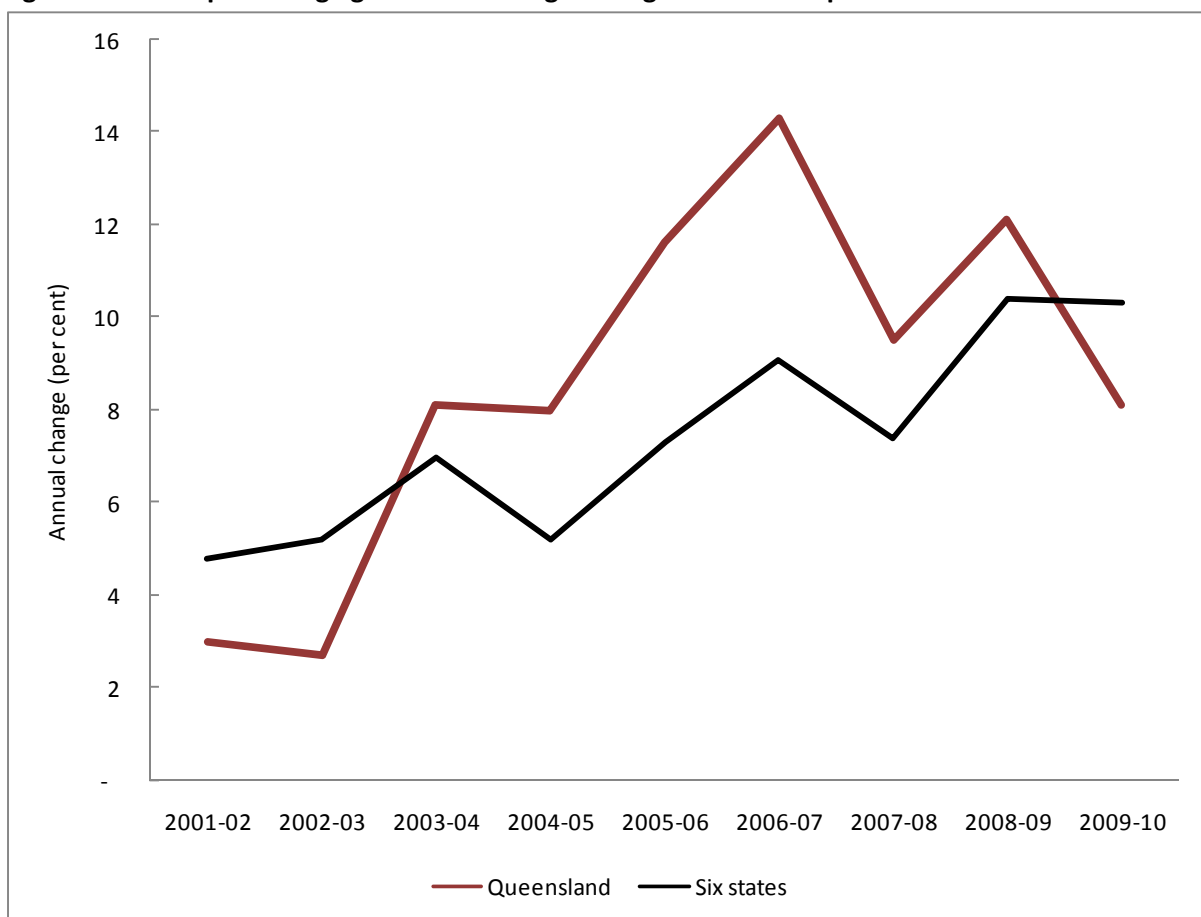
A significant proportion of the government's R&D grant funding has been channelled through universities and government-sponsored research institutions, both of which have a notoriously poor record of transforming the outcomes of research into commercially successful ventures.

The appropriate role for government in the support of innovation is one that provides an institutional environment conducive to value adding market activities. To quote Australian political scientist Scott Prasser, '[a] more deregulatory framework, improved state taxes, and better allocation of government spending on projects that make a difference are ... more appropriate policy responses. In other words, let's make Queensland have the right competitive environment for business to come here and to make profits.'

Source: ABS, Research and Experimental Development, Businesses, Australia, cat. no. 8104.0; Scott Prasser, 2008, 'Queensland, the Smart State', On Line Opinion; Queensland Government, 2009, 'Queensland Government R&D expenditure 2008-09 report', Office of the Queensland Chief Scientist; Frédéric Sautet, 2002, 'Economic Transformation, the Pretence of Knowledge and the Process of Entrepreneurial Competition', New Zealand Treasury Economic Transformation Project, Preliminary draft paper.

The rate of growth in general government sector expenditure in Queensland over much of the past decade not only outstripped growth in revenue, but had exceeded growth in spending undertaken by the six states (Figure 4). It is notable that in 2006-07, when current Premier Anna Bligh was Treasurer, expenditure within the general government sector increased by over 14 per cent compared to the previous year.⁵²

Figure 4: Annual percentage growth of state general government expenditures



Source: State government budget papers and annual financial reports.

As a consequence of the growing propensity by the state government to spend at significant rates the maintenance of Queensland's low taxation status has come under extreme pressure. Indeed, as noted above, most of the available indicators of taxation competitiveness suggest that Queensland has ceded its low tax position to other states such as Tasmania, Western Australia or Victoria.

⁵² This performance may be explained, at least in part, to population growth in Queensland during this period which was roughly twice that of Australia as a whole, with net interstate migration of about 25,000-30,000 people. However, separate analysis undertaken by the author indicates that the rate of growth in actual general government sector expenditure was in excess of combined inflation and population growth since the early 2000s.

While the tax policy actions of other states can influence the relative competitiveness of Queensland on the taxation front, the loss of the low tax state mantle for Queensland has also been due to an explicit policy emphasis towards greater expenditure. As Premier Anna Bligh remarked in June 2007, 'Queensland wants to remain a competitive tax state. We don't want to be the state with the worst services and the state with the least infrastructure. We want to be competitive, but that doesn't mean we're going to be the lowest on every single indicator.'⁵³

The political retreat from low state taxation in Queensland has also been reflected in successive Budget papers which increasingly refer to policy preferences to maintain a 'competitive,' as distinct from 'low,' state taxation environment.

In the 1998-99 Budget the intention to implement a 'Charter of Social and Fiscal Responsibility' was specified, in turn to be informed by five underlying principles including '[t]he maintenance of a competitive tax environment.'⁵⁴ A year later it was noted in Premier Beattie's Budget Speech that '[t]he Government is committed to ensuring that State taxes and charges remain competitive with those of other States and Territories.'⁵⁵

Prior to the implementation of national taxation reform in 2000, Premier Peter Beattie and Treasurer David Hamill raised concerns that the replacement of a number of state own-taxes for commonwealth GST revenue grants would threaten Queensland's low taxation status. According to Treasurer Hamill, 'Queensland's tax competitiveness is being undermined, through the insistence of the Commonwealth that Queensland pay for the abolition in other States of taxes that are not even levied in Queensland, specifically Financial Institutions Duty and Bed Taxes.'⁵⁶

It is true that other states imposed taxes slated for abolition under the GST agreement, which either did not exist or were imposed at lower rates in Queensland. However, there a number of factors which effectively dispel the claim that the Howard tax reforms were the leading cause of Queensland's loss of its low taxation status.

While Queensland adhered to the timetable for the abolition of certain state taxes some high-taxing jurisdictions (for example, NSW, Western Australia and South Australia) did not in every respect which, other things being equal, would undermine their state tax competitiveness compared with Queensland.

The former Premier and Treasurer were also correct to state that Queenslanders would pay a ten per cent GST where none existed previously. However when all commonwealth government subsidies (including grants, benefits to individuals and service provision), and taxes, to, and from, each state are considered Queensland has been a substantial net recipient of commonwealth funds since the introduction of the GST, if not beforehand.⁵⁷

⁵³ Sean Parnell, 2007, 'Bligh swaps low-tax title for better services', *The Australian*, 7 June.

⁵⁴ Hon David Hamill MLA, 1998, Budget Speech, 1998-99 State Budget, p. 9.

⁵⁵ Hon Peter Beattie MLA, 1999, Budget Speech, 1999-2000 State Budget, p. 17.

⁵⁶ Hon David Hamill MLA, 2000, Budget Speech, 2000-01 State Budget, p. 25.

⁵⁷ Information based on Western Australian Treasury analysis of the interstate redistributive impact of commonwealth government policies.

In addition the abolition of a number of state taxes such as bank account debits tax, marketable securities duty, as well as reduced gambling taxes, has not prevented Queensland (or, for that matter, any other state or territory) from unilaterally reducing their remaining own taxes (e.g., payroll tax, land tax, conveyancing duty, gambling taxes, insurance taxes, motor vehicle taxes) to gain an advantage in attracting capital and labour.

Furthermore Queensland remains free to capitalise on growth in untied GST revenue grants (which are received, due to fiscal equalisation, by Queensland in an amount greater than its implied per capita share) to fund state tax cuts if it so chooses.

The fact of the matter is that the burden of Queensland state taxation has increased, compared with other states, on the basis of deliberate policy decisions by Queensland to accommodate demands for additional public expenditures across most categories.

However these developments have coincided with a sharp deterioration in fiscal sustainability, reflected in Queensland losing its historically much-vaunted AAA credit rating in 2009 and now assuming the dubious distinction of possessing the worst budget outcome of all the Australian states and territories of budget deficits across the forward estimates.

Should Queensland once again become the low tax state?

As described above there are a number of theoretical arguments supporting the case for lower taxation by state governments. Equally it could be argued that Queensland enjoyed a range of beneficial economic and fiscal outcomes during the low taxation era, with the prospect of gains acquired once again should policymakers agree to substantially reduce the state tax burden.

Arguably the most tangible benefit of the previous low taxation era from the 1970s to late 1990s was the influx of Australians from other states into Queensland. This boost to net migration not only contributed to an emergence of a critical mass of consumers in the state, but brought with it skilled labour and business entrepreneurs expanding the long term capacity for Queensland economic growth.

While there are unquestionably a multitude of factors that explain migration patterns, including Queensland's much renowned warm climate and relaxed lifestyle compared to Sydney and Melbourne, some studies suggest that policies that reduced the burden of taxes encouraged growth in interstate migration, at least in response to a 'demonstration effect' implying that Queensland was open for people and business.

The American economist Philip Grossman found that during the period from 1977 to 1982, the average quarterly increase in Queensland's population from interstate migration was approximately 70 per cent higher than the average for the periods 1972 to 1975 and 1983 to 1985. Based on an empirical analysis, population growth in Queensland during the first three years after abolishing

death duties was on average 0.2 per cent higher due to migrants avoiding the death duties of the other five states (even if they had already announced timetables for tax abolition).⁵⁸

Noting that Queensland's share of the Australian population grew from 14 per cent in 1971 to 18 per cent in 1996, with interstate migration accounting for a significant proportion of the overall state population growth, Queensland Treasury economists Christine Williams and Jim Hurley sought to empirically estimate the determinants of net interstate migration into Queensland.

They found that interstate tax differentials were a statistically significant factor in attracting migrants from other states into Queensland: '[t]his result is stronger than expected, indicating that removal of the State tax differential would reduce net interstate migration by around 88%. However, it is possible that it is the perception of Queensland as a low tax state, rather than the actual amount saved in reduced taxes, which is the driver of such large positive net interstate migration.'⁵⁹

Coupled with the growing share of population, Queensland also increased its share of national investment by an average of 1.3 per cent per annum between 1984-85 and 1994-95 (behind WA's growth in investment share of 3.6 per cent per annum). Queensland also recorded an increase in its share of national production over the period (1.5 per cent per annum between 1984-85 and 1994-95).⁶⁰

In its assessment of relative state performance, the former commonwealth Bureau of Industry Economics observed that 'Queensland's good financial management contributed to its having the lowest state taxes and the lowest debt-to-GSP ratio. This contributed to its good growth performance by fostering internal growth and attracting new firms and industries.'⁶¹

A longstanding anecdotal observation has been that Queensland lacked a manufacturing base comparable to that of the larger states of NSW and Victoria, distorting the state's industry structure and depriving it of alternative opportunities to obtain additional economic growth:

*'Because of its primary industry base, historically Queensland has occupied a precarious position in the national economy, with most of the nation's wealth and population concentrated in New South Wales and Victoria - states which dominated the manufacturing industries. ... because of uneven regional and urban development patterns in a state whose capital city remained underdeveloped and was never the centre of Queensland's economic life, the south was the only area to achieve any satisfactory degree of economic diversification. By 1939 it was the only region to have diversified into agricultural, manufacturing and pastoral and mining industries, whereas the north, with its dependence on pastoral, mining and sugar production, and the centre, with its reliance on the pastoral industry, remained bounded within a framework of primary production.'*⁶²

Notwithstanding the fundamental inaccuracy of this widely held view, given the historical dominance of high-growth *service* industries to the Queensland economy, it can be argued that the

⁵⁸ Philip J Grossman, 1990, 'Fiscal Competition Among States in Australia: The Demise of Death Duties', *Publius* 20 (4): 145-159.

⁵⁹ Christine Williams, Jim Hurley and Beverley Morris, 1999, 'An Economic Model of Interstate Migration', *Economic Analysis & Policy* 29: 93-112.

⁶⁰ Bureau of Industry Economics, 1996, 'Looking behind the differences in state growth', Australian Industry Trends (May).

⁶¹ *Ibid*, p. 61.

⁶² Murphy, Joyce, Cribb and Wear, *The Premiers of Queensland*, op cit, p. 334.

maintenance of low taxation was (intended or otherwise) a rational policy response to the national tariff protection regime that developed from the early 1900s.

In an analysis of the effects of Federation upon the Queensland economy, Jon Stanford wrote that '[t]he battle over Free Trade or Protection had been effectively resolved in favour of Victoria so that the tariff imposed by the Commonwealth Government became progressively more protectionist and less important as a revenue item. The tariff ensured that industrial development proceeded in the locations where it had originally begun that are in Victoria and New South Wales.'⁶³

While Stanford contended that the consequence of the tariff was 'freezing the Queensland economy into an overdue dependence on primary production, into a "branch office" structure and generally into lower economic production than would otherwise have been possible,'⁶⁴ low state business taxes nonetheless helped to offset the cost disabilities of high tariffs imposed upon agricultural, mining and services industries in Queensland which depended upon imported capital equipment for their development.

Indeed, the low tax state policy assisted Queensland in other ways which were quite possibly unintended, or not comprehended fully, by the National-Liberal and Labor governments that endorsed this principle. Specifically, the historically high tariff level distorted the structure of production in the southern states, whose large manufacturing industries came to rely upon import protections for their very survival.

While the revenue raising capacities of NSW, Victoria, South Australia and Tasmania were unquestionably greater due to industrialisation via tariff protection, the relatively greater levels of spending on services by these states proved to be unsustainable once the commonwealth government undertook the necessary, and overdue, steps to reduce tariffs in an effort to foster an outward looking, export-oriented Australian economy.

In addition the reduction in tariffs, and the maintenance of low state taxes during the 1990s, enabled Queensland to develop its niche manufacturing sector whilst the southern states grappled, and continue to grapple, with the damaging consequences of structural adjustment in their inefficient manufacturing sectors (Table 2).

⁶³ Jon Stanford, 1988, 'The Long-Term Effect of Federation on the Queensland Economy', University of London, Sir Robert Menzies Centre for Australian Studies, Working Paper No. 37, p. 8.

⁶⁴ Ibid, p. 2.

Table 2: Distribution of manufacturing activity by state

	Value-added			Employment		
	1977-78	2000-01	Change	1977-78	2000-01	Change
	Per cent	Per cent	Percentage points	Per cent	Per cent	Percentage points
NSW	38.1	32.1	-6.1	37.5	31.3	-6.2
Vic	34.2	32.3	-1.9	34.6	31.9	-2.7
Qld	10.4	14.3	4.0	9.8	16.1	6.4
WA	6.0	9.4	3.4	5.7	7.9	2.1
SA	8.3	8.6	0.3	9.6	9.8	0.2
Tas	2.5	2.4	0.0	2.4	2.2	-0.2
ACT	0.3	0.4	0.1	0.3	0.4	0.2
NT	0.3	0.4	0.1	0.1	0.3	0.2

Source: Productivity Commission, 2003, *Trends in Australian Manufacturing*, Commission Research Paper, AusInfo, Canberra, p. 73.

The varied critics of the low taxation regime repeatedly pointed to the relative shortfall of public expenditure in Queensland compared with other states, including Victoria during the Cain-Kirner era. As late as 2002 the then state secretary of the Australian Workers Union, Bill Ludwig, stated that '[i]t's an absolute fact that low taxes mean low services.'⁶⁵

However, information provided in previous state Budget Papers indicate that 'Queensland is one of the more efficient providers of government services among the States,'⁶⁶ as reflected in the relatively lower costs of services such as hospitals, prisons, courts and public housing. The 1996 Queensland Commission of Audit report assessed the financial position of the Queensland government and concluded that:

*'Queensland is a low-tax State compared with other States. While this may suggest that service quality has suffered in Queensland, the findings ... of this Report suggest that, in the main, Queensland Government services are being delivered more efficiently than those in other States.'*⁶⁷

The maintenance of a low taxation environment in Queensland was arguably associated with a more thorough pursuit of value-for-money in government services provision than what had occurred in other states. Indeed the very basis of a 'low tax constitution' - enshrined in Queensland's case as a desirable policy moral by successive governments - is to restrain the spending proclivities of government enabling citizens to retain greater disposable incomes for use in addressing their own needs than would otherwise be the case.

Conversely, once expenditure norms consistent with a low tax position are relaxed the risk is that policymakers will be motivated to expend on activities with questionable tangible benefits, such as the Smart State policy.

⁶⁵ Craig Johnstone, Rosemary Odgers and Chris Jones, 2002, 'Low tax state', The Courier Mail, 3 August.

⁶⁶ Queensland Government, 2000, Budget Overview 2000-01, p. 74.

⁶⁷ FitzGerald, V W, Carmichael, J, McDonough, D D and Thornton, B, 1996, *Report of the Queensland Commission of Audit*, Volume I, The Commission, Brisbane, p. 162.

Conclusion

The low tax state policy, which was implemented in a bipartisan manner from the early 1970s to the late 1990s, delivered a host of benefits for the Queensland economy and society.

As suggested above policies under the low tax state regime signalled to the rest of Australia, and indeed the world, that Queensland was open to people and business.

In one of the rare cases of Tiebout competition in the Australian context, the abolition of death duties and the maintenance of low, business friendly tax rates encouraged an influx of migrants, providing their skilled labour and entrepreneurial ideas, and underpinned the basis for increasing business investment that transformed Queensland from what was perceived to be an economic and cultural backwater to the thriving place it is today.

In other words, although Queensland is no longer the low tax state of Australia the benefits of that era continue to reverberate through the state economy to this day.

While the current government can exclaim that it has presided over a 'competitive tax state' the policy retreat from low taxation, borne from a policy acceptance of questionable claims that low levels of public expenditure necessarily implied service deprivation, puts at risk Queensland's capacity to realise her full potential in a competitive world.

It is little coincidence that bequeathing the low tax state status to the likes of Tasmania and Western Australia, and even Victoria on some measures, has coincided with a retreat from other fiscal morals such as surplus budgeting and low public debt that previous Queensland governments had worked tirelessly to maintain.

As noted above, and with the 2011-12 state Budget imminent, Queensland is now in the unfortunate position of presiding over the worst set of budget outcomes of all states and territories. Given this situation, it is not possible for the state to reclaim her mantle as Australia's lowest taxing state soon.

In the short term the Queensland government must maintain its focus upon restoring sustainable public finances, which were damaged by years of excessive spending, whilst maintaining the state's current tax competitiveness.

The privatisation program will be instrumental in this regard, for as long as the proceeds of asset sales are directed towards repaying the burgeoning public debt, and the government should now focus on reducing its input costs including through a rationalisation of the public service. With the current version of the Smart State strategy due to end in 2012 it would be expedient to cease further implementation beyond that time, at least pending a review of the effectiveness of the program.

On the basis of estimates for 2009-10 the taxation per capita gap between Australia's lowest taxing jurisdiction, Tasmania, and Queensland is about \$356. In terms of taxation as a share of GSP the Tasmania-Queensland gap is approximately 0.1 per cent of GSP.

The challenge for Queensland in the short term, as it seeks to repair its budget, is to do so without further diluting its tax competitiveness. As noted above, this suggests that Queensland's fiscal adjustments should target expenditure reductions and not widen the tax discrepancy between itself and the lowest taxing state.

Notwithstanding the short term difficulties, it should be feasible for the government to publicly establish a plan to reinstate Queensland as Australia's low tax jurisdiction in the medium term – with a process of systemic tax reductions occurring from, say, 2015-16 onwards.

This plan could be framed about the government's policy priorities in response to contemporary economic and other challenges as they emerge. For example, tax reductions could centre upon improving the overall productivity of the Queensland economy by targeting the reduction of those taxes (typically those based upon market transactions) that impose the greatest deadweight costs, or promoting the employment of labour during a period of anticipated skills shortages by targeting reductions in payroll taxation, or a combination thereof. In any case, the overriding objective should be to transition Queensland back to being the low taxing state.

The nineteenth century English novelist and observer of Antipodean life, Anthony Trollope, observed that 'Victoria claims supremacy, New South Wales disputes it, and Queensland looks to a future in which she will become as large as either.'

There is little question that the modern self-confident Queensland sees herself as least as an equal to her more established cousins to her south. But for the state to attain the position as the jewel in the crown of Australian federalism it will need to once again embrace fiscal best practice, of which the maintenance of low taxation is a crucial element.