

Address to ALSF 2006 Activist Conference, 2 Dec 2006

“Some Challenges Not Being Addressed by the Liberal Party”

by Des Moore

As I grow older my recollections of earlier happenings start to fade a bit. But I do remember the opening words of a song that was quite popular a few years ago. I am *not* referring here to songs such as “When You are Old and Grey” or even “National Brotherhood Week” composed by Tom Lehrer over 50 years ago and now brilliantly revived in the Melbourne Theatre Company’s “Tomfoolery”. Of course, such songs are only suitable to be heard on stage and you will be pleased that I have no intention of embarrassing you here. Apart from the risk of audience walk-out, any attempt to sing might, as Lehrer found when he visited Australia, run the risk of censorship.¹

But the song I thought worth drawing to your attention is, I hope, a totally inoffensive one that starts with the simple phrase “Just a Few More Years”. My suggestion for today is that the Victorian Liberal Party should adopt this song and perform it every time it meets. After all, if the two party preferred gap is closed at the same rate as over the past four years Liberals will definitely be returned to office in 2014. “Its just a few more years ... everything will be different by then”.

What could we then expect the Liberal Party to do? Assuming he is still leader that might give Ted Baillieu the opportunity to implement his promise to make Victoria the lowest taxed state in that year. But that might also require some different spending and other policies to those adopted in the recent election campaign. The general approach in that campaign seemed to be not greatly different from the Labor Party’s, but perhaps it reflected a hope the Victorian electorate would see Liberal politicians as better able to deliver – kind of like the song that started “I can do it better than you: no you can’t, yes, I can”.

But, as the Herald Sun pointed out, those policies “failed to produce the point of difference” required and Alan Wood rightly described them as “unimaginative with an unhealthy dose of me-tooism”. Surprisingly, despite the absence of any substantive differentiation, opposition leader Baillieu is reported as rejecting a proposal by Liberal Party President for an independent policy review.

What policies might or should have been pursued? My basic proposition is that the Liberal Party should present itself as the party of small government and private enterprise. But while this is already supposed to be part of the party’s platform, well meaning suggestions that policies should be framed around such an objective have been given a cold shoulder. An even colder shoulder has been given to suggestions that the

¹ In South Australia Lehrer was not allowed to sing five songs, including “When You Are Old and Grey”.

Victorian Liberal Party should base its policies around the reforms introduced under the Kennett government, let alone flaunt the apparent benefits from those reforms.

This despite the fact that, under that government, Victoria experienced the *fastest* growth in living standards of any state or territory *and* the largest proportionate fall in the average unemployment rate even in the face of the much publicised reduction in public sector employment. Even more remarkable is that the Liberal Party has failed to draw attention to the increase under the Kennett government in the size of the private sector from 75 to 80 % of GSP. When I pointed out to the previous Liberal leader that this was partly due to the successful privatisations by that government, I was told that privatisation is now a no, no politically in Victoria.

After that discussion it so happened that even Premier Beattie started to reverse his anti-privatisation policy and he has just sold his electricity retailers for twice the expected price. But no change seems to have occurred in the attitude of the Victorian Liberal Party and, as far as I know, the only reference to privatisation policy by the current leader was a reported indication during the election campaign that no public hospital would be privatised.

Mention of Premier Beattie and public hospitals brings me to the report I prepared for the Chamber of Commerce in Queensland on the role of government in that state. That report, copies of which are available for those who might be interested, outlined the general approach and some specific policies that could be used by the Victorian Liberal Party as a future basis for substantive differentiation from Labor. That is, I suggest, the challenge that needs to be addressed by the Liberal Party – and not only in this state but in other states too. Right around Australia the only thing that at present seems likely to cause a Labor loss is not different policies presented by Liberal parties but the now widespread misbehaviour of ministers that reflects governments which have clearly been in office too long. It is surely time for some brave Liberal politician to, using Tennyson's words, start to "Ring out the old, Ring in the new ... Ring out a slowly dying cause".²

Let me outline the approach I adopted in my Queensland report.

My general thesis there was that it is in the government's own interests to maximise the role of the private sector in the provision of services that have traditionally been regarded as the responsibility of governments. The dividing line between the private and government sectors has ceased to be clearly defined because, partly through contracting type arrangements, it is now increasingly realised that the private sector has the capacity to provide a large proportion of what have hitherto been regarded as public goods.

Why should it be in the government's own interests when an increase in the private sector's role will mean a smaller government sector? The basic answer is that the provision of services through a competitive framework will benefit the consumers of those services - that is, the voters in the state. Whether assessed in terms of economic

² From Tennyson's poem "In Memoriam".

prosperity or social well-being, such a framework provides a more efficient and higher quality way of delivering essential services wherever that is practicable.

Today, this is not a view confined to one side of politics. Shadow Federal Finance Minister Lindsay Tanner told the Centre for Independent Studies in March that “public ownership is less important than it once was ...regulation and competition can now contribute a great deal more to social outcomes than they could fifty years ago”. In some ways this was a remarkable statement – even fifteen years ago the then Labor Shadow Finance Minister would never have even thought of addressing the CIS. And as young Federal Labor MP, Craig Emerson, recently pointed out, “If we are to achieve excellence in education, schools and universities will need increasingly to specialise in a more competitive environment ...competition can no longer be a dirty word” (AFR 10 April).

Moreover, because an increased private sector role offers potential for a lower level of taxation as well as better services it is difficult to see that any government implementing a pro-private sector role would fail electorally. In short, a properly explained reform program by the Liberal Party should be both economically and politically saleable.

A deliberative policy of increasing the competitive environment for service provision can be implemented in two ways - first, by acting directly to improve the performance of those services retained *within* government and, second, by taking steps to encourage a major increase in the proportion of such services provided by enterprises operating *outside* the government sector.

The direct approach can be implemented by an overt policy under which the government would retain full responsibility for funding but the actual delivery of some major services by the state would be opened to competition from the private sector. For example, hospitals policy could start by giving public hospitals greater autonomy and the right (and financial incentive) to contract out the provision of discrete services such as pathology and certain types of surgery. In the case of schools policy, the provision of increased autonomy to headmasters over staffing decisions would improve the capacity to effectively manage the work force and reduce restrictive union practices. Some more competitive mechanism might also be proposed to overcome deficiencies in the curriculum agenda that the education bureaucracy seems to regard as its own. Looking ahead, and drawing on developments under the Blair Government - which include substituting private operators where public ones have failed to perform - one prominent economic analyst in the United Kingdom has suggested that governments could eventually cease to be *direct* employers of teachers or doctors.

Most state governments, including Victoria, are also already making some use of the private sector to construct and maintain public hospitals and schools.³ But why not make this a general policy?

³ The NSW government has had a private sector firm finance, design and construct nine schools and, according to a NSW Treasury analysis, these schools were built for much less and two years earlier than would have been possible under a traditional public sector contract. The contractor has also effectively taken over the administration of the schools for 30 years.

The second - or what might be called the indirect - approach would be to further encourage the development of private sector services that compete with government services or that take over the public sector role where that appears likely to improve the efficiency and quality of services. State governments already give some financial help to private schools but no effective funding to private hospitals.⁴ The Federal government also provides considerable financial assistance to non-government schools and, through rebates of premiums paid to health insurance funds, to private hospitals as well. However, users of these private sector services still have to pay considerable fees as well as taxes to fund their public sector equivalents. Despite this, there has been a considerable expansion of school and hospital services in recent years, with associated savings to state budgets. This has clearly been driven by the increasing acceptance in the wider community that the private sector is offering services of a higher quality and the wider choice that modern society wants.

This is reflected in the fact that, since 1992, the proportion of students attending fee-charging non-government schools in Victoria has increased from 32 to over 35 per cent and the almost 290,000 students attending such schools in 2005 effectively saved the Victorian Government and hence the taxpayer over \$2 billion net in that year. The proportion of patients treated at fee-charging private hospitals has also increased substantially and had reached over 36 per cent in 2004-05, again saving the Victorian Government over \$2 billion a year. It is clear that the development of private hospitals means they now have the capacity to increasingly take over the role of public hospitals.

There is here a major challenge for the Liberal Party to adopt policies that have potentially double or even triple whammy beneficial effects. Such policies would help meet the increasing underlying demand that obviously exists for private sector school and hospital services, would reduce the net burden on state budgets and, at the same time, would allow lower levels of taxation. This is a challenge which all state liberal parties, and the federal liberal party too, should address in their own interests. Indeed, a carefully framed federal policy that added either directly or indirectly to assistance for users of private schools and hospitals would help both electorally and in improving the functioning of society.

I have referred to schools and hospitals mainly because they account for about half of expenditure by state governments. But there is scope to extend the private sector's role in the provision of other state services too. One obvious area relates to the extensive services still provided by government trading enterprises in key sectors of all state economies, including electricity, water, urban transport, railways, ports and forestry. In its 2004-05 report⁵ on 83 of such enterprises the Productivity Commission noted that they controlled assets valued at no less than \$186 billion and generated \$63 billion in revenue,

⁴ Australian Hospital Statistics, 2004-05, published by the Australian Institute of Health and Welfare indicate that some state governments provide a very small proportion of private hospital funding. However no such funding is provided in Victoria.

⁵ Financial Performance of Government Trading Enterprises 2000-01 to 2004-05, Productivity Commission Research Paper.

which might be compared with total revenue of about \$150 billion generated by state government budgets. The Commission's analysis also showed, however, that nearly half such corporations earn less than the bond rate and have not improved earning rates since 1999-00.

This situation provides a strong basis for a Liberal Party policy of privatising most remaining state trading enterprises. A good deal of resistance to such a policy would come from the usual quarter, namely the union movement which would be trying to protect against the likely reduced employment in a more competitive environment. However, the pursuit of a policy of greater private sector involvement should be saleable on the basis that the capital of such enterprises would be used more efficiently and the services would likely be provided to consumers at a lower cost and higher quality.

Analysis by the Australian Council for Infrastructure Development (Aus CID) shows that the involvement of the private sector in Victorian public sector type investments has been more extensive than in other states both in terms of sectors covered and overall. Between 1988 and 2004 the total project values of various forms of private sector involvement⁶ in Victoria exceeded \$40 billion. While this mainly reflects the privatizations under the Kennett government, privately oriented projects have been quite extensive under the Bracks government⁷, which has also renewed the agreements by the Kennett Government to franchise to the private sector the operation of the Melbourne public transport (train and tram) system. It is worth noting that in September 2005 the Victorian Auditor General reported that the (then) new "agreements represent reasonable value-for-money" and that the Community Service Obligation payments negotiated with the franchisees "were close to the best possible prices it could have negotiated for the sustainable operation of the metropolitan train and tram system".

Against this background it is puzzling, to say the least, as to why the Victorian Liberal Party has not adopted a policy directed at further increasing the role of the private sector in enterprise-type activity. Trading enterprises which remain in Victorian government hands include water, ports, forestry and part of rail and it is difficult to imagine that the privatization of water, at least in terms of operations, could have produced a worse situation than we now face.⁸ It is also relevant that the reduction in the relative contribution of the Victorian public sector to growth from 75 to 80 per cent has almost certainly improved the functioning of the Victorian economy even though the Bracks government has made no further reduction. Despite the commodity driven expansion in Western Australia and Queensland, average per capita incomes in Victoria have increased since 1998-99 at about the same rate as the average for Australia whereas those in public sector oriented NSW have increased at a much slower rate.

⁶ BOOs (Build, Own, Operate), BOOTs (Build, Own Operate, Transfer), privatisations, and Public Private Partnerships.

⁷ See Attachment A to Statistical Appendix in my May 2006 report on The Role of Government in Queensland.

⁸ The water and sanitation network in England and Wales (but not Scotland or Ireland) was fully privatised under the Thatcher government and the operation (but not the assets) of such networks is privately run in France.

I hope that what I have outlined so far has given a perspective to the challenges not addressed – or at least not addressed adequately – at the state level by the Liberal Party. As I have suggested, this should not simply be a matter for individual state liberal parties but should be pursued at a national level.

This brings me to the challenges not being adequately addressed in regard to policies that are more directly the function of the federal government and hence the federal party. There are a number of issues that could be pursued here if time permitted. These include what is probably the most important issue facing Australia today, namely the terrorist threat. While the federal government has increased security services and tightened anti-terrorism legislation, it seems to be reluctant to identify that the source of that threat is Islamic extremists and to effect a tightening in immigration eligibility. Another important issue not adequately dealt with is climate change, where the government is failing to identify the many flaws in the global warming thesis. A copy of a critique by the Secretary of the Lavoisier Society, of which I am a member, is available for those interested.

However, for present purposes I put these important challenges aside and focus on the failure of the federal government to pursue policies consistent with the Liberal Party's supposed support of small government. Regrettably, the situation is worse than this because senior ministers are claiming that they *have* effected a major reduction in the size of government despite the fact that it is clear from data published by the Australian Bureau of Statistics they have not done so. The correct picture is outlined in my article on "When Will the Leviathan Fade Away" in the latest issue of Policy published by the Centre for Independent Studies. In that article I point out that, between 1995-96 and 2004-05, discretionary spending – that is excluding inescapable spending on interest on debt – actually increased from 23.3 to 24.2% of GDP and the burden of taxation increased from 22.3 to 25.7% of GDP.

Contrast this with Treasurer Peter Costello's claim in March that 'from 1995-96 through to 2005-06 the Australian⁹ Government's spending has declined from 26.3 per cent of GDP to 21.6 per cent' and his remarkable assertion that 'one of the values Liberals hold dear is to be disciplined with government spending'. In similar vein, the Prime Minister claimed in April that 'the Australian Government's overall tax share has fallen as a proportion of GDP from 23.1% in 1996-97 to an estimated 21.0% in 2005-06'.¹⁰ In reality, even with the tax reductions in the last budget it is clear that the Coalition is the heaviest taxing government we have ever had in Canberra.¹¹ By comparison, under the

⁹ In this context "Australian Government" means the Commonwealth government.

¹⁰ The main problem with the ministers' figures is that the pre 2000-01 data include large general revenue grants to the states and the taxes to pay for them while the ones for recent years exclude from expenditure the GST payments now made in lieu of those grants and exclude from taxes the revenue from the GST itself. This means that none of the ministers' comparisons has a valid, let alone meaningful basis.

¹¹ As noted, in 2004-05 the tax burden imposed by the Commonwealth was over three percentage points higher than in 1995-96 and, even on the improbable assumption that all the \$10 billion 'black hole' left by

Whitlam government the total tax take was 8 percentage points of GDP lower than now, equivalent in today's terms to a tax cut of over \$70 billion.

The public has been seriously misled by these ministers, who should make a full explanation and public apology for presenting such a distorted picture of federal fiscal performance. This is a major challenge yet to be addressed by the Liberal Party and, in addressing it, the Charter of Budget Honesty should be amended to ensure accurate data is published in future.

The hand-out proclivities of the Coalition are revealed in other various ways. The *Budget Measures* document for 2006-07, for instance, shows that decisions made after the 2005-06 budget are estimated to cost about \$47 billion net over three years and the document describing the decisions taken is the largest ever, comprising 357 pages and explaining close to 1,000 new expenditure measures alone. This kind of behaviour smacks of government losing control.

There are also a very large number of concessions, benefits or incentives provided through the tax system. The latest Tax Expenditure Statement runs to over one hundred and sixty pages (again the largest ever) and reveals these concessions cost over 4% of GDP.

Then we have Australia's superannuation arrangements, under which employers are legally liable to pay a superannuation guarantee charge equivalent to a 9% payroll tax if they do not make a superannuation contribution for their employees. This contribution is not treated as a tax - because it is not paid into government accounts but straight to superannuation funds - but it is tantamount to one and the resultant payout from super funds to contributors is a disguised form of government expenditure.

Finally, the 2006-07 Budget estimates hold out no promise of any change in direction. Spending is projected to stay around the same proportion of GDP which means that, without a major policy change in policies, they are likely to *increase further* as new spending decisions are made.

What is driving this high level of spending? Basically, the Coalition has since 1995-96 maintained assistance for welfare, health, and education at around 14-15 % of GDP. But in circumstances where average incomes have increased significantly, and unemployment has fallen from about 8% to 5%, there should have been significant reductions in such expenditure. Moreover, a major proportion of spending on welfare, health and education is provided to households with incomes in the top two quintiles.¹² This is all the more remarkable when it is realized that a substantial proportion of such

Opposition Leader Kim Beazley in that year would have had to be filled by higher taxes, the resultant tax burden would still have been about one percentage point of GDP higher.

¹² My May 2005 report to the Australian Chamber of Commerce and Industry on "Commonwealth Spending (And Taxes) Can Be Cut - And Should Be" showed that over 30 per cent of such spending goes to such households and that these are equivalent to 47 per cent of the taxes they pay.

payments consist simply of churning taxes back whence they came, that is, to higher income groups themselves.

The case for reducing government outlays in Australia was given additional weight by the *Intergenerational Report 2002-03*, circulated by Treasurer Costello but clearly sounding warning bells from Treasury. The obvious implication is that the ageing of the population will in due course require a large increase in taxation if existing spending policies are continued. But, although this heightens the economic and social case for early action to reduce education, health and welfare programs, Treasurer Costello has done little to promote the necessary policies, viz the tightening of eligibility for obtaining benefits so that recipients are concentrated in the lower income groups.

In my article in Policy I have made some suggestions for meeting this challenge. But what seems to be missing is a champion of the private sector and the individual. The recent death of Milton Friedman provided a stark reminder that we are badly missing such a person. This is disappointing after ten years of a Coalition Government that supposedly believes in smaller government and in giving greater responsibility to individuals, who are nowadays more able to take care of themselves. Let us hope that, in its policies for the next election, the Coalition will go one better than the Opposition's pledge not to increase the tax to GDP ratio.

Des Moore is a former Deputy Secretary, Commonwealth Treasury and is now Director, Institute for Private Enterprise.