

Re: think discussion paper submission

For there to be a productive discussion that will lead to genuine reform of the taxation system, we need to challenge long held assumptions and beliefs and examine some first principles of government finances. A good starting point to kick off this discussion is to:

- **Debunk the myths that are perpetuated in mainstream economic commentary and**
- **Examine the function and purpose of the taxation.**

I think it would be fair to say that many Australians believe running the federal budget is just like running a household or business budget. And why wouldn't they? Mainstream commentary from our politicians and the financial media generally support this notion. However, this comparison is bogus; the finances of a sovereign government with its own fiat currency bear absolutely no resemblance to the finances of a household or a business. (What is fiat currency? - fiat money is currency the government has declared to be legal tender that is neither tied to a physical commodity or to a fixed exchange rate. The "paper" money issued has no intrinsic value, it's simply a certificate that we use in exchange for goods and services).

I believe most Australians don't really understand the government's role as the issuer of the currency. However, without this knowledge and believing that running the federal government budget is just like running a household budget, it will be difficult if not impossible for Australians to make a reasonable assessment of any proposed taxation or expenditure policy. To make matters worse, policy makers will never form practical economic policy while they continue to believe that government spending is constrained by the revenue raised by taxation payments.

The *Re: think Tax Discussion Paper* is predicated on the following statement:

"The tax system raises the revenue required to fund public services".

In other words, government spending is limited by its ability to tax. This simply isn't true. As the issuer of the currency, the operation of the federal government is not constrained by tax revenues. The government can fund all of its public services no matter how few taxes it collects. Despite what we are led to believe, the government can make any and all payments in its own currency, the point being, there is no solvency risk; the government cannot go broke. In fact, taxpayers don't "fund" anything at the federal level. Tax obligations enforced by the federal government simply take money out of the system. Taxation is an instrument used to manage private sector demand. If demand rises faster than the private sector's ability to increase output, inflation occurs. In that situation the government can increase taxation in order to remove spending power from the private sector and cool an overheating economy. If, on the other hand, demand is too low to buy all of the economy's real output (i.e. All the goods and services produced by the private sector) the government can cut taxation in order to leave more money in the hands of households and firms to stimulate sales, output, and job creation. In other words, taxes function to regulate the economy, not to get money for the federal government to spend.

As long as government continues to believe that it needs taxation to get money to spend they will continue to support policies that constrain output and employment and prevent us from achieving what are otherwise readily available economic outcomes now and in the future.