Vern's Guide to Making a Budget Surplus a Reality

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Ever since the hapless Wayne Swan deputised as Treasurer, budget surpluses have remained elusive. Like the Scarlet Pimpernel, they seek them here, and they seek them there, but they cannot be found anywhere.

Every year we're told that just over the horizon is the promise of a wafer-thin surplus.

Really, *truly*, it is coming…*pinky promise*.

But the devil is always in the detail. The surplus promise is always conditional upon 'pie in the sky' forecasts.

The Treasury has a problem. Revenue is (highly) variable. Spending is fixed and escalating. A buffer needs to be built…lower spending.

Here's my solution to achieving a surplus in 2050.

The subject of 'government is the problem and not the solution' should be a compulsory addition to the educational curriculum.

The sooner we start weaning society off its dependency on government, the better for everyone.

Personal responsibility and independence of thought are going the way of the dinosaur.

Government is not the solver of problems.

Bureaucratic interference always has unintended and expensive consequences.

People need to be taught that the market is the most efficient and least-costly solution.

You may not like the market-delivered verdict, but that's life. Suck it up. Every kid cannot be a winner.

Sometimes you're given the short end of the stick and you have to make the best of it.

Educating the youth of today to be less reliant on government might, in decades to come, ease the pressure on budget expenditure.

The system has conditioned people to Pavlovian responses.

Not enough money for a house? Government will provide assistance.

Not enough money to have children? Government will provide maternity leave.

Not enough money to pay for childcare? Government will provide further benefits.

Not enough for retirement? Government needs to pay more in welfare and other subsidies.

Not enough money for medical expenses? Government will provide more funding for healthcare.

Not enough money for education? Government will throw another few billion at schools.

Not enough money to maintain a good life? The RBA will provide lower interest rates.

The list of ‘not enoughs’, while far from exhaustive, has probably touched a raw nerve with some readers.

No doubt a valid argument can be made as to why a particular ‘not enough’ warrants special treatment.

And therein lies the problem.

Everyone’s ‘not enough’ is the one that shouldn’t be subject to budget restraint.

The fact I’ve dared to touch on some ‘sacred cows’ indicates how protective we’ve become of our particular share of the government pie.

Politicians are well aware that, when it comes to votes, it’s ‘entitlements or else’.

The fear of ‘ballot box’ retribution is why spending cuts are off-limits.

Hoping we can change this mentality with education is, in reality, a pipe dream.

The truth is that government does not have a problem with revenue.

The budget forecast tax receipts of nearly $440 billion.

That’s a serious amount of money. And yet the Treasurer still can’t find anything to put aside for a rainy day. Pathetic.

What we have is a spending problem…*want, want, want*.

Ask and you are all but assured to receive…on the proviso it generates votes.

The more that’s given, the more that’s demanded. Enough is never enough when it comes to government spending.

In a recent report released by KPMG, it was found that (emphasis mine):

> ‘*…60 percent of* [Australian] *households pay the same or lower amounts of income tax compared to the payments they receive from the government — in essence,* ***40 percent of households are subsidising income for 60 percent of households****…*’

This is patently ridiculous and clearly not sustainable.

What does the Treasurer do about this absurdity? Rein in benefits and subsidies?

No. He decides to up the tax take…more revenue is needed.

Treasurer Morrison has given us his version of Swanny’s ‘Resource Super Profits Tax’ (RSPT).

It's been a few years since Swanny's brainwave, so here's a quick recap.

The initials RSPT actually stood for 'Really Stupid Policy, Treasurer'.

Swanny's 'genius' tax grab was replaced (in the blink of an eye) with the 'Minerals Resource Rent Tax' (MRRT).

And we all know that MRRT ended up being an abbreviation for 'Miners Ran Rings around Treasurer'.

Treasurer Morrison, in an attempt to compensate for being too gutless to tackle our runaway spending, has decided on a bank levy.

Hitting the Big Four banks and Macquarie with a sort of 'Banking Super Profits Tax' (BSPT).

According to SBS News: '*Mr Morrison insists the banks can absorb the new tax, which is set to raise $6.2 billion over four years.*'

Earth to Scotty, the banks are not going to absorb the new tax.

Yes, the optics are great politically. People love to hate the banks.

The executives earn far too much. Accounts are gouged for fees. Deposit holders are screwed on rates. Wealth-management divisions are mired in scandal. Cuts in cash rates are never passed on in full to borrowers.

The banks' public image is one of money first and customers coming a very distant second.

In playing to the crowd, Morrison looks to be on a winner. Clip a few dollars off the big end of town…they can afford to pay it.

The reality is the banks won't pay it.

Scotty is getting into our pockets via the banks.

Deposit rates will be clipped. Loan rates raised. Account-keeping fees pushed up a few dollars.

Little by little the banks will slice and dice accounts to pay Scotty his BSPT.

But, as always, nothing is ever one-dimensional. For every action, expect a reaction.

The Australian reports (emphasis mine):

> '*The government's new bank levy* ***will raise far less than the forecast $6.2 billion if lenders pass on the costs through higher interest rates to property investors****, thanks to negative gearing rules that allow interest charges to be claimed back through the tax system.*'

Investment loans are the softest target to hit with increased interest rates.

Negative gearing means the higher interest costs are tax-deductible.

This is from *The Australian* article:

'*UBS analyst Jonathan Mott said a 40-basis-point interest rate rise on investment-property loans would recover the annual cost of the levy for the banks, recouping about $1.56bn a year from investors in extra interest payments.*'

Got that? Raise interest rates on investment loans by 0.4% and the levy is fully funded.

And here's the twist (emphasis mine):

> '*But according to prominent economist Saul Eslake,* ***such interest rate increases would mean about a third to a half of the cost of the bank levy would be borne not by the banks but by taxpayers****, due to the government's generous tax breaks for property investors through negative gearing rules.*'

Here's the circle of stupidity created by Treasurer Morrison's attempted tax grab.

The banks are forced to do the government's dirty work and collect the extra $1.56 billion in revenue by charging investment loans a higher interest rate.

Investors claim the higher loan charges as a tax deduction. Of the $1.56 billion raised by the bank levy, the tax office refunds between $500–700 million back to investors.

Politically brilliant, Scotty. But financially dumb.

Seriously, what hope do we ever have of achieving a budget surplus…let alone addressing our ballooning debt levels?

Our collective selfishness means there is only one outcome to address our spending problem.

The imbalances cannot continue. Something is going to give, and it won't be pleasant.

The market is going to provide the solution to the government's problem.

It'll be brutal. It won't be fair. And the lessons will last for a generation or more.

By the way, a lesson our Treasurer is going to learn is that BSPT actually stood for 'Banks Sidestep Paying Tax'.

Regards,

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Vern Gowdie

Vern Gowdie has been involved in **financial planning** in Australia since 1986. In 1999, *Personal Investor* magazine ranked Vern a Australia's Top 50 financial planners. His previous firm, Gowdie Financial Planning, was recognized in 2004, 2005, 2006 %26 2007, Independent Financial Adviser magazine as one of the top five financial planning firms in Australia. He is a feature editor to *Markets Money* and is Founder and Chairman of the *Gowdie Family Wealth* advisory service and editor of the *Gowdie Letter*To follow Vern's financial world view more closely you can you can subscribe to *Markets and Money* for free here.

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