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FINANCIAL REVIEW

CBA board puts shareholders first

Is the Commonwealth Bank of Australia's appointment of retail banking head Matt Comyn to take over from Ian Narev crazy brave or just plain crazy? It's a legitimate question because CBA, whose real and imagined missteps – particularly around CommInsure, its financial planning business and the AUSTRAC money-laundering breaches – helped create the political conditions for the budget bank tax and the banking royal commission.

Current chief executive Mr Narev is departing because of those problems but the bank has decided not to recruit an external culture-busting CEO, instead promoting an internal protege of his. In doing so, it has clearly decided that continuity, shareholders and employees come first, while perceptions – particularly the sort that feed politicians' behaviour – that the bank has some sort of deeply ingrained culture problem, come second. At one level, putting shareholders first is reassuring. Serious mistakes have occurred, but no systemic wrongdoing has been established and attacks on the bank have been more about advancing the careers of the now former (and disgraced) senator Sam Dastyari and his ilk, than actual poor bank behaviour or systems failures.

And if shareholder returns are the main consideration, continuing a Narev-style regime seems a no-brainer. Under his watch, CBA delivered a full-year profit of $9.9 billion for 2016-17. In a golden era of Australian banking, he made CBA the first among equals, leading the pack on retail consumer satisfaction and technology. But Mr Comyn, who grew CBA's retail banking revenue by 7 per cent in 2016-17, will face a very different immediate task: managing perceptions. He was an executive when a number of the so-called "scandals" that prompted this wholly unnecessary royal commission occurred. That's a key risk in his appointment. In today's febrile populist atmosphere, appointing a CBA insider to the top job could just be grist to the mill of those, like Treasurer Scott Morrison, who reckon that banks can be whacked with impunity because "no one likes you anyway".

Arming our exporters

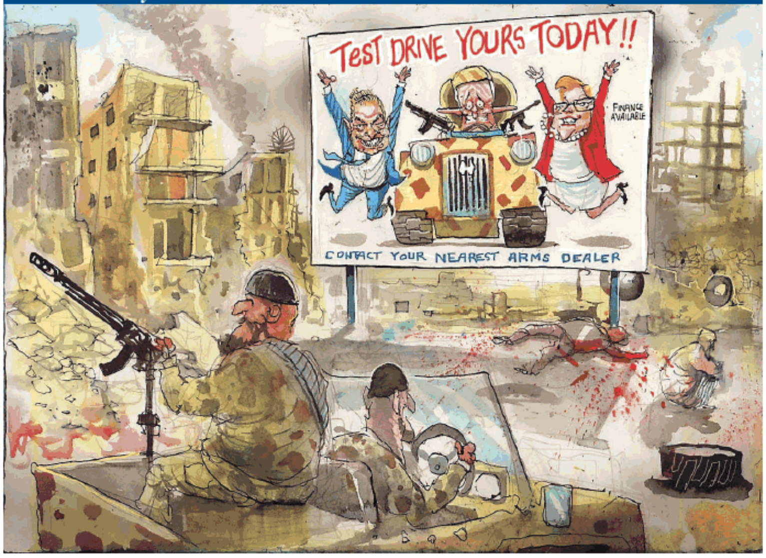
Hard power now counts in our contested region, reflected in the $195 billion that Australian taxpayers are spending over the next decade as we replace submarines, frigates and strike aircraft. Such a build-up must bring opportunity too. Few other national capitals will have hosted as many heavyweight defence sales missions from the US, Europe and Asia in recent times as Canberra: enough perhaps for the government to realise that Australia can lift its own underdone defence export game.

Despite our big purchases overseas, too much of our defence investment has been politically driven by job creation in marginal electorates, building submarines and frigates in South Australia at a massive domestic price premium that robs the Australian Defence Force of other capabilities it might have had. If we make these regrettable decisions, then we must at least make local projects more viable with export sales that will tide them over peaks and troughs in Australian demand, with less need for future taxpayer rescues.

Australia already has niche excellence in radar, electronics, fast warships and armoured vehicles to offer. The new $3.8 billion loan scheme will help in some markets where banks are shy. But local defence companies yearn most for the government-backed clout and diplomatic door-opening that US or British defence contractors take overseas with them. The new defence export office should provide that missing help.

Defence is undergoing a revolution. For the first time in decades, Western armed forces are scrambling to stay ahead of the new fleets and armies of the revived great powers of China and Russia. Integrating ourselves into the supply chains of sophisticated overseas projects that run for decades makes economic and strategic sense. We make desirable, high-tech partners. But we also bring a high cost base, with inflexible labour and expensive electricity. That's a good reason too to tame our inefficiencies.

From the Gallery — David Rowe



Cut corporate tax to cut inequality

Taxation

New evidence shows that company tax cuts benefit low-skilled, young and female workers the most. No one in politics should oppose it.

Richard Holden

One of the big political fights in 2018 is going to be over company tax reform: who actually pays the tax and who benefits from its reduction.

The United States slashed its corporate rate from 35 per cent to 21 per cent on January 1.

Meanwhile, over the past 15 or so years Australia has gone from having one of the lowest company rates in the Organisation for Economic Co-operation and Development to one of the highest.

The government's "enterprise tax plan", which seeks to lower the rate to 25 per cent over a decade has been meet with resistance from the Senate crossbench, and outright hostility from the Labor opposition.

Labor paints the government's plan as a "giveaway to the big end of town", while Treasurer Scott Morrison emphasises international tax competitiveness, and importance of business investment for jobs and wages.

Who's right? As a matter of economic theory either side could be.

While the "statutory incidence" of company taxes is on business, the "economic incidence" is on whoever ultimately ends up paying it, which could be capital, labour, or some combination.

It depends on how relatively mobile capital and labour are. That is an empirical question, and a tricky one to answer well.

When considering a change to tax policy – or any other policy for that matter – we want to know the causal effect of the policy change. That means that simply looking at what tax rates and wages different countries have is not much help – as that simply reveals a correlation that could arise for a host of reasons that have nothing directly to do with company taxes.

It's a bit like observing that children whose mothers eat a lot of fish during pregnancy have better health outcomes and primary school standardised test scores.

It could be because of the in utero health benefits of fish. Or it could be because wealthier mothers tend to eat more fish and children of wealthier people tend to have better health and educational outcomes.

Collective bargaining allows workers to share a portion of the economic pie created by both them and the company: and taxes shrink that pie.

Thankfully, a recent empirical study by three German economists, published in the flagship *American Economic Review*, contains an ingenious way to get at the causal effect of company tax rates on wages.

They utilise the fact that in Germany the company tax rate is determined in part by the federal government and in part by local government. This gave rise to a staggering 17,999 tax changes in 10,001 municipalities between 1993 and 2012.

Just as importantly, the authors were also able to obtain administrative data on wages paid by employers.

So rather than having a survey with dubious reliability, they know what workers at different employers in different municipalities actually got paid.

Finally, because they have had so many local changes over two decades, they are able to factor out general economic trends over time, and other municipality-specific influences, and hone in on wage differences that are directly due to employers facing different tax rates.

The answer is that, on average, workers bear 51 per cent of the total company tax burden. And because of their worker-level data, the authors can speak to which workers are affected the most and hence the distributional consequences of company taxes.

They find that higher company taxes reduce wages most for the low-skilled, women, and younger workers. Overall, this implies that once the hit that workers take from company taxes is factored in, personal income tax systems in countries like Germany and the US are as much as 40 per cent less progressive than one would otherwise have concluded.

These lessons are highly applicable to Australia. The authors are even able to test how different labour market institutions – like collective bargaining at the company and industry level (enterprise bargaining) – affect the nexus between taxes and wages. They find that there are stronger wage effects for firms that collectively bargain – just as theory would predict.

That's because this form of collective bargaining allows workers to share a portion of the economic pie created by both them and the company: and taxes shrink that pie. Australia's enterprise bargaining system fits right in with this.

The striking implications of how high company taxes can undermine the progressivity of the income-tax-transfer system certainly apply to Australia, too.

The best, most credible evidence we have suggests that a cut in the Australian company tax rate is not a gift to the so-called "big end of town". It provides a benefit to businesses and workers in fairly equal measure. And the benefits to workers tend to flow disproportionately to women, young people, and the less skilled.

Cutting the Australian company tax rate from 30 per cent to 25 per cent is not just good for business, and workers. It also helps to redress economic inequality.

Surely this reform is something that deserves across-the-board political support when it comes before Parliament again this year.

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