

# Vested interests are killing our capitalist democracy

by **Ross Garnaut**

Capitalist democracy has fallen upon hard times in the early twenty-first century. The way in which private interests fund political parties and campaigns is part of the cause. Political reform to constrain the influence of money in the political process is important for the health of democracy and the prospects for prosperity in Australia. It is also important for the future prospects of democracy everywhere.

The reform era from 1983 to 2000 gave Australians unprecedented productivity growth in the nineties and then an unprecedented quarter century of unbroken economic growth. That era was built on an understanding that globalisation and productivity-increasing reform raised average incomes, but not necessarily the standards of living of ordinary Australians. All could benefit if and only if carefully directed fiscal interventions accompanied greater reliance on markets for goods, services and capital.

So it was no accident that the period that saw Australia move from high protection to nearly free trade and the top marginal income tax rate fall from 60 to about 50 per cent also saw the introduction and entrenchment of Medicare, a large increase in the proportion of Australians completing high school and entering university, introduction of taxes on capital gains and fringe benefits, assets tests on pensions and substantial social security payments for low-income families with children.

The governments of the reform era – Hawke, Keating and early Howard – were able to appeal successfully for majority support for changes that in themselves damaged some private interests, to advance a broad conception of the public interest.



Ross Garnaut is a Professorial Research Fellow in Economics at the University of Melbourne. *Jesse Marlow*

## A different country

Australia in that era now seems a foreign country.

Two things have changed.

It has become more difficult to maintain broadly based growth in living standards in the 21st century. In the developed countries as a whole, total productivity growth is lower than in earlier periods of modern economic growth.

Planned private investment is consistently lower than planned private savings, dragging down economic growth and employment. While internationalisation of markets for goods, services and capital is raising global economic growth, for the time being it is placing downward pressure on middle and lower incomes in the developed countries.

These challenges of the 21st century make it even more important to secure broad community support for reform in the public interest than it was in the reform era of the late 20th century.

Vested interests have become more effective at shaping policy. The policies that emerge from the democratic process today are more likely to benefit special interests over the broader community than they did in the past.

These changes have caused standards of living of large numbers of people across the democratic developed world to stagnate or fall – including in Australia since a new model of economic growth in China announced the end of the resources boom in 2011.

## An unhappy electorate

Downward pressures on living standards for ordinary people have created grumpy citizens and voters, much less likely to support open trade, productivity-raising reform and prudent restraint on public debt. Donald Trump is merely the most consequential product of the new circumstances.

Policy now has to run the gauntlet of a double veto. Vested interests veto policies that promote the public interest if they challenge their own. And a grumpy electorate finds ways of blocking change that seems to damage living standards for significant numbers of people and dumps governments that do not reverse the decline in the living standards of most citizens.

Discussion of taxation policy in Australia in the six years since the Henry Review illustrates the problem. Ken Henry favoured increased taxation on mineral and land rents and on external environmental costs, alongside reduced corporate income taxes. He thought he had defined a set of policy changes that improved efficiency while increasing the standards of living of most Australians.

After various false starts, the debate on tax reform has excluded from the Henry recommendations those changes that impose costs on corporate interests and kept in play those that distribute income towards corporate interests.

Distortions from the influence of money in politics is as evident in Australia as in other developed democracies. While campaign funding is only one of several avenues to subversion of political processes in contemporary democracy, reform of political donations is a necessary condition for re-establishing policy-making in the public interest.

## Palmer's power

In the Commonwealth Parliament that has just been dissolved, considerable influence was exercised for a while by a new political group, the Palmer United Party. The group's meteoric rise was assisted by large campaign spending, [financed by donations from a company associated with the group's leader](#). With the company facing severe financial problems a couple of years later, the leader justified donations to political campaigns as highly profitable investments.

They had secured the numbers in the Senate without which carbon pricing would still be operating today. Carbon pricing, if it had continued, the leader said, would have cost much more than the campaign that led to the Palmer United Party having the balance of power in the Senate on repeal of carbon pricing.

Such explicit linking of campaign donations to parliamentary votes is illegal in other developed country democracies and would once have been morally obnoxious in Australia.

That is simply the most egregious of many campaign financing distortions of the 21st century policy-making process. The distortions have affected both sides of the partisan political divide. They have involved trade union as well as corporate donations.

I discussed and provided recent examples of the increasing role of vested interests in the policy process in my book *Dog Days: Australia After the Boom*. Former Prime Minister Malcolm Fraser raised these comments from *Dog Days* with me in my last long conversation with him, not long before his death last year.

Fraser noted the contrast between political fundraising practices today with those when he was active in politics. When he was a young member for the Victorian federal seat of Wannon, his campaigns were well furnished financially by a local committee of the Liberal Party. Under rules established by Liberal Party founder Robert Menzies, Fraser was not allowed to know the identity of donors. Today, he noted, people seeking to discuss policy with ministers are expected to pay a large sum for a seat or a table at a dinner or to contribute in some other way to a fundraising event.

## Some good news

Two recent developments have improved the outlook for Australian reform of campaign funding.

One is the Premier of New South Wales' support for far-reaching reform after coming to power in circumstances which give him unusual authority on these matters. His early personal support for strict limits on donations and for timely disclosure and his commissioning of the Schott Report laid the foundations for a concerted national effort to clean up the Australian problem of money in politics.

The second is the positive electoral response that has accompanied recent decisions of the federal opposition to hold its ground on policies that have confronted some interests that can be expected to respond with campaign finance retribution – for example, in relation to negative gearing.

My own view is that solution of the problem would ultimately require donations to political campaigns to come only from individual citizens and be subject to a moderate limit. For the time being, the Schott report's careful and cautious recommendations on expenditure limits (including for third-party campaigns) and immediate disclosure are a good immediate objective for national and not only NSW legislation and regulation. The recent problems in NSW underline the importance of embedding good state practice within a national regime.

The capacity for the combination of political democracy with market exchange of goods, services and capital to deliver rising living standards for most people was decisive in the victory over authoritarian central planning during the Cold War. Without reform, we are not in such good shape for the different and more challenging contests over political systems that lie ahead.

*Ross Garnaut is a Professorial Research Fellow in Economics at the University of Melbourne*