



“What’s so wrong with GST-free fruit and veg?”
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At the last election National stood by its 2010 tax reform that raised the rate of GST but refused to give exemptions for fresh fruit and vegetables, or indeed anything else. If you supported exemptions for fresh fruit and vegetables you needed to vote Labour.

Now, even the Labour party has ditched the policy and proposes to keep GST pretty much as it is now. So, does anyone in Parliament now represent poorer consumers who spend proportionately more on fruit, veg and other foods than richer voters? And if it is such a bad idea to exempt foodstuffs from GST why do so many other countries do it?

At first sight, GST exemptions might seem like a good idea. After all, eating more fruit and vegetables is alleged to have all sorts of health benefits – everything from improved sperm count to fighting cancers, if you believe the latest research. Poorer people also tend to spend proportionately more of their income on food, but generally have worse health outcomes.

So, engineering a shift in their diets towards more fruit and veg by making them cheaper could have a double bonus – those on lower incomes are better off and healthier.

Now, I don’t know whether eating more fruit and veg would improve most people’s health. But, as far as helping to raise the real purchasing power of lower income consumers is concerned, exempting fruit and veg from GST is a bad idea.

In short, if you want to help the poor, there are better, more targeted, ways of doing it that don’t have the unintended side-effects that GST exemptions have.

I don’t know of any countries that specifically exempt fruit and vegetables from their GST regimes (usually called VAT – value added tax – in other countries). Denmark recently experimented with something similar – a higher tax rate on some fatty food. It has just abandoned it.

But many countries exempt foodstuffs more generally, motivated mainly by the fact that the exemptions help to bring some progressivity to the GST, making it more like income tax. Effectively the government takes a bigger tax slice from a high income person’s weekly shopping basket than from a low income person’s basket.

The trouble is, if you earn ten times as much as me, you will spend a lot more money on food, including fruit and veg, than me, even if this represents a smaller share of your income than mine. So exempting food from GST means big spenders get a big tax break.

And it’s not just that richer consumers buy more food. They also tend to spend on higher quality, more expensive, food items. But it’s not really possible to tax ‘high quality’ foods and exempt ‘low quality’ foods. Start by trying to define the ‘quality’ of a chicken breast, say, and then think of the message that “making low quality food cheaper” gives!





Richer consumers also tend to live in wealthier suburbs where prices in their local food stores are probably higher than those in poor neighbourhoods. So, all in all, rich people pay a lot of GST on their food.

But there is a more important reason not to exempt food - or any sub-group like fruit and veg – from GST. The lost revenue from exempting food from GST has to be raised from somewhere else. If the objective of the exemption is to help those on lower incomes then the obvious choice is to raise the lost revenue by raising the higher rates of income tax.

Then high income, not low income, earners would pay all of the extra tax (because they'd face a higher tax rate on all their income above a tax threshold). This is why income tax is sometimes called 'direct' tax – it targets income directly, whereas GST targets it 'indirectly' depending on how you spend it.

But there's the rub! If we can use income tax to target tax more efficiently towards high income earners why would we want to use a GST exemption when it clearly doesn't target high earners as well?

Generally, rather than lose revenue from a GST food exemption which doesn't target the poor, it would be better to raise the same revenue from an income tax (even if it was levied on everyone) and channel the extra income tax revenue to the poor. We have plenty of mechanisms to do that – like family income tax credits.

So next time a political party proposes GST exemptions, think of 'horses for courses'. GST is an efficient revenue-raiser but not very good at redistribution. Income tax and credits are less good at revenue-raising but much better at redistribution. So we shouldn't try to do everything with each tax. They can be tailored to fit.

And by the way – the Danish fat tax 'surcharge' didn't work either – for many Danes, getting their daily intake of burgers cheaper across the border in Germany, proved too tempting!

