

Medium Term Priorities in Tax Reform

Greg Smith

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Vision: tax agenda in the long term

Driver	Implication
Economic – factor mobility	Rent, consumption favoured over income bases
Economic – growth imperative	Reduce company tax rates – but note global focus on fiscal imbalances
Economic – two speed economy (structural pressure from Asia)	Infrastructure Productive and competitive cities
Demographic (age and late age)	Longevity, aged care and disability Participation policies
Technological (digital age)	New tax-transfer delivery models
Environmental/energy	Replacement of fossil fuels (ultimately cease as a tax base)

The Henry vision - long term

- Concentrate on four broad, efficient tax bases
 - Personal Income
 - Business Income
 - Consumption
 - Immobile rents (land and natural resources)
- Abolish other revenue taxes (mainly state taxes)
- Rebalance: less business income, more rent and consumption
- Comprehensive personal income tax/transfer reform
 - Simplified structure with new delivery platform
 - Complementary means tests and other transfer design
 - 40 percent discount on savings
- Efficient Pigovian taxes and user charges
- Retirement income reforms reconfigured to address longevity, aged care and disability/carer needs

Short term: 2010-2011 measures

Measures announced	Henry Recommendation
29% company tax rate	25% company tax rate
22.5/40% narrow-base MRRT/PRRT	40% broad-base brown tax
Uplift infrastructure c/f losses	Universal one year loss carry back
Remove IWT from financial sector	Remove IWT from financial sector
50% interest exclusion to \$1000	Uncapped 40% discount on savings
Standard WRE deduction	Standard WRE deduction
25% increase in tobacco excise	Increase and index excise
12 percent super guarantee	9% SG with major design reform
Remove spouse offset	Comprehensive structural reform
Small business concessions	Concessions to \$5m turnover
FBT standard car value	Car value, and wider FBT reform
Charities Commission	Charities Commission

Medium term constraints

Current Specific Issues

- Fiscal - very limited room through mid-decade
- Economic uncertainty and expectations
 - terms of trade uncertainty
 - Household disposable income expectations
- Informational - institutional
 - Inadequate knowledge and institutions in areas such as cities, roads and housing

Perennial constraints

- Time horizon problem – short run costs for long run return
 - Weak impulse for reform
- Australia's deep federal entanglement
- The myth of smaller government (tax cut dreams)

The strategic imperative: combining stronger growth, participation and equity

❑ Some steps in the 2011 Budget

❑ Infrastructure, training, minor tax-transfer reform

❑ 3 critical strategic directions to 2020

• Productivity policy goal: 2% pa

tax, skills and infrastructure

• Social policy reform

Unmet needs and participation

• Cities – land use and transport reforms

Almost nothing yet

A two-part strategy

- Some time after the tax forum, announce a strategic direction for the tax and transfer system
- In addition, commit to an ongoing supportive strategy for community engagement in a future reform agenda

Part One: the medium term strategy

- Schedule cuts to company tax to 25% by 2020
 - For natural resource companies, apply an offsetting higher resource tax
- Abolish specific insurance taxes
- Develop personal tax and transfers reforms based on simplification, transparency and participation
- Replace, or divert, the SG increase to longevity and aged care (and disability insurance) needs

Carbon pricing and tax

- Carbon pricing should be seen as an opportunity for productivity reform
 - Other measures that typically encourage low efficiency investments should be phased out
- To the extent that producers generate immobile economic rents, there is no need for industry assistance (carbon tax acts as a rent tax)
- There is scope to reduce existing tax expenditures that harm the environment

Part two: investing in future reform

- Instead of just promising solutions, government should invest more in promoting others to define situations, challenges and options
- This investment involves a different type of politics:
 - Allowing more community discussion on issues before decision-taking
 - Facilitating more realistic community expectations
 - Opening government data and information bases
 - Starting a more comprehensive reconsideration of the federation
- For tax: after the coming tax forum we should hope for
 - An open approach to tax and other analytical reform information
 - The open development of optional tax reform pathways for Australia
 - Reform with no change to consumption tax
 - Reform with consumption only to the extent needed to replace other inefficient narrow taxes
 - Unconstrained reform – architecture for growth