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A productivity agenda for Australia: Submission to the Economic Reform Roundtable

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Summary

We welcome the opportunity to provide input to the federal government's Economic Reform Roundtable.

The government has rightly identified that improving productivity, building economic resilience, and strengthening budget sustainability will be critical to Australia's long-term prosperity.

Productivity growth is the key to raising our living standards in the long term. While the federal government doesn't hold all the levers, it can strengthen the foundations: a competitive economy, a well-functioning labour market, the conditions for people to flourish (housing, health, education, and social cohesion), and the right infrastructure, tax, and regulatory settings.

Grattan Institute has published research on all these topics and more, and its current suite of recommendations for the federal government is consolidated in the **attached** report, *Orange Book 2025: Policy priorities for the federal government*.

This submission aims to focus attention on three major economic reform opportunities where this roundtable could make substantive progress:

1. **Tax reform** to improve the efficiency of Australia's tax system and strengthen budget sustainability.
2. **Reducing barriers to work** to ease workforce pressures and maximise our talent pool.
3. **Better infrastructure, including more housing,** to meet our urgent housing needs, support the economic transformation to net-zero, and better target public spending.

The *Orange Book 2025* identifies and prioritises a wide range of policy reforms to boost economic growth, tackle the structural budget problem, improve health and education, make housing more affordable, reduce emissions, more sustainably meet the needs of an ageing population, and strengthen our political institutions.

1 Opportunity 1: Tax reform

Improving the efficiency of the tax system, by shifting Australia's tax mix from more-costly to less-costly taxes, could materially boost Australians' living standards.

More revenue will also be needed to manage the budgetary costs of rising community expectations and an ageing population, especially if economic growth remains lower for longer. Our tax burden is currently low by OECD standards.[1]

Meaningful tax reform is never easy, precisely because it affects many, if not most Australians. This is the 'grand bargain': we contribute as we are able, benefit from broad-based investment in health, education, research, infrastructure, and other services, and receive safety nets when we need them.

The following sections identify some of the best opportunities to reform Australia's tax system.

1.1 Support states to replace stamp duties with general property taxes

The biggest tax reform prize in Australia would be to replace state stamp duties with general property taxes.

Stamp duties are inefficient taxes: they discourage people from moving to housing that better suits their needs, and distort people's choices about where they live and work.

The federal government should encourage the states and territories to make this tax switch. The principle of federal financial support for state-level reform is well-established. Under the National Competition Policy reforms that started in the mid-1990s, the federal government paid the states nearly $6 billion over 10 years in exchange for much-needed regulatory and competition reform.

1.2 Reduce income tax breaks

There are many concessions and minimisation opportunities in Australia's personal income tax system. Curbing these 'leakages' would broaden the income tax base and, over time, reduce governments' temptation to rely on bracket creep to do the 'heavy lifting' on budget repair.

Broadening the income tax base offers a major opportunity for structural reform, would reduce distortion of economic behaviour, and has the potential to raise more than $20 billion a year.

In particular, superannuation tax concessions go far beyond their intended purpose and should be tightened. The government is

[1] Based on 2022 data and including state taxes, Australia is the ninth-lowest country in the OECD for tax collection relative to our economy's size, with tax revenue at 29.4 per cent of GDP compared with the OECD average of 34 per cent: OECD (2024a). Australia's taxes on individuals are also lower than the OECD average, even if you count compulsory superannuation contributions: Wood and Chan (2023).

pursuing reforms to tax earnings on very large super balances. But these reforms don't go far enough.

Further opportunities include taxing all superannuation earnings in retirement at 15 per cent (saving more than $5.3 billion a year),[2] and lowering the cap on pre-tax super contributions from $30,000 a year to $20,000 a year (saving about $1.6 billion a year). More options to curb superannuation tax breaks are detailed in Chapter 9 of the attached Grattan Institute report, *Orange Book 2025: Policy priorities for the federal government.*

Beyond super, substantive options include reducing the Capital Gains Tax (CGT) discount from 50 per cent to 25 per cent, winding back negative gearing, and setting a minimum 30 per cent tax on all trust distributions.[3]

The CGT discount and Australia's unusual negative gearing arrangements distort investment decisions, increase price volatility in property markets, and marginally increase house prices. They provide limited benefit in terms of increasing the rate of new housing development.

1.3 Broaden and/or raise the GST

Australia collects less in consumption taxes than similar countries, and our GST tax base is narrow by international standards. The GST base is also being eroded over time as a growing share of consumer spending goes on GST-free items.[4]

Increasing collections from the GST by broadening the base and/or raising the rate would diversify Australia's tax base. Raising more tax through the GST would also make Australia's tax system more efficient, because the GST creates less distortion in incentives to save and invest. It is a hard tax to avoid, and it acts as a lump-sum tax on accumulated wealth by collecting from households such as well-off retirees who are living off savings and otherwise pay little tax.

But because it is a flat tax, it hits low-income-low-wealth households hardest, since they spend a larger share of their income on essentials. Some of the income from raising and/or broadening the GST would need to be used to cushion the impact on vulnerable households.

GST reform has been politically challenging because the revenue is passed through to the states and territories, but the federal government wears the political costs of reform and would foot the bill to cushion the impact on vulnerable households.

But the states have limited options to raise revenue efficiently themselves, and face increasing spending pressures, particularly in health and education.

Extra revenue from GST reform could be shared between the federal government and the states and territories to bring everyone to the table.

[2] That would mean retirees would then pay some tax on their superannuation savings – as working people already do – but a tax rate of 15 per cent is still much less than younger workers pay on their wages.
[3] See Wood et al (2023).

[4] NSW Treasury (2021) estimated that by 2029-30 the share of consumption subject to GST would decline to about 50 per cent, down from more than 60 per cent when the GST was introduced in the year 2000.

There are two ways to increase GST revenue. The first is to raise the rate. In 2015, Grattan Institute analysis showed that a 15 per cent GST with a compensation package that on average compensated the bottom 40 per cent of households could raise about $11 billion after compensation.[5] If federal and state governments shared the extra revenue 50:50, this would raise about $6 billion (in today's dollars) for the federal budget.

The second way is to broaden the GST base by removing some of the concessions that currently apply. Growth in exempt items, including private healthcare and education spending, as a share of household consumption, have contributed to the erosion of the GST base over time. Including these areas would help GST revenue keep pace with economic growth.

1.4 Redesign resource rent taxation

Australia is a major producer and exporter of fossil fuels, yet despite the extraordinary profitability of fossil fuel extractors, government revenues from fossil fuels are relatively small. Giving Australians a greater share of resource rents offers much less economic downside than increasing other taxes on business.

The government should consider a resource rent tax on non-renewable resources such as coal and iron ore.[6] The government should also consider including critical minerals such as lithium, cobalt, and rare earths in any future resource rent tax, because these minerals will be in strong demand in coming years to meet the demands of a net-zero global economy.

The Petroleum Resource Rent Tax (PRRT) should be redesigned to raise more revenue and support the energy transition. There have been several reviews of the PRRT that have led to some changes, but the government should revisit options for a more fundamental redesign.

1.5 Other options to consider

There are a range of other tax reforms the federal government could consider, including:

- Reform of household savings taxation. A more consistent treatment of household savings would encourage households to seek the best pre-tax return on their savings, and to invest their savings in assets that best suit their circumstances and risk-preferences.[7]
- Wholesale reform of Australia's corporate tax system to boost business investment. Options include a destination-based cashflow tax or an allowance for corporate equity.[8]
- Inheritance taxes have substantial economic merit because they are less distorting than most other taxes (including income taxes).[9] Taxes on inheritances are deeply unpopular though, so it will be necessary to identify the right model, and bring the Australian people along. At the very least, we should stop subsidising inheritances. This means ending rules that feed the size of bequests at the expense of taxpayers,

[5] Daley and Wood (2015).
[6] Henry et al (2009, pp. 47-48) recommended a uniform resource rent tax set at 40 per cent, administered by the federal government, with the allocation of revenue and risks negotiated between the federal and state governments.
[7] Henry et al (2009, p. 62). See also Varela et al (2020).
[8] Garnaut et al (2020).
[9] Henry et al (2009, pp. 137-140).

including overly generous tax treatment of the family home and overly generous superannuation tax breaks.

1.6 A 'package' might be needed

A tax reform 'package' might be needed to share the costs more broadly and to raise enough revenue to be able to compensate those who can least afford it.

For example, a tax reform package to improve work incentives could include broadening the tax base through reducing income tax breaks, and more consistent taxation of savings, to support a lowering of headline income tax rates,[10] and/or to fund additional investment in childcare to improve work incentives for the group most responsive to tax and welfare changes.[11] Reforms to family payments could proceed alongside this package. This sort of package would be entirely within the power of the federal government.

A different option to help repair both federal and state budgets would be a GST Grand Bargain involving the Commonwealth and the states and territories: broadening and raising the GST, with income tax and welfare changes to compensate the most vulnerable households, while also resetting the formula for GST distributions to reflect the original equalisation principles.

History shows that reform packages can work well. In 1985, reforms that broadened the income tax base were bundled with income tax rate cuts and measures to reduce tax avoidance – a coherent story to sell to the public. And in 1999, the removal of narrow and inefficient – but lucrative – state taxes, and widely variable wholesale sales taxes, made sense in the context of the broader GST deal shoring up state budgets.[12]

But we cannot splash money around to ensure there are 'no losers' from tax changes: the current fiscal environment does not allow it, and given demographic, environmental, and geopolitical trends, the fiscal environment looks even more challenging ahead.

Rather, the government, along with experts, peak bodies, and the media, will need to be upfront with the Australian people about the tough collective choices we need to make to sustain our quality of life amid a changing world and an ageing Australia.

[10] High 'effective marginal tax rates' (EMTRs) are not the norm, but Australia's tax and transfer system does generate high EMTRs for about 9 per cent of the working-age population: Phillips (2024).

[11] There is a broad consensus in the literature that women with children are the group most likely to change their working hours in response to tax and welfare changes: see Wood et al (2020) for a summary. Phillips (2024) shows that even after the recent Child Care Subsidy increases, a quarter of working-age women who use childcare still face high or very high EMTRs (greater than 60 per cent).

[12] Wood (2023).

2 Opportunity 2: Reduce barriers to work

A well-functioning labour market enables the growth that comes with making full use of the talents of all Australians.

With a tight labour market, and with labour market tightness expected to persist,[13] reducing barriers to work should be a priority. The main opportunities to increase workforce engagement are for women with young children, older workers, and migrants.

It is not just participation in the workforce that matters, but also that people can work the hours they need and want, that there is efficient matching between jobs, education, and skills, that people can move to higher-paid jobs over time, and that workers are able to adapt to the needs of a changing economy.

2.1 Childcare reforms remain critical

Australia's tax and transfer system features steep taper rates, which help to deliver benefits more efficiently, but can also create significant barriers to paid work, particularly for women with children.[14]

Federal and state governments have made important progress in recent years on reducing barriers to work for parents with young children. Improvements to childcare and parental leave policies, and agreement across jurisdictions on universal access to public pre-school, all help make it easier for parents to choose to work or work more if they want.

But there is more to be done. In 2024, nearly 300,000 parents reported that childcare-related issues such as cost or lack of availability affected their ability to work and their decisions about how much to work. Almost all these parents (93 per cent) are mothers.

Even after the recent Child Care Subsidy increases, a quarter of working-age women who use childcare still face high or very high 'effective marginal tax rates' (greater than 60 per cent).[15]

Older women are also less likely to work than men of the same age.[16] Many older women care for children (21 per cent of women in their 60s),[17] probably grandchildren, but their lower workforce engagement may also be a carry-over effect from having had children earlier in life.

Ensuring high-quality childcare is broadly available and affordable will reduce barriers to work for parents and older carers too,

[13] The OECD expects labour market tightness to persist across most advanced economies due to shortages of high-skill workers, an ageing population, and a cyclically strong labour market: OECD (2024b).
[14] There is a broad consensus in the literature that women with children are the group most likely to change their working hours in response to tax and welfare changes.
[15] Phillips (2024). Effective marginal tax rates (EMTRs) are the proportion of additional income lost to taxes, reduced welfare payments, additional childcare costs, and HELP repayments. When EMTRs are high, there is less incentive to work.
[16] About 46 per cent of women aged 55-59 are engaged in work or education, compared to 68 per cent of men the same age. And this drops to just 27 per cent of women aged 60-64, compared to 50 per cent of men aged 60-64: ABS (2024).
[17] Compared to 13 per cent of men in their 60s: ABS (2021).

helping to boost our talent pool. Federal and state governments should be taking a more active market stewardship role, and working together to test alternative funding models (including flat fee models, tendering, and direct provision) to ensure quality and value for money.

Governments can further support older-worker engagement through supporting healthier ageing and flexible work. Preventing chronic disease, and better supporting GPs to manage chronic disease, will be critical to healthier ageing.[18]

2.2 Support flexibility in the labour market

A flexible labour market helps more Australians enter and stay in the workforce, and enables them to find work that better suits their needs and circumstances.

Flexible, hybrid, and remote work are particularly important to reducing barriers to work for people with caring responsibilities, people with disability, and older Australians. Hybrid working can lift participation among under-represented groups, increase happiness, and doesn't appear to weigh on productivity.

The federal government should pursue reforms to enable people to more easily move to jobs that better suit their skills and needs. It should:

- Enable workers and employers to negotiate more flexible workplace conditions. In particular, the government should not try to limit remote working that enables hybrid work practices.
- Ensure non-compete clauses do not unnecessarily restrict job switching, particularly for low-wage workers.
- Support states to replace stamp duty with a broad-based land tax and change planning laws and processes to allow higher-density housing in inner-urban areas and established suburbs.[19]
- Improve transport project selection to make it easier for workers to move around our cities,[20] and pursue other reforms to enable more efficient use of our existing infrastructure.[21]

2.3 Improve skilled migration

Skilled migration delivers huge economic benefits for Australia, and there is room to boost these benefits. The current program is slow, expensive, and doesn't always select the most-skilled candidates. Many migrants face barriers in Australia to maximising their potential and/or reside here with long delays or no prospect of gaining permanent residency.

The federal government can deepen Australia's talent pool and reduce barriers to work for skilled migrants by:

[18] Six in 10 Australians now have a chronic disease (such as cardiovascular disease, diabetes, or dementia), and many chronic diseases can be prevented through better diets, more physical activity, fewer drugs, less alcohol, and more social connection. Australia's investment in prevention is poor by international standards and there are many opportunities to do it better. See Chapter 6 of the attached Grattan Institute report, *Orange Book 2025: Policy priorities for the federal government*.

[19] See Chapter 5 of the attached Grattan Institute report, *Orange Book 2025: Policy priorities for the federal government*.

[20] Terrill and Bradshaw (2024).

[21] Wood et al (2022).

- Reforming the points test by allocating visas to migrants who are likely to make the biggest economic contribution to Australia.

- Abolishing state and regional points-test visas and expanding the number of skilled independent visas granted each year.

- Making permanent employer-sponsored visas available for workers in all occupations, provided the job pays at least $90,000 a year, and temporary employer-sponsored visas to all those earning at least $76,500 per year.

- Investing more in attracting skilled migrants to Australia and supporting them when they arrive.

The current skills recognition process also needs reform. Under the current system, many skilled migrants have to complete a skills assessment, and then separately meet ‘occupational licensing’ requirements (professional standards to be able to practice in their profession). For some skilled migrants, it can take months or years before they can work in their field of study. This slow process is a major contributor to many migrants working in jobs below their skill level.

Occupational licensing requirements also affect Australian workers. Some workers need to be registered and/or hold a licence in the state or territory where they wish to work, which can impede the movement of skilled workers across Australia. Occupational licensing is more stringent in Australia than in the best-performing OECD countries.

The government should commission a review to recommend ways to streamline the skills recognition process for skilled migration. The federal government should also work with state and territory governments to streamline occupational licensing; this could be done as part of the National Competition Policy reforms.

Further detail on these reforms is provided in Chapter 2 of the attached Grattan Institute report, *Orange Book 2025: Policy priorities for the federal government*.

3 Opportunity 3: Better infrastructure, including more housing

Given the infrastructure requirements for the net-zero transition, the construction requirements to meet our housing needs, and the substantial build up in the public infrastructure pipeline, governments need to carefully prioritise on major infrastructure projects. This is critical both in terms of ensuring the highest-value use of public spending, and ensuring capacity in the economy is not over-crowded, escalating cost and making delivery harder.

3.1 Get the major projects right

Governments need better upfront assessments of Australia's transport infrastructure and defence capability needs, to strengthen discipline in decision-making and improve procurement processes.

Premature, often politically motivated decisions have proved very costly, especially as 'megaprojects' have become more common. Bigger projects carry much bigger risks, and evolving scope is common.[22] Weak assessment of costs means these contingencies are not properly built in and planned for – and are exacerbated by poor processes and decisions along the way.[23]

Governments need to do more rigorous cost-benefit analysis, use more appropriate discount rates, and should get better at coordinating projects[24] (including being open to mothballing projects and pausing new ones in an overheated market). Buying smaller, more regularly, and 'off-the-shelf' reduces risks and cost.[25]

3.2 Sharpen states' incentives to boost housing supply

Australia has among the least housing per person of any OECD country, and is one of only four OECD countries where the amount of housing per person went backwards over the past two decades. The federal government has committed to building 1.2 million homes over the next five years – an important but ambitious target that will be challenging to meet.

To help get more housing built, the federal government should sharpen states' incentives, including by:

- Adjusting the baseline housing targets for states at which the New Homes Bonus becomes payable, to better align them with cyclical housing conditions.[26]

- Bringing forward the New Homes Bonus to be paid in instalments rather than at the end of the five-year period.[27]

The federal government should also extend its new National Competition Policy to cover reforms to residential land-use planning rules, such as setting minimum national standards for residential zones to allow more townhouse and duplex developments, reforming the process for new heritage listings and

[22] Terrill et al (2020 and 2021); Terrill (2016).
[23] Terrill et al (2021).
[24] Wood et al (2022).
[25] Wood et al (2023).

[26] For example, the targets could be adjusted each year in line with factors known to affect housing starts, such as changes in interest rates and house prices.
[27] Subject to progress towards meeting the recalibrated baseline.

overlays, and limiting third-party appeal rights to block residential construction.

Further detail on priority housing reforms is provided in Chapter 5 of the attached Grattan Institute report, *Orange Book 2025: Policy priorities for the federal government*.

3.3 Deliver a consolidated Net Zero Plan to guide the net-zero transition

All governments need to plan more directly for the physical and economic consequences of a changing climate, and to integrate climate change issues into all decisions on infrastructure planning, land use, and resource extraction. This will require greater policy coordination across jurisdictions.

Emissions-reduction targets play an important role in guiding the transition and providing a predictable environment for investors and consumers. The federal government should maintain the 2030 target, and set the 2035 target as a range of 65 per cent to 75 per cent below the 2005 level.[28] The federal government will then need to work with the states and territories, which have their own targets, to develop and implement workable policies to meet the national target.

The federal government is developing plans intended to provide a policy framework to reduce emissions in every sector towards the net-zero goal. These plans should be consolidated into a national Net Zero Plan, and the government must signal that every sector has to reduce emissions from current assets and activities. In particular, action is required in agriculture, industry emissions outside the Safeguard Mechanism, and transport beyond light vehicles.

The Plan should also lay out a framework such that decisions on future assets and activities are made with net zero in mind. This includes government decisions (for example on infrastructure); and private sector and household decisions, from opening new mines to building new housing or buying a new car. In this way, the costs of achieving net zero will be efficiently distributed, and the national target can be achieved.

Further detail on priority reforms for the net-zero transition is provided in Chapter 3 of the attached Grattan Institute report, *Orange Book 2025: Policy priorities for the federal government*.

[28] Climate science tells us that 65 per cent is the minimum target that Australia should adopt if we are to contribute to the objective of limiting the global temperature rise to 1.5°C above pre-industrial levels. The risks to Australia from unmitigated climate change are very bad and the opportunities in a net-zero world are very good. Australia is a small, open economy and should make the 75 per cent target conditional on similar commitments and actions by our biggest trading partners.

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