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Thanks very much. It's an honor to be here. Thank you so much for the invitation. I know the Assistant Treasurer is in the Expenditure Review Committee. It does make you wonder whether perhaps they're also reviewing revenue in as we speak in this in this committee sorry, in this very important summit. So thanks to the Australia Institute for having me and of course I'd also like to acknowledge the traditional owners of the land on which we're meeting today, the Ngunnawal people and pay my respects to elders.

So Richard Denniss invited me to speak because, you know, he saw the months before the budget. Someone should say something about the stage three tax cuts. And I said, well, I think it's been done, hasn't it? It's. Is that really what you want me to talk about? So let's turn our attention to the UK in a talk about taxes, work and care.

It's rather hard to go past the events of the last few days in the UK and clearly we do still look to that nation. In some respects I've just come back from a trip to in fact I landed at Heathrow the night the Queen died, and there were there were signs in black all around the airport that night.

It was a dark and stormy nights. There was a disturbance in the force and we're still feeling it. So the UK tax cut Flip-Flop thing that we saw this last few days, you know, it's fascinating watching UK politics, isn't it? It's like they just put it all out there on display and we can just watch and learn and supranational in domestic, local.

So the proposal to flatten that top tax rate abandoned, you know, initiated and then then immediately abandoned by politicians listening, I think, to their constituents as well as to economic advisers, because even the Tories could not stomach it was rather extraordinary to watch. So the UK tax rate structure, without telling you the details of the thresholds, runs from 0%, 20%, 40%, 45%.

The 45% rate kicks in at £150,000, which you know, used to be about half 1,000,000 AUD, but is is now about 260,000 AUD. The zero bracket, interestingly, given a Labor spend, has come in, the zero bracket is income tested in the UK. If you earn over £125,000 in the UK, you do not get the zero bracket. So that's an interesting thing.

So they maintain a progressive rate structure that is rather similar to ours. So the debate in the UK, it's important to note that that cut in the top tax rate was only about 2 billion of revenue in that year out of a massive tax cut package that the Tories have taken to to the Parliament, their £45 billion in total in a total fiscal expansion package of about £100 billion.

So, you know, that includes a whole range of subsidies and also cuts to lower tax rates. And another flip flop, the last year they raised the National Insurance Contribution, which is their Social Security tax, and they were going to drop it again. So the point of telling you this, I guess, is that the story about the top rate cut in the UK that we've just seen play out is not really or is only partly about revenue.

And it's only partly about the deficit. What it really is about is about fairness, both perceptions of fairness and the reality of who bears the tax burden. And I think that associated with that, it's also about the long term sustainability of the the income tax in that political and economic context. And it was clearly going to be unsustainable to change that top rate.

Meanwhile, in Australia we have had the opposite of weekly flip flopping of policy. We have a tax cut legislated more than two parliaments ago to take effect in two years time in completely different economic and fiscal conditions legislated before the pandemic, legislated before the massive growth in government debt and of course, geopolitical crisis and the lack of resilience.

And Rod Sims did talk about the resilience of our economic structure. His and also I would assert the resilience of our fiscal systems is something we need to be very aware of. So I've said from the beginning, I'm opposed to that. I'm not going to keep going on that. I'm just going to put that again on the record.

The particular element of the stage three tax cut, though that concerns me most, is the removal of the 37% rate, the dropping of 32.5% to 30%. Well, that sounds a little bit like some kind of fetishizing of round numbers, you know, that we feel happier if it's 30 than saying 32.5. It's kind of a bit of a mouthful.

We have to remember that previously really only a decade ago we had a 49% rate, a 42% rate, a sort of mid-thirties rate, a 21% rate. So we have had a decade of lowering of those marginal rates. I wouldn't be so concerned about that 30% change, but I would like to see it combined with base broadening in the income tax and ensuring, for example, that people who have access to income splitting through trusts are not doing that with adult children, then taking advantage of that 30% and lower tax rates in the progressive rate structure.

I think there are some other things the Government could be paying attention to, but I do think it's really critical that we do not remove that middle right, that 37% rate. I think we heard from the senator earlier today that there is a real risk that if we do that, we tip over into a permanently flatter income tax rate structure that we cannot recover in a time when we actually have concentrations of income and wealth inequality.

So let me leave leave it there. I'll come back to a couple of aspects in a minute. So if we take a step back from the kind of immediacy, you know, of the the fascination of the rate debate and have a think about why the income tax is important and also why taxing work is important. So why do we need to protect that income tax and value it?

Because it taxes income from all sources. It should be taxing that reasonably equally no matter where we're deriving our income. But nonetheless, we have to acknowledge that the lion's share of the income tax is raised from workers, that it's raised from people who are earning wages, whether relatively low or relatively high. Everyone in the wage earning system is paying some income tax, and that's actually a really critical element of its success.

So government in the 20th century succeeded in raising sufficient revenues to finance the welfare state and secure economic welfare and public goods. And taxing work was crucial to that fiscal bargain. What that depends on, though, and we've heard quite a bit about it today, is it depends on the return to work wages being adequate, reliable, secure and growing.

Right. So it returns. The tax system we had already depends on having an adequate and more than adequate return to labor. And so the more fundamental problem in the economy is that we have seen a shift in a greater return to capital, return to profit and lower return to labor, and that undermines the resilience of our income tax base.

Taxing capital is more difficult than taxing labor. Capital is more mobile than labor. We would all like to be taxing somebody else. Robots, multinational enterprises. We certainly should do that as well. I'm not saying we don't do that, but we do have to remember that we need to protect the labor income tax base. And just thinking more broadly about, you know, well, well, what has the tax system ever done for us?

So people forget that Adam Smith, of course, advocate of the free market and the invisible hand, was also a supporter of taxation. In fact, he saw taxation as the only way to finance government in a market economy. Other revenues and debt are useful, but I'm not going to do the bulk of the work. So a good tax reform is to increase wages, and that's the first point.

Rather than fiddling with the right structure, effective taxation of work was actually impossible before the existence of a mass labor market paying adequate wages and before the existence of pay as you go withholding it actually depends on a bargain with employers, with business, right? As well as with individuals after World War Two, which is when pay as you go withholding was introduced in Australia, those higher tax collections were repurposed.

We didn't reduce the revenue much. Taxes and social spending stayed high under conservative governments. The top marginal tax rate for 20 years under Menzies and others was 66%. Now the demographics very, very different. So let me turn to sort of the tax and work and care dynamic and have a think also about who pay, who really does face the higher tax rates in our economy as a whole.

The demographics after World War Two, of course, there were a lot more children being, being, being head. Fertility was 3.5, which was an average, of course. So there was some very large families. Life expectancy was much lower of a 60 to 65. So as people know, we have an aging population. We have declining fertility this year, estimated at 1.6.

That's below replacement and substantially below replacement. Migration helps a lot and we're a very good country, we're very good at migration and we need to keep doing that. But actually we need to sustain our willingness as families. We need to support women in having having children and caring for them appropriately and what that actually means is that we need to socialize the care of children.

We have been operating in a tax system that still through the combination of the tax system, the design of childcare subsidies being means tested on joint income of families and the design of our child allowances, our family payments, FTB, A and B, all of these payments are tested on joint income and are phased out just at the point in time when the second earner in the household, usually a woman is going to be facing is going to be moving into kind of half time or full time labor.

It is those workers who are facing the highest tax rates in our system. It is not individuals on 140,000 a year. Right. Or even on 190,000 a year. So we need to deliver a tax cut, but it's the tax cut to those second income earners who we would like to move into the labor market, into the market economy, to expand our tax base, to make our income tax resilient.

So how do we achieve that? Well, the best tax cut is actually expenditure. It's actually expenditure on childcare and on a full year, I would say, if paid parental leave, this looks expensive. Right. So when you see it from sort of the budget line or the government side, it looks like this is very costly. But what you have to realize is that actually in an era where we're having 1.6 children in in households, we are over specializing in home based care of children for very long periods of time.

And we are losing the skills and capability and human capital, mostly of women from our market economy. And we're also losing our tax revenue. So when we think about taxes on the labor market, that's the first thing we need to be thinking about, is actually bringing our most mobile labor force second earners who are currently working half time or less than half time for decades of their working lives into the market economy.

Now, I'm not saying we mean everybody has to do childcare all the time and this is mandatory, right? What I'm saying is we need to remove the impediments to participation in the market from our tax and welfare system. So a couple of other ways that we might want to think about taxes. And you've already seen that. What I've had to do to do that thinking is to take a step back from the rate structure and the base of the income tax and to think about how the tax law interacts with other policy regimes.

Right. So how does the tax law interact with childcare? How does it interact with the welfare system? How does it interact with the age, pension and superannuation, retirement saving? It's that policy interaction that generates incoherence in our system. Coherence was one of the goals of the Henry tax review coherent policy coherence, and it's that interaction that we need to unpick as a matter of law reform.

So the childcare interaction is one of them. I think that in terms of raising children in families, the other thing that that has not really been properly put on the table yet is the design of family tax benefit A and B, so these two child allowances for START, why do we have to child allowances? Why don't we just have a single per child allowance?

They both tested on joint income, couple income Family Tax Benefit B is tested as soon as the second earner, the primary care removes in and start spending really a very small amount of income around about five or 6000 a year. That family starts losing that child allowance. So the design of these things and then they're tapered at 20 or 30%, that is, you lose 20 or $0.30 in the dollar of the child allowance as you start to earn income, as that person starts to earn income.

So these the family tax benefit and B date back to the Howard era. They were designed, you know, we had a previous time when we had universal child allowances. In fact earlier in Australia's history in the 20th century, we have paid out per child allowances to most families with children. And the other thing to remember, when you think about the long term history, the century really when we've had a highly effective income tax in Australia, is that in the early days wages were paid as a as a family wage.

It was a breadwinner, homemaker family, it was a gendered or patriarchal family, but it was an adequate wage designed intended to be an adequate wage to pay for children. So what has happened through the 20th century is we've moved, wages have come down and we've heard in the last decade wages have are going backwards in real terms. Wages have come down dramatically.

They're now based only on your individual requirements. We deliver some subsidies to families with children, but we really tightly target those subsidies such that we penalize when those families choose to try to have dual earners in the household. So we need to kind of reverse that and think about subsidizing care properly, paying for care properly. We will we will reap the rewards in economic growth and productivity and in tax revenues.

A couple of other areas in our system where we have workers who think I've got my 5 minutes, where we have workers who are facing unfairly high tax rates and also inefficiently high rates. And again, these arise because of interactions in the system that actually before I get to that, let me say something very briefly about care workers.

You heard about that this morning. Already wages in that sector are ridiculous ously low and do have to come up. And of course, a wage increase in that sector is also good for the tax system. Right. So a wage increase is a way to draw more return out of corporates and out of capital and bring that into our kind of democratic system of sharing and allocating resources, which is what our tax system is.

The other two examples I want to briefly mentioned in the time I've got are students on Youth Allowance and young people seeking work who in the gig economy are either working part time or are looking for extra shifts or operating on a casualised, increasingly casualised and risky basis? Even in the era of low unemployment, they face tremendously high effective tax rates because of the withdrawal of income support, jobseeker or youth allowance are both too low.

That is inadequate and withdrawn too quickly over too short a range of income. So that's one area where we are overtaxing. To be honest, I think we're overtaxing students. I know I'm an academic, so a little bit of self self promotion for the universities, but we are squeezing our students between nearly full time work and nearly full time study and they are they're either in a poverty trap or they or they do not have time.

They do not have time to invest in their human capital. And we've already heard about failing to invest in the skills and tape sector. The other example that I won't spend time on now, because running out of time is actually older people right? So we have a two tier system for the retirees of this country who would like to work.

If you have the benefit of superannuation, you face very low tax rates, you're exempt on your super your earnings, you get the senior Australians Pensioners tax offset and then you face the normal marginal rate structure. If you are on the age pension, if especially if you're in a couple, you actually face very high effective marginal tax rates on your labor income, are going to work.

So again, we've created the top 20% healthy, have income and can work. The bottom 80% cannot write and face barriers and we need to redesign that as well. So to wrap up then I want to kind of circle back around to sort of in defense of the income tax. We've heard that perhaps we rely too heavily on income tax.

My response to that is that that is not so. But that's not to say we shouldn't raise other revenues. The big challenge that you heard from Rod Sims this morning is actually we need more revenue. And you've heard lots of good ideas as to how we would achieve that with other taxes, resource taxes, land taxes. What we need to do with the income tax is to protect its progressivity and bring more people into the base.

And if we do that, we will maintain its its resilience. So we need to just remember the centrality of that fiscal bargain that we have made and we have successfully made it in Australia. You'd have to say it's a good news story, having a situation where we have longevity, population, aging and now we're thinking how do we maintain our health and wellbeing in these difficult times?

You know, we've done very well actually, but this bargain is fraying at the edges and it is challenged by this global digital economy and increased economic risk and environmental risk. And so we don't like we don't have to like taxes. But what we do have to understand is that this is the way that we manage to live together in this society.

Thank you.