

## 'My dream Budget'

The *Sydney Morning Herald* and *Melbourne Age* newspapers' senior economics writer last week asked five economists their views as to what should and shouldn't be in this week's 2020-21 Federal Budget. Her article was published on Sunday [here](#).

As always, Jessica was only able to use a small part of each economists' answers. Here are her questions, and my responses to them, in full.

### WELFARE/CASH PAYMENTS

Q. More one-off cash payments? **YES/NO** For whom? **NO**

Q. Extend JobKeeper eligibility beyond March 28? **YES/NO** **YES** (or at least, indicate a willingness to do so if labour market is still weak then, or particular sectors still being affected by government restrictions)

Q. Boost JobSeeker payments (currently scheduled to return to old rate of \$565 per fortnight come January)? **YES/NO** By how much? Temporarily or permanently? **YES**, to about 80% of the age pension, and permanently

Q. Anything else? No but see my answer to the next question (and decide for yourself which category it belongs in)

### TAX CUTS

Q. Pull forward Stage 2 of personal income tax cuts to 2021-22? **YES/NO** **NO**

Q. Pull forward Stage 3 of personal income tax cuts to 2021/22? **YES/NO** **NO**

Q. Do you have an alternative personal income tax plan? Please detail **YES**

Leave the tax cuts to come in as scheduled (I'm not opposed to them), but apply the revenue which would have been foregone by bringing them forward by whatever period the Government is planning to, instead to providing households with time-limited but tradeable vouchers (eg, they expire worthless if not used by, say, 30 June 2022, but if you can't use them for whatever reason you can sell them to someone else who can).

The vouchers could be used for:

- (a) spending in areas that are still adversely affected by ongoing government restrictions (most obviously tourism and the arts);
- (b) spending in areas that would help people get into, or back into, work (most obviously childcare and training/retraining);
- (c) 'essentials' like electricity, gas or water bills;
- (d) possibly for renovations or even towards a deposit on a first home.

Vouchers could be distributed through the ATO (for taxpayers) or Centrelink (for nontaxpayers), and when redeemed could be converted into cash when the businesses whose products are paid for using them file their BAS's. If you wanted to you could exclude taxpayers in the top bracket from eligibility for the vouchers (although I'm not advocating that).

The Parliamentary Budget Office has [estimated](#) that the cost in terms of revenue foregone of bringing forward the tax cuts currently scheduled to take effect on 1 July 2022, to 1 July 2021, would be \$14.14bn (or \$27.8bn if they were brought forward to 1 July 2020, ie in effect made retrospective).

So, divide that by 10.5 million (roughly the number of households, and you're talking about vouchers worth \$1350 each if they are to replace bringing forward the tax cuts by 1 year, or \$2650 each if they are to replace bringing the tax cuts forward by 2 years

The great advantage of this, by comparison with bringing forward tax cuts, is that you guarantee the money *will* be spent (which both economic theory and recent history says you can't with bringing forward tax cuts, especially if they are – as they almost unavoidably are, given the steeply progressive nature of Australia's personal income tax system – skewed towards middle- and upper-income households); it will be spent *when* it is most helpful for it to be spent; and it will be spent *in areas most in need of stimulus or in ways that are most likely to result in increased employment*. Bringing forward tax cuts doesn't do any of that.

## INFRASTRUCTURE

[Q. Boost infrastructure spending?](#) YES/NO **YES**

[Q. If yes, where should the money be directed?](#) As RBA Governor Phil Lowe advises, a large number of small projects, rather than a small number of large ones – and spending at least as much on repair, maintenance and upgrade of existing infrastructure as on building new infrastructure (even though that provides fewer opportunities for politicians to cut ribbons or unveil plaques with their own names on them).

[Q. What's your dream nation building project?](#) This won't surprise you – Project Marinus, the proposed undersea electricity cable(s) between Tasmania and the North Island, which would enhance the capacity of mainland solar and wind generators to make 'firm' (ie, guaranteed) offers of electricity supply into the mainland grid, and hence speed the transition to a low-emissions economy – and, moreover, do it more cheaply than the Federal Government's Snowy 2.0 (which, although it obviously doesn't require undersea cables, *does* require longer land-based transmission, and in particular requires a lot more tunnelling – which is the most expensive part of pumped hydro schemes, take it from someone who was on the Hydro Tasmania board for 10 years until 2018 – than Tasmania's scheme does).

## CORPORATE TAX CUTS

Q. Extend the recent company tax cut (to 26%) for small business (under \$50m turnover) to all business with under \$1 billion annual turnover? **NO!!** Instead, drop the tax preferences for small businesses – which have had *no effect whatsoever* in boosting either employment, investment or innovation – and replace them with more generous concessions for *new* businesses (eg, a company tax rate of, say, 15% for the first five years).

Despite accounting for over 40% of private sector jobs, as its advocates are so fond of quoting, small businesses have created only 3% of the *increase* in private sector employment since the preferential company tax rate for small businesses commenced in July 2015; and capex by small businesses has fallen by more than by medium-sized or large businesses since both the lower tax rate and the 'instant asset write off' for small businesses were introduced (see [here](#) for the evidence from ABS).

We've already got plenty of other supports for small business (including the government loan guarantee, the loan deferral holiday, the cash flow support scheme for small businesses, preferential access in the form of a less onerous turnover test to JobKeeper, and the relief from the duty to avoid trading while insolvent).

Why should they get a lower tax rate as well - especially when [ATO Tax Gap research](#) shows that (contrary to the almost universal public perception) small business accounts for almost half of the 'gap' between what the ATO actually collects by way of personal and company income tax, and what they estimate they would collect if there was 100% compliance – cf. large corporate groups only 7% and high net worth individuals 3% of the tax that isn't collected).

By contrast, *new* businesses are

- (a) more likely to be in sectors that have good prospects longer-term (cf. small businesses usually being in the sector they're in because that's what they were in when great-grandpa started the business);
- (b) are more likely to create jobs (whereas small businesses typically already have all the staff they need);
- (c) are more likely to innovate (the desire to bring to market a new good or service, or to produce an existing one in a new way, is the main reason for starting a new business; (d) much less numerous than small business, and hence the concessions won't have as big a cost to revenue even if they are more generous; and
- (e) can't stop from eventually becoming an older business, so there aren't the perverse incentives to stop growing at just below the threshold at which they cease to be 'small' for the purpose of determining eligibility for preferential treatment.

Also note that if Joe Biden wins the US elections (and if there is a God, and that God cares about the world He made, then Biden will win), he will reverse Trump's corporate tax cut, and one of the main arguments pushed by proponents of cutting the corporate rate will disappear.

Q. Do you think the tax burden on business needs to fall? No, not really ... again, see answer to previous question. Q. If so, how?

Q. What's the best way to incentivise more business investment? See, in part, my earlier answer to your question about corporate tax cuts – replace tax preferences (both lower rates and the instant asset write off) for *small* business with more generous (but less costly in terms of total revenue foregone) preferences for *new* business.

The other way to incentivise more business investment is to give business more reason to be confident that demand for their product will continue to grow. It is also worth noting, however, that almost all capital goods are imported: so, the immediate stimulatory effect of incentives for capital expenditures is less than meets the eye.

## JOBS

Q. What's the best way for the government to create jobs? To remember that governments *don't* actually create jobs (except in the provision of public services, and there's absolutely nothing wrong with that) – even though they like to tell voters that they have, or will. It's businesses (mostly) that create jobs.

But certainly, persisting with policies that *don't* work, in the face of *compelling evidence* that they don't work – such as giving tax breaks for small businesses *just because they are small*, based on a completely nonsensical belief that there's something inherently more noble about running a small business than working for a big one, or for a government or a not-for-profit, which makes people running small businesses morally superior human beings who are therefore deserving of paying less tax on a given amount of income than everyone else (something which as the ATO's Tax Gap research suggests they will try to do anyway, whether it is legal or not) – is *not* the best way for the government even to try to claim the credit for 'creating jobs'.

Rather, it reminds me of Einstein's definition of madness – doing the same thing over and over again and expecting the result to be different next time.

## ANYTHING ELSE?

Q. Do you have a burning policy recommendation that has not been covered? No ... my 'burning recommendations' are in my answers to your questions.

Q. Final thoughts? Maybe answering surveys like this, making the same recommendations over and over again despite the fact that they've less chance of being implemented than Tasmania has of getting an AFL team we can call our own, is

another illustration of Einstein's definition of madness. No disrespect to you at all, dear Jess! I actually enjoyed writing it (and might even post it on my website, since of course you can't possibly use all of the above).

Saul Eslake

4<sup>th</sup> October 2020