

Five ways the Treasurer could boost the budget bottom line

Written by Danielle Wood, Program Director, Budget Policy and Institutions, Grattan Institute

Treasurer Scott Morrison faces a difficult balancing act in the federal budget. He wants [to cut income taxes](#), deliver new [infrastructure spending](#) and still reach a surplus by at least 2019. If he's serious about maintaining the surplus, here are five ways the Treasurer could boost revenue to make the numbers work.

1. Scrap age-based tax breaks

Winding back tax breaks for older Australians could boost revenue by [A\\$700 million a year](#).

Many seniors pay less than younger workers, on the same income, as a result of the [Seniors and Pensioners Tax Offset](#)

and a

[higher Medicare levy income threshold](#)

. Seniors currently do not pay tax until they earn A\$32,279 a year, whereas younger households have an effective tax-free threshold of A\$20,542.

These tax breaks – along with the introduction of [tax-free superannuation](#) for retirees – have [almost halved the proportion of older Australians](#) paying tax in the past 20 years.

For a start, the government could scale back the Seniors and Pensioners Tax Offset so that only pensioners qualify, while those with enough income to not qualify for a full Age Pension should pay some income tax. The higher Medicare levy income threshold for seniors should also be abolished.

2. Better target the research and development tax incentive

The government will forgo A\$3.5 billion in revenue this year through the research and development tax incentive. Tightening eligibility could substantially reduce the cost of the scheme.

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The research and development tax incentive was introduced in 2011 to encourage activities that otherwise would not be conducted, including by smaller firms. But the cost has blown out and there are concerns that [the scheme is being rorted](#). The scheme now accounts for around one third of total government support for innovation.

[A 2016 review of the incentive](#) concluded the scheme could be made more sustainable by tightening the definition of eligible research and development. This includes an emphasis on novelty, capping the annual amount that is refundable in each year (as well as a lifetime cap) for smaller business, and making the scheme available only to larger businesses that allocate more than 1% of their total spending to research and development.

3. Wind back negative gearing and reduce the capital gains tax discount

Winding back negative gearing and reducing the capital gains tax discount to 25% would boost revenue by [A\\$5.3 billion a year](#).

These tax breaks distort housing investment decisions, leading investors to favour capital gains over rental returns, and to maximise borrowing, to fund the investments. This [makes housing markets more volatile](#)

and

[reduces home ownership](#)

. Like most tax concessions, the tax breaks [largely benefit the wealthy](#)

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Negative gearing should change so that investment losses can't be written off against labour income, [in line with international practice](#). Reducing the capital gains discount to 25% would still allow some compensation for the effects of inflation on investment returns, but it would reduce some of the distortions in investment decisions created by the current discount.

4. Abandon planned increases in the Super Guarantee

Abandoning plans to increase compulsory super contributions to 12%, could boost revenues by A\$500 million in 2021-22, rising to over [A\\$2 billion a year by 2025-26](#).

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The Super Guarantee is legislated to [rise](#) from 9.5% of wages today to 12% by July 2025. But increasing compulsory super contributions will reduce wages today and [do little to boost the retirement incomes](#) of many low-income workers.

It will also cost the Budget billions in extra super tax breaks. Instead of workers receiving wages tax at full marginal tax rates, the extra super contributions will be taxed at a flat 15%. The 2014–15 budget calculated that delaying an increase to the Super Guarantee of 0.5 percentage points [saved A\\$440 million in 2017–18](#).

These budget savings would endure even in the long-term: a [Treasury analysis](#) estimated the tax revenue foregone as a result of a 12% Super Guarantee would exceed the budgetary savings from lower age-pension spending until about 2060.

5. Offer another scheme in place of company tax cuts

The government could boost investment at a lower long-run cost to the budget by replacing the proposed reduction in company taxes to 25% with a [permanent accelerated depreciation scheme](#).

Accelerated depreciation schemes allow businesses to depreciate their capital investments at a faster rate. These schemes cost less than company tax cuts in the long run for a given boost to investment, but the cost to the budget in the initial years is higher.

An immediate tax deduction of 22% on all new capital purchases would cost the government about a third more than a company tax cut in the first year, and it would not be until the sixth year that the annual budget cost would fall below that of a tax cut. However, by the tenth year the cost of the accelerated depreciation scheme would be 18% lower than a company tax cut and after two decades it [would cost 40% less per year in forgone revenues](#).

This is clearly a pre-election budget. But whatever announcements are made, the [planned return to surplus](#) shouldn't be sacrificed. The government should tighten spending wherever possible. But they will also need to sure up revenues if they cut income taxes.

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