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The Taxpayers Research Foundation Limited

THE TAXPAYERS RESEARCH FOUNDATION

The Taxpayers Research Foundation Limited

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EDITORIAL

For years, Australia has been able to rely on a familiar story: steady economic growth, comparatively low public debt, and a tax system that—while imperfect—continued to deliver enough revenue to meet expectations. At a distance, that story still looks intact. Debt remains moderate by international standards, and the economy continues to expand. But the surface calm masks a more difficult truth: the era of easy fiscal choices is ending, and the country is running out of simple ways to fund the level of government Australians expect.

Across this edition, a clear message emerges. The pressures reshaping the budget are not short-term fluctuations that can be managed with incremental adjustments. They are structural forces that will define the next several decades. An ageing population is shifting the balance between those who fund services and those who rely on them. Health spending continues to rise faster than national income. Defence commitments are expanding in scale and complexity. And the energy transition demands sustained investment, not one-off injections. These are long-term obligations, not temporary spikes.

Yet the tax system remains anchored to a model built around personal income tax, supported quietly by bracket creep and constrained by longstanding political caution. The result is a growing mismatch between what governments are expected to deliver and the revenue tools they are prepared to use.

The contributors in this edition approach the issue from different angles, but the pattern is unmistakable. The IMF points to the need for base broadening and greater efficiency. Brennan examines the limits of the current revenue mix. The Productivity Commission raises questions about how federal transfers shape incentives and accountability. Deloitte outlines what a more balanced system could look like. The challenge is not a lack of analysis. It is the difficulty of turning analysis into action.

Much of the public conversation still proceeds as if trade-offs can be avoided. But the choices are real and unavoidable. A broader tax base means more people contribute. Reducing reliance on income tax implies higher consumption or wealth taxation. Keeping the system unchanged means accepting either rising debt or tighter public services. Pretending these choices do not exist only postpones the reckoning.

That is the shift now underway. The debate is no longer about fine-tuning the existing system or adjusting a few parameters at the edges. It is about choosing the direction of the system itself—what Australians want government to do, how much they are prepared to pay for it, and how the burden should be shared.

This journal does not attempt to settle that question. Instead, it aims to do something more constructive: to set out the constraints clearly, connect the policy threads, and make explicit what is often left unsaid. Australia can continue on its current path, but only if it is prepared to rethink how it pays for the services, protections and opportunities it values. The easy options are gone. What remains is a national conversation about priorities, trade-offs, and the fiscal architecture that will shape the country's future.

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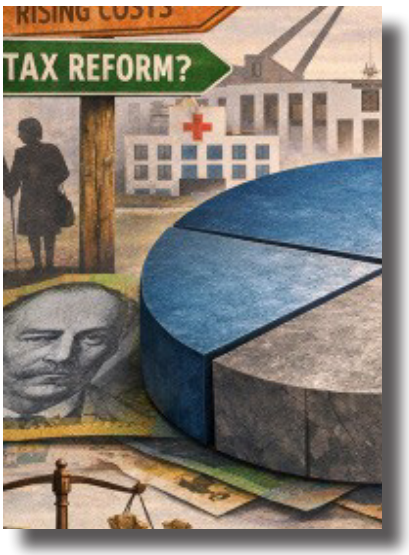
Australia faces growing fiscal pressures as major spending programs expand and the population ages. In its 2024 Article IV consultation, the International Monetary Fund argues that the country's tax system may no longer be well aligned with these realities.

This article examines the IMF's assessment and explores the policy choices confronting Australia's tax and spending framework.



RETHINKING THE TAX MIX

Australia's fiscal debate often assumes governments can expand services without changing the tax system. Michael Brennan, in Australia's Public Revenue Constraint, challenges this by arguing that the Commonwealth is reaching the limits of a revenue model dominated by personal income tax.

With demographic pressures, rising expenditure and strong public expectations, he suggests the real issue is no longer short-term budgeting but whether the current tax mix can realistically fund the level of government Australians appear to want.

GST DISTRIBUTION REVIEW

Australia's GST distribution system sits at the core of federal financial relations, using Horizontal Fiscal Equalisation to ensure states can provide comparable services. While the principle has long been accepted, its practical operation has become increasingly contested.

The Productivity Commission's 2018 inquiry highlighted these tensions, examining whether the current model strikes the right balance between fairness across states and incentives for economic growth and policy reform.

THE LEVEL OF STATE & FEDERAL DEBT

Australia's public debt is rising faster than expected, driven largely by state borrowing and growing structural pressures across health, infrastructure and services.

While still low by international standards, the nation's fiscal buffer has narrowed, interest costs are climbing, and maintaining stability will increasingly depend on how governments choose to adjust revenue and spending in the years ahead

RETHINKING AUSTRALIA'S TAX MIX

Australia's tax system remains relatively efficient by global standards, but growing fiscal pressures and a changing economy are sharpening questions about its long-term sustainability.

In this context, Deloitte has become a leading advocate for comprehensive reform, arguing that Australia must shift away from its heavy reliance on income tax toward a broader base that includes greater use of consumption and wealth measures—reflecting both established economic thinking and the widening gap between current tax settings and future fiscal needs.

AUSTRALIA'S TAX REALITY CHECK

Australia's tax debate often sidesteps the uncomfortable reality that rising spending and an ageing population cannot be met by a system still leaning heavily on personal income tax. Across this journal, contributors—from the IMF to Brennan, the Productivity Commission and Deloitte—converge on the same point: the current model is running out of easy options.

For years, governments have relied on small tweaks to bridge the gap, but the pressures now emerging demand a more honest conversation about the choices ahead.

A SYSTEM UNDER PRESSURE

At one level, Australia's tax system still appears steady. Revenue continues to grow, debt remains manageable relative to many advanced economies, and the overall framework has avoided the kind of instability seen elsewhere. Yet that surface stability is increasingly misleading. Beneath it, structural pressures are building in ways that are becoming harder to ignore.

At the centre of the issue is a widening gap between what governments are expected to deliver and how those commitments are funded. Public spending is no longer driven primarily by short-term policy choices or economic cycles. Instead, it reflects long-term forces: an ageing population, rising health and aged care costs, increased defence requirements, and the fiscal demands of economic transition. These are not temporary spikes. They are embedded trends that will shape the budget for decades.

Against that backdrop, the tax system has remained relatively static. Australia continues to rely heavily on personal income tax, supported quietly by bracket creep and constrained by political reluctance to broaden the base. While this model has been resilient, it is also narrow. As spending pressures increase, that narrowness becomes more significant, concentrating the revenue burden and limiting flexibility in how governments respond.

This edition examines that tension from multiple angles. It begins with the International Monetary Fund's assessment of Australia's fiscal outlook, which places the relationship between spending pressures and tax design at the centre of its analysis. The IMF's message is measured but clear: maintaining fiscal resilience will require more than incremental adjustments.

From there, the focus shifts to Michael Brennan's work on Australia's public revenue constraint. His argument cuts through much of the political framing that often surrounds tax debate. Rather than asking how to raise additional revenue at the margins, he questions whether the existing tax mix is capable of supporting the level of public services Australians appear to expect. In doing so, he reframes the discussion as one of structural alignment rather than short-term budget repair.

The journal then turns to the mechanics of the federation, examining how Goods and Services Tax distribution and Horizontal Fiscal Equalisation influence incentives across states and territories. These arrangements are often treated as technical, yet they shape real economic behaviour. Decisions about investment, reform and service delivery are all affected by how revenue is shared. As the analysis shows, the design of these systems carries implications that extend well beyond fiscal fairness.

This broader context is grounded in current fiscal reality through an examination of state and federal debt. While Australia's overall debt position remains comparatively moderate, the trajectory has shifted. State borrowing, in particular, has increased significantly, driven by infrastructure investment and ongoing expenditure pressures. The result is not a crisis, but a narrowing of fiscal space. Future policy choices will need to operate within tighter constraints than in the past.

The final section considers reform proposals, including Deloitte's framework for rebalancing the tax system. These proposals reflect a growing consensus among economists that the current mix could be improved. Shifting towards broader consumption taxes, reducing reliance on income taxation, and increasing the role of wealth-based measures are all presented as ways to enhance efficiency and sustainability. Yet each comes with distributional and political challenges that cannot be easily resolved.

Taken together, these contributions highlight a shift in the nature of Australia's tax debate. The discussion is moving beyond questions of efficiency and simplicity towards more fundamental issues of sustainability and fairness. The central challenge is no longer whether the system works in a technical sense. It is whether it remains aligned with the scale and structure of government activity.

Australia's Fiscal Crossroads: Tax Reform, Spending Pressures and the IMF's Warning

Australia faces growing fiscal pressures as major spending programs expand and the population ages. In its 2024 Article IV consultation, the International Monetary Fund argues that the country's tax system may no longer be well aligned with these realities.

This article examines the IMF's assessment and explores the policy choices confronting Australia's tax and spending framework.

Australia's fiscal debate increasingly centres on a structural tension between expanding government commitments and a tax system that has changed little over time. The International Monetary Fund's 2024 Article IV consultation on Australia places this relationship at the centre of its assessment of the country's fiscal outlook. In the IMF's view, rising expenditure pressures are occurring alongside a tax base that remains relatively narrow and heavily reliant on labour and capital income.

At the core of the IMF's analysis is the fiscal arithmetic facing the Australian budget. While many pandemic-era support measures have unwound, several major policy commitments have lifted the ongoing spending baseline compared with the pre-COVID period. Programs such as the National Disability Insurance Scheme (NDIS), aged care reforms, increased defence spending and investments associated with the energy transition have all contributed to structurally higher public expenditure. Demographic ageing and health-care costs are expected to intensify these pressures over time. Although Australia's public debt remains relatively modest compared with many advanced economies, the IMF notes that fiscal buffers are gradually narrowing and that maintaining resilience to future shocks will require careful policy management.

In that context, the IMF encourages policymakers to rebuild fiscal buffers during periods of stronger economic performance. Strengthening the budget position when economic conditions are favourable helps preserve the capacity to respond to downturns or unexpected shocks. This approach reflects a broader theme in the consultation report: fiscal sustainability is more easily maintained through gradual reform than through adjustments imposed during periods of economic stress.

Attention then turns to the structure of the tax system itself. The IMF reiterates a long-standing observation that Australia relies heavily on direct taxation, particularly personal income tax, while making relatively limited use of broad-based consumption taxes and stable property-based revenue sources. As spending pressures grow, this structure increases reliance on bracket creep as a mechanism for raising additional revenue. The Fund observes that such reliance can gradually increase effective tax rates without explicit policy decisions and may weaken transparency in the tax system.

Within this broader framework, the IMF highlights several tax concessions that narrow the revenue base and add complexity. The capital gains tax (CGT) discount and concessional taxation of superannuation receive particular attention in the report. According to the IMF, these concessions reduce revenue capacity and tend to deliver larger benefits to higher-income households. The consultation suggests that scaling back such concessions could strengthen the tax base while improving the distribution of the tax burden.

Efficiency considerations also feature prominently in the IMF's analysis. Economic research — including modelling undertaken by the Australian Treasury — suggests that different taxes impose different economic costs. Company income taxes and transaction-based stamp duties are often considered among the more distortionary sources of revenue because they can discourage investment or alter economic behaviour. By contrast, broad-based consumption taxes and recurrent land taxes are generally regarded as less distortionary. Shifting the composition of taxation toward these sources could therefore allow governments to raise revenue with smaller impacts on investment, labour supply and economic activity. The IMF also links tax design to Australia's long-term productivity outlook. Productivity growth has slowed in recent years, raising concerns about the economy's future capacity to generate income and support public services. Tax systems that impose high marginal rates on labour or discourage capital investment can weigh on economic performance over time. From this perspective, tax reform is presented not simply as a revenue-raising exercise but as part of a broader strategy to support sustainable economic growth.

Distributional considerations are also acknowledged in the report. Heavy reliance on personal income taxation means that a significant share of the revenue burden falls on working-age households. At the same time, certain tax concessions — particularly those related to capital gains and retirement savings — can disproportionately benefit higher-income individuals. Reforming these settings could potentially address concerns about the intergenerational distribution of the tax burden, although such reforms inevitably raise broader questions about incentives to save and invest.

Not all tax reform challenges lie within the direct control of the Commonwealth. The IMF notes that some of the most economically inefficient taxes in Australia are levied by state governments, particularly stamp duties on property transactions. These taxes can discourage mobility and distort housing market behaviour. Economists have long proposed replacing transaction-based stamp duties with recurrent land taxes, yet such reforms require coordination between federal and state governments and often encounter significant political resistance.

While the report gives considerable attention to revenue policy, it also emphasises the importance of expenditure discipline. The IMF encourages continued evaluation of major public programs such as the NDIS and aged care, along with structural reforms aimed at moderating long-term health-care costs. It also notes the potential value of the Australian Government's "Measuring What Matters" framework, which seeks to link public spending to broader wellbeing outcomes rather than focusing solely on traditional economic indicators. However, the report cautions that performance frameworks are effective only when they meaningfully influence budget decisions.

Political constraints inevitably shape the scope of fiscal reform. Expanding the base of the GST or implementing broader land taxes has historically proven difficult in Australia. Nevertheless, the IMF warns that reliance on incremental measures such as bracket creep, temporary levies or sporadic spending reductions may not be sufficient to stabilise public finances in the face of rising structural pressures.

The IMF's analysis therefore highlights a broader policy tension confronting Australia. Governments can maintain or expand large social programs in areas such as disability support, health care and aged care, but doing so sustainably requires a tax system capable of supporting those commitments. Alternatively, limiting the overall tax burden would require more explicit decisions about the scope of public services and the scale of government activity.

The consultation report does not prescribe a single political solution to this tension. Instead it emphasises that fiscal sustainability, economic efficiency and distributional considerations are closely linked to the structure of the tax system and the level of public spending. For policymakers, the central challenge lies in determining how best to align these elements in a way that preserves economic resilience while maintaining public confidence in the fairness and effectiveness of the tax system.

Reference: International Monetary Fund, Australia: 2024 Article IV Consultation, IMF Country Report, 2024.

Australia's Public Revenue Constraint: Rethinking the Tax Mix

Australia's fiscal debate often proceeds as though the country can sustain expanding public services without materially altering the structure of its tax system. In Australia's Public Revenue Constraint, Michael Brennan of the e61 Institute challenges that assumption.

His argument is that the Commonwealth is approaching the limits of a revenue model heavily dependent on personal income tax while political debate continues to avoid the broader choices implied by demographic change, rising spending pressures and voter expectations. The paper therefore shifts attention from short-term budget management to a more fundamental question of tax design: whether Australia's current tax mix can realistically fund the level of government Australians appear to demand.

Michael Brennan's paper "Australia's Public Revenue Constraint", published by the e61 Institute, confronts a question often avoided in Australian fiscal debate: whether the current tax system can sustain the level of public spending Australians appear to expect. Brennan's argument is direct. The existing revenue model, heavily reliant on personal income tax, is approaching its limits, yet policy debate continues to assume that expanding public services can occur without broader changes to the tax base.

At the centre of the analysis is a structural shift in spending pressures. An ageing population, rising health and aged-care costs, increased defence commitments and the fiscal demands of decarbonisation all point toward a higher long-term share of GDP devoted to government expenditure. At the same time, Australians have developed strong expectations around the availability and quality of public services. Brennan describes this as a "revealed preference" for a moderately larger state, despite political rhetoric often suggesting otherwise.

Within this context, Brennan identifies several constraints embedded in the tax system.

The first is Australia's reliance on personal income tax. A relatively large share of revenue is collected from this source compared with other OECD economies. The progressive structure means higher-income households contribute a significant proportion of total receipts, while bracket creep has gradually increased the effective tax burden. Many lower-income households, by contrast, face limited net tax once transfers are taken into account. The issue is not progressivity itself, but the vulnerability created by reliance on a relatively narrow base.

A second constraint arises from exemptions and concessions. GST exclusions on fresh food, health and education, alongside superannuation tax concessions, the capital gains tax discount and numerous deductions, narrow the effective tax base. Individually, these measures reflect policy choices. Collectively, they reduce efficiency, limit revenue capacity and require higher rates elsewhere.

The third constraint is political. Despite broad agreement among economists that the tax mix could be improved, there has been limited willingness to advocate structural reform. Public debate often assumes that additional spending can be funded by a small group of taxpayers, such as multinational corporations or very high-income individuals. Brennan argues this framing obscures the underlying fiscal reality. Sustained increases in public spending are unlikely to be financed without broader participation in the tax system.

Rather than proposing a single reform package, Brennan outlines several directions. A broader Goods and Services Tax, potentially combined with a higher rate and compensation for lower-income households, is one option. Greater use of land and resource taxation is another, particularly where economic rents are present. On corporate taxation, Brennan's approach aligns with concepts explored in the Henry Review and by the Productivity Commission, focusing on taxing excess returns while reducing taxes on normal investment.

He is cautious about proposals often presented as simple solutions, such as flat taxes or pure expenditure taxes, noting the distributional and transition challenges they raise. Instead, he identifies scope to improve the design of personal income tax. Reducing high effective marginal rates at low and middle incomes — particularly where tax interacts with the withdrawal of transfers — could improve work incentives while maintaining progressivity. This may involve a higher tax-free threshold and a simplified rate structure.

For tax policy analysis, Brennan's paper is valuable in linking tax design directly to fiscal sustainability. It challenges both advocates of smaller government, who rarely specify the spending reductions required, and those supporting expanded public provision, who do not always identify the necessary revenue sources.

The central question is straightforward. If Australia expects a certain level of public services, the tax system must be capable of funding them. The issue is not whether trade-offs exist, but whether there is sufficient willingness to address them directly.

Productivity Commission and the GST Allocation System

Australia's system for distributing Goods and Services Tax (GST) revenue sits at the centre of the country's federal fiscal architecture. Through the principle of Horizontal Fiscal Equalisation (HFE), GST revenue is redistributed among the states and territories so that each jurisdiction has the capacity to provide comparable public services if it makes an average effort to raise its own revenue.

While this principle has long enjoyed bipartisan acceptance, the practical operation of the system has become increasingly contested. The Productivity Commission 2018 inquiry into HFE brought these tensions into sharp focus, examining whether the existing model appropriately balances fairness between states with incentives for economic growth and policy reform.

Debate over Australia's Goods and Services Tax distribution has intensified in recent years, placing renewed attention on the principles underpinning Horizontal Fiscal Equalisation (HFE). The 2018 inquiry by the Productivity Commission remains the most influential modern examination of the system and its consequences for federal fiscal relations. Its report sought to explain how GST revenue is distributed between the states and territories and to assess whether the mechanism strikes an appropriate balance between fairness and economic incentives.

Australia's GST revenue is distributed among the states based on recommendations from the Commonwealth Grants Commission. The Commission applies the principle of Horizontal Fiscal Equalisation, under which each state should have the fiscal capacity to provide a comparable level of public services if it makes an average effort to raise revenue and operate efficiently. In practice, this means that GST allocations are adjusted to account for differences in revenue-raising capacity and expenditure needs across jurisdictions.

For many years the system aimed to equalise states to the fiscal capacity of the strongest state. During the iron-ore boom this effectively meant equalising to Western Australia. As mining royalties surged, WA's measured fiscal capacity rose sharply, causing its share of GST revenue to fall dramatically while other states received higher per-capita allocations. The resulting distribution proved politically contentious and highlighted the volatility inherent in equalising "to the last dollar" of fiscal capacity.

The Productivity Commission concluded that the existing system had become overly complex and at times produced outcomes that were difficult to justify publicly. It also raised concerns that extremely tight equalisation could weaken policy incentives for state governments. If the fiscal benefits of economic growth or policy reform were largely offset through the equalisation process, the reward for productivity-enhancing reforms could be diluted.

To address these issues, the Commission recommended moving toward what it described as "reasonable equalisation." Instead of equalising every state to the strongest jurisdiction, the benchmark would be set at the fiscal capacity of the second-strongest state. This approach aimed to maintain the principle of comparable service provision while reducing volatility and improving incentives for economic development. The Commission also recommended clearer governance arrangements and greater transparency so that both governments and taxpayers could better understand how GST relativities are calculated.

Subsequent Commonwealth reforms adopted elements of this approach. The system now incorporates a floor on GST shares, along with transitional "no-state-worse-off" payments funded from outside the GST pool. These changes were intended to stabilise allocations and address the political tensions surrounding Western Australia's very low share during the mining boom. The resulting framework, however, represents a hybrid arrangement that combines formula-based equalisation with explicit political guarantees.

Beyond the technical debate over relativities, the deeper issue concerns the design of fiscal incentives within Australia's federal system. A tightly equalising framework can shield states from the fiscal consequences of weak policy choices and reduce the gains from growth-oriented reforms. Conversely, a looser

"THE REAL QUESTION IS NOT ONLY HOW GST IS COLLECTED, BUT HOW ITS DISTRIBUTION SHAPES INCENTIVES FOR REFORM ACROSS AUSTRALIA'S FEDERATION."

equalisation model risks widening disparities in service delivery between jurisdictions. The Productivity Commission's work therefore frames a fundamental policy question: should HFE primarily pursue fairness in fiscal capacity across states, or should it place greater weight on maintaining strong incentives for economic reform?

Recent work by the Productivity Commission, including its inquiry into creating a more dynamic and resilient economy, returns to this theme. It emphasises that intergovernmental transfers – including GST revenue – represent a substantial share of state budgets and could potentially be designed to encourage reform in areas such as housing supply, planning regulation, infrastructure delivery and human capital development.

A smaller but illustrative example of how the system evolves involves adjustments to expenditure assessments related to Indigenous populations. Historically, GST allocations incorporated population measures based on individuals identifying as Indigenous in census data. The Commonwealth Grants Commission later reviewed the rapid growth in identification between censuses and refined its methodology. Greater weight is now placed on Indigenous populations in remote communities, where service delivery costs are demonstrably higher, rather than applying the same adjustment across urban areas. The change reflects an effort to align funding assessments more closely with underlying expenditure needs.

Viewed in this broader context, GST distribution is no longer simply a technical dispute over fiscal relativities. It has become a central component of Australia's federal financial architecture. Any future reform that alters the GST rate or broadens the tax base will inevitably intersect with the politics and economics of Horizontal Fiscal Equalisation. A credible national tax reform agenda therefore cannot avoid engaging directly with the institutional design of the HFE system and the incentives it creates for state governments.

THE LEVEL OF STATE AND FEDERAL DEBT

Australia entered the pandemic with relatively low public debt compared with other advanced economies. That position has shifted. Debt is now materially higher and continuing to rise. This does not amount to a fiscal crisis, but it does narrow the room available to respond to future shocks and fund new policy priorities.

Data from the Australian Bureau of Statistics indicate that combined ("all Australia") general government net debt reached approximately $846.6 billion in 2023–24, or 31.7 per cent of GDP. The increase has been driven primarily by the states and territories. Their borrowing rose sharply—by more than 25 per cent in 2023–24—reflecting large infrastructure programs and persistent operating pressures. Commonwealth net debt, by contrast, recorded only modest growth over the same period.

On current projections, the Commonwealth's position appears relatively contained. Budget and MYEFO estimates suggest that gross federal debt will stabilise in the mid-30s as a share of GDP, peaking at around 37 per cent in 2029–30 before gradually declining. Net debt is now expected to remain below earlier projections, supported by stronger nominal growth and higher-than-anticipated revenue.

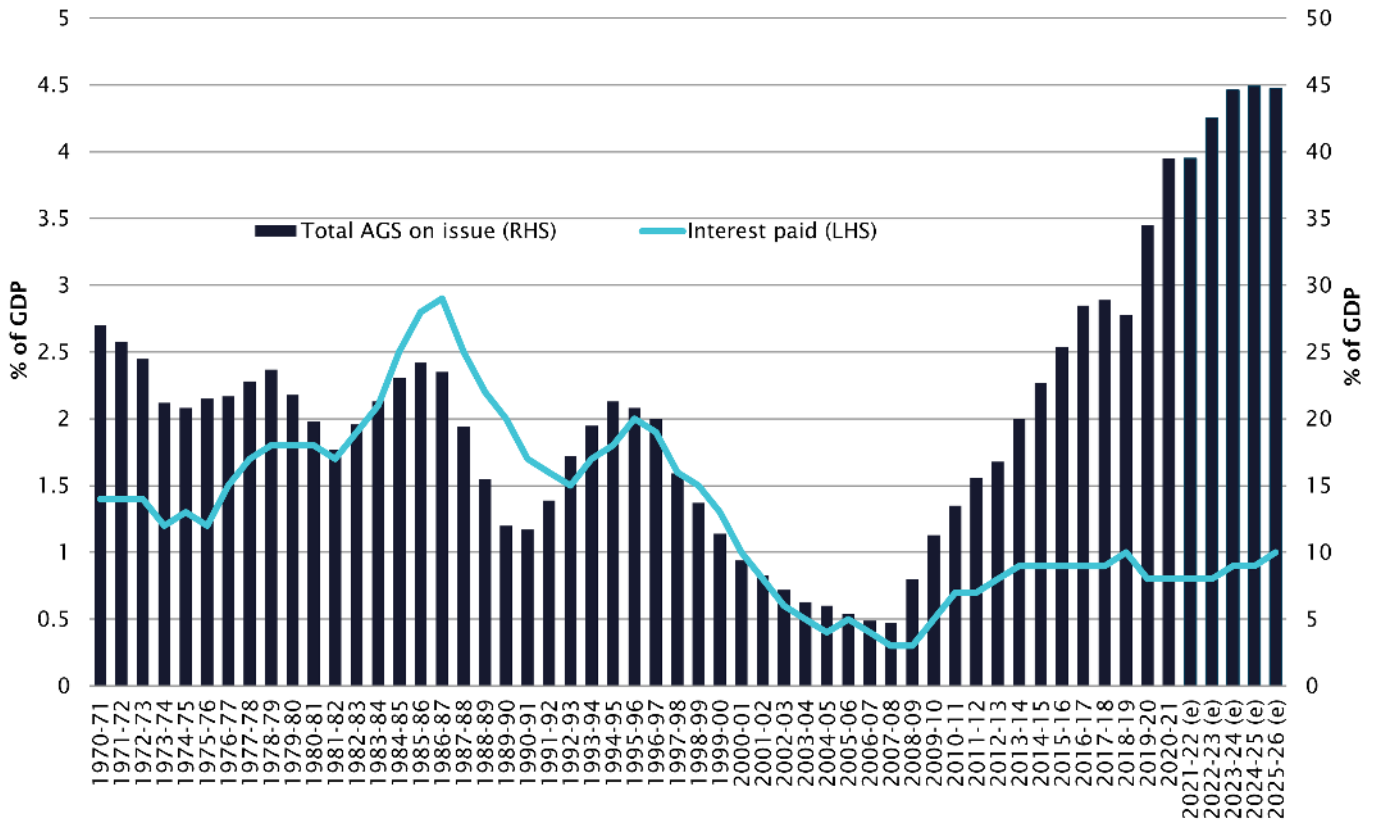
A different trajectory is evident at the state level. The Parliamentary Budget Office projects that state net debt will rise from around 13 per cent of GDP ($357.5 billion) in 2024–25 to close to 15 per cent ($471.9 billion) by 2027–28. Infrastructure-intensive jurisdictions, particularly Victoria and New South Wales, account for a substantial share of this increase. At the same time, smaller states such as Tasmania are facing significant near-term deficits as expenditure—especially in health—continues to outpace revenue.

Taken together, national public debt—combining Commonwealth and state positions—is approaching, and on some measures slightly exceeding, its COVID-era peak. It is projected to rise towards the high-50s per cent of GDP by the late 2020s before stabilising. Even so, Australia's public debt burden remains lower than that of many OECD peers. The margin of fiscal comfort, however, is clearly narrower than it was a decade ago.

The more significant constraint lies in the structure of the budget rather than the headline debt ratio. Interest payments are increasing and are forecast to reach around 1.9 per cent of GDP by 2027–28. This represents a growing claim on public resources and limits flexibility across other areas of spending. With total government expenditure across all levels now approaching $1 trillion annually, relatively small changes in revenue or spending settings translate into substantial fiscal impacts.

For tax policy, the implications are difficult to avoid. Maintaining a broadly stable debt-to-GDP ratio while meeting rising demand for public services will require

either an increase in revenue, a moderation in expenditure growth, or a combination of both. The pre-pandemic assumption that economic growth alone would restore fiscal balance is no longer persuasive. Any credible tax reform agenda—whether through base broadening, adjustments to the GST, more effective taxation of economic rents, or a reduction in concessions—ultimately reflects a policy choice about how the fiscal adjustment associated with this debt profile is to be shared.



This graph shows that Australian Government debt remained relatively stable at around 20 per cent of GDP from the early 1970s through to the mid-1990s, before declining steadily in the lead-up to the Global Financial Crisis as successive budget surpluses reduced public liabilities.

From 2008–09, debt increased as a share of GDP following fiscal support measures associated with the GFC, and has continued to trend upward since, with only a brief decline in 2018–19.

While debt levels are now elevated relative to recent decades and are projected to rise further in the near term, they remain well below historical peaks observed in the post-war period.

Source: Australian Government, Budget Strategy and Outlook: Budget Paper No. 1: 2022–23, p.348.

Rethinking Australia's Tax Mix: Deloitte's Blueprint for Structural Reform

Australia's tax system has long been regarded as relatively efficient by international standards. Yet, as fiscal pressures intensify and the structure of the economy evolves, questions around sustainability, equity and efficiency are becoming more pronounced. Within this context, Deloitte has emerged as a prominent voice advocating for comprehensive tax reform.

Rather than incremental adjustments, Deloitte argues for a rebalancing of the tax base—shifting away from reliance on income taxation towards broader consumption and wealth-based measures. This position reflects both economic orthodoxy and a growing recognition that Australia's current tax settings are increasingly misaligned with long-term fiscal and productivity objectives.

Structural Pressures on the Tax System

At the core of Deloitte's analysis is the interaction between demographic change, expenditure growth and a relatively narrow tax base.

Australia faces sustained increases in government spending, particularly in health, aged care and disability services. At the same time, revenue growth is constrained by slower productivity gains and an overreliance on personal income tax. According to Deloitte's economic commentary, this combination places structural pressure on the Commonwealth budget over the medium to long term.

Compounding this issue is the phenomenon of "bracket creep", whereby inflation pushes taxpayers into higher marginal tax brackets without corresponding real increases in income. While this temporarily boosts revenue, it does so in a manner that Deloitte considers economically inefficient and inequitable.

Rebalancing the Tax Base

Deloitte's central proposition is that Australia's tax mix should be recalibrated to improve both efficiency and resilience.

In economic terms, taxes on labour and capital are generally more distortionary than taxes on consumption. High marginal tax rates can discourage workforce participation and investment, while a narrow consumption tax base limits revenue stability.

Consequently, Deloitte advocates a shift towards:

Broader consumption taxation
Reduced reliance on personal and corporate income taxes
Greater taxation of accumulated wealth

This framework aligns with recommendations from earlier reviews, including the Henry Review, which similarly emphasised the benefits of taxing less mobile bases.

Deloitte supports simplifying the personal income tax system by reducing the number of brackets and lowering marginal rates. Indexation of tax thresholds is also proposed to address bracket creep and provide greater transparency in the tax burden over time.

From a policy perspective, this approach aims to strengthen labour supply incentives while improving horizontal equity.

Corporate Tax and Economic Rents

A notable feature of Deloitte's framework is the proposal for a uniform 20% corporate tax rate, coupled with a mechanism to tax "super profits" or economic rents.

This reflects a shift towards taxing returns above a normal rate of profit, rather than taxing all business income uniformly. In theory, such an approach reduces disincentives for investment while ensuring that excess returns—often linked to market power or resource endowments—are appropriately captured.

This concept has parallels with rent-based taxation models explored by the Productivity Commission and in international tax policy debates.

Goods and Services Tax (GST) Expansion

Deloitte's recommendation to broaden and potentially increase the GST represents one of the more contentious elements of its reform agenda.

Australia's GST base is relatively narrow compared to other OECD jurisdictions, with significant exemptions in areas such as food, health and education. Deloitte argues that broadening the base would enhance efficiency and provide a more stable revenue stream.

However, such reforms would necessitate compensatory measures to address distributional impacts, particularly for lower-income households.

Capital Gains Tax (CGT) Concessions

Deloitte has also proposed reducing the CGT discount for individuals from 50% to 33%.

The current concession is viewed as contributing to distortions in investment decisions, particularly in the housing market, and as favouring capital income over labour income. Reducing the discount would, in Deloitte's view, improve neutrality and broaden the tax base without increasing headline rates.

Inheritance Taxation

Perhaps the most politically sensitive proposal is the reintroduction of an inheritance tax.

Australia is unusual among advanced economies in not levying a broad-based tax on intergenerational wealth transfers. Deloitte contends that this represents a gap in the tax system, particularly in the context of rising wealth inequality.

From an equity perspective, inheritance taxes are seen as a means of addressing intergenerational disparities while allowing for reductions in more distortionary taxes elsewhere.

Efficiency and Equity Considerations

Deloitte's reform framework rests on a dual objective: enhancing economic efficiency while improving fairness.

From an efficiency standpoint, the emphasis is on reducing distortions to work, saving and investment decisions. Lower income and company tax rates are

expected to support productivity and economic growth.

From an equity perspective, the proposed shift towards taxing consumption and wealth seeks to rebalance the distribution of the tax burden. Deloitte argues that the current system disproportionately taxes labour income while under-taxing accumulated wealth.

That said, the distributional impacts of such reforms are complex and would require careful policy design, particularly in relation to GST expansion and inheritance taxation.

Political and Practical Constraints

Despite the economic rationale underpinning Deloitte's proposals, implementation remains challenging.

Reforms to the GST and the introduction of inheritance taxes have historically faced strong political resistance in Australia. Similarly, changes to CGT concessions and corporate taxation are likely to generate significant stakeholder debate.

Accordingly, Deloitte acknowledges that any reform pathway would need to be gradual, well-communicated and supported by appropriate transitional arrangements.

Deloitte's contribution to the tax reform debate is notable for its scope and clarity. Rather than focusing on marginal adjustments, it presents a comprehensive framework aimed at addressing structural weaknesses in Australia's tax system.

The underlying message is that the current tax mix, while functional, is increasingly ill-suited to the demands of a modern economy characterised by demographic change, evolving labour markets and growing fiscal pressures.

Whether such reforms are politically achievable remains uncertain. Nonetheless, Deloitte's analysis reinforces a broader consensus within the policy community: meaningful tax reform in Australia will require not only technical precision, but also a willingness to engage with difficult trade-offs.

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Productivity Commission, tax and productivity reports
Australian Treasury, Budget Papers (latest forward estimates)
OECD, Tax Policy Reviews and Consumption Tax Trends

YOU CANT HAVE IT BOTH WAYS: AUSTRALIA'S TAX REALITY CHECK

Australia's tax debate has a habit of avoiding the uncomfortable part.

Everyone agrees on the diagnosis. Spending is rising. The population is ageing. Health, aged care and defence costs aren't going backwards. At the same time, the tax system is doing what it has always done — leaning heavily on personal income tax, quietly boosted by bracket creep.

Yet the conversation still behaves as if none of this requires a real choice.

That's the problem.

Across this journal, different voices circle the same conclusion. The IMF points to a narrowing fiscal buffer. Brennan argues the current revenue model is reaching its limits. The Productivity Commission highlights distortions in how revenue is raised and shared. Deloitte goes further, laying out what a redesigned system might actually look like.

Taken together, they don't describe a system in crisis. They describe a system running out of easy options.

For years, governments have managed the gap between spending and revenue through small adjustments. A tweak here. A threshold shift there.

A reliance on inflation to do the heavy lifting. It works — until it doesn't.

Bracket creep is the clearest example. It raises revenue without a headline decision, which makes it politically convenient. But it also quietly increases the tax burden on working Australians, particularly those in the middle. Over time, it becomes less a feature of the system and more a crutch.

So what replaces it?

That's where the debate gets uncomfortable. Because every serious alternative is visible, immediate, and harder to ignore.

A broader GST makes economic sense. It's more efficient, harder to avoid, and widely used internationally. But it shows up straight away in prices. People feel it. That makes it politically difficult, even if compensation is built in.

Cutting back concessions — whether on capital gains or superannuation — sounds reasonable in principle. In practice, it affects investment decisions, asset values and long-established expectations. The benefits are long term. The backlash is immediate.

Even the idea of taxing wealth more directly, including inheritance, runs into the same wall. Economically defensible. Politically volatile.

This is the core tension. The reforms economists tend to agree on are the same ones voters tend to resist.

Meanwhile, doing nothing isn't neutral. It simply means the adjustment happens in less visible ways — through bracket creep, rising debt, or gradual pressure on services. The cost is still there. It's just less explicit.

There's another layer. Australia's tax system doesn't operate in isolation. State taxes — particularly stamp duties — continue to distort behaviour, discourage mobility and complicate reform. Everyone agrees they should be replaced with land taxes. Almost no one wants to be the one to do it.

So the system holds together, but not neatly.

What makes this moment different is not that these issues are new. It's that they are converging. Spending pressures are rising at the same time as the limits of the current tax mix are becoming more obvious. The space for avoiding trade-offs is shrinking.

At some point, the debate has to shift from how do we improve the system to who actually pays.

Because that is what tax reform is. Not a technical exercise. A distribution decision.

Who carries more of the load? Workers? Consumers? Asset holders? Future taxpayers through higher debt?

There isn't a version of reform where no one notices.

Australia is not facing a fiscal crisis. But it is approaching a decision point.

The system still works. Just not without consequences.

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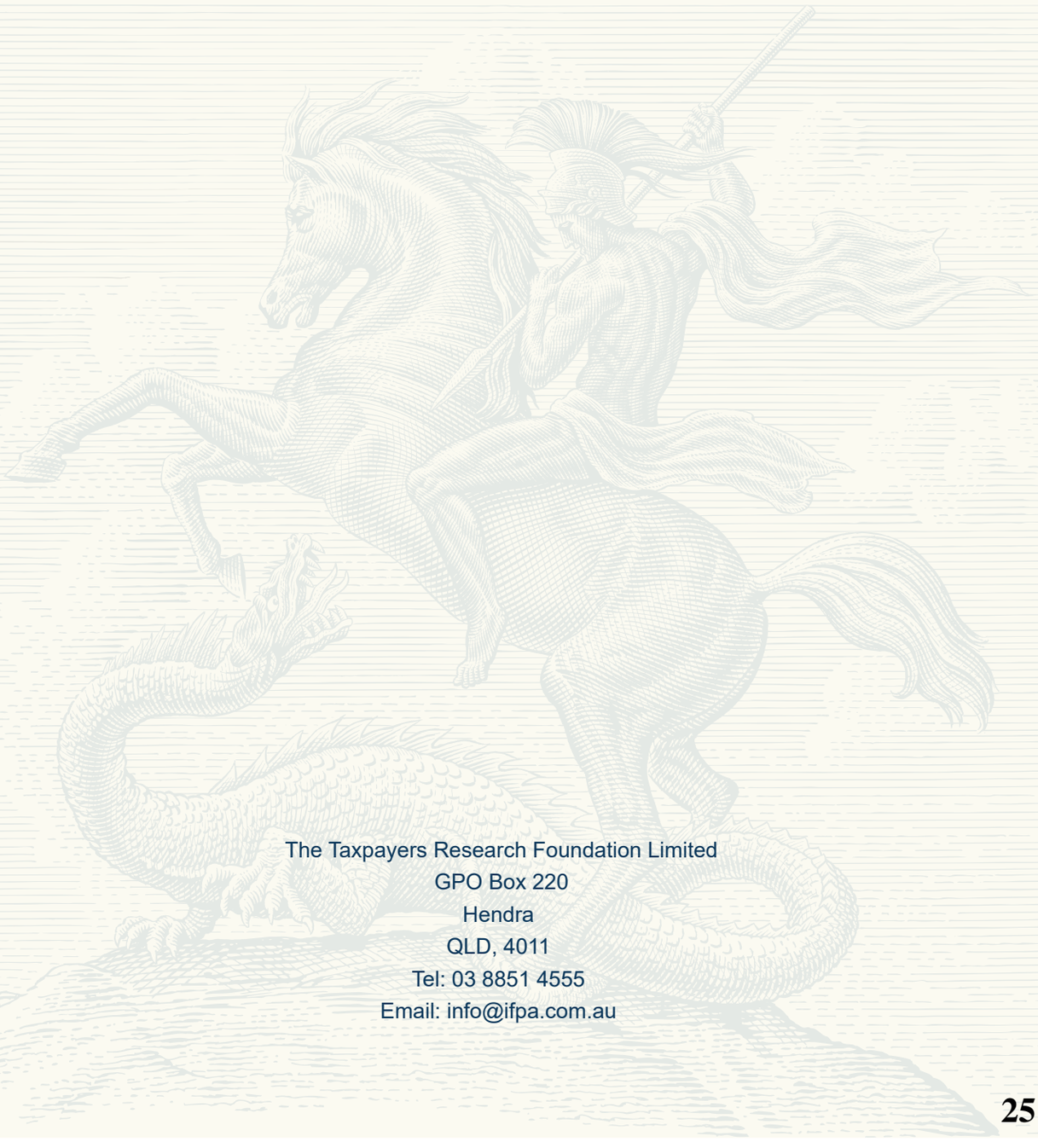

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