



INSTITUTE OF
PUBLIC
ACCOUNTANTS*

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Productivity Commission
GPO Box 1428
Canberra City ACT 2601

By email to: 5pillars@pc.gov.au

Five Productivity Inquiries

The Institute of Public Accountants (IPA) welcomes the opportunity to make a submission in relation to the Productivity Commission's five productivity inquiries.

The IPA is one of the three professional accounting bodies in Australia, representing over 50,000 members and students in Australia and in over 100 countries. Approximately three-quarters of the IPA's members work in or are advisers to small business and small to medium enterprises.

We welcome the Government's commitment to lifting Australia's productivity and the commissioning of these inquiries. Fundamental reforms aimed at boosting the rate of productivity growth are overdue. We urge the Government to take a longer-term view based on a clear, determined and well communicated path for the Australian economy and Australian society.

Our submission focuses on Pillars 1 and 2. Our detailed comments are contained in the following pages.

If you have any queries or require further information, please don't hesitate to contact [REDACTED] at [REDACTED] or on [REDACTED].

Yours sincerely

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Pillar 1: Creating a more dynamic and resilient economy - support business investment through corporate tax reform

The IPA makes the following points in relation to the corporate tax reform project:

- An examination of the corporate tax system should incorporate a review of the personal tax regime, which is integral to the taxation of business profits
- Any reduction to the existing corporate tax rates may result in resident shareholders paying more top-up tax or receiving lower tax refunds due to the imputation system
- Consideration should be given to the tax incentives aimed at encouraging and supporting start-up businesses
- In relation to the small business income tax offset, the maximum offset and the eligibility turnover threshold be increased
- The tax regime should reflect the business lifecycle — with concessions appropriately targeting the risky start-up phase and to encourage the transfer of profitable and productive businesses when owners exit
- A continued use of investment allowances may incentivise investment by reducing the upfront cash flow burden
- The tax system should assist and encourage businesses to invest in intangibles and digitalisation
- The regulatory burden of employment needs to be reduced to encourage businesses to employ high skilled staff, ensure compliance with employment obligations and redirect resources to productive uses.

The relevance of the personal tax regime

Any examination of the corporate tax system should incorporate a review of the personal tax regime. Personal taxation is integral to the taxation of business profits, regardless of the legal structure through which the business operates.

Australian Bureau of Statistics (ABS) data shows that as at 30 June 2024, over half - 57 per cent - of more than the 2.6 million private sector businesses in Australia were operating through sole proprietorships, partnerships and trusts. Companies comprised the remaining 43 per cent.¹

A significant 30 per cent of businesses are sole proprietorships where the business's taxable profits are directly taxed in the hands of the individual carrying on the business in the year the taxable income is derived.

18 per cent of businesses operate through trust structures and 8 per cent operate as partnerships. Trusts and partnerships are generally not treated as separate taxable entities. Taxable profits will often be directly taxed in the hands of the individual partner or beneficiary. (Where there is an interposed company there may be a deferral of personal taxation.)

¹ ABS, Counts of Australian Businesses, including Entries and Exits, June 2020 to June 2024, Table 10.

For the 43 per cent of businesses which operate through companies (and for companies interposed between trusts or partnerships and individual shareholders), the imputation system ensures that corporate profits which are distributed to shareholders at any time - even many years after the profits are derived - will generally be subject to the individual tax regime in the year of the distribution. Although trading companies are separate taxable entities, generally any corporate profits paid out to individual owners, who are Australian tax residents, will bear the individual's effective tax rate, by way of the individual either paying top-up tax or receiving a refund of imputation credits.

Any reduction to the existing corporate tax rates - currently 25 per cent or 30 per cent depending on the financial profile of the company - in the pursuit of encouraging business investment in Australia without a complementary change to the personal tax and/or imputation rules is likely to result in the following implications at the ultimate individual owner level:

- franked dividends will have fewer imputation credits attached
- resident individuals in the three highest tax brackets will generally pay more top-up tax on their dividends (and ultimately pay the same effective tax rate on the underlying company profits as under current law)²
- resident individuals in the lower tax brackets will receive lower imputation credit refunds, i.e. the after-tax return on their shareholding will be reduced compared to current settings³
- non-resident individuals may receive a higher after-tax return than under current law.⁴

A tax system which encourages sustained business productivity must incentivise ultimate owners to take on the risks of their long-term investments along with re-investing profits back into the business.

Issues which may potentially require consideration in a holistic review of the corporate tax system include:

- the rules relating to the quantum of imputation credits which may be attached to distributions
- the refundability of imputation credits
- the impact of the personal and corporate tax regimes, including the imputation system, on decisions for a business to invest in productivity measures
- the impact of the change to a two-tier corporate tax system
- taxation of dividend income flowing through trusts and partnerships
- tax concessions available to individuals carrying on a business
- tax concessions available to investors in start-up businesses.

² Being 30 per cent, 37 per cent and 45 per cent plus 2 per cent Medicare levy (based on current tax rates).

³ Being 16 per cent plus a scaled rate of up to 2 per cent for Medicare levy from taxable income of \$26,000 (\$41,089 if entitled to the seniors and pensioners tax offset), and nil per cent (based on current tax rates).

⁴ Non-residents are not subject to further Australian tax on franked dividends and are not entitled to claim imputation credits. Therefore, a company which pays less corporate tax may distribute the higher after-tax profit as a franked dividend to the non-resident shareholder who is not subject to further Australian tax on the dividend.

Encouraging entrepreneurship

A review of the tax system in relation to its effects on productivity should include a consideration of the tax incentives aimed at encouraging and supporting start-up businesses.

The current small business income tax offset available to sole traders, individual partners, and beneficiaries should be retained. Increases to the maximum offset of \$1,000 and turnover threshold of \$5 million should be considered to encourage more individuals to invest in new businesses or to scale up existing businesses. The former entrepreneurs tax offset had a limit of up to 25 per cent of the income tax liability, whereas the current offset is limited to 16 per cent. The former offset was also available to companies, not only individuals.

The tax regime should also reflect the business lifecycle — in particular, that the start-up phase of a business is in most cases characterised by higher risk of failure, lower profitability and greater need for founders to invest their own time and capital. Options to consider for the initial few years could include:

- reduced tax rates for business entities
- tax offsets for investors
- accelerated capital allowance deductions to ease the cash flow burden of investments
- bonus deductions to encourage particular behaviours or investments.

Tax measures tailored to the other end of the business lifecycle should also be reviewed to ensure that they encourage the transfer of productive and profitable businesses to a new owner. While the small business CGT concessions assist business owners seeking to exit their businesses, the aggregated turnover eligibility threshold of only \$2 million is not reflective of what is considered to be a small business in modern times, and the rules are overly complex and difficult to apply accurately. There are also concessions available in the trading stock, capital allowances and CGT regimes for transfers of business assets, and the going concern GST exemption. The whole suite of these concessions should be reviewed, from the perspectives of both the vendor and the purchaser, to ensure that they are effective in encouraging succession of productive businesses.

Investment allowances

A continued use of investment allowances may incentivise businesses of all sizes and legal structures to invest in capital purchases to drive economic activity, business expansion, improved efficiencies, innovation and productivity by reducing the upfront cash flow burden at a time when an investment may not yet be producing the intended increased revenue or cost savings.

The permanent statutory threshold for the capital allowances immediate deduction for small businesses (known as the instant asset write-off) should be permanently increased from \$1,000. It was introduced in 2015 and has not been increased in 10 years despite the marked rise in the cost of doing business in the same amount of time. All increases legislated by both the Coalition and Labor governments have been temporary, and at times enacted only at the end of the relevant income year. The threshold has not been at \$1,000 since 30 June 2016. A higher permanent threshold would provide businesses with certainty for long-time planning and better reflect modern costs of business.

We also support the continued use of targeted investment allowances which allow for an additional or ‘bonus’ deduction to promote and boost the rate of investment for specific purposes — for example the small business technology investment boost and small business energy incentives which ended on 30 June 2023 and 30 June 2024 respectively. These types of concessions can be used to focus businesses towards areas where more investment is needed.

Investment allowances, bonus deductions and tax offsets should be further utilised to drive investment in specific industries where a need for productivity growth is identified, especially in industries with long lead times before profitability or revenue generation. As examples, the Hydrogen Production Tax Incentive and Critical Minerals Production Tax Incentive were introduced to support the Government’s Future Made in Australia agenda.

Incentivising digitalisation

The PC’s recently released research paper titled *Productivity before and after COVID-19* noted that capital investments can generate labour productivity growth by contributing to growth in the capital-labour ratio or by increasing the efficiency of the production process.

For example, the use of technology in the finance sector led to the development of new financial products, less face-to-face interactions and less dependence on physical offices and workers, which has been linked to productivity growth. In particular, investment in intangibles and information technology may enable innovation in products and processes.

Moreover, intangible capital may have greater spillover effects than traditional forms of capital. If one business invests in intangible capital (e.g. worker skills or new knowledge), the productivity benefits may ‘spill over’ to other workers within the same business and also to other businesses through knowledge transfer and labour movement.⁵

The tax system could and should play a role in assisting and encouraging businesses to invest in intangibles and digitalising operations where such investments are appropriate and likely to lead to improvements in productivity. Depending on the industry this may include using sophisticated software to improve the efficiency of completing rote and repetitive tasks, integrating artificial intelligence into business systems for employee or client/customer interactions improving automated phone answering systems and websites to allow clients/customers to complete routine tasks.

For a tax system to enhance productivity it must encourage businesses to embrace technology and digitalisation for improving business efficiencies. This is particularly the case for micro and small businesses which generally have less access to capital and other resources for digitalisation than larger businesses.

⁵ PC research paper, *Productivity before and after COVID-19*, 28 May 2025, page 19. The report acknowledges that the relationship between intangible capital and productivity growth varies by country, industry and over time, and that pandemic-era investments are not fully comparable to historic investments.

The small business technology investment boost measure for the 2022-23 financial year is one example of such an incentive. Subject to a review of the impact of the measure once data becomes available, a similar investment incentive could be considered for a permanent basis for sustained incentivisation and longer-term planning. A permanent measure could be appropriately targeted and limited, for example, to particular categories of expenditures and/or limited to businesses below a certain turnover threshold.

Any such taxation measure should be accompanied by a broader whole-of-government approach to ensure that new and small businesses have access to free and low-cost expert advice and other resources in how to select, implement and use technology to improve business productivity.

Reducing regulatory burden of employment

Businesses should be encouraged to employ high skilled staff who make a positive contribution to the business's productivity. However the myriad of overlapping regulatory regimes relating to employment is burdensome and costly for businesses and take vital resources away from productive use.

Some relevant aspects of the tax system which we recommend should be considered include the following:

1. Distinguishing between employees and contractors and the burden of employer obligations

The multitude of 'employee vs contractor' rules for the purposes of pay as you go (PAYG) withholding tax, superannuation guarantee and employment law is confusing and difficult for employers to navigate and comply with their obligations. Many aspects of determining whether a worker is entitled to employee entitlements is subject to judicial decisions, ATO interpretations and Fair Work decisions. The large number of awards and agreements also make it difficult for employers even where they have correctly determined that a worker is an employee. Recent wage underpayment scandals involving large supermarket chains and universities indicate that compliance is an issue even for larger businesses with the most resources. A simplification and harmonisation of the rules may reduce the compliance burden and lost productivity for employers, and encourage the hiring of workers.

2. Payroll tax

Aspects of the payroll tax rules have been harmonised to an extent but employers with employees in more than one state/territory still bear a large compliance burden. To reduce this non-productive burden consideration could be given as to whether it may be possible for the compliance to be managed by a central regulator, such as the ATO, so that employers with a national workforce may report and pay once, with the revenue disbursed to the relevant states and territories.

3. Fringe benefits tax (FBT)

FBT is an inefficient tax. In 2021-22 it comprised less than one per cent of the government's total revenue but it imposes a significantly disproportionate compliance cost on employers. Further, for the same year, the net FBT gap estimate was \$1.9 billion or 34.8 per cent — that is, the ATO collects less than two-thirds of the correct FBT liabilities.⁶ The FBT rules have become antiquated and need reforming to reflect contemporary work practices and behaviours.

We believe that shifting the taxation of benefits from employers to employees, in conjunction with simpler valuation principles, would provide a more equitable solution to many of the current problems.⁷ Taxing fringe benefits at the employee level has the potential to deliver greater neutrality in the treatment of cash and non-cash remuneration while reducing the compliance costs for both employers and employees. The Henry Review⁸ supported such a proposal (see Recommendation 9). Removing the FBT burden from employers would eliminate a major source of business inefficiency and non-productivity and allow employers to divert the resources to more productive uses.

⁶ ATO, *Fringe benefits tax gap — Latest estimate and trends*, 1 November 2024.

⁷ Refer to the IPA's policy paper *Tax Reform — Time to Act* (January 2025) for more detail.

⁸ *Australia's Future Tax System Review Final Report*

Pillar 1: Creating a more dynamic and resilient economy - reduce the impact of regulation on business dynamism

Given the economic significance of the small business sector, it has the potential to positively influence productivity growth. Australian small businesses operate in an increasingly complex global environment of increased interconnectedness, interdependence, uncertainty, and change. For this reason, and others, the sector requires support to become more innovative and efficient, to employ more people and to export more. There is an urgent need to ease the disproportionate regulatory compliance burden on small business and SMEs.

Data from the Australian Small Business and Family Enterprise Ombudsman (ASBFEO) reveals a disturbing trend: their contribution to GDP has plummeted from 40per cent in 2006 to just 33per cent today, while their share of private sector employment has fallen from 53per cent to 42per cent⁹.

Summarised below are a number of recommendations regarding reducing the regulatory impact on small business, along with a proposal for a 'one-stop shop' government, which could provide a range of support services for small business and assistance to navigate a range of state and federal agencies they may need to interact with.

Regulatory burden overload

Consideration needs to be given to easing the regulatory burden on small businesses. Complex and excessive regulations are stifling growth, hindering innovation, and making it increasingly difficult for small businesses to remain competitive.

Nearly half of our small businesses are operating at a loss, and the majority of self-employed business owners earn less than the average full-time wage, which is unsustainable.

Without meaningful reform, compliance costs will keep rising, limiting their ability to invest in growth, create jobs, and contribute to economic prosperity.

Regulatory compliance continues to be one of the most significant challenges for small businesses, consuming valuable time and resources that could be better spent on expansion and productivity. A simplified, risk-based regulatory framework would allow SMEs to focus on driving innovation and job creation rather than being bogged down by unnecessary red tape.

Designing a regulatory framework with small business at the forefront is a would provide an opportunity to restore small business productivity. A 'small-first' risk-based approach would ensure low-risk businesses are not subjected to disproportionate scrutiny, allowing them to focus on operations rather than bureaucratic hurdles.

Simplifying tax, employment, and financial reporting regulations would make compliance more manageable and less time-consuming,

⁹ ASBFEO, Small business is in decline and it is a big deal, February 2025.

Aligning Australian regulations with global best practices, particularly OECD standards, would improve efficiency and international competitiveness. Moreover, establishing a system of periodic reviews would ensure that regulatory agencies remain accountable for the regulatory burden they impose on businesses.

Recommendations

1. A 'risk-based' approach to regulation is applied, so individuals and entities that are at a 'low risk' of non-compliance are not subjected to inappropriate and unnecessary regulatory scrutiny. The EU style 'small first' approach should be adopted¹⁰.
2. The government contribute to and be guided by the work of the OECD in enhancing global awareness of and applying good regulatory practice.
3. Meaningful and genuine periodic reviews are conducted of regulatory agencies/bodies and statutory boards to ensure that public interest is well served. Despite numerous reviews, taskforces and so on, there is only minor improvement, if any, in the overall regulatory burden placed on small business and all business in general.
4. The Office of Impact Analysis is adequately resourced to undertake genuine evidence-based cost-benefit analysis, and that its work should not be impacted by political imperative.
5. Consideration is given to the role of regtech (technology-based solutions applied to regulatory compliance) and facilitate the introduction, development, and application of regtech solutions (especially by small business) as a means of easing the regulatory burden.

Establishing a small business assistance agency

Consideration be given to the establishment of an Australian national small business agency similar to the US Small Business Administration (SBA) agency, which would support the growth and sustainability of the nation's economically vital small and medium-size enterprises (SME) sector.

Created in 1953, the US SBA agency helps 'small business owners and entrepreneurs pursue the American dream'. It is the only Cabinet-level federal agency fully dedicated to small business and provides counselling, capital, and contracting expertise as the nation's only go-to resource and voice for small businesses. Its resources for small business are extensive, providing business guides, funding programs (loans, investment capital, disaster assistance, grants, surety bonds), federal contracting, a learning platform, and advocacy. There is also local assistance – contracting, access to capital, export and trade assistance, resource partners and so on.

Its strategic goals include ensuring equitable and customer-centric design and delivery of programs to support small businesses and innovative startups, and specifically, to 'build a thriving national innovation ecosystem that promotes investments in all small business communities'.

¹⁰ <https://www.europarl.europa.eu/factsheets/en/sheet/63/small-and-medium-sized-enterprises>

A 'one-stop shop' agency modeled on the SBA could potentially improve productivity by providing a range of support services tailored to small business, such as the following, from a single central source.

- Access to capital
- Business development support
- Access to markets
- Technology and innovation support
- Regulatory assistance
- Disaster recovery.

A more detailed analysis is provided in the IPA Deakin SME Research Centre white paper *The Case for a National Australian Small Business Agency*.

A range of Australian agencies undertake many of these functions, although perhaps not as extensively and not in one place. Despite the support provided by agencies such as the Australian Small Business and Family Enterprise Ombudsman (ASBFEO) and the state based small business commissioners, there is still confusion and complexity in the Australian system.

Bringing these functions and resources into one agency would be of benefit to small business and consumers, making it significantly easier to navigate the plethora of government support.

Pillar 2: Building a skilled and adaptable workforce - Support the workforce through a flexible post-secondary education and training sector

Beyond reforming the post-secondary education system, consideration should be given to supporting workers to undertake further education to build their skills and knowledge, upskill or reskill, along with enabling their employers to support them.

An important lever to enable this would be through tax incentives such as:

- Expanding the tax deductibility rules around education
- reinstating the small business skills and training boost

Expand deductibility rules around education

Consideration should be given to the proposal to allow individuals to deduct education and training expenses they incur, where the expense is not related to their current employment but is intended to lead to a different income-earning avenue.

In the 2020-21 Budget, the former Government announced that it would consult on allowing individuals to deduct education and training expenses they incur, where the expense is not related to their current employment. We are supportive of initiatives that encourage individuals to continue upgrading their human capital skills over their working life. In an ever-changing labour market, few expect a job for life, and it is more likely that individuals will have multiple careers over their lifetime. The increased rate of globalisation and technological change are other drivers that are contributing to the need for continued upgrading of skills. Our current tax settings do not support or encourage the retraining and reskilling of individuals once they have commenced earning an income in their chosen field.

There are a number of existing support mechanisms for higher education. This reform would add to the current support for higher education but also addresses a void in the existing arrangements for individuals who are currently earning an income and may be unable to access any of the existing support initiatives. For this cohort, the existing tax arrangements represent a deterrent to reskilling. In particular, the requirement for a tax deduction is limited to expenses in gaining or producing assessable income. This limits deductions to an individual's current employment activities that either maintain or improve the specific skills required for that employment or lead to an increased income in the individual's current employment. Education expenses that do not have a sufficient connection to an individual's current employment are therefore not deductible.

This proposal could work hand in hand with the exemption for FBT employer-provided education. Since October 2020, employer-provided retraining and reskilling benefits to redundant, or soon-to-be-redundant, employees where the benefit may not relate to their current employment are exempt from FBT. This allows the employer to bear the cost of retraining and reskilling without incurring FBT. To provide equity to individuals who do not have employer support for reskilling or retraining, it is important to extend a similar tax concession to individuals who undertake further education at their own cost. The benefit to an individual of incurring the cost themselves will, however, be dependent on the individual's marginal tax rate.



There are wellbeing and economic benefits that quality education skills provide, which generally outweigh the cost of providing further support. There is a strong business case for providing additional support, especially if it is directed to areas where there is a skills shortage. Many skilled individuals have been displaced and can be easily redeployed into other less affected sectors with retraining. The proposal also bodes well for individuals who wish to continue to work but for a number of reasons may not be able to do so (ie physical limitations, age, mental burnout), or where the Australian need for their experience has been or will be greatly reduced (e.g. car manufacturing) and need to reskill to remain in the workplace. There are a lot of occupations where the physical demands of the job cannot be sustained beyond a certain age, and therefore, retraining offers an opportunity to extend an individual's working life. This is particularly relevant if we are looking at a tsunami of baby boomers approaching retirement in the near future. We need to look at ways to add to the supply side of the labour market, and this proposal, if properly targeted, can contribute to adding capacity where it is needed. Increasing the ability to claim deductions comes with a cost and therefore there needs to be integrity measures to ensure the proposal achieves good economic outcomes worthy of the tax concession.

ABS data indicates that the job mobility rate (i.e. the rate at which Australians changed jobs) was 8 per cent in the year to February 2024 having fallen from 9.6 per cent in the previous 12 months, with younger workers (aged 15 to 24) being more mobile. Further, the University of Queensland ('How many career changes in a lifetime?' published 19 June 2023) notes that an average person may accumulate around 16 jobs in their lifetime, representing between 3 and 7 careers. Significantly, this number may be more like 5 to 7 for the current and upcoming generations. It is no longer a society in which it is common to have one job or profession for life. Changing jobs and careers is now a characteristic of the Australian workforce. Government policy that financially supports workers in reskilling will encourage more people to contribute to a new chosen industry and to the Australian economy.

Reinstate the small business skills and training boost

In relation to training and education related to an individual's current employment, consideration should be given to the small business skills and training boost being reinstated. This incentive previously provided a bonus 20 per cent deduction for eligible expenditure incurred from March 2022 to June 2024. This will encourage employers to pay for their existing employees to upskill, thereby bridging an identified skill gap in the business, or allowing the business to deliver higher value services and offer new revenue-generating services.

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