

AUSTRALIA'S UNPRECEDENTED WORKER SHORTAGE: CAUSES AND SOLUTIONS



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Executive Summary

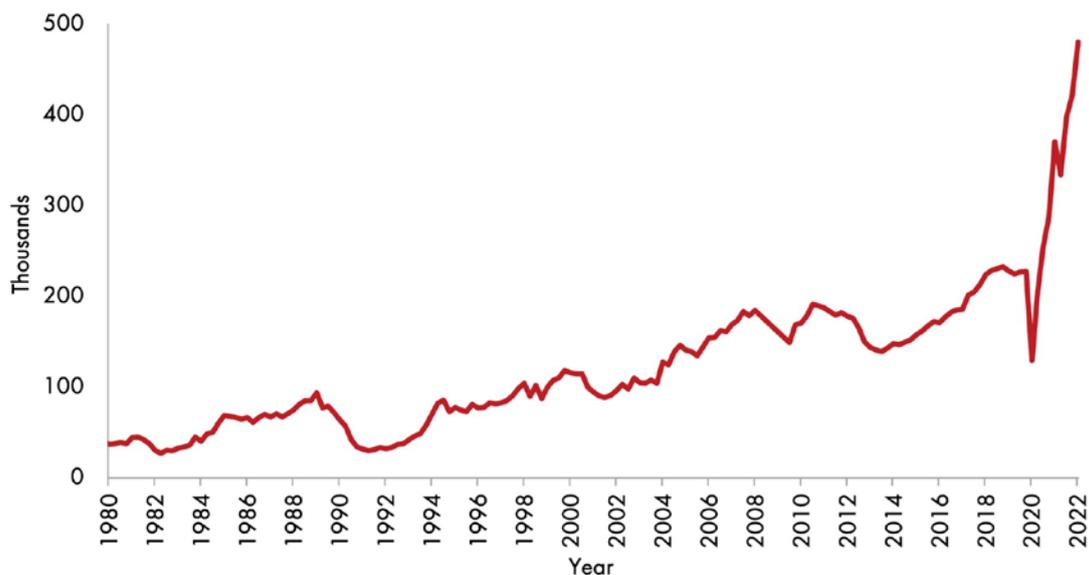
- Australia is currently facing an unprecedented, country-wide shortage of workers, with advertised job vacancies having increased by 270 per cent over the two years from May 2020 to May 2022 (most recently available data). Urgent government action is needed to resolve this shortage.
- More than one quarter of businesses across Australia have reported experiencing labour shortages.
- There are a range of costs associated with labour shortages, including forgone investment, output, and economic growth.
- One cost which has been overlooked is the forgone direct income tax revenue associated with labour shortages.
- Preliminary research by the Institute of Public Affairs estimates that the current level of worker shortages has resulted in \$32.2 billion forgone worth of wages and is costing the federal government \$6.62 billion each year in forgone income tax revenue, which is the equivalent to approximately 3 per cent of personal income tax raised in 2021-22.
- There are a number of policies available to governments to address worker shortages, one of which is to reduce the financial disincentive facing Australian pensioners returning to work.
- On 4 August, Senator Dean Smith introduce a private members bill into the senate, *Social Services Legislation Amendment (Enhancing Pensioner and Veteran Workforce Participation) 2022* which proposes to double the Work Bonus available to age pensioners from \$300 to \$600 per fortnight
- The scheme was estimated to have a direct annual fiscal cost of approximately \$145 million. However, the scheme could pay for itself:
 - Currently only 3 per cent (75,000) of the 2.55 million Age Pension recipients are in paid work.
 - Only 3,713 out of the 1,701,256 Australians currently receiving the maximum age pension would need to enter the workforce on the average weekly salary for the policy to pay for itself in terms of the direct fiscal benefits. This equates to a 0.21% increase in workforce participation.

Introduction

Australia is currently facing an unprecedented, country-wide shortage of workers. This is undermining economic output and growth by limiting the ability of businesses to meet their production, and as a result there are flow-on effects on wages and government revenue.

Addressing this worker shortage should be a high priority for state and federal governments. Australia's international borders have been re-opened since the beginning of 2022, yet worker shortages are still increasing, with the Australian Bureau of Statistics reporting 480,100 job vacancies in the May 2022 quarter. More than a quarter of businesses across the country report being affected by this issue.¹

Chart 1: Job vacancies across Australia



The three industries which are affected most by worker shortages are:

- Health Care and Social Assistance (69,000 worker shortage)²
- Accommodation and food services (52,000 worker shortage)³
- Professional, Scientific, and technical services (43,000 worker shortage)⁴

1 Australian Bureau of Statistics, "Job Vacancies, Australia, May 2022," June 2022, <https://www.abs.gov.au/statistics/labour/jobs/job-vacancies-australia/may-2022>.

2 Australian Bureau of Statistics, "Job Vacancies, Australia, May 2022," June 2022, <https://www.abs.gov.au/statistics/labour/jobs/job-vacancies-australia/may-2022>.

3 Ibid

4 Ibid

Table 1: Three Industries Most Affected By Worker Shortage

Industry	Job Vacancies: May 2020 (000's) ⁵	Job Vacancies: May 2022 (000's)	% Increase
Health Care and Social Assistance	19.7	68.9	250%
Accommodation and Food Services	5.0	51.9	938%
Professional, Scientific and Technical Services	13.1	42.9	227%

Further increasing migration is not an adequate solution. According to data reported in the *Australian Financial Review*, of the almost 60,000 permanent visa applications the government is fast-tracking to address the worker shortage, only 438 are health professionals, and just 32 are registered aged care nurses.⁶ At a time where an estimated one quarter of aged care shifts are going unfilled,⁷ there is a clear need for a more effective solution. Rather than taking the short-sighted option of simply further increasing migration, governments should immediately change policy settings to allow for greater workforce participation. One of the most obvious solutions lies in changing the current rules surrounding the ability of pensioners to work if they choose to. Currently, pensioners can earn only \$300 per fortnight before their pension payments are reduced. This is the equivalent to working only six hours a week on the current minimum wage. Senator Dean Smith recently introduced a plan to the senate to double the Work Bonus available to age pensioners to \$600 per fortnight.⁸

This is a step in the right direction, and the federal government should immediately adopt the expanded Work Bonus to allow pensioners to re-join the workforce or increase their hours of work if they so choose.

According to the most recent data available from the Department of Social Services, in March 2022, there were 75,706 Age Pension recipients who had earnings from employment. This is just 3% of the 2.55 million Age Pension recipients.⁹

In other words, 97% of Age Pension recipients in Australia do not work.

Australia's policy settings surrounding working pensioners provide significant disincentives for work. Once pensioners earn more than \$480 per fortnight, their pension is withdrawn at a rate of 50 cents in the dollar. This is an effective marginal tax rate (EMTR) of 50%, and increases rapidly as income tax thresholds kick in. Pensioners who want to work more face disincentives, and their EMTR can quickly move to 69% and above.

5 Ibid

6 David Marin-Guzman, "Of 60,000 visa applicants in the queue, 32 are aged care nurses," *Australian Financial Review*, 24 July 2022, <https://www.afr.com/work-and-careers/workplace/of-60-000-visa-applicants-in-the-queue-32-are-aged-care-nurses-20220724-p5b419>.

7 Sarah Martin, "Absolutely a crisis: almost a quarter of Australia's aged care shifts unfilled each week," *The Guardian*, 3 February 2022, <https://www.theguardian.com/australia-news/2022/feb/03/absolutely-a-crisis-almost-a-quarter-of-australias-aged-care-shifts-unfilled-each-week>; ACIL Allen, "Implications of Labour Shortages in the Aged Care Sector, Final Report," December 2021, https://acilallen.com.au/uploads/projects/445/ACILAllen_ImplicationsLabourShortagesWA_2022.pdf.

8 Social Services Legislation Amendment (Enhancing Pensioner and Veteran Workforce Participation) Bill 2022, August 2022 https://parlinfo.aph.gov.au/parlInfo/download/legislation/bills/s1347_first-senate/toc_pdf/22S0620.pdf;fileType=application%2Fpdf

9 Department of Social Services, "DSS Payment Demographic Data," March 2022, <https://data.gov.au/data/dataset/dss-payment-demographic-data>.

To provide international context, in New Zealand pensioners do not face high EMTRs if they choose to work. They simply pay income tax on those earnings. As a result, according to data from the OECD, the labour force participation rate in New Zealand is 24.8%. Similarly, the comparable participation rate is 35.3% in South Korea and 25.5% in Japan.¹⁰

The direct fiscal cost for FY22-23 of doubling the Work Bonus is estimated to be \$145 million.¹¹

However, this fiscal cost will be more than offset through higher tax revenues which result from having more Australians working and earning a wage.

Previous IPA research found that Australia's total worker shortage sees \$32 billion in forgone wages each year.¹²

The forgone wages are causing a reduction to direct income tax revenue to the federal government of \$127.2 million per week, or \$6.62 billion per year.

This estimate is based on the current level of worker shortages (proxied by advertised job vacancies), and the associated forgone wages and therefore forgone income tax revenue.

Specifically, the calculation is based on the following methodology, with all data obtained from the Australian Bureau of Statistics:

- The number of job vacancies per industry is multiplied by the average wage rate for that industry, to derive the total forgone wages from the job vacancies.
- The forgone wages by industry are then multiplied by the average personal income tax rate to estimate the total forgone income tax from the current level of worker shortages.
- Job vacancy data was taken from the ABS' *Job Vacancies, Australia* dataset.¹³ Average wages data were taken from the ABS' *Average Weekly Earnings, Australia* dataset.¹⁴ Foregone personal income tax revenue was calculated based on average per worker weekly earnings in each industry using the Australian Taxation Office's weekly tax table.¹⁵

In addition to the income tax revenue would be other revenue gains, for example through payroll tax, GST, and second-round effects associated with the higher consumer spending resulting from more people being employed.

10 OECD, "Labour force participation rate," OECD Data, <https://data.oecd.org/emp/labour-force-participation-rate.htm>.

11 Peter Dutton, "Older Australians Should Keep More of What They Earn," (2022) <https://www.peterdutton.com.au/older-australians/>

12 Daniel Wild, "Australia's Worker Shortage See's \$32 Billion In Wages Lost", Institute of Public Affairs, August 2022, <https://ipa.org.au/publications-ipa/media-releases/australias-worker-shortage-sees-32-billion-in-wages-lost>

13 Australian Bureau of Statistics, "Job Vacancies, Australia, May 2022," June 2022, <https://www.abs.gov.au/statistics/labour/jobs/job-vacancies-australia/may-2022>.

14 Australian Bureau of Statistics, "Average Weekly Earnings, Australia, November 2021," February 2022, <https://www.abs.gov.au/statistics/labour/earnings-and-working-conditions/average-weekly-earnings-australia/nov-2021>.

15 Australian Taxation Office, "Weekly tax table", <https://www.ato.gov.au/rates/weekly-tax-table/>.

The Pension System

Under the current system, a pensioner can receive a maximum of \$493.80 a week on the age pension. If an age pensioner earned the average weekly salary of \$1,328.90¹⁶ a week as per the ABS, they would:

- Receive no pension, as half of the pensioner's income after the \$245 work bonus and income test free threshold is taken off the \$1,328.90 is over \$493.80.
- Pay income tax on the \$1,328.90 they earned at a weekly rate of \$276.
- Have a post-tax income of \$1,052.90 a week.

Under the Pension Work Bonus plan, the \$490 fortnightly income ceiling before the pension starts to be reduced at 50% for every extra dollar earned will be increased to \$790.

The average weekly salary of every employed Australian is \$1,328.90. If a pensioner who was not working previously and received the maximum pension of \$493.80 a week entered the workforce and earned the average weekly salary of \$1,328.90, the combined weekly work bonus and income test free of \$395 would be deducted, leaving \$933.90. Then 50c from each dollar would be clawed back through reduced pension payments, reducing their pension from \$493.80 to \$26.85. The pensioner's taxable income would then be the sum of the remaining pension and the \$1,328.90, this is an effective weekly rate of \$284.¹⁷

The pensioner would have \$1,071.75 in post-tax income per week. Regarding pensioners who would earn the average salary regardless, this would result in \$980.20 in additional disposable income annually.

¹⁶ Australian Bureau of Statistics, "Average Weekly Earnings, Australia, November 2021," February 2022,

¹⁷ Australian Taxation Office, "Weekly tax table", <https://www.ato.gov.au/rates/weekly-tax-table/>

Financing The Work Bonus Plan

If a pensioner shifts from just receiving the maximum pension to earning an average salary under the proposal, it will result in a net benefit to the budget of \$750.95 per week per pensioner, equal to \$39,049.40 annually per pensioner. This is comprised of the reduced amount of pension paid and the income tax received.

The direct cost of the expanded Work Bonus scheme is estimated to be approximately \$145 million per year.

What this means is that only 3,713 out of the 1,701,256 Australians currently receiving the maximum age pensions would need to enter the workforce for the policy to pay for itself. This equates to a 0.21% increase in workforce participation.

Unlocking this potential workforce is vital during the current worker shortage. In addition, it will provide economic benefits in the longer term, and help to address structural issues Australia faces with an aging population.

A Deloitte Access Economics report published in 2012 found that if Australia were to achieve a 3-percentage point increase in mature age participation over and above that currently, annual economic output would be \$33.0 billion, or 1.6%, larger. A 5-percentage point increase would lead to a \$47.9 billion, or 2.4%, boost to GDP.

Adjusted for inflation, the latter is equivalent to about \$60 billion today. A recent survey from National Seniors found that 20% of pensioners would consider re-entering paid work, in addition to the 16% who already have.¹⁸ This implies that up to an additional 510,000 pensioners could consider re-entering the workforce.

Table 2: Worker Shortages By State

State	Job Vacancies: May 2020 (000's) ¹⁹	Job Vacancies: May 2022 (000's) ²⁰	% Change	Total Pensioners (000's) ²¹
Australia	129.2	480.1	272%	2,554
NSW	39.8	145.1	265%	791.9
Victoria	28.7	120.1	318%	601.8
Queensland	25.2	78.6	212%	511.4
South Australia	6.8	24.5	260%	216.7
Western Australia	16.8	65.2	288%	240.2

¹⁸ National Seniors Australia, "Why pensioners want to work," 14 April 2022, <https://nationalseniors.com.au/news/featured-news/why-pensioners-want-to-work>.

¹⁹ Ibid

²⁰ Ibid

²¹ Department of Social Services, "DSS Payment Demographic Data," March 2022, <https://data.gov.au/data/dataset/dss-payment-demographic-data>.

Further Reform Opportunities

The work bonus proposal is a promising first step onto greater reform that is required to motivate more pensioners to work amidst this labour shortage crisis. There are three further reform options which could also be pursued.

Double the proposed bonus from \$600 to \$1,200 per fortnight

One potential policy is doubling the work bonus from the proposed \$600 to \$1,200 a fortnight. Pensioners earning the weekly average salary would have a taxable income of \$1,505.75 a week, which would be taxed at \$337 a week²² and have a post-tax income of \$1,168.75 a week. Compared to the current proposal, the pensioner would have \$5,044 more in disposable income annually that can be invested into their local communities and economies. The federal government would have an annual net benefit of \$34,005.40 for each pensioner that shifted from earning the maximum pension to earning the average weekly salary.

Halve the pension reduction rate

A different policy could be to half the rate at which the pension is reduced from 50c of the dollar after the work bonus to 25c of the dollar. Applying the current work bonus and income free test threshold of \$245, if a pensioner earned the average weekly salary of \$1,328.90, they would have a taxable income of \$1,551.73 with a weekly tax rate of \$353.²³ This is a post-tax income of \$1,198.73 a week and, compared to the current proposal, equals to \$6,602.96 more in annual disposable income. The annual net budget benefit arising from the sum of less pension paid and more income tax received would be \$32,446.70.

Remove the pension claw-back altogether

Lastly, the federal government could remove the work bonus system all together, and have pensioners pay income tax on the combined pension and earned income total over the tax bracket. Under this scenario, if a pensioner earned the average weekly salary, they would just pay income tax on the combined \$1,328.90 and \$493.80 at a weekly rate of \$446.²⁴ This would leave pensioners with a weekly income of \$1,376.70 and have \$15,857.40 more in annual disposable income compared to the current proposal.

22 Australian Taxation Office, "Weekly tax table", <https://www.ato.gov.au/rates/weekly-tax-table/>

23 Ibid

24 Ibid

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The IPA supports the free market of ideas, the free flow of capital, a limited and efficient government, evidence-based public policy, the rule of law, and representative democracy. Throughout human history, these ideas have proven themselves to be the most dynamic, liberating and exciting. Our researchers apply these ideas to the public policy questions which matter today.

About the authors

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