



Further Submission to the Productivity Commission Inquiry into the Greater Use of Charges to Determine the Intake of Entrants to Australia

Thank you for providing the opportunity to provide a submission on your draft report on the migrant intake into Australia.

Our comments focus on the Commission's Technical Supplement B, but we expect that if they were accepted, the discussion, findings and potential recommendations in the final report would be substantially altered relative to the draft report.

Specifically, we consider that the Commission's assertion that imposition of an immigration tariff would lead to a less productive mix of migrants is substantially driven by unjustified assumptions.

Access to welfare

The terms of reference require the Commission to examine a scenario involving the provision of limited access to social security or subsidised education, housing or healthcare to migrants. The draft report does not examine such a scenario. This not only represents a failure to comply with the terms of reference and a lost opportunity to inform the public of alternatives, but misrepresents the immigration policy of the Liberal Democrats.

To comply with the terms of reference, to fully inform the public of alternatives, and to avoid further misrepresentation, the final report should examine the scenario set out in the terms of reference.

A scenario in which there is limited access to social security or subsidised education, housing or healthcare should not be dismissed as politically unacceptable. It is not the role of the Commission to make political assessments.

Moreover, such a scenario should not be discounted at all. Australian governments currently restrict access to social security as well as subsidised education, housing and healthcare for tourists, other temporary residents and permanent residents in the initial period of their residency. Prior to World War Two Australian governments did not provide social security and subsidised education, housing and healthcare comparable to current systems. Moreover, numerous countries differentiate between citizens and other residents when providing access to various government services.

A scenario involving limited access to social security or subsidised education, housing or healthcare could involve refugees and pre-existing residents maintaining access as per current arrangements.

It would be entirely feasible for non-refugee migrants to gain access to various social security payments after ten years of residency and achievement of citizenship, for which ten years' residency, the successful completion of a basic citizenship test in English, evidence of likely continued employment or means to support themselves, links to the Australian community and no criminal record could be prerequisites.

It would also be feasible for non-refugee migrants to gain access to the age pension after twenty years of residency and achievement of citizenship. Exceptions could apply for migrants from countries with which we have an International Social Security Agreement.

Access for non-refugee migrants to public schooling prior to ten years of residency and achievement of citizenship could be subject to existing charging arrangements for certain temporary visa holders in various states and territories (e.g. <http://www.detinternational.nsw.edu.au/media-assets/trp/fees.pdf>).

Non-refugee migrants could gain access to public housing after ten years of residency and achievement of citizenship, at least for 'general' rather than 'priority' applicants. Note that public housing waiting times for general applicants exceed 10 years in many jurisdictions (e.g. <http://www.housingpathways.nsw.gov.au/NR/rdonlyres/9C300EE3-F53A-46C9-A43B-48A8CBA05003/0/2015EWTOverviewtable.pdf>).

Non-refugee migrants could be denied access to Medicare until ten years of residency and achievement of citizenship unless a reciprocal health care agreement applies. At present Medicare is not available for most temporary non-refugee residents. Eligibility for the Pharmaceutical Benefits Scheme would continue to be tied to eligibility to Medicare.

Baseline demand

The Commission states that 'the number of secondary applicants attached to each primary applicant was fixed' (page 10).

This and other factors driving the mix of immigration should not be fixed. If a charge were imposed on each migrant, the number of migrating secondary applicants for each primary applicant would fall, and the skills and youthfulness of migrating secondary applicants would increase, making the mix of immigrants more productive.

Additional demand and the currently ineligible

The Commission apportions additional demand (i.e. extra demand if the marginal costs of migration were zero) across skill categories based on the skill profile of the regions rather than the skills of recent immigrants from those regions. The Commission states that 'this approach was taken because many potential migrants who want to come to Australia do not meet current qualitative requirements'.

The Commission appears to do this for all categories of migrant, not just the 'currently ineligible' migrant. This is inappropriate. For example, to the extent that removal of the marginal costs of migration would prompt extra demand from potential migrants currently

eligible under the points-tested category, this extra demand would consist of migrants with a skills profile similar to recent points-tested migrants.

More broadly, the assumption that migrants in any category would have the skills-profile of their region of origin fails to account both for the high minimum wage in Australia and the unavailability of unemployment payments and other government benefits for non-refugee migrants under the scenario that should be modelled. These factors would lift the skills profile of potential migrants above the profile of their region of origin.

The Commission should explicitly discuss and assess the income-earning prospects of currently-ineligible migrants. The Commission should take account of a distribution of income-earning prospects, rather than just an average. The Commission should assess some currently-ineligible migrants as having greater income-earning prospects than migrants currently eligible under skills streams, in acknowledgement that bureaucracy is not perfect in selecting the skills with the greatest income-earning potential, or in verifying that approved migrants actually have those skills.

The Commission should also recognise that currently-ineligible migrants include those skilled migrants whose starting wage in Australia would fall between Australia's minimum wage and the income threshold for skilled migration, and who would enjoy significant wage growth thereafter.

Maximum willingness to pay based on income factors

Willingness to pay of secondary applicants

The Commission states that 'potential income earned by secondary applicants, such as spouses, has not been considered, which is likely to understate willingness to pay'. More importantly, such an approach will fail to differentiate the combined willingness to pay of a primary applicant accompanied by a skilled and young secondary applicant, from the combined willingness to pay of a primary applicant accompanied by an unskilled and old secondary applicant.

Proper consideration of the varying skills and ages of secondary applicants is fundamental to an analysis of a tariff-based immigration system. At a minimum, assumptions should be made about the skills and age of secondary applicants, and secondary applicants should be separated into two groups for the purpose of analysis: low-skill and old secondary applicants, and high-skill and youthful secondary applicants.

Such analysis would change the mix of secondary applicants under a tariff-based system, with more having skills and youth. It would also boost the aggregate willingness to pay of all potential migrants, boosting tariff revenue for a given migrant intake.

Distribution of income

The Commission states that 'each migrant was assigned the average income difference depending on their characteristics (region of origin, visa category, skill level and age). The distribution of income for particular types of migrants has not been considered explicitly' (page 13).

The failure to explicitly consider the distribution of income for particular types of migrants would likely have the effect of artificially reducing the share of migrants who are productive in Australia, and the aggregate willingness to pay of all potential migrants, and tariff revenue for a given migrant intake.

- Currently the Commission uses ad hoc, after-the-fact fixes to explain why any ‘type B’ people apply to migrate to Australia, when the average income on offer at home is the same as, or higher than, the average income on offer in Australia. Explicit consideration of the distribution of income would lead to a more robust explanation. For example, even if the average income on offer in the US to a group of people matched that on offer in Australia, for around a quarter of the Americans in that group, the actual US income on offer could fall short of the actual Australian income on offer. Using this approach, such ‘type B’ migrants would be coming to Australia for the money (rather than the lifestyle, as the Commission essentially assumes at present), and would make Australia more productive than the Commission currently assumes.
 - In some instances, the maximum willingness to pay of ‘type B’ migrants could even exceed the level imposed by the Commission after its ad hoc after-the-fact fixes. In such instances, the aggregate willingness to pay of all potential migrants would be boosted, leading to boosted tariff revenue for a given migrant intake.
- Similar improvements in productivity in Australia and tariff revenue would also seem likely if the distribution of income were explicitly considered for ‘type A’ migrants.

Income prospects in different currencies

The Commission appears to convert future income streams in two economies into the one currency simply through the use of current purchasing power parity exchange rates. However, not all income is consumed, and purchasing power parity and market exchange rates should converge over time.

As such, some consideration of current (and possibly forward) market exchange rates would seem appropriate. Such consideration would tend to increase the maximum willingness to pay of skilled migrants from developing countries.

Some impacts on willingness to pay from the deviation from the terms of reference

The Commission states that ‘migrants are assumed to have the average labour market outcomes of the cohort that they age into’. This reflects the Commission’s failure to model the scenario set out in the terms of reference, wherein all migrants would have the right to work and have limited access to social security or subsidised education, housing or healthcare. Modelling should reflect this scenario, so that the rate of unemployment among migrants would be reduced relative to what has been modelled to date.

The Commission also states that ‘the Australian Government Actuary (2008) estimated that the lifetime costs to government of Contributory Parent Visa holders was between \$232,000 and \$284,000 per entrant. A midpoint of this range has been used to proxy the value of government payments and services available in Australia.’

The use of such a value is inappropriate given the requirement to model a scenario involving the provision to migrants of limited access to social security or subsidised education, housing or healthcare. Instead, the expected income differential for such potential migrants should be used.

This would serve to further shift the mix of migration towards more skilful, youthful and productive migrants.

Maximum willingness to pay based on non-income factors

In a discussion of family migration that would also apply to the Commission's analysis of currently ineligible migrants, the Commission states that 'the greater role of non-income factors for these groups means that they are less likely to be deterred by price'.

This is wrong and raises significant concerns about the Commission's modelling.

Individuals in the skilled stream of migration have significant variations in the income differentials attracting them to Australia. This should lead to a steep demand curve for skilled migrants and a view that such demand is inelastic and 'less likely to be deterred by price'.

Individuals in the family stream of migration do not have significant variation in the income differentials attracting them to Australia. This should lead to a flat demand curve for family migrants and a view that such demand is elastic and *more* likely to be deterred by price.

For non-income factors to generate inelastic demand, there would need to be a view that some potential migrants in a group put an extremely low value on Australia's safety, climate and lifestyle while others place an extremely high value on these things. Such a view lacks credibility and has not been argued by the Commission.

Moreover, for this inelasticity-generating phenomenon to arise with respect to family migration but not with respect to skilled migration, the appreciation of non-income factors amongst potential family migrants would need to differ wildly from the appreciation of non-income factors amongst potential skilled migrants. There is no basis for believing in such differences between potential family migrants and potential skilled migrants in the appreciation of Australia's safety, climate and lifestyle.

Supply curves

The Commission appears to assume different migration agent costs (as a proxy for migration compliance costs) for different classes of migrant. Presumably such compliance costs are higher for skilled migrants than for family reunion migrants, given that demonstrating that you have the required skills is more difficult than demonstrating that you have the required family connection. If the Commission's modelling does not reflect the higher compliance costs that skilled migrants would seem to face, the Commission should reconsider its reliance on migration agent costs as a proxy for compliance costs.

However, the Commission does not appear to reduce these migration agent costs upon the introduction of the scenario where skill and family pre-requisites are removed. This is a flaw,

as applying to migrate would be markedly simpler, and subject to far less uncertainty, if skill or family criteria do not need to be demonstrated. Compliance costs should be dropped to a uniformly low level for all classes of migrant upon the introduction of the scenario.

This reduction in compliance costs would directly translate into increased tariff revenue for any given level of migration.

There should be particularly low confidence in the marginal cost calculations given the reliance on migration agent costs and the crude assumption that all migrants face the same transport costs. However, the Commission arbitrarily rotates its demand curves so that real world behaviour aligns with the marginal cost calculations.

In the process the Commission effectively jettisons its more robust calculations on income-based maximum willingness to pay and additional demand. A likely consequence of this approach is to artificially boost demand by non-skilled migrants, and so increase non-skilled migration under the modelled scenario.

Discount rates

In assessing the willingness of skilled migrants to pay an immigration tariff and migrate to Australia, the Commission discounts the extra income a skilled migrant could expect to earn in Australia compared to in the migrant's home country, by 10 per cent each year in the central case.

This discounting depresses the maximum willingness to pay of skilled migrants, which serves to shift the mix of migration under the modelled scenario away from skilled migrants. Reducing the maximum willingness to pay of skilled migrants also serves to reduce the overall willingness to pay of all migrants, which reduces immigration tariff revenue.

In contrast, when assessing a trade-off between early immigration tariff revenue and later fiscal costs¹, the Commission only discounts the later fiscal costs by 3 per cent each year in the central case.

The use of this 3 per cent discount rate in the central case is flawed and not supported by Harrison 2010 — despite the citation of this work — or in earlier work by the Commission (Best Practice Regulation Handbook 2007) or Department of Finance (Handbook of Cost Benefit Analysis 2006).

Consider a \$40,000 immigration tariff, the payment of which would entitle a potential migrant to government payments equivalent to \$300,000 in thirty years' time. If the Government allowed a migrant to migrate on this understanding, incumbent Australians would be taxed \$40,000 less than would otherwise be necessary. The incumbent Australians could invest that \$40,000 so as to have an investment worth \$700,000 in thirty years' time (using a rate of return on capital of 10 per cent).

¹ Many of these fiscal costs should not be included given the requirement to model a scenario where migrants are provided only limited access to social security or subsidised education, housing or healthcare.

Even after the incumbent Australians pay the tax required to fund government payments to the migrant equivalent to \$300,000 in thirty years' time, the incumbent Australians, other things being equal, would be better off because of this migration. This suggests that such a cost-of-capital-based discount rate should be used when considering the trade-off between early immigration tariff revenue and later fiscal costs.

Each of the aforementioned works recommends the use of such cost-of-capital-based discount rates where government investment (in this instance, forgoing \$40,000 by not introducing an immigration tariff) comes at the expense of private investment (a \$40,000 private financial investment).

Each of the aforementioned works also recommend against assumptions that government investments are risk-free. A government's decision to not pursue immigration through an immigration tariff may reduce government welfare payments in the future, but this is hardly a risk-free proposition. In particular, each of the aforementioned works dismisses the use of risk-free discount rates simply because governments can assign risk to taxpayers.

None of the aforementioned works recommend the use of different discount rates within the same study for the same time period.

And none recommends that a special approach is warranted when the project in question can be cast as involving short-term *revenue* and long-term *expenses*.

Migrating elsewhere

The Commission refers to potential migrants migrating elsewhere upon the introduction of an immigration tariff in Australia. This assumes that other countries do not increase immigration charges in the years and decades ahead, despite fiscal difficulties and rising concerns about people flows.

The Commission should include modelling of an alternative assumption wherein other countries increase immigration charges.