

Regressing on tax

The tax cuts announced in the budget will make Australia's income tax system less progressive, hand billions to high income earners and for every dollar in tax cuts to females, males will get two dollars

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The centrepiece of this budget is large income tax cut that builds on the large income tax cuts in the last budget. Together, these cuts represent over \$300 billion in lost revenue over 10 years and a radical reshaping of the purpose of income tax. Income tax in Australia has been a progressive tax where those on higher incomes pay a larger proportion of their income in tax. This funded universal services like health and education.

The government's income tax plan would fundamentally change this, making income tax flatter and less progressive. If this income tax plan comes into effect, it will mean that in the future those on higher incomes will pay less tax as a proportion of their income and the amount of income tax collected will be far less. The consequences will be less revenue for essential government services. These are the same services that are relied on by both the rich and poor.

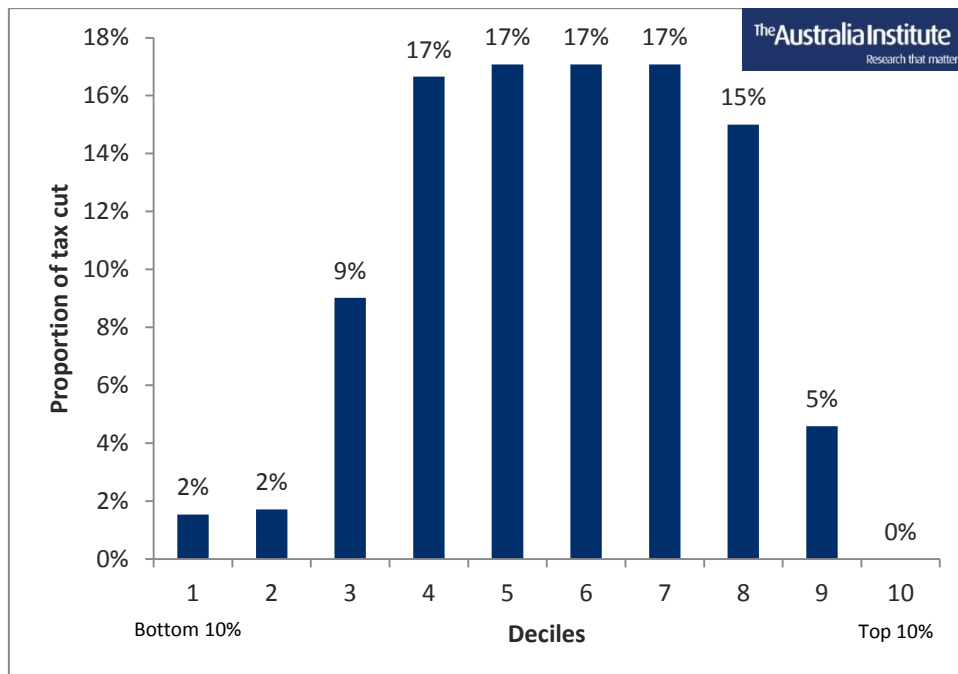
The government's tax plan has two parts. The first part is tax cuts for low and middle income earners that begins at the end of this financial year and expires in 2021-22. The second part is a radical flattening of the income tax scales that begins after 2022-23 and will be fully implemented by 2024-25.

TAX CUTS FOR MIDDLE INCOME EARNERS

The first part of the government's tax plan is the Low and Middle Income Tax Offset (LMITO). This is a tax refund paid after middle income taxpayers submit their tax returns. The distribution of these tax cuts is well targeted at mainly middle income

earners. If we look at who this will benefit in 2019-20 we can see that the majority of the benefits go to the middle of the income distribution. This is shown in Figure 1.

Figure 1 – Distribution of changes in LMITO in 2019-20



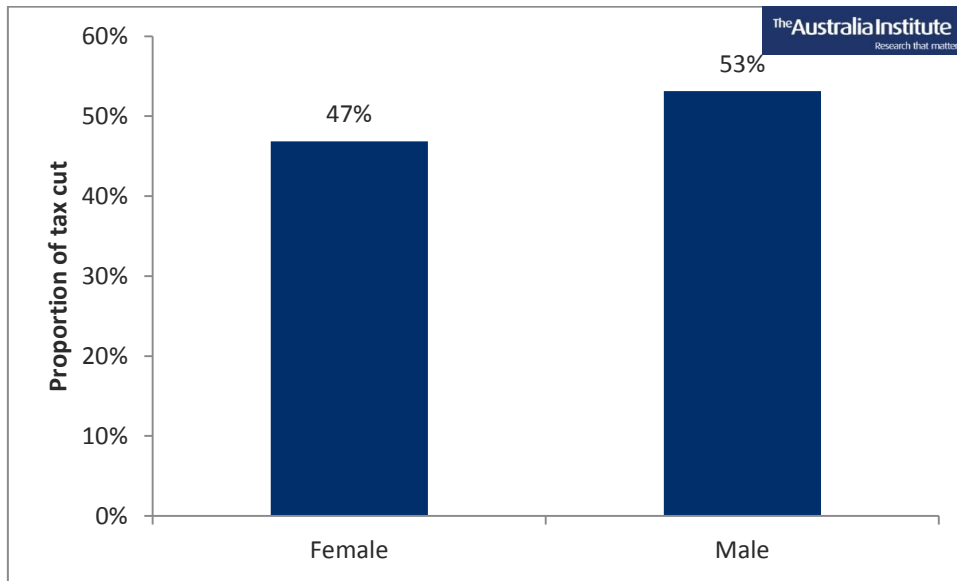
Source: Budget Paper 2, 2019-20 and author calculations (see Appendix 1: Method)

Figure 1 breaks down taxpayers into 10 equal groups called deciles. The first decile consists of the 10 per cent of taxpayers on the lowest income. The second decile consists of the next lowest income taxpayers and so on until the 10th decile consists of the top 10 per cent of taxpayers.

We can see that over 80 per cent of the tax cut goes to the 50 per cent of taxpayers between the 4th and 8th decile. The top 20 per cent get less than five per cent of the tax cut although this is still more than the bottom 20 per cent get.

The gender split of this part of the tax cut is fairly even with females getting 47 per cent of the tax cut and males are getting 53 per cent of the tax cut.

Figure 2 – Gender distribution of LMITO in 2019-20



Source: Budget Paper 2, 2019-20 and author calculations (see Appendix 1: Method)

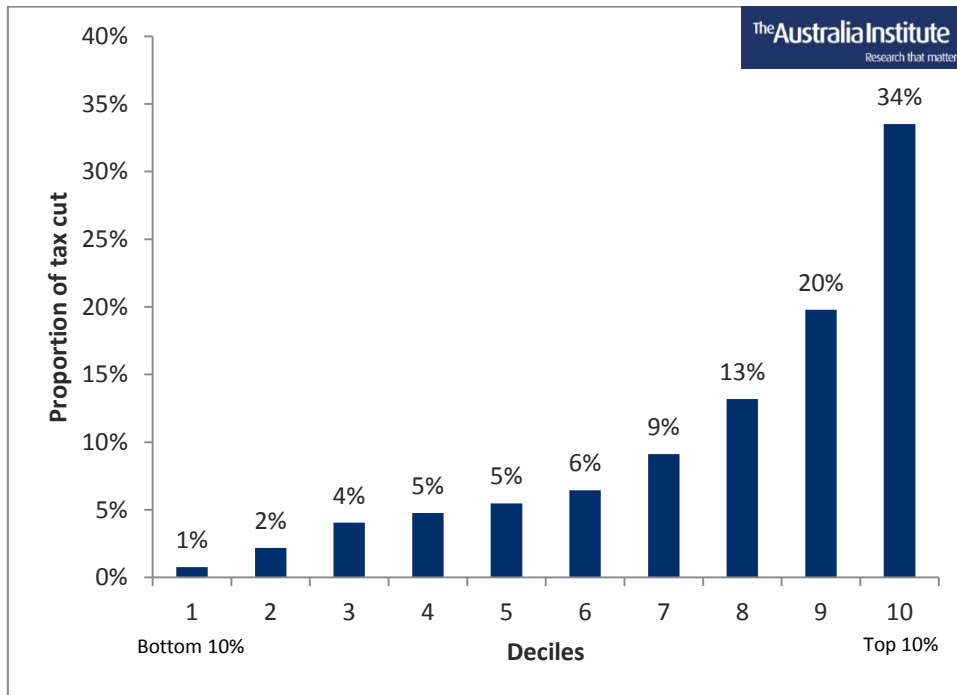
THE PRICE OF FLATTENING INCOME TAX SCALES

The second part of the proposed tax cut, which will be fully implemented in 2024-25, will see the removal of the 37 cent tax bracket and a decrease in the 32.5 cent tax bracket to 30 cents. It will also remove the LMITO and replace it with an expanded Low Income Tax Offset and an increase in the 19 cent tax bracket from \$37,000 to \$45,000.

Who benefits from these changes in 2024-25 is very different to the LMITO. A third of the benefit of flattening the tax scales will go to the top 10 per cent of taxpayers, with more than half going to the top 20 per cent. At the other end of the distribution the bottom 10 per cent get less than one per cent of the benefit while the bottom 30 per cent get only seven per cent of the benefit.

The income distribution is shown in Figure 3.

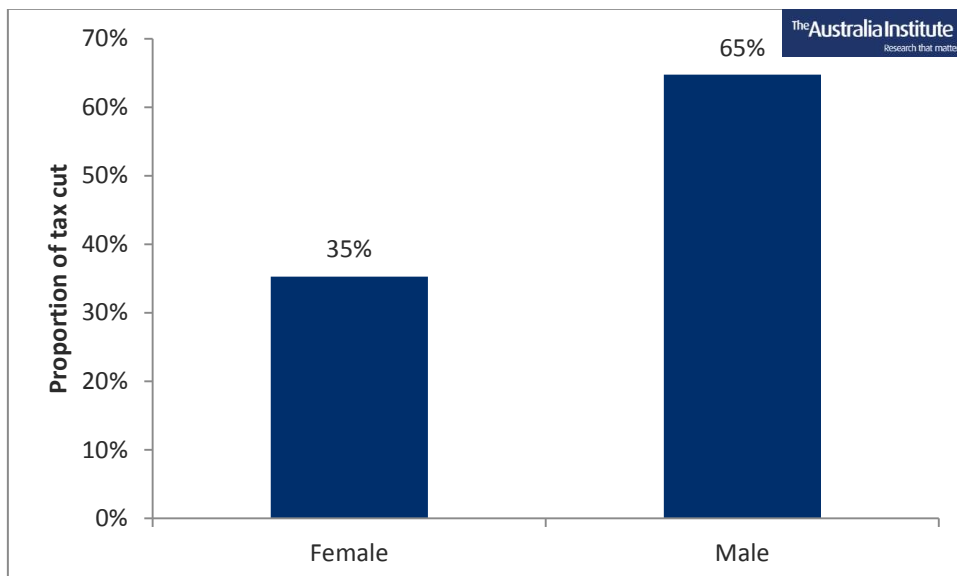
Figure 3 – Income distribution of tax cuts in 2024-25



Source: Budget Paper 2, 2019-20 and author calculations (see Appendix 1: Method)

The gender distribution from flattening the tax scales is also very skewed. For every dollar of tax cuts females get, males get two dollars.

Figure 4 – Gender distribution of tax cuts in 2024-25

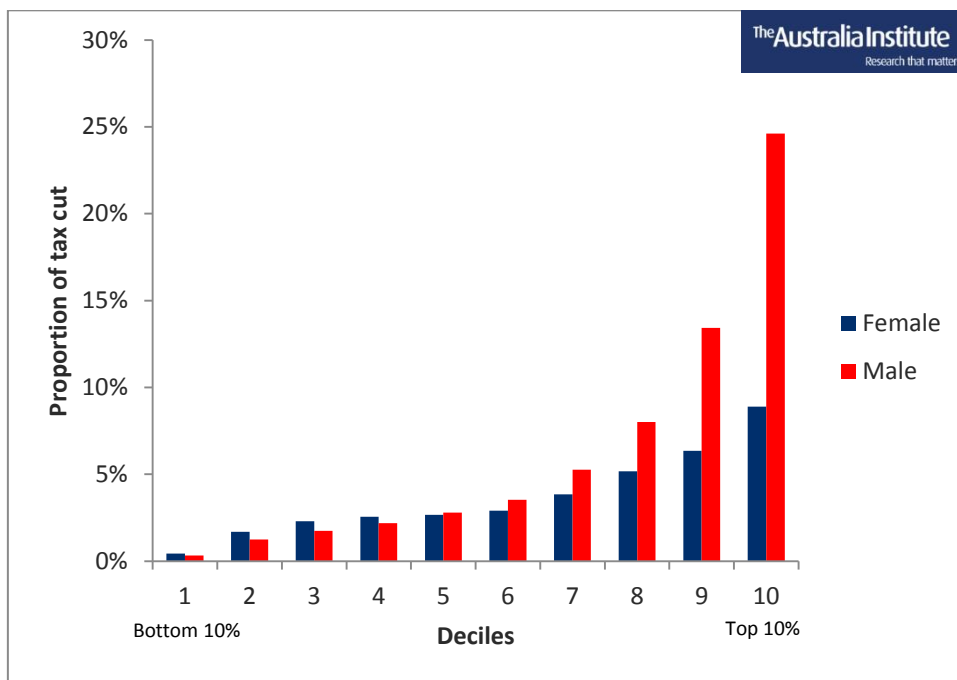


Source: Budget Paper 2, 2019-20 and author calculations (see Appendix 1: Method)

The skewed gender distribution is in large part because males are over represented at the top of the income distribution, who get most of the benefit of the tax cut, and females are over represented at the bottom of the income distribution, who get very little of the tax cut. The gender pay gap is already an issue in Australia, and income tax cuts that favour males over females will only further widen the gap in post-tax income of males and females.

Figure 5 looks at the gender distribution of the tax cuts by decile. We can see that females get more benefit than males for the first four deciles, but these deciles get very little of the overall benefit. As we move up into the higher decile of the income distribution males get an increasingly larger share than females. In the top decile males get almost three times more benefit than females.

Figure 5 – Income distribution of the tax cuts by gender in 2024-25



Source: Budget Paper 2, 2019-20 and author calculations (see Appendix 1: Method)

CONCLUSION

What the LMITO shows us is that the government can focus tax cuts to middle income earners with a fairly even gender distribution. But the LMITO makes up only a small part of this tax cut plan. The overwhelming majority of it is targeted at high income earners as the government reduces the progressive nature of the income tax rates by flattening the income tax scales.

This will not come cheaply. While the full cost of all the income tax changes in 2019-20 are expected to be less than \$8 billion, the full cost of the tax cuts in 2024-25 are expected to be well over \$35 billion. The tax cuts over the next 10 years are going to cost the budget more than \$300 billion.

Large income tax cuts during the mining boom reduced the budget's ability to generate revenue for more than a decade. The subsequent budget deficits have been used by the current government as a reason to cut spending. If it is implemented, the tax plan in the budget will reduce the government's ability to generate income into the future. This could well be used by future governments as an excuse to cut and refuse government services that the Australian public demand.

APPENDIX 1: METHOD

We have calculated the benefit of the tax cut flowing to females and males and by income deciles using the latest taxation statistics. Using the taxation statistics we have constructed a model of Australia's income tax system. We then broke down all taxpayers into 100 groups from the lowest income earners to the highest and the proportion of females and males in each group. By inflating income by nominal GDP and calculating how much tax each group pays as the income tax cut is introduced, we then calculated how much of the tax cut went to each income decile and how much went to female and male recipients.