

# High income earners the big winners from scrapping 37% tax bracket

***High income earners will get 80% of the benefit from removing the 37% tax bracket and 60% of taxpayers will get no benefit.***

***By Matt Grudnoff, May 2018***

In the 2018 Budget, the government announced a radical plan to reshape the income tax system over the next seven years. While the first stage of the plan largely involves tax refunds for low and middle income earners, stage two and three would remove the 37 per cent tax bracket – and, as a consequence, flatten Australia’s tax system.

Part of stage two and all of stage three would increase the 32.5 per cent tax threshold from \$90,000 to \$200,000 and remove the 37 per cent tax bracket. When the plan is fully implemented in 2024-25, it would mean that someone on \$41,001 would face the same marginal tax rate as someone on \$200,000 and 83 per cent of all taxpayers would be in the same tax bracket.

Previous Australia Institute modelling shows that if all three stages of the tax package were implemented, the benefits would go overwhelmingly to high income earners – with 62 per cent going to the top 20 per cent of tax payers.<sup>1</sup>

Stage one of the tax plan, which mainly benefits low and middle income earners, appears to have enough support to pass the parliament. The Labor Party supports this part of the government’s tax plan.<sup>2</sup> The Labor Party has yet to announce support for stage two and three of the plan and so there is still doubt about whether this part of the plan will pass.

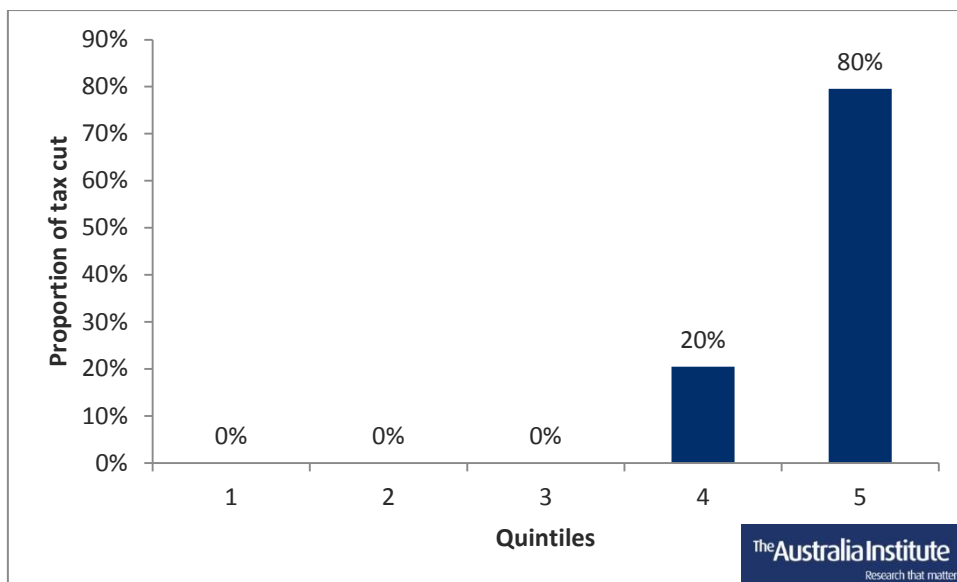
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<sup>1</sup> Grudnoff M (2018) *Radical plan to increase inequality in Australia revealed in the budget*, The Australia Institute, 10 May, available at <<http://www.tai.org.au/content/62-tax-cuts-benefits-go-highest-income-earners>>

<sup>2</sup> Bagshaw E (2018) *Tax cuts set for delay as Coalition, Labor fail to agree on third stage*, SMH, 24 May, available at <<https://www.smh.com.au/politics/federal/tax-cuts-set-for-delay-as-coalition-labor-fail-to-agree-on-third-stage-20180524-p4zh8m.html>>

The Australia Institute has modelled just the income distributional impacts of increasing the 32.5 cent threshold from \$90,000 to \$200,000 and the removal of the 37 cent bracket. This represents part of stage two and all of stage three of the government’s tax plan. The results are shown in Figure 1.

**Figure 1: Benefit of removing 37 per cent tax bracket by quintile in 2024-25**



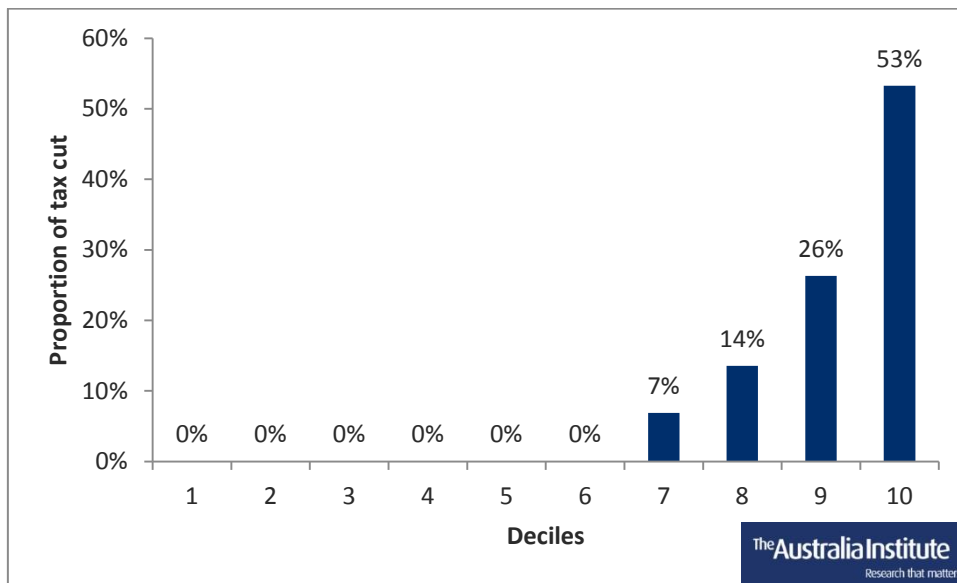
Source: ATO (2018) *Taxation Statistics 2015-16* and Australia Institute calculations

Quintiles split taxpayers into five equal groups based on their incomes. The bottom 20 per cent of taxpayers are in the first quintile, the next 20 per cent are in the second quintile, and so on until you have the highest 20 per cent of income earners in the fifth quintile.

As Figure 1 shows, the top quintile of taxpayers (the top 20 per cent) gets 80 per cent of the benefit from removing the 37 per cent bracket. The next 20 per cent of taxpayers receive the rest of the benefit. The remaining 60 per cent of taxpayers get no benefit.

If we split taxpayers into smaller groups, we can look at the benefit of removing the 37 per cent tax bracket by decile. Deciles are like quintiles, but break taxpayers into 10 equal groups rather than five. The benefit of getting rid of the 37 per cent tax bracket by decile is shown in Figure 2. It shows that just 10 per cent of taxpayers get over half the benefit of the tax cut.

**Figure 2: Benefit of removing 37 per cent tax bracket by decile in 2024-25**



Source: ATO (2018) *Taxation Statistics 2015-16* and Australia Institute calculations

The government’s budget papers look at the impact of policy changes over the next four years. They show that the cost of the income tax cuts will be \$13.4 billion over that four year period.

The problem is that the tax plan makes changes over seven years, and the significant part of the tax cut starts in the fifth year – just outside the forward estimates. These final three years of the tax plan, which cost the budget significantly more than the first four years, were not subject to the same level of scrutiny because they do not fall within the budget forward estimates.

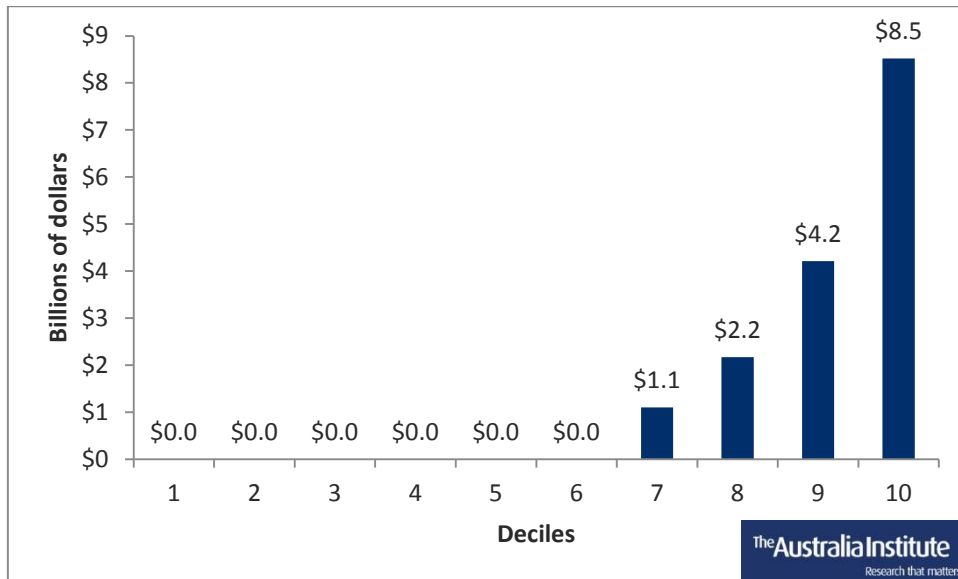
The only information that the government initially released about the impact of the tax plan beyond the forward estimates was the expected cost to the budget over 10 years – which is \$140 billion. The government refused to release more detail at that time.

More recently, the government has relented and announced that the 10 year figure has increased to \$144 billion and that stage one and two will cost \$102 billion over 10 years. We can deduce that stage three will cost \$42 billion over 10 years – but since stage three does not start until the seventh year, in fact that \$42 billion cost is for just four years. The government continues to refuse to provide a year by year breakdown of the 10 year figures.

In the absence of this information from Treasury, various organisations – including The Australia Institute – have modelled the income tax cuts in order to calculate their impacts. This modelling shows that in 2024-25 the removal of the 37 per cent tax bracket will cost the budget \$16 billion.

The distribution of this benefit by decile is shown in Figure 3.

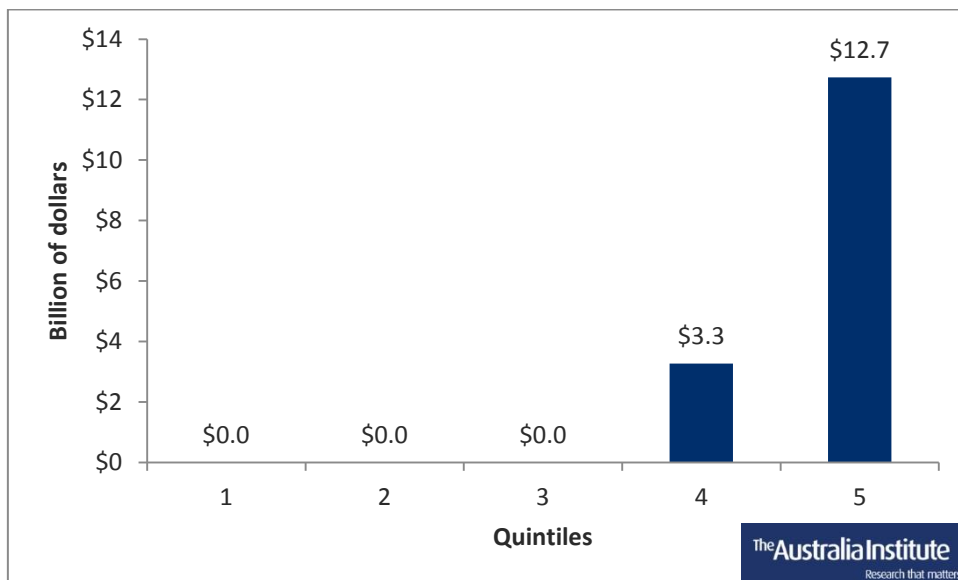
**Figure 3: Benefit of removing 37 per cent tax bracket by decile in 2024-25**



Source: ATO (2018) *Taxation Statistics 2015-16* and Australia Institute calculations

Figure 3 shows that, in 2024-25 alone, the top 10 per cent of taxpayers will get \$8.5 billion from the tax cut. The top 20 per cent will get \$12.7 billion, as shown in Figure 4.

**Figure 4: Benefit of removing 37 per cent tax bracket by quintile in 2024-25**



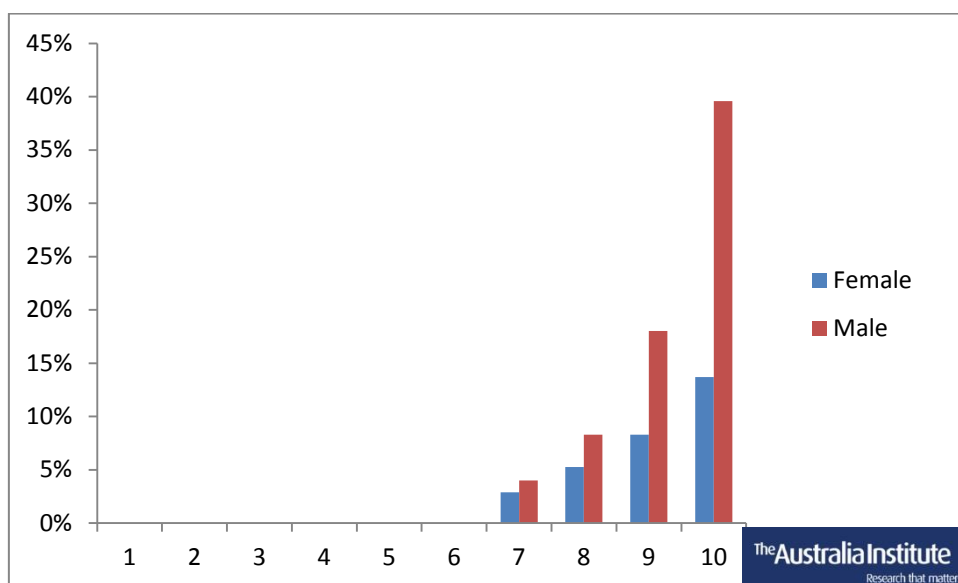
Source: ATO (2018) *Taxation Statistics 2015-16* and Australia Institute calculations

## Gender distribution of removing 37 per cent tax bracket

Men are overrepresented among high income earners. Because high income earners receive the greatest share of the benefits, most of the tax cut will go to men. Men will receive 70 per cent of the benefit of the tax cut and women only 30 per cent. For every dollar of the tax cut women receive, men will get \$2.32.

For the year 2024-25, men will receive a tax cut of \$11.2 billion, while women will receive \$4.8 billion. The effect of removing the 37 per cent bracket by gender is shown in Figure 5.

**Figure 5: Benefit of removing 37 per cent tax bracket by quintile in 2024-25**



Source: ATO (2018) *Taxation Statistics 2015-16* and Australia Institute calculations

## Method

We have calculated the benefit of the tax cut by income and by gender 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 identified the proportion of females and males in each group. By inflating income by nominal GDP and population growth we calculated how much each group pays as the income tax cut is introduced. We then calculated how much went to each income decile and quintile and how much of the tax cut went to women and men.

## Conclusion

The parts of the government's income tax plan that are at risk of not passing the Senate are the parts that will overwhelmingly go to high income earners. The government has provided no compelling argument for giving such largesse to so few taxpayers.

The government's tax plan will flatten income tax and make it less progressive. The progressive nature of Australia's income tax has been an important feature for decades. Flattening income tax reduces the tax take from high income earners, which ultimately means either worse government services or higher taxes on middle and low income earners.

These tax cuts will also reduce the government's ability to raise revenue in the future, which will prove unsustainable if the economy slows and government revenues fall. Will a future government be willing to restore income tax rates for high income earners, or will they cut government services?

These tax cuts will also widen the post-tax gender income divide by cutting the tax bill of men far more than women. Gender inequality will get worse until governments start to consider the gender implications of their policy changes.

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