

Tax targets

The Government's unlegislated tax cut proposed for 2024-25 will see \$33 billion over five years flow to those earning over \$180,000 and \$26 billion flow to those earning over \$200,000

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In a previous paper The Australia Institute did an income distributional analysis of stage 3(a) of the tax cuts.¹ This paper will look at the income distributional analysis of stages 1(a) and 2(a). It will also look at a different income distributional analysis of stage 3(a). The previous paper looked at the benefit of stage 3(a) that went to different deciles. This paper will look at the benefit of stage 3(a) going to two fixed income groups, those earning more than \$180,000 and those earning more than \$200,000.

The paper finds that those earning more than \$180,000 will get \$33 billion from the unlegislated stage 3(a) of the tax cut over the five-year period from when it first starts in 2024-25. It also finds that those earning over \$200,000 will get \$26 billion over the same period.

It also finds that about half the benefit from stage 2 and stage 2(a) will go to middle-income taxpayers. High-income taxpayers will get 38 per cent and low-income taxpayers will get just 13 per cent.

Stage 1(a), which is the increase in the LMITO, shows us the Government can target tax cuts at middle-income taxpayers. The benefit of increased LMITO flows mainly to middle income taxpayers. The benefit from the increased LMITO also costs considerably less. It is expected to cost about \$15 billion over four years from 2018-19 to 2021-22. Stage 3(a) is expected to cost \$95 billion over five years from 2024-25 to 2028-29. The increased LMITO will cost the budget less money and proportionately benefit more people.

¹ Grudnoff M (2019) *The distribution of the Government's stage 3(a) tax cuts*, The Australia Institute, 31 May, available at <<http://www.tai.org.au/content/new-analysis-over-50-stage-3a-tax-cuts-benefit-go-highest-income-earners>>

Previous analysis by The Australia Institute showed that at least \$77 billion would go to those on more than \$180,000 per year.² This was from all of stage 3, both the legislated part (stage 3) and the unlegislated part (stage 3(a)). The same analysis showed that at least \$64 billion would go to those earning more than \$200,000.

THE COMBINED TAX PLAN

The Government is hoping to expand the tax cuts it legislated last year. Just like last year's tax cut plan, this latest plan has three stages. Each stage in this new plan expands a stage in the currently legislated tax cut plan.

The Government's tax plan has been put forward in the 2018 budget (2018 tax plan) and expanded on in the 2019 budget (2019 tax plan). The 2018 tax plan has already been legislated. None of the additional tax cuts in the 2019 tax plan have yet been legislated. The 2018 tax plan had three stages.

Stage 1: This part of the plan comes into effect in 2018-19. It introduces a Low- and Middle-Income Tax Offset (LMITO) for a four-year period from 2018-19 to 2021-22. It also increased the threshold for the 32.5 per cent personal income tax bracket from \$87,000 to \$90,000.

Stage 2: This stage comes into effect in 2022-23, the year that the LMITO ends. It increases the Low-Income Tax Offset (LITO) which increases the maximum rate from \$445 to \$645. Stage 2 also increases the 19 per cent personal income tax bracket from \$37,000 to \$41,000. It also increases the 32.5 per cent personal income tax bracket from \$90,000 to \$120,000.

Stage 3: This stage comes into effect in 2024-25. It increases the upper bound of the 32.5 per cent personal income tax bracket from \$120,000 to \$200,000, which eliminates the 37 per cent personal income tax bracket and increases the threshold at which the top tax bracket of 45 per cent begins (previously it started at \$180,001, now it starts at \$200,001).

The 2019 tax plan introduces an expansion to the 2018 tax plan. It made changes to all three stages of the tax plan. For simplicity we will call these unlegislated stages 1(a), 2(a) and 3(a) to differentiate them from stages 1, 2 and 3 in the 2018 tax plan.

² Grudnoff M (2019) A bit rich: A Government plan to makes tax less progressive, The Australia Institute, 18 April, available at <<http://www.tai.org.au/content/new-analysis-77-billion-goes-those-earning-over-180000>>

Stage 1(a): This increases the amount of money available through the LMITO, increasing the maximum payment from \$530 to \$1080. The period that the LMITO has been legislated for (the four years 2018-19 to 2021-22) remains unchanged.

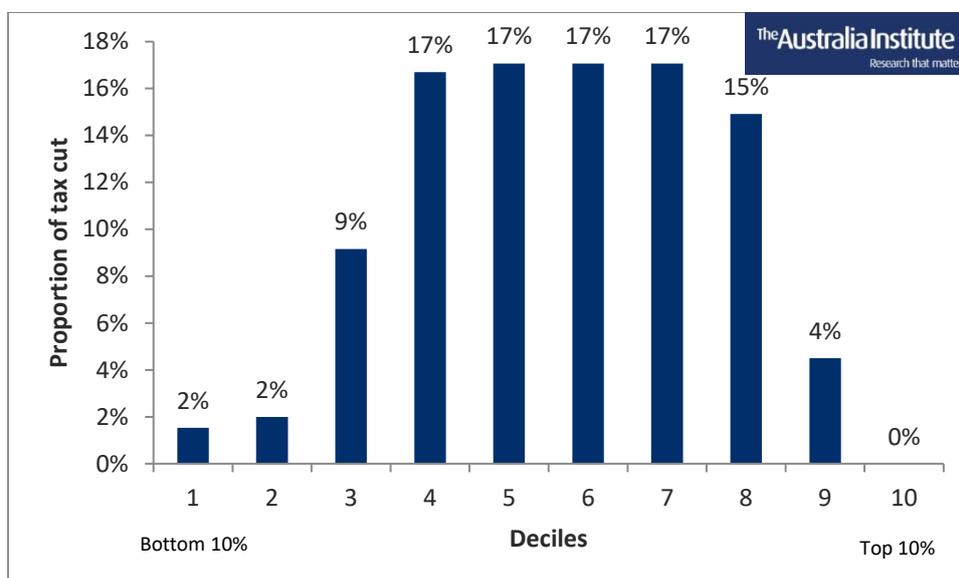
Stage 2(a): This stage still comes into effect in 2022-23. It increases the LITO further, so the maximum rate is now \$700 (stage 2 increased it to \$645). It adds to the increase in the 19 per cent personal income tax bracket by increasing it to \$45,000 (stage 2 increased it to \$41,000).

Stage 3(a): This stage decreases the 32.5 per cent personal income tax rate to 30 per cent.

DISTRIBUTION OF STAGE 1(A)

Stage 1(a) of the tax cut plan, which enjoys bi-partisan support, is far more targeted at middle income earners. This part of the plan is an extension of the LMITO and lasts for four years from 2018-19 to 2021-22. Figure 1 shows the distributional impacts of stage 1(a) by decile in the first year it is in place, 2018-19.

Figure 1 – Income distribution of stage 1(a) in 2018-19



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

Most of the tax cut goes to middle-income taxpayers. We split taxpayers into three groups, low-income, middle-income and high-income taxpayers. Low-income taxpayers are those in the bottom 30 per cent, high-income taxpayers are those in the top 20 per cent and middle-income taxpayers are the remaining 50 per cent.

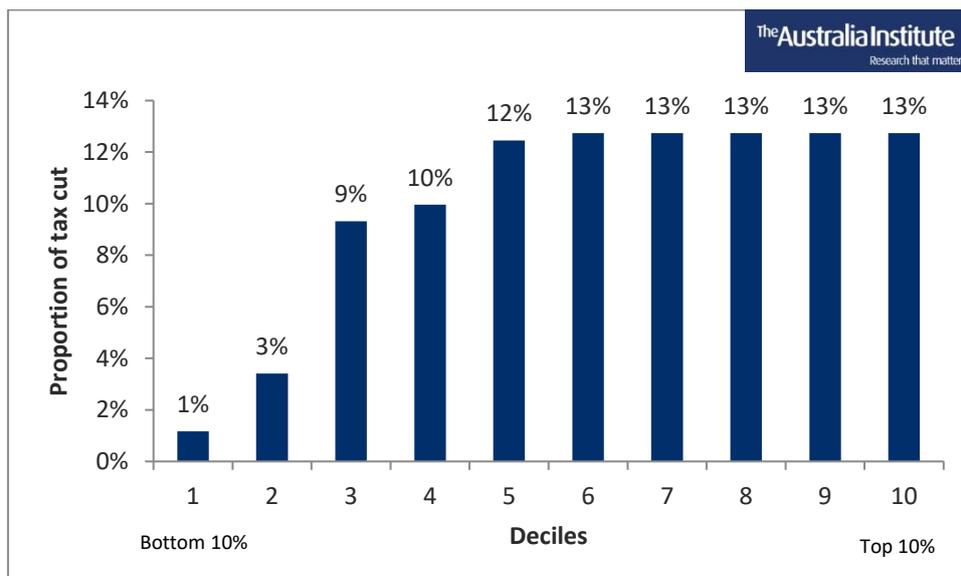
Figure 1 shows that 83 per cent of the tax cut goes to middle-income taxpayers. Low-income taxpayers get 13 per cent and the remaining four per cent goes to high-income taxpayers. This highlights that the Government can successfully target tax cuts to middle-income taxpayers.

DISTRIBUTION OF STAGE 2(A)

Stage 2(a) sees the removal of the LMITO. Low- and middle-income taxpayers are compensated for the removal of the LMITO by a combination of an increase in the LITO and an increase in the top of the 19 per cent tax threshold from \$37,000 to \$45,000. This also means that many high-income taxpayers who were previously missing out on the benefit of the LMITO get the equivalent of the full benefit of the LMITO through the increase in the tax threshold.

Figure 2 shows the distribution of stage 2(a) of the tax cut

Figure 2 – Income distribution of stage 2(a) in 2022-23

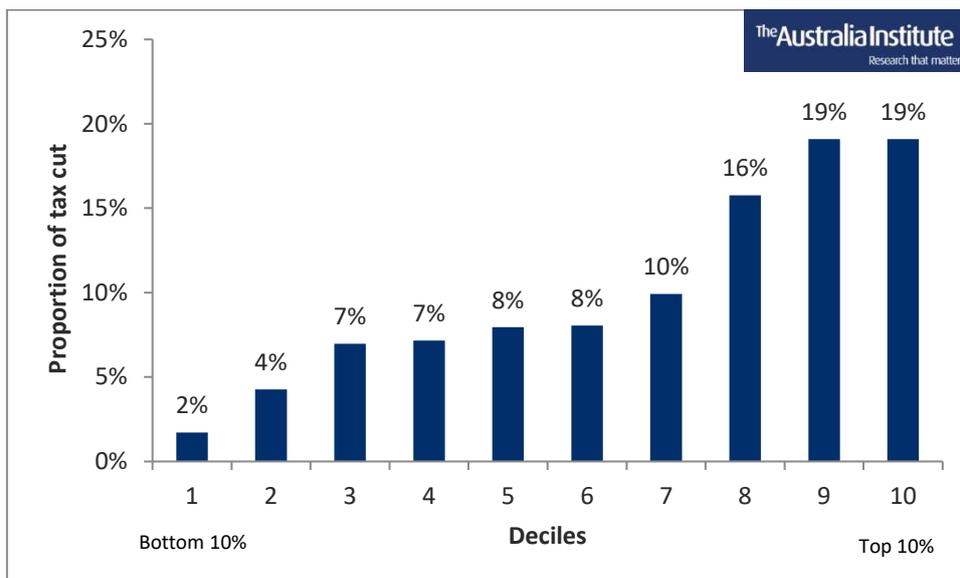


Source: Budget Paper 2, 2019-20 and author calculations (see Appendix 1: Method)

The proportion of the benefit flowing to middle-income earners falls from 83 per cent in stage 1(a) to 61 per cent in stage 2(a). Low-income taxpayers remain largely the same, getting 13 per cent of the benefit. The biggest winners are high-income taxpayers whose share of the tax cut goes from four per cent to 26 per cent.

The distribution of stage 2(a) is more evenly distributed because much of the benefit for high-income earners is in stage 2, which was legislated in 2018. Figure 3 looks at the income distribution if we combine both stage 2 and stage 2(a).

Figure 3 – Income distribution of stages 2 and 2(a) in 2022-23



Source: Budget Paper 2, 2018-19 & 2019-20 and author calculations (see Appendix 1: Method)

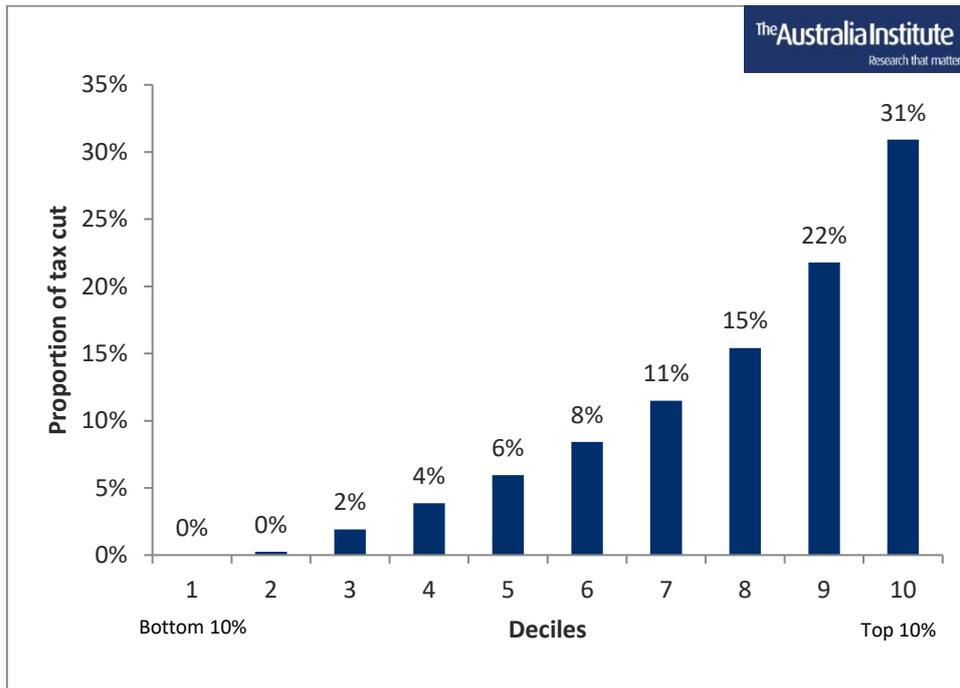
Compared to just stage 2(a), the combined stage 2 and 2(a) is less evenly distributed. Low-income taxpayers share stays the same at 13 per cent but middle-income taxpayers share falls from 61 per cent under stage 2(a) to 49 per cent under a combined stage 2 and 2(a). High-income taxpayers share increases to 38 per cent compared to 26 per cent under just stage 2(a).

DISTRIBUTION OF STAGE 3(A)

Previous analysis shows that stage 3(a) flowed mainly to high income earners with almost a third going to the top 10 per cent of taxpayers and more than half going to the top 20 per cent.³ The bottom 10 per cent got none of the benefit and the bottom 20 per cent got 0.2 per cent. This is shown in figure 4.

³ Grudnoff M (2019) *The distribution of the Government’s stage 3(a) tax cuts*, The Australia Institute, 31 May, available at <<http://www.tai.org.au/content/new-analysis-over-50-stage-3a-tax-cuts-benefit-go-highest-income-earners>>

Figure 4 – Income distribution of stage 3(a) of the tax cuts in 20-24-25

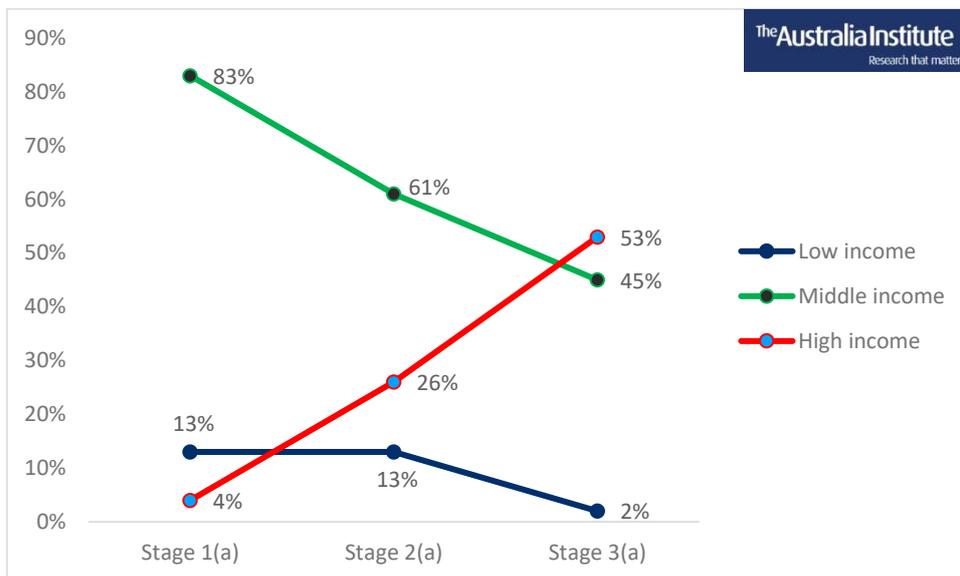


Source: Grudnoff M (2019) *The distribution of the Government's stage 3(a) tax cuts*, The Australia Institute, 31 May, available at <<http://www.tai.org.au/content/new-analysis-over-50-stage-3a-tax-cuts-benefit-go-highest-income-earners>>

Using our definitions of high, middle- and low-income taxpayers, we can see that when stage 3(a) comes into effect low-income tax payers share falls from 13 per cent, under stage 2(a) to just two per cent. Middle-income taxpayers share also falls from 61 per cent to 45 per cent. High-income taxpayers share rises from 26 per cent to 53 per cent.

The proportion of the benefit changes as we move from stage 1(a) (in 2018-19 to stage 2(a) (in 2022-23) to stage 3(a) (in 2024-25). This is shown in figure 5. It shows that low- and middle-income taxpayers share goes down as the tax plan progresses through the stages while high-income taxpayer share increases.

Figure 5 – Share of tax cut going to low, middle and high-income taxpayers as the tax plan moves through the three stages



Source: Budget Paper 2, 2018-19 & 2019-20 and author calculations (see Appendix 1: Method)

BENEFIT FLOWING TO FIXED INCOME LEVELS

If the Government’s 2019 tax plan is legislated, then over the next 10 years stage 3(a) will cost the budget \$95 billion. Stage 3(a) does not come into effect for five years, which means the \$95 billion cost will be for a five-year period from 2024-25 to 2028-29.

Currently the top marginal tax rate starts at incomes of more than \$180,000. Looking just at stage 3(a), \$33 billion of the \$95 billion will go to those earning more than \$180,000. When stage 3(a) comes into effect in 2024-25 the threshold for when the top marginal tax rate begins will increase to incomes above \$200,000. Looking again at just stage 3(a), \$26 billion will go to those earning more than \$200,000.

This puts into perspective the significant amounts of money that will flow to very high-income taxpayers. The biggest beneficiaries of the Government’s 2019 tax plan were already the biggest beneficiaries of the Government’s 2018 tax plan. They are a small number of very high-income taxpayers.

The LMITO shows us that this does not have to be the case. Tax cuts can be targeted at middle income taxpayers very effectively. Doing this will cost the budget less money and proportionately benefit more people. The LMITO is estimated to cost the budget about \$15 billion over the four years it will be in place.

APPENDIX 1: METHOD

We have calculated the benefit of the tax cut flowing to taxpayers 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. 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.