

Briefing Note: Are government plans to tackle bracket creep good for average people?

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Introduction

The government has spent a considerable amount of time talking about bracket creep with a [particular focus](#) on average incomes 'creeping' into the second top tax bracket. The government seems increasingly likely to focus any income tax cuts to prevent these average wage earners from being pushed into the second highest tax bracket. An example of how the government could achieve this is by increasing the threshold of the second highest tax rate from \$80,001 to \$100,001.

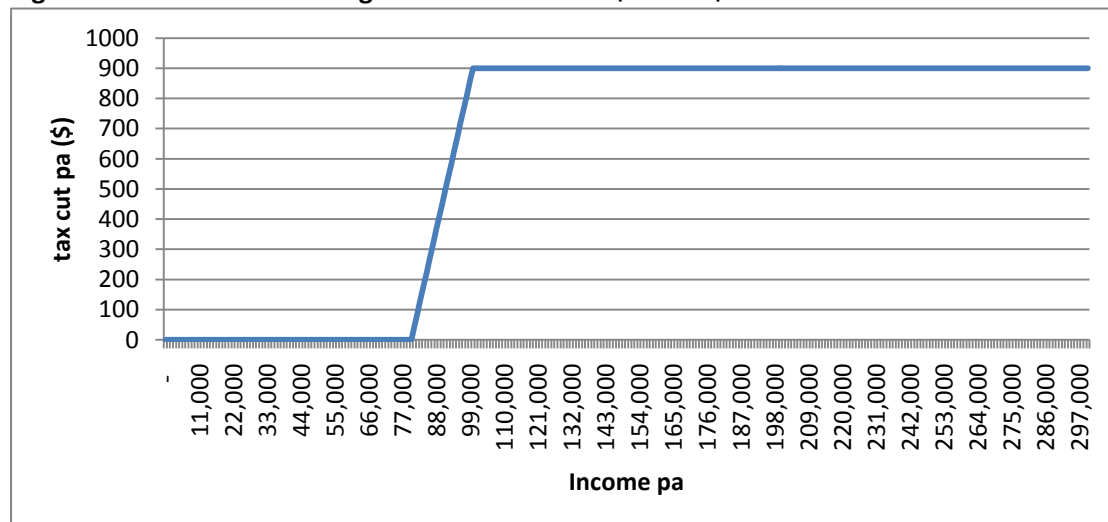
While the discussion has left the impression that these tax cuts are designed to give tax relief to average Australians the reality is very different. Most of the benefit of such a tax cut is likely to flow to high income earners. They are also likely to flow overwhelmingly to men.

Income distribution of the tax cut

Lifting the second highest tax rate threshold will only benefit those on above average full-time incomes. Income earners on below average full time incomes, who also suffer bracket creep, will not get any benefit from the tax cut. At the other end of the income spectrum those on high incomes will get the largest benefit from the tax cut.

Below Figure 1 shows the beneficiaries of our hypothetical tax cut where the government increases the threshold of the second top tax rate from \$80,001 to \$100,001. It shows the size of the tax cut per annum at various income levels. Those on incomes below \$80,000 get no benefit. Those on incomes between \$80,001 and \$100,001 will see some benefit while all tax payers above \$100,001 will get the maximum benefit.

Figure 1: Benefit of increasing tax threshold from \$80k to \$100k



This means that someone who is on close to average full time income that gets a pay rise that puts them on \$82,000 would get a tax cut of \$90 per year (about a \$1.70 per week). While someone on \$102,000 per year would get a tax cut of \$900 per year (about \$17 per week). Someone on just below average full time income who is earning \$72,000 per year would get no tax cut.

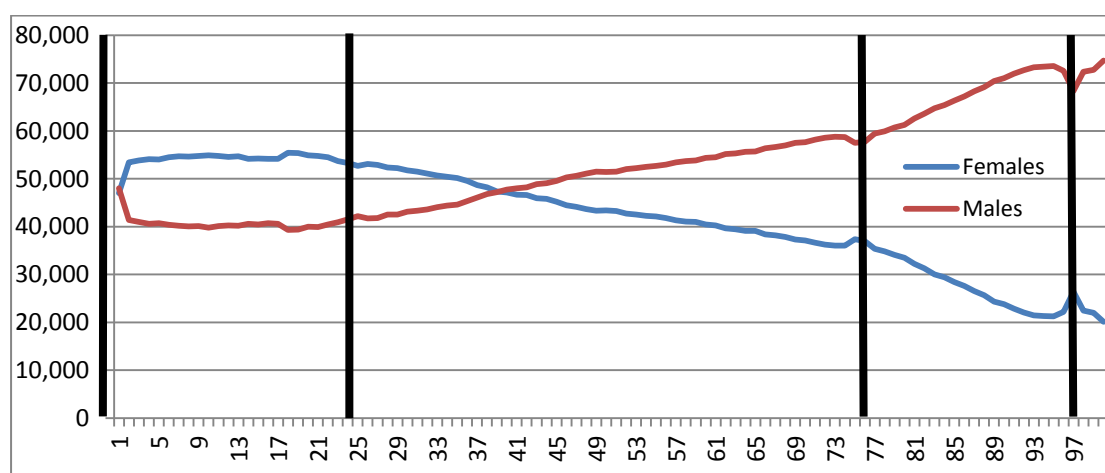
While the rhetoric around these tax cuts might be that they are aimed at average income earners, the reality is that the benefit will flow overwhelmingly to higher income earners and those on below average full time income will get no benefit at all.

Gender implication of the tax cut

This income tax cut will also be inequitable between males and females. Figure 2 breaks up all tax payers into 100 equal sized groups with those on the lowest income in group one and those on the highest incomes in group 100. The figure shows the number of females and males in each group. The black lines represent the cut in points for the different income tax rates.

The figure shows that as income rises the number of women earning that amount of money falls. Of those earning an income of \$80,000 (the income point that the government is claiming it is concerned about bracket creep) only 39 per cent are women. This continues to fall so by the time the highest tax bracket cuts in at \$180,000 only 28 per cent are women.

Figure 2: Number of male and female tax payers across the income spectrum



Source: Taxation statistics 2012–13 Individuals: Percentile distribution of taxable individuals, by taxable income and gender, 2012–13 income year

If we construct a simple model using the ATO's confidentialised two per cent sample file of detailed income tax statistics (individuals), for 2012-13 we can calculate that increasing the second highest tax rate threshold from \$80,001 to \$100,001 will cost the budget \$1.7 billion per year.¹

Using this simple model also shows that only 27 per cent of the benefit goes to women while 73 per cent goes to men.² Since the benefit flows overwhelmingly to high income earners and high income earners are predominantly men, this result is not surprising. But it is

¹ Note that this is using 2012-13 tax data (the most recent available data). This is likely to be an underestimate of the full cost to the budget as the number of tax payers and average income levels have risen since 2012-13.

² While using 2012-13 data is likely to underestimate the total cost of the tax cut to the budget it is less likely to have a material impact on the split between males and females. As such the gender estimate is likely to be of reasonable quality.

surprising when we consider that most of the government rhetoric is about helping average income earners.

Figure 1 demonstrates that all the benefit of the tax cut goes to those above \$80,001, with the largest benefit going to those earning more than \$100,001. Figure 2 shows these beneficiaries are predominately males.

Average or middle

The debate about bracket creep and the need to prevent average wage earners from entering the second top marginal tax break has centred on the idea that average wage earners shouldn't be pushed into a higher tax bracket. The public's understanding of what average means and what is actually being discussed are likely to be quite different.

While it is true that the average full time wage is getting close to \$80,000, that is not the same as saying that half of people are earning more than \$80,000 and half are earning less than \$80,000. Average wages tend to be pushed up by the fact that there are some people on very high incomes which push the average up.

To avoid the problem of averages being distorted by a small group of outliers, median incomes can be used instead of average incomes. The median income is the middle income. That is if you lined up all income earners by how much they earn then the median income would be the amount the person in the middle earns. This is likely to express more accurately what the general public thinks an average income is.

According to the ABS the median full time income in Australia in May 2014 was \$69,000 while the average wage was \$10,000 higher at \$79,000.³ High income earners have pushed up the average by \$10,000 per year.

These figures are only for full time workers. Excluding part time workers has implications for gender equity since women are more likely to be in part time employment. When we include all employees (both full time and part time) the average falls \$17,000 to \$62,000. The median also falls \$17,000 to \$52,000.

This means that the general public's understanding of average income, as those whose earnings are in the middle of the income distribution are more accurately seen as \$52,000 rather than \$79,000. This shows up in the ATO's tax data on income distribution of tax payers with those on \$80,000 being in the top 25% of income earners. This is a long way from those in the middle of the income distribution.

Conclusion

Preventing average wage earners from entering the second top marginal tax rate has been justified as a measure to improve fairness. But by either accident or design those on low incomes get nothing, those on average incomes get very little, while those on high incomes, who are mostly men, get the most benefit.

Bracket creep affects all tax payers not just those in the top quarter of income earners. If the government is really concerned about bracket creep then it would be better off cutting income tax at the bottom rather than near the top. The government could instead increase the tax free threshold. This would give tax relief to all those affected by bracket creep not just those on high incomes.

³ ABS (2014) 6306 - Employee Earnings and Hours, Australia, May 2014, available at <<http://www.abs.gov.au/AUSSTATS/abs@.nsf/DetailsPage/6306.0May%202014?OpenDocument>>