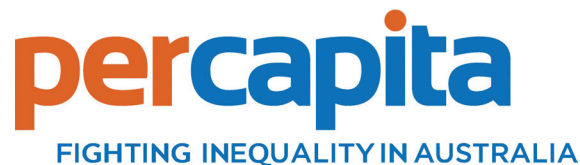


THE COST OF PRIVILEGE

A Research Paper by Per Capita for Anglicare Australia

March 2018

Emma Dawson
and
Warwick Smith



About Per Capita

Per Capita is an independent progressive think tank, dedicated to fighting inequality in Australia. We work to build a new vision for Australia based on fairness, shared prosperity, community and social justice.

Our research is rigorous, evidence-based and long-term in its outlook. We consider the national challenges of the next decade rather than the next election cycle. We ask original questions and offer fresh solutions, drawing on new thinking in social science, economics and public policy.

Our audience is the interested public, not just experts and policy makers. We engage all Australians who want to see rigorous thinking and evidence-based analysis applied to the issues facing our country's future.

About the Authors

Emma Dawson is the Executive Director of Per Capita. Formerly, she was a senior advisor on Digital Inclusion at Telstra, Executive Director of the Institute for a Broadband Enabled Society at the University of Melbourne, and a senior policy advisor in the Rudd and Gillard governments.

She has published articles and opinion pieces on a wide range of public policy issues, which have appeared in the Sydney Morning Herald, The Age, the Guardian, The Australian, and a number of online publications. She is a regular panelist on The Drum on ABC TV and various Sky News programs.

Emma holds a BA with First Class Honours from LaTrobe University and an MA with Distinction from Monash University. She sits on the board of the Prader-Willi Research Foundation Australia and is an Honorary Fellow in the School of Social and Political Sciences at the University of Melbourne.

Warwick Smith is Senior Economist at Per Capita. He has previously worked as a research economist, consultant and freelance writer. His particular areas of expertise include the economics of ageing populations, environmental, gender and taxation economics and the history and philosophy of economics.

Warwick has a Bachelor of Arts from the University of Melbourne and a Bachelor of Science (Hons) from the ANU. He is an Honorary Fellow in the School of Social and Political Sciences at the University of Melbourne.



About Anglicare Australia

Anglicare Australia is a peak, membership organisation which represents and brings together over 40 independent community service organisations, all with links to the Anglican Church. We work in many hundreds of communities, in every State and Territory, as we focus on responding to the multiple and complex needs of people and families across Australia.

Building on our wisdom and practice across all our members and over 150 years of shared experience we aim:

- » To influence social and economic policy across Australia with a strong prophetic voice; informed by research and the practical experience of the network; called to speak out for those most disadvantaged.
- » To enable the potential, strength and sustainability of the members, ensuring that they have the capacity to serve the needs of all Australians with dignity, respect and care.
- » To create a network whose members challenge, support and lead each other in the development of social services and the people and communities with whom we work.
- » To recognise and celebrate the Anglican faith base and inspiration of our work.

Acknowledgements

The authors wish to thank Kasy Chambers and Imogen Ebsworth from Anglicare Australia for their leadership in devising this project, and for their valuable input to the research process. Any errors or omissions are the responsibility of the authors.

Contents

Executive summary	5
Introduction	6
Our findings	6
Household snapshots	7
Household One – Kevin and Andrea	7
Household Two – Anthony and Maria	7
Household Three – Michael and Gillian	7
Household Four – Tim and Michelle	8
Methodology	9
Principle place of residence Capital Gains Tax exemption	9
Superannuation	10
Capital gains tax concessions and negative gearing	10
Private healthcare GST exemption	11
Private education GST exemption	11
Discretionary trusts and family companies	12
Methods and assumptions for family profile calculations	12
Household One	12
Household Two	13
Household Three	13
Household Four	14
Conclusion	16
References	16

Executive Summary

As an organisation that speaks for the country's most disadvantaged people, Anglicare Australia asked Per Capita to undertake modelling to understand how the tax and transfer system operates across different income quintiles, and to determine to what extent measures within the system support the richest versus the poorest Australians.

The modelling assessed the various tax concessions and other benefits available to high-income earners and contrasts them with well-understood direct income support measures for low-income earners and those reliant on our social security safety net.

This report quantifies the annual cost to the federal budget of various measures that allow Australians in our wealthiest quintile to minimise their taxable income, thereby reducing government revenue that pays for services for all citizens.

These measures include superannuation tax concessions, negative gearing, capital gains tax concessions, the use of discretionary trusts, the exemption from the Goods and Services Tax (GST) of private health insurance and education, and the exemption from Capital Gains Tax (CGT) of the principal place of residence. All of these concessions disproportionately benefit high income and high wealth households. Our analysis shows that, in combination, these measures impose a cost on the federal budget that easily outstrips that of any single welfare recipient group.

According to our calculations, the cost of foregone tax revenue from the richest 20% of Australians is over AU\$68 billion per annum. That's around \$37 a week from every worker in the country.¹ In contrast, the cost of income support in the 2016-2017 financial year was, by group:

Age Pension	\$44.468 billion (\$35 a week per worker)
Assistance to families with children	\$36.404 billion (\$20 a week per worker)
Assistance to people with disabilities	\$31.721 billion (\$17 a week per worker)
Newstart (unemployment benefits)	\$10.994 billion (\$6 a week per worker)

¹ Calculated using the methodology outlined in Answer to Question On Notice No: 257, Taxation paid and 2016-17 Financial Year, what was the total government spend? Senate Economics Legislation Committee, Treasury Portfolio, Budget Policy Division, Supplementary Budget Estimates 2017 - 2018

To illustrate how the tax and transfer system works at the personal level, we created four typical household scenarios, two in the highest and two in the lowest quintile. For the purposes of comparison, all the hypothetical families include two parents and two school-aged children, and live in major cities. The results are at Table 1.

Household	Household Income After Tax	Tax and Transfer Benefit
Kevin and Andrea. Both parents on Newstart.	\$42,103.13 per year, or \$809.67 per week.	\$42,103.13 per year, or \$809.67 per week.
Maria and Anthony. One parent on Disability Support Payment, one parent working part-time.	\$59,541.69 per year, or \$1145.03 per week.	\$36,824.32, or \$708.16 per week.
Michael and Gillian. One parent working full-time, one parent working part-time.	\$215,446 per annum, or \$4,143.19 per week.	\$71,705 per year, or \$1,378.94 per week.
Tim and Michelle. Small business owners, one parent working full-time, one parent not working.	\$208,421 per year, or \$4008.10 per week.	\$99,708 per year, or \$1,917.46 per week.

If the Government is serious about balancing the budget while retaining a fair and just society, the place to cut government spending is on the cost of subsidising the accumulation of wealth by rich Australians, not reducing essential support to our poorest citizens.

Introduction

Australian society is becoming increasingly stratified, with growing inequality of wealth and income.

Too often, our political and economic debate is dominated by a narrative that paints those Australians with the lowest household incomes as a drain on the public purse, depicting the cost of our welfare state as unsustainable.

Recent headlines asserting that the “average” Australian worker pays \$83 per day to provide for the welfare budget typify the commentary around our tax and transfer system, which is amongst the most tightly targeted in the world.

But income support is not the only means by which the Australian tax and transfer system redistributes income amongst citizens.

This report demonstrates the cost to the federal budget of tax concessions and other economic transfers to the highest 20% of Australian income earners.

By analysing data from the Australian Bureau of Statistics (ABS), Treasury Budget Statements and the University of Melbourne’s annual Household Income and Labour Dynamics in Australia (HILDA) report, the authors have established that the cost to the federal budget of the highest-income Australian households outstrips that of any single welfare recipient group.

Our findings

While the various tax concessions and exemptions that account for the cost to the budget of support for wealthy Australians are also available to low income citizens, the benefits of such measures disproportionately favour those in the highest wealth quintile.

A direct comparison shows that the bottom 20% of Australians by wealth collectively receive just \$6.1 billion in such benefits, while the top 20% receive ten times as much, at over \$68 billion.

Benefit	Total expenditure (\$B)	Bottom 20% (\$B)	Top 20% (\$B)
Principle residence CGT exemption	74	5.1	31.8
Superannuation – earnings	19.25	-0.06	11.1
Superannuation – contributions	16.9	-0.05	9.75
Capital gains tax concession	10.3	0.23	8.4
Negative gearing	4.55	0.3	1.73
Private health GST exemption	4.3	0.22	2.26
Education GST exemption	4.1	0.4	1.51
Discretionary trusts	2.0	0	2.0
Total	135.4	6.14	68.55

These findings expose the falsity of much government rhetoric about the benefits of tax concessions to “average” Australians.

For example, half of the foregone revenue from negative gearing goes to the top 20%, while just 6.2 per cent goes to the bottom quintile.

Similarly, more than 80% of the savings from the capital gains tax concession go to the wealthiest quintile, and just 2% to the bottom 20%.

It also appears that the foregone revenue from discretionary trusts is entirely received by the wealthiest 20% of Australians, although it should be noted that it is difficult to calculate precisely the lost tax revenue from discretionary trusts based on available data.

Household snapshots

The examples below illustrate the outcomes of the modelling undertaken to assess the amount of taxpayer support to different households, using hypothetical families to demonstrate the differences between typical circumstances for many Australians. Detailed information on these calculations and assumptions are provided in the Methodology chapter.

Household One – Kevin and Andrea

Kevin and Andrea rent a two bedroom apartment in the suburbs of Adelaide with their boys, Liam, aged 11 and Noah aged 9. The boys go to the local state primary school.

Andrea left her part time job as a book-keeper when Liam was born; Kevin lost his job last year when the Holden factory closed down and hasn't yet found another position.

Both Kevin and Andrea are looking for work. Andrea is undertaking online courses to bring her skills up to speed with online accounting programs but can't afford to attend a formal course and get new qualifications.

The family is currently relying entirely on income support. They are both receiving Newstart, and Family Tax Benefits A and B, and get Rent Assistance.

The total cost to the budget of income support for Kevin and Andrea's family is \$42,103.13 per year, or \$809.67 per week. This is their total household income.

Household Two – Anthony and Maria

Anthony and Maria have two kids, Alice, aged 10, and Ella, aged 7. They rent a two bedroom house in the outer suburbs of Melbourne, and the girls attend the local state primary school.

Anthony has been unable to work since his Multiple Sclerosis progressed to the point where it severely limited his movement three years ago. He receives the Disability Support Payment.

Maria works part-time as a retail assistant at a large chain store in the local shopping centre, five hours a day during school hours. She is otherwise a full-time carer for her husband and children. Anthony's mum and sister take turns coming to the house to care for Anthony while Maria is at work.

Maria's take home pay, after tax of \$1059.63, is \$22,717.37 per year, or \$436.87 per week. Anthony's DSP provides an additional \$23,254.40 per year, or \$447.20 per week. The family also receives Family Tax Benefit A and Rent Assistance, bringing their total household income to \$59,541.69 per year, or \$1145.03 per week.

Of this, the amount received from the taxpayer in income support is \$36,824.32, or \$708.16 per week.

Household Three – Michael and Gillian

Michael and Gillian have two children, Isabella, aged 12 and Max, aged 8.

They paid off their mortgage two years ago and live in a four bedroom house in a bayside suburb of Melbourne. Isabella and Max go to the local Catholic primary school and will go on to Catholic secondary college. The family has intermediate hospital and extras private health insurance.

Michael is a Team Leader at a large telecommunications company, and earns \$230,000 per year. Gillian works 20 hours a week, during school hours, in the HR department of a major bank, and earns \$60,000 per year.

Both Michael and Gillian salary sacrifice into their superannuation accounts up to the \$25,000 concessional cap. While Michael can only contribute an extra \$3,150 of his pre-tax income to super on top of the \$21,850 in compulsory contributions already made by his employer, Gillian can contribute \$19,000, reducing her taxable income to \$41,000.

They own a three bedroom house in Rye, which they rent out through AirBnB as a holiday home and negatively gear, allowing them to reduce Michael's tax by a further \$9,400.

The value of the capital gains tax concession on their holiday home gives them \$4,500 in concessional benefits annually, and the tax exemption of their family home in Melbourne provides another concession of \$23,500 per year.

Michael and Gillian also receive GST tax exemptions on their private health and education costs to the value of \$3,250.00 per year.

Their combined family income after tax is \$215,446 per annum, or \$4,143.19 per week.

The total amount received from the taxpayer in tax concessions for this family is \$71,705 per year, or \$1,378.94 per week.

Household Four – Tim and Michelle

Tim and Michelle have two children, Tom, aged 9 and Amelia, aged 7.

They own their own home in an inner suburb of Sydney, and both the children are enrolled in a private, Prep to Year 12 college. The family has top hospital and extras private health insurance.

Tim owns his own business, with a business profit of \$230,000 per annum. Michelle doesn't work, but is listed as a Director of Tim's company, primarily for tax purposes.

Both Tim and Michelle contribute the maximum \$25,000 pre-tax contributions to their superannuation accounts. They have two negatively geared investment properties, including a holiday house in Byron Bay which is rented privately for short-term holiday leases through a local real estate agent, and a three bedroom house in Surry Hills that is leased long-term to a tenant.

The family uses a discretionary trust to distribute income from the business, including \$54,000 annually to Michelle and the maximum amount allowed for the children. Combined with Michelle's \$10,000 Director's fee, this keeps her total income just inside the lowest marginal tax rate after she contributes \$25,000 of pre-tax income to her superannuation and deducts

purchases of family items used primarily for entertainment, such as their broadband service and mobile phones, through home office expenses.

Tim and Michelle each drive luxury vehicles purchased through novated leases through the family business costing \$19,414 each per year.

The value of the capital gains tax concession on their holiday home gives them \$4,500 in concessional benefits annually, with another \$4,500 from the rental property in Surry Hills, and the tax exemption of their family home in inner Sydney provides another concession of \$23,500 per year.

Tim and Michelle also receive GST tax exemptions on their private health and education costs in the value of \$3,250.00 per year.

Although the business earns \$230,000 a year, by using all of these methods, Tim reduces his taxable income to just \$58,340 and Michelle's is \$37,000. Together they pay a total of \$21,579 in tax, including \$7500 in superannuation contribution tax.

Tim and Michelle therefore have combined family income after tax of \$208,421 per year, or \$4008.10 per week.

The total amount received from the taxpayer in tax concessions for this family is \$99,708 per year, or \$1,917.46 per week.

Methodology

Per Capita analysed relevant government and other data sets and existing research. This included data from HILDA,¹ the ABS,² ATO,³ PBO⁴ and Budget Papers and Budget Papers, to quantify the annual cost to the federal budget of measures that allow high income Australians to minimise their taxable income, thereby reducing government revenue that pays for services for all Australians.

It's important to note that our income quintiles are calculated based on taxable income. Some relatively high-income earners manage to reduce their taxable incomes substantially through tax planning mechanisms, including, but not limited to, those included in this report (see Household four in our family profiles in the main body of this report). This means that the distributions of concessions going to high-income individuals is actually higher than reported here.

Detailed methodology for each measure is outlined below.

Principle place of residence CGT exemption

The 2017 Tax Expenditures Statement (TES) lists the following items in relation to principle place of residence:

Table 1. Main residence tax expenditures

Tax expenditure	Forgone revenue (\$m)
Main residence exemption – discount component	40,500
Main residence exemption	33,500

1 Household Income and Labour Dynamics in Australia
2 Australian Bureau of Statistics
3 Australian Taxation Office
4 Parliamentary Budget Office

These two tax expenditures represent a breakdown of the 100% CGT concession for principle place of residence into the value of the standard 50% CGT concession for individuals (the discount component) and the exemption for the main residence that takes the concession to 100%.

We used 2016 data from the Household Income and Labour Dynamics in Australia (HILDA) survey to calculate average house values by equivalised household income quintile.

Equivalised household income was generated using the following formula:

$$\text{Equivalised household income} = \frac{\text{Total annual household income}}{(1 + 0.5 * (\text{number of adult household members} - 1) + 0.3 * (\text{number of children 0-14 in the household}))}$$

Home ownership rates and average home value were calculated for each income quintile. These were used to calculate average home values across both owners and renters. Proportions of main residence exemption were then assigned to quintiles according to the proportion of total home values for those quintiles (see Table 2). This is only a rough estimate of proportion of capital gain and will result in an underestimate for higher quintiles as capital growth tends to be proportionally higher in high value suburbs.

Table 2. Calculations for proportion of home value

Quintile	% Rent	% Own	Average value	Average across pop'n	Proportion of total value
1	0.51	0.49	249752	122443	0.07
2	0.43	0.57	287464	164373	0.10
3	0.32	0.68	373521	253707	0.15
4	0.23	0.77	531569	409156	0.25
5	0.17	0.83	851582	705898	0.43

Result

The top quintile of income earners holds 43% of the main residence value. By assuming that this translates into 43% of the capital gain, we estimate that \$31.8B of main residence tax expenditures go to the top quintile.

By contrast, using the same methodology we estimate that \$5.1B (7%) of main residence tax expenditure goes to the bottom quintile.

Superannuation

The 2017 Tax Expenditures Statement lists the following items in relation to superannuation:

Table 3. Superannuation tax expenditures

Tax expenditure	Forgone revenue (\$m)
Concessional taxation of superannuation entity earnings	19,250
Concessional taxation of employer superannuation contributions	16,900

These concessions were apportioned to quintiles using proportions calculated by the Australian Treasury in 2012. While changes to superannuation legislated in 2016 will have altered these ratios slightly, the authors believe this will not cause a substantial change in the short term. Updated distributional figures after the 2016 changes are not yet available.

Result

A total of 57.7 percent of total concessions (\$36.15B) go to the top quintile = \$20.8B. The lowest quintile receives -0.3% of the concessions. This is driven by the lowest decile many of whom earn less than the tax-free threshold, meaning the 15% tax on superannuation contributions and

earnings is higher than their marginal rate. The Low Income Superannuation Tax Offset (LISTO) now returns most of the tax on contributions but not the tax on earnings. Therefore, tax “concessions” on superannuation cost the lowest quintile \$108m.

Capital gains tax concessions and negative gearing

The 2017 Tax Expenditures Statement lists the following items in relation to the capital gains tax concession.

Table 4. Capital gains tax concession for individuals and trusts

Tax expenditure	Forgone revenue (\$m)
Capital gains tax discount for individuals and trusts	10,270

According to Grudnoff (2015), 81.7 % of the Capital Gains Tax (CGT) discount goes to the top quintile and 2.2% to the bottom quintile. This means that \$8.4B in CGT discount goes to the top quintile and \$226 million to the bottom.

Negative gearing costs are not directly measured but can be confidently assumed to be between \$3.7B in 2014/15 (Grudnoff, 2015) and \$5B (Eslake, 2013). Phillips (2016) estimated that negative gearing would cost \$4.3B in 2017/18, neatly in the middle of the above estimates. For the purpose of this exercise we have adopted the Phillips (2016) estimate as being the most recent and sitting in the middle of other estimates.

Calculations by Gudnoff (2015) found that 49.8% of negative gearing concessions went to the top 20% and 6.2% to the bottom quintile. Phillips (2016) estimated 52.6% to the top quintile and 5.1% to the bottom quintile. These estimates are very close and we have chosen the Phillips (2016) figure as it is more up to date. That’s \$2.26B negative gearing benefits to the top 20% and \$219m to the bottom 20%.

Private healthcare GST exemption

The 2017 Tax Expenditures Statement lists the following items in relation to the GST exemption for healthcare.

Table 5. Healthcare tax expenditures

TES Item	Tax expenditure	Forgone revenue (\$m)
H19	Health – medical and health services	4,100

HILDA households were divided into income quintiles (see Principle Place of Residence section) and mean expenditure on private health insurance was calculated for each quintile. These were used to calculate proportion of total expenditure which was then applied, per quintile to the total GST exemption tax expenditure listed in the 2017 TES (see Table 2).

Table 6. Hilda mean expenditure by quintile on private health insurance by quintile

Quintile	Mean	Proportion
1	555.24	0.08
2	830.21	0.12
3	1214.45	0.18
4	1726.18	0.26
5	2339.71	0.35
Total	6665.78	

Using the above calculations from HILDA, 35% of expenditure on healthcare by the top quintile equals \$1.51B and 8% to the bottom quintile equals \$0.4B.

Private education GST exemption

Table 7. Education GST exemption tax expenditures

TES Item	Tax expenditure	Forgone revenue (\$m)
H16	Education GST exemption	4,550

HILDA households were divided into equivalised income quintiles (see Principle place of residence section above) and mean expenditure on education was calculated for each quintile. These were used to calculate proportion of total expenditure which was then applied, per quintile to the total GST exemption tax expenditure listed in the 2017 TES (see Table 3).

Table 8. Quintile calculations for proportional GST exemption for education tax expenditures

Quintile	Mean exp	Prop expenditure	Total concession	Quintile concession
1	654.0225	0.066466	4.55	0.302422
2	1235.277	0.125538	4.55	0.571197
3	1744.248	0.177263	4.55	0.806547
4	2471.569	0.251179	4.55	1.142862
5	3734.773	0.379554	4.55	1.726972

Discretionary trusts and family companies

Precisely calculating the lost tax revenue from discretionary trusts is impossible because there's no definitive answer regarding the marginal tax rate that would be payable if the trust structure was not used. However, the parliamentary budget office calculated that ALP policy proposal (Australian Labor Party, 2016) that would tax discretionary trusts at a minimum of 30% would raise an additional \$1.5B per year once fully operational.

Boccabella (2017) estimates total tax losses through discretionary trusts conservatively at \$2b. Given the PBO costing above uses a 30% tax rate and most earners using discretionary trusts to distribute income to family members would have higher marginal tax rates than 30%, the \$2B figure appears plausible, if conservative. While acknowledging it is only a rough estimate and is likely to be an underestimate, the authors have decided to adopt this figure for this report.

The evidence available strongly suggests overwhelming majority of discretionary trusts are utilised by the top 10% of income earners as part of legal tax minimisation measures. The greater the marginal tax rate, the greater the benefit from setting up a discretionary trust. Average tax payers, using average tax accountants, would very rarely make use of such tax arrangements. We therefore assume that all of the \$2B is attributable to the top quintile.

Methods and assumptions for family profile calculations

All families consist of two parents and two school age children between the ages of six and fourteen. All parents in all scenarios are 45 years old.

Household One

- » Both parents are on Newstart
- » Renting a house in Adelaide for \$350 per week
- » Public schooling

The benefit calculator from Department of Human Services web site was used to calculate their benefits.

Household 1	Benefit
Family tax benefit A	\$9,507.68
Family tax benefit B	\$2,824.64
Newstart allowance	\$25,708.80
Rent assistance	\$4,062.24
Superannuation earnings concession	-\$1500.00
Education GST exemption	\$20.00
Total government benefit	\$42,123.36

Household Two

- » Mother working part-time at 25 hours per week at the minimum wage
- » Father on Disability Support Pension
- » Renting in outer Sydney for \$400 per week

The benefit calculator from Department of Human Services web site was used to calculate their benefits.

Household 2	Benefit
Family tax benefit A	\$9,507.68
Disability support pension	\$23,254.40
Rent assistance	\$4,062.24
Salary	\$23,777.00
Superannuation contribution concession	\$90.35
Superannuation earnings concession	-\$1000.00
Education GST exemption	\$100.00
Total government benefit	\$35,934.67

Household Three

- » Father earns \$230,000 salary
- » Mother working part time earning \$60,000
- » Both parents salary sacrificing to super up to the \$25,000 concessional cap
- » They own their home outright in Melbourne
- » One negatively geared investment property
- » Private health insurance
- » Private schooling

Key calculations

- » Both are topping up their compulsory super to the full \$25k pre-tax cap. He can only contribute an extra \$3,150 pre-tax but she can contribute \$19,000, reducing her taxable income to \$41,000.
- » Principle place of residence tax exemption is calculated by assuming a modest \$50,000 per year real increase in residence price (5% for a \$1m home) over ten years and the total concession annualised an average of the mother and father's marginal tax rate.
- » Negative gearing calculations are made by assuming an \$8000 rental loss based on interest and repair costs plus \$12,000 depreciation for the investment property.
- » Capital gains tax concession of \$4500 assumes a modest annual capital gain on investment property of \$30,000 realised after ten years.
- » Education GST exemption assumes a moderate \$15,000 per child per year spent on private education.

Household 3	Benefit
Superannuation contribution concession	\$19,875.00
Negative gearing	\$9,400.00
Superannuation earnings concession	\$14,805.00
Principal place of residence tax exemption	\$19,875.00
Capital gains tax concession	\$4,500.00
Private health insurance GST exemption	\$250.00
Education GST exemption	\$3,000.00
Total benefit	\$71,705.00

Household Four

- » Father earning \$230k business income
- » Mother not working but on the books as Director of Father's business primarily for tax purposes
- » Both parents salary sacrificing to super up to the \$25,000 concessional cap
- » They own their home outright in Sydney
- » Two negatively geared investment properties in Sydney
- » Family discretionary trust for distributing business income
- » Home office expenses used to deduct purchases of family items used primarily for entertainment and media consumption
- » Private health insurance
- » Private schooling
- » Two negatively geared investment properties and also includes family discretionary trust and use of company for vehicles, home office etc.

The calculations of taxable income deductions are made by assuming the baseline scenario involves the business owner paying himself all \$230,000 as a salary + super (\$210,000 salary and \$20k super). All of the advantages calculated are then relative to that baseline scenario.

Key calculations

- » Both parents contribute the maximum \$25,000 pre-tax contributions to superannuation.
- » Two cars are purchased by the directors through novated leases through the company. Annual tax calculation was made using Fleet Partners novated lease calculator on two BMW 4 series coupes at \$19,414 each p.a.
- » Home office expenses are a rough estimation of share of internet, phones, mobiles, IT equipment depreciation etc. The benefit assumption here is that these are all items that the family would have purchased anyway, without the business but are able to deduct from tax due to the inclusion of both parents on the payroll of the company.
- » Negative gearing calculations are made by assuming an \$8000 rental loss based on interest and repair costs plus \$12,000 depreciation for each property.
- » The discretionary trust allocates \$54,500 to the mother of the house and the maximum allowed for children. The amount allocated to the mother is precisely enough, combined with her \$10,000 director's fee, that she falls into the lowest marginal tax rate after she makes her maximum pre-tax contribution of \$25k to super and deducts home office expenses (When the children are over 18 and are at university the trust will be able to assign them each \$18,200 with zero tax, thus reducing the taxable income of the father by an additional \$36k p.a.). She ends up paying 19c in the dollar for her income over the \$18,200 tax free threshold plus she pays 15% tax on her \$25k super contribution.

- » Principal place of residence tax exemption is calculated by assuming a modest \$50,000 per year real increase in residence price (2.5% for a \$2m home) over ten years and the total concession annualised at the father's marginal tax rate.
- » Capital gains tax concession of \$4500 assumes a modest annual capital gain on each of two investment properties of \$30,000 p.a. realised after ten years.
- » Education GST exemption assumes a moderate \$15,000 per child per year spent on private education.

Household 4	Deduction	Benefit
Tax deductions		
Company cars	\$38,828.00	\$18,249.00
Home office etc	\$5,000.00	\$1987.00
Superannuation contribution concession	\$50,000	\$23,500.00
Negative gearing (rent minus interest and depreciation)	\$40,000	\$18,800.00

Concessions that do not directly affect income tax		
Superannuation earnings concession		\$14,805.00
Principal place of residence tax exemption		\$23,500.00
Capital gains tax concession		\$9,000.00
Private health insurance GST exemption		\$250.00
Education GST exemption		\$3,000.00
Total benefit		\$99,708**

* Benefits itemised below are for each benefit in isolation (i.e. assuming no other tax concessions).

** Total benefit is not simply the sum of the above items. When combined, the benefit amount falls as incremental deductions reduce taxable income into lower marginal tax rate brackets. Total benefit is, therefore, calculated by subtracting tax paid under the family scenario described above from tax that would be payable if the company owner simply paid himself the \$230,000 in superannuation and salary. To this number is then added all of the concessions that do not directly affect cash flows or income tax.

Conclusion

The modelling presented in this report clearly demonstrates that the benefits provided to high-income earners through tax concessions easily outweigh the benefits of direct income support payments to welfare recipients.

In seeking budget savings, governments could close various loopholes and reduce tax concessions that are disproportionately used by wealthy Australians without causing hardship to our most vulnerable citizens.

It should be noted that the tax and transfer system is not the only part of government expenditure that disproportionately benefits high income earners, and there is an inter-relationship between government expenditure on the private sector and how such funds then benefit individuals with high wealth.

Some areas that have been explored (Murray & Frijters, 2017) include government direct grants to private businesses public- private partnerships, and government contracts to private suppliers.

However, the tax and transfer system is the most direct and easy to both quantify and demonstrate the impact it has on the lived experience of Australians in different life circumstances.

Our report shows that characterisations of the poorest Australians as a burden on the economy are inaccurate and, if we are to worry about unnecessary imposts on the budget, there is a very strong case for reducing tax concessions and other direct benefits to our wealthiest citizens.

References

- Australian Labor Party. (2016). *A Fairer Tax System: Discretionary Trusts Reform*. Canberra, ACT.
- Boccabella, D. (2017). *Family trusts often cause more harm than good*. Retrieved February 15, 2018, from <https://theconversation.com/family-trusts-often-cause-more-harm-than-good-81551>
- Eslake, S. (2013). *Australian Housing Policy: 50 Years Of Failure*. Submission to the Senate Economics References Committee, (September), 1–16.
- Grudnoff, M. (2015). *Top Gears : How negative gearing and the capital gainst tax discount benefit the top 10 per cent and drive up house prices*.
- Murray, C. K., & Frijters, P. (2017). *Game of Mates: How favours bleed the nation*. Brisbane: Cameron Murray and Paul Frijters.
- Phillips, B. (2016). *Distributional Modelling of Proposed Negative Gearing and Capital Gains Taxation Reform*. Canberra, ACT. Retrieved from http://csrcm.cass.anu.edu.au/sites/default/files/docs/Distributional_Modelling_of_Negative_Gearing_and_Capital_Gains.pdf
- The Australian Treasury. (2012). *Distributional analysis of superannuation taxation concessions: A paper to the Superannuation Roundtable*. Retrieved January 20, 2018, from <https://treasury.gov.au/programs-and-initiatives-superannuation/distributional-analysis-of-superannuation-taxation-concessions/>