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No. 145 2003–04

Tax Law Amendment (Personal Income Tax Reduction) Bill 2004

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No. 145 2003–04

Tax Law Amendment (Personal Income Tax Reduction) Bill
2004

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Law and Bills Digest Section
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Tax Law Amendment (Personal Income Tax Reduction) Bill 2004

Date Introduced: 13 May 2004

House: House of Representatives

Portfolio: Treasury

Commencement: On receipt of Royal Assent

Purpose

The purpose of the Tax Law Amendment (Personal Income Tax Reduction) Bill 2004 (“the Bill”)¹ is to amend the *Income Tax Rates Act 1986* to increase the personal income tax thresholds for the 42 per cent and 47 per cent tax brackets.

Background

The income tax cuts announced in the 2004-2005 budget

The Bill gives effect to the Personal Income Tax cuts announced by the Federal Government on 11 May 2004 in the 2004-2005 Federal Budget.

In his second reading speech, the Treasurer, The Hon. Peter Costello MP, described the Government’s proposal to reduce income tax as follows:

The tax reductions will be delivered by increasing the income thresholds for the top two tax brackets. The thresholds will be lifted in two stages. From 1 July this year the 42 per cent threshold will be increased from \$52,000 to \$58,000, and the 47 per cent threshold is to be increased from \$62,500 to \$70,000. From 1 July 2005, the 42 per cent threshold will be further increased to \$63,000 and the 47 per cent threshold to \$80,000.²

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The proposed changes will result in income tax cuts worth \$14.7 billion over the next four years. The financial impact can be broken down into the following figures per financial year:³

2004-2005	2005-2006	2006-2007	2007-2008
\$1.925 billion	\$3.8 billion	\$4.25 billion	\$4.75 billion

The budget reply – no concrete plan... yet.

Whilst not revealing details of the Labor Party's foreshadowed income tax cuts, the Opposition leader indicated in his Budget Reply that the Opposition will be implementing 'a bigger program of tax relief—a broader and fairer tax plan for the future.'⁴

Media and political reaction to the proposed income tax cuts

The media and political reaction to the income tax cuts as proposed by the Federal Government were mixed and the issues raised can be grouped as follows.

The income tax cuts are not equally enjoyed by all taxpayers

The income tax cuts proposed by the Federal government effect only the highest tax brackets. Therefore, the changes will only benefit those income earners who earn more than \$52 000 a year.

Senator Andrew Bartlett, Australian Democrats spokesperson for Treasury, criticised this alleged inequality and stated that:

The Federal Governments inevitable budget tax cuts should be shared equally by all taxpayers, and services should be funded from closing loopholes and tax concessions used by the wealthy, [...].⁵

Likewise it was observed that the income tax cuts would be a 'blow to country people', 'because incomes are much lower in the bush'.⁶

Senator John Cherry, Australian Democrats spokesperson for Regional Development & Services, pointed out that '57 of the 64 localities with an average income above \$50 000

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are metropolitan, but 119 of the 134 localities with an income below \$30 000 are rural.’ In addition, the Senator argued that:

The tax cuts will go disproportionately to urban Australia, adding to the many benefits in terms of extra services and tax cuts that the Howard Government has already given to high income earners.⁷

The income tax cuts aim at creating an incentive to work

In his second reading speech, the Treasurer, The Hon. Peter Costello MP, pointed out that:

These changes are specifically targeted at encouraging Australians to increase their work force participation.

People on middle incomes should not face the top rate of income tax. Policemen and women, fire officers who work harder, who go for a promotion, who do some overtime, cannot be expected to pay 47 cents in the dollar on each additional dollar that they earn. As a matter of incentive, this bill will move that top income tax threshold.⁸

However, it was noted that the income tax cuts are possibly not sufficient:

The [...] problem in our system is that we penalise effort. Many people on low-to-middle income incomes find that additional earnings trigger both tax deductions and a fall in welfare payments, so they end up losing 60 ¢ or more in every extra dollar earned. [...] The budget has eased the disincentive problem without solving it.⁹

The income tax cuts and bracket creep

It was further discussed that bracket creep will have a significant impact on the income tax cuts and comments were made about the Government’s decision not to index the income tax cuts to inflation. One commentator noted that:

The Treasurer has reduced but not abolished bracket creep. Average tax rates will rise, even for those taxpayers whose top marginal rate remains constant at 30 per cent. In fact, bracket creep will make quite a handy contribution to the financing of the Howard government’s election-year spending promise. Most spending programs are costed for four or five years. Over that period, bracket creep will claw back between 9 billion and 13 billion.¹⁰

Australian Taxpayers Inc. stated that:

[T]he Government has raised the income thresholds and tried to claim it has solved bracket creep. That claim is simply untrue.¹¹

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Senator The Hon. Helen Coonan, Minister for Revenue and Assistant Treasurer, countered the above arguments in the Senate, explaining that:

When taken together, these three tax cuts [2000, 2003 and 2004] will have more than returned bracket creep since 1996. In 2004-05, someone on average weekly earnings—around \$40,000 under the new tax scales announced in the 2004 budget—will be about \$550 better off than if the tax scales had been indexed to the CPI. The finding that taxpayers are better off is true for those earning half average weekly earnings or twice average weekly earnings.¹²

Another commentator, whilst acknowledging that Peter Costello has been “dishonest” in

[R]unning the line that no one earning between \$21,600 and \$52,000 a year has suffered from bracket creep because they haven’t been pushed out of the 30 per cent tax bracket,

stated that bracket creep is

[T]he least painful way for politicians to deliver us better schools and hospitals. If we did have full tax indexation, and explicit tax increases were needed to pay for expanded and improved public services, it’s likely those increases would be infrequent and our public hospitals and schools would be in even worse shape than they are.¹³

Mixed support for the income tax cuts

The Labor Party apparently is supporting the tax cuts.

The Shadow Treasurer, Simon Crean, stated that the Labor Party ‘will pass this budget, but we will be presenting our alternatives to it.’¹⁴ The Leader of the Opposition, Mark Latham, confirmed this when asked whether his Party ‘will pass the budget and, in particular, these tax measures’. He answered: ‘Yes, we will. We think that the tax relief from \$52 000 to \$80 000 is needed.’¹⁵

The Democrats and Greens oppose the tax cuts as unfair.

Senator Bob Brown told the media that ‘The Greens will oppose the \$14.7 billion tax cuts to invest the money instead in public health, public education, public housing and parental leave.’¹⁶

For the Democrats, Senator Andrew Bartlett, Australian Democrats spokesperson for Treasury, concluded that

The strong economic position of this country is not only due to the handiwork of Peter Costello but also the sound, responsible management of the Senate. The Democrats will continue that approach with this pre-election Budget. We will not support unfair tax cuts and we will scrutinise expenditure.¹⁷

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Main provisions

The Bill envisages the increase of the income tax thresholds in two steps – Step one will take effect for the financial year 2004-2005; Step two will take effect for the financial year 2005-2006 and later years.

Thresholds for resident taxpayers

The table in Clause 1 of Part 1 of Schedule 7 of the *Income Tax Rates Act 1986* sets out the tax thresholds and rates for resident individuals.

Item 1 of Schedule 1 of the Bill repeals this table and substitutes a table setting out the proposed tax thresholds that will apply for the 2004-05 income year, and for the 2005-06 income year and later years.

The table below sets out the thresholds for resident individuals for the year 2003-04, and the proposed thresholds for the year 2004-05 as well as the year 2005-06 and later years.

2003/04	2004/05	2005/06 (and later years)	Tax Rate
tax thresholds (\$)	tax thresholds (\$)	tax thresholds (\$)	(%)
0 - 6,000	0 - 6,000	0 - 6000	0
6,001 - 21,600	6,001 - 21,600	6,001 - 21,600	17
21,601 - 52,000	21,601 - 58,000	21,601 - 63,000	30
52,001 - 62,500	58,001 - 70,000	63,001 - 80,000	42
62,501 +	70,001 +	80,001 +	47

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Thresholds for non-resident taxpayers

The table in Clause 1 of Part 11 of Schedule 7 of the *Income Tax Rates Act 1986* sets out the tax thresholds and rates for non-resident individuals.

Item 2 of Schedule 1 of the Bill repeals this table and substitutes a table setting out the proposed tax thresholds that will apply for the 2004-05 income year, and for the 2005-06 income year and later years.

The table below sets out the thresholds for non-resident individuals for the year 2003-04, and the proposed thresholds for the year 2004-05 as well as the year 2005-06 and later years.

2003/04	2004/05	2005/06 (and later years)	Tax Rate
tax thresholds (\$)	tax thresholds (\$)	tax thresholds (\$)	(%)
0 - 21,600	0 - 21,600	0 - 21,600	29
21,601 - 52,000	21,601 - 58,000	21,601 - 63,000	30
52,001 - 62,500	58,001 - 70,000	63,001 - 80,000	42
62,501 +	70,001 +	80,001 +	47

Concluding comments

Apart from the reason given by the Government that the tax cuts create an incentive to work, the cuts:

- re-establish the Government's commitment that at least 80 per cent of taxpayers will have a top tax rate of no more than 30 per cent.¹⁸

The 80 per cent level will be met in 2004-05 with the threshold increase to \$58 000; with the threshold increase to \$63 000, 82 per cent of taxpayers will pay

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no more than 30 per cent in 2005-06 and 80 per cent in 2006-07. However, by 2007-08, it is likely that the proportion would have fallen to 78 per cent,¹⁹ and

- halt the imbalance that has occurred over the years whereby much larger proportions of taxpayers have fallen into the top tax bracket.²⁰

This has been caused because the top income threshold has become a smaller multiple of average earnings—1.3 times average earnings²¹ in 2002-03 compared with 8.1 times thirty years earlier. Also, the top taxpayers are paying a larger proportion of total income tax paid—43.7 per cent in 2000-01 compared with 9.5 per cent twenty years earlier.

Endnotes

- 1 The Tax Law Amendment (Personal Income Tax Reduction) Bill 2004 can be found at <http://parlinfoweb.parl.net/parlinfo/Repository/Legis/Bills/Linked/13050400.pdf>.
- 2 The Hon. P Costello, Treasurer, “*Second Reading Speech: Tax Laws Amendment (Personal Income Tax Reduction) Bill 2004*”, House of Representatives, 13 May 2004, at p. 28439.
- 3 *Explanatory Memorandum*, at p 1. The Explanatory Memorandum to the Tax Law Amendment (Personal Income Tax Reduction) Bill 2004 can be found at <http://parlinfoweb.parl.net/parlinfo/Repository/Legis/ems/Linked/13050405.pdf>.
- 4 M Latham, Leader of the Opposition, “*Second Reading Speech: Appropriation Bill (No. 1) 2004-2005*”, House of Representatives, 13 May 2004, p. 28520.
- 5 Senator Andrew Bartlett, “*Democrats propose a fair tax cut - \$13 a week for all*”, media release, available http://www.democrats.org.au/news/index.htm?press_id=3517&display=1, accessed 18 May 2004.
- 6 A Rehn, “*Tax cuts blow to country people*”, Herald Sun (Melbourne), 13 May 2004, at p. 9.
- 7 Senator John Cherry, “*Tax cuts leave open new city/country divide*”, media release, 12 May 2004, available on http://www.democrats.org.au/news/index.htm?press_id=3575&display=1, accessed 18 May 2004.
- 8 The Hon. P Costello, Treasurer, “*Second Reading Speech: Tax Laws Amendment (Personal Income Tax Reduction) Bill 2004*”, House of Representatives, 13 May 2004, at p. 28439.
- 9 P Saunders, “*Move in the right direction but more needed*”, Australian Financial Review, 13 May 2004, at p 79.
- 10 A Mitchell, “*Brackets will creep back*”, Australian Financial Review, 13 May 2004 at p. 78.
- 11 Taxpayers Australia Inc, “*Budget Cuts Inadequate*” media release, available on http://www.taxpayer.com.au/press_releases.asp, accessed 18 May 2004.
- 12 Senator The Hon. Helen Coonan, Minister for Revenue and Assistant Treasurer, “*Budget 2004-05, Question without Notice*”, Senate, 12 May 2004, at p. 22941.

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- 13 Ross Gittins, “*Those tax creeps are the lesser evil*”, Sydney Morning Herald, 19 May 2004, p. 17.
- 14 Simon Cream, Shadow Treasurer, “*Matters of Public Importance: Budget 2004-2005*”, House of Representatives, 12 May 2004, at p. 28311.
- 15 Mark Latham, Leader of the Opposition, Interview with Mike Carlton, 2UE, Sydney, 12 May 2004.
- 16 Senator Bob Brown, The Greens, “*Greens will oppose tax cuts in favour of public health, education and infrastructure*”, media release, 11 May 2004, available on: <http://www.greens.org.au/bobbrown.htm>, accessed 18 May 2004.
- 17 Senator Andrew Bartlett, Australian Democrats, “*Senate must change Budget tax cuts*”, media release, 11 May 2004, available on: http://www.democrats.org.au/news/index.htm?press_id=3558&display=1, accessed on 18 May 2004.
- 18 Made in 1998 when explaining the introduction of the ANTS package tax cuts <http://www.aph.gov.au/parlinfo/billsnet/1e98214.pdf>. Although this was the goal, at least one commentator, states it was never achieved. N Warren, “*Tax: facts, fiction and reform*”, Australian Tax Research Foundation, Research Study 41, p. 110.
- 19 Parliamentary Library estimates, unpublished.
- 20 Stephen Barber, “*Taxpayers in the top tax bracket*”, Parliamentary Library, *Research Note* 47, 2003-04, 29 March 2004.
- 21 Male total average.

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