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Tax Laws Amendment (Personal Income Tax Reduction) Bill 2005

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Law and Bills Digest Section

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Tax Laws Amendment (Personal Income Tax Reduction) Bill 2005

Date Introduced: 12 May 2005

House: House of Representatives

Portfolio: Treasury

Commencement: On Royal Assent

Purpose

The purpose of the Tax Law Amendment (Personal Income Tax Reduction) Bill 2005 (the Bill) is to amend:

- the *Income Tax Rates Act 1986*—to reduce the lowest marginal tax rate from 17 to 15 percent and increase the personal income tax thresholds for the 42 per cent and 47 per cent tax brackets, and
- the *Medicare Levy Act 1986*—to increase the income threshold applicable to taxpayers eligible for the senior Australians tax offset.

Background

Position of significant interest groups/press commentary

The announcement to cut interest rates especially for the two top marginal tax brackets received various responses. Supporting the cuts, the Australian Industry Group (AIG), for example, noted that:

> The Budget makes substantial progress in reforming personal income taxation. These reforms, also advocated by AI Group, will add much-needed incentive to workforce participation; saving and business investment.[1]

The Business Council of Australia (BCA), in a media release issued on Budget night, shared this view and 'welcomed the planned program of substantially reducing the income tax on individuals over four years.' However, Mr Hugh Morgan, President of the BCA, was cited as noting that:

> the underlying issue of bracket creep and international competitiveness of the individual and business and tax regime remained on the agenda for further examination.[2]

The issue of bracket creep is also a concern for the Australian Council of Trade Unions (ACTU). In a media statement, the ACTU announced its view, stating that:

> The tax cuts are biased in favour of high income earners and fail to compensate low and middle income Australians for bracket creep and the rise in cost of housing, health, education, childcare and other basic services under the Howard Government. [3]

Responding to the release of the 2005 Federal Budget, ACTU President Sharan Burrow was cited saying that:

> As a result of the last two Budgets high income earners stand to gain more than $130 a week in tax and superannuation relief while more than 75% of working people - everyone earning less than $58,000 a year - gets between zero and $6 a week.[4]

The major Australian political parties have responded to the Budget, some by announcing their own plans in relation to tax cuts.

Labor's response to the Government's proposed income tax reductions —the Budget Reply

Unlike Labor's Budget Reply for the 2004-2005 Budget, this year's Budget Reply delivered on 12 May 2005 contained specific tax measures.[5] Branding the Government's announced changes to the personal marginal tax rates unfair, Labor Opposition Leader Kim Beazley revealed his own vision of a fairer reduction of personal marginal tax rates.[6] He proposed the following:

> The government should raise the threshold where the 30c rate cuts in from $21,600 to $26,400. It should implement a welfare to work bonus that would provide an effective $10,000 tax-free threshold for people earning up to $20,000 per year. […] In addition, from 1 July 2006 the government should raise the threshold where the 42c rate cuts in from $63,000 to $67,000 and raise the threshold where the 47c rate cuts in from $80,000 to $100,000. This package would deliver a tax cut of up to $9 a week for those earning up to $25,000—double what the government is offering. It would deliver a $12 tax cut for those earning from $25,000 to $70,000—double what the government is offering. It would preserve the government's tax cut for people earning from $70,000 up to $100,000. We recognise that people on around $80,000 are not rich, but politicians on $105,000 and over are doing all right. This package would deliver $40 to people who earn $105,000 and above—one-third less than what the government is offering; a much fairer outcome.

In addition to presenting and outlining Labor's own vision of fairer income tax reductions, Kim Beazley also announced that Labor will attempt to veto in the Senate the cuts as proposed by the Government. During a radio interview with Radio 2GB, he justified this decision saying that:

> I want to, for the Labor Party, I've got to do two things: I've got to hold the Government accountable and I've got to make a stand on what we think is good policy. We'll lose the votes, that's what happens when you're in Opposition, but at least we'll make the point.[7]

The Democrat's response to the Government's proposed income tax reductions

The Australian Democrats released their own Budget Address in Reply.[8] In this Reply, the Democrats noted that:

> High income earners have done very well but those on the lowest incomes must be satisfied with the crumbs. A person on only $10,000 a year will receive a tax cut of $80 a year while a person on $125,000 gets a tax cut of $4,500 a year, plus a superannuation tax cut of around $1,500 a year.[9]

To achieve a fairer distribution of tax cuts, the Democrat's proposal has the following three features:

- every taxpayer would receive tax savings equivalent to $680 a year,
- the tax-free threshold would be lifted to $10 000, and
- marginal tax rates would be indexed to address bracket creep.

Pointing towards several tax measures already available to higher and high income earners to reduce their tax burden, including, for example, negative gearing or capital gains tax cuts, the Democrats announced that they will not:

> ….support tax cuts for high income earners while Australians in poverty pay income tax. Our priority is tax cuts for lower income earners. The Democrats have often spoken here in the Senate about the importance of reforming the tax system to prevent poverty traps and encourage people off welfare and into work.[10]

The Greens' response to the Government's proposed income tax reductions

In various media releases, the Greens also pointed out that the income tax reductions as proposed by the Government would lead to unfair results. Senator Bob Brown noted that the tax cuts announced by the Treasurer:

> will accelerate the growing gap between rich and poor. The budget tax cuts for low income earners are tiny compared to those for the rich. The poor get the mouse's share.[11]

Arguing that this is a 'budget that attacks the poor and advantages the wealthy',[12] Senator Nettle stated in a media release that:

> This budget hurts low-income families and poor Australians while squandering the surplus on billion-dollar handouts to the wealthy … "This is a blueprint for a less compassionate society".[13]

Other parties' and independents' responses to the Government's proposed income tax reductions

At the time of writing this Bills Digest, no official comment had been released by Family First. Senator Meg Lees is in favour of a fairer tax package and has reportedly expressed an intention to oppose the reductions as announced.[14] In the same article it was noted that Senator Harris announced not to oppose the reductions whilst the other two independent Senators, Senator Harradine and Senator Murphy, had not yet stated a position.[15]

Any consequences of failure to pass?

A failure to pass this legislation due to lack of support in the Senate will only cause a short-lived delay of its passage until the Government obtains control in the upper house on 1 July 2005. However, there is a discussion as to whether the tax cuts can become effective on 1 July 2005, even though the Bill has not been passed through Parliament. This issue is dealt with in more detail below under 'Concluding comments'.

Main Provisions

Resident taxpayers

The table in Clause 1 of Part I of Schedule 7 of the *Income Tax Rates Act 1986* sets out the tax thresholds and rates for resident individuals. **Item 1** of the Bill repeals this table and substitutes a table setting out the proposed tax thresholds that will apply for the 2005-06 income year, and for the 2006-07 income year and later years.

For ease of comparison, the table below sets out the currently applicable thresholds and respective tax rates for resident individuals for the year 2004-05 (light grey), and the proposed thresholds and respective tax rates for the year 2005-06 as well as the year 2006-07 and later years (dark grey).

2004/05 tax thresholds ($)	Tax Rate (%)	2005/06 tax thresholds ($)	2006/07 (and later years) tax thresholds ($)	Tax Rate (%)
0 – 6 000	0	0 – 6 000	0 – 6 000	0
6 001 – 21 600	17	6 001 – 21 600	6 001 – 21 600	**15**
21 601 – 58 000	30	21 601 – **63 000**	21 601 – **70 000**	30
58 001 – 70 000	42	**63 001 – 95 000**	**70 001 – 125 000**	42
70 001 +	47	**95 001** +	**125 001** +	47

Bold figures highlight the changes proposed by the Bill

Non-resident tax payers

The table in Clause 1 of Part II of Schedule 7 of the *Income Tax Rates Act 1986* sets out the tax thresholds and rates for non-resident individuals. **Item 2** of the Bill repeals this table and substitutes a table setting out the proposed tax thresholds that will apply for the 2005-06 income year, and for the 2006-07 and later income years.

The table below sets out the current thresholds and respective tax rates for non-resident individuals for the year 2004-05, and the proposed thresholds and respective tax rates for the year 2005-06 as well as the year 2006-07 and later income years.

2004/05 tax thresholds ($)	Tax Rate (%)	2005/06 tax thresholds ($)	2006/07 (and later years) tax thresholds ($)	Tax Rate (%)
0 – 21 600	29	0 – 21 600	0 – 21 600	29
21 601 – 58 000	30	21 601 – **63 000**	21 601 – **70 000**	30
58 001 – 70 000	42	**63 001 – 95 000**	**70 001 – 125 000**	42
70 001 +	47	**95 001** +	**125 001** +	47

Bold figures highlight the changes proposed by the Bill

Medicare levy threshold

After the above amendments have taken effect, senior Australians who receive the Senior Australians' Tax Offset will be able to earn up to $21 968 before they become liable for income tax. To address the fact that the Medicare levy will kick in prior to this tax liability arising, **item 4** of the Bill proposes the necessary amendment which will increase the Medicare levy threshold from $20 500 to $21 968. Note, however, that the Bill will only increase the Medicare levy threshold for individual taxpayers, the family Medicare levy threshold will not be increased because, according to the Explanatory Memorandum, 'the current senior family threshold of $31 729 is already sufficient to ensure that senior couples do not incur the Medicare levy until they incur an income tax liability.'[16]

Likewise, **item 3** of the Bill proposes a change to the phase in limit for a single senior Australian who is eligible for the Senior Australians' Tax Offset, increasing the limit from $22 162 to $23 749.

Concluding Comments

Costs of the measure

According to the Explanatory Memorandum, this measure will have the following financial impact over the next four years:[17]

2005-06	2006-07	2007-08	2008-09
$3.1 billion	$5.6 billion	$6.3 billion	$6.7 billion

Compliance cost impact: Nil.

Delay in the Senate: no tax cuts on 1 July 2005?

Before the government takes control of the Senate on 1 July 2005, the Labor party under Kim Beazley is determined to veto the proposed income tax package. Similarly, the Greens and the Democrats have also announced that they would oppose the package as it stands. In contrast, the Government is determined to implement the changes sooner, rather than later, so that the changes will have the desired immediate effects for the taxpayers.[18]

There has been considerable debate as to the possible implications of the Bill's delay in the Senate. The question is whether the changes can take effect from 1 July 2005 even though they are vetoed by the opposition. To achieve tax cuts for income earners from 1 July 2005, a number of possible courses of action have been suggested, including that the Senate including the new Senators may sit on 1 July 2005, or early the following week, or that the changes could be backdated.[19]

With respect to the backdating of the legislation, however, the Treasurer announced on 12 May 2005, that he had received advice from the Commissioner of Taxation that a tax can only be cut on the basis of legislation and concluded that:

> you cannot cut taxes until the legislation is passed and so if the legislation is not passed, people, if Mr Beazley is able to defeat the legislation, I am afraid Australians can't have a tax cut on 1 July of 2005.[20]

This summary of the Tax Commissioner's advice seems to suggest that, if backdating the legislation is possible, the tax cuts will nevertheless not be available on 1 July 2005. This announcement warrants the following observations:

Professor Ratnapala has argued, that the 'application of the most fundamental rule of constitutionalism' commands that any compulsory exaction of monies may only occur on the basis of properly enacted law.[21] This does not preclude taxation laws, enacted to authorise the exaction of monies, being retrospective in operation.[22] Indeed, the High

Court has held on several occasions that the Australian Parliament has very broad powers to make retrospective legislation.[23] This includes the area of tax legislation where so called 'legislation by press release' has become common place.[24] Once the compulsory exaction of monies is authorised by properly enacted laws, the collection of those monies becomes an administrative issue. This raises at least two further issues:

First, in relation to the withholding of income tax, the Commissioner has the power to determine and issue the income tax withholding schedules to be applied to the taxpayer's income under the provisions of the *Taxation Administration Act 1953* (TAA).[25] These schedules are the basis for the administrative implementation of the law, authorising the income tax exaction. Under section 15-15 of the TAA, the Commissioner has the power to vary, even to nil, the amount payable by one or a group of taxpayers under the withholding schedules. Under this section, modifications to the schedules are possible so long as they reduce the taxpayer's tax burden. Considering this power to vary the withholding schedules, it is possible that the Commissioner may exercise his discretion to vary the withholding schedules in anticipation of the proposed income tax reductions.

Parliament should note that the withholding schedules, as well as any modification of those schedules for a group of taxpayers, are likely to be legislative instruments within the meaning of the *Legislative Instruments Act 2004* (LIA).[26] It follows that the instrument must be registered in the Federal Register of Legislative Instruments and will be subject to Parliamentary Scrutiny and the disallowance procedures set out in the LIA.

Second, the Commissioner has implemented an administrative framework to anticipate retrospective tax legislation, adopting specific administrative guidelines to deal with the administrative 'anticipatory' implementation of retrospective taxation laws. These guidelines are designed to identify possible steps taxpayers may take to already meet their prospective obligations under the announced measures and allow the Commissioner 'in limited situations, [to] advise taxpayers to meet their obligations by anticipating the effects of a proposed change to the law.'[27] The guidelines, which can be accessed together with further information on the ATO's webpage, require the ATO before advising taxpayers of how to comply with the announced tax measure, to have regard to factors such as the likelihood of the legislation passing in Parliament and the impact on tax revenue.

Under this administrative framework, it seems at least possible that those collecting income tax could be permitted to take steps necessary to anticipate the impending tax changes, including the reduction of income tax deductions, without being penalised for passing on the reduced collection to the ATO.[28]

Endnotes

1 H. Rideout, *A Budget of conviction that makes progress on Key National Objectives*, media release, 10 May 2005.

2 Business Council of Australia, *With 'Election' Budget Out Of The Way, Focus Can Now Switch To Serious Reform*, media release, 10 May 2005.

3 Australian Council of Trade Unions, *Budget is no lifeline for working families: surplus squandered,* media release, 11 May 2005.

4 ibid.

5 T. John, 'Tax Laws Amendment (Personal Income Tax Reduction) Bill 2004', Bills Digest no. 145, Parliamentary Library, Canberra, 2003-04.

6 K. Beazley MP, 'Second reading: Appropriation Bill (No. 1) 2005-2006', House of Representatives, *Debates*, 12 May 2005, p. 81.

7 K. Beazley MP, Interview with Ray Hadley, Radio 2GB, Sydney, 11 May 2005.

8 Note that at the time of writing this Bills Digest, the Budget Reply available on the democrat's web-page was still at the draft stage.

9 Senator L. Allison, *Budget Address in Reply*, draft speech, 12 May 2005, accessed 24 May 2005.

10 ibid.

11 Senator B. Brown, *Costello puts his political future first*, media release, Hobart, 10 May 2005.

12 Senator K. Nettle, 'Budget: Statements and documents', Senate, *Debates*, 12 May 2005, p. 80.

13 Senator K. Nettle, *Budget hurts families and poor*, media release, Surry Hills, 10 May 2005.

14 M. Grattan and P. Hudson, 'Lees bid for fairer tax deal', The Sunday Age, 15 May 2005, p. 2.

15 ibid.

16 Explanatory Memorandum, op. cit., p. 6.

17 Explanatory Memorandum, op. cit., p. 1.

18 At the time of writing the digest, it was unclear how the micro parties and independents would vote in the Senate. See brief discussion above on page 5 of this Digest.

19 A list of possible solutions can be found in M Grattan's article, 'Hard line, harder sailing', *The Sunday Age*, 15 May 2005, p. 19.

20 P. Costello, Treasurer, *Doorstop Interview*, Ministerial Entrance, Parliament House, Canberra, Thursday, 12 May 2005

21 S. Ratnapala, *Australian Constitutional Law, Foundations and Theory*, Oxford University Press, Melbourne, 2001, p. 242.

22 Retrospective legislation is not lesser or 'deficient' legislation—retrospective legislation is legislation properly so called from the moment of its stipulated commencement day.

23 Arguably the most important cases confirming this principle are *R v Kidman* (1915) 20 CLR 425; *R v Humby; Ex parte Rooney* (1973) 129 CLR 321 and *Polyukhovich v The Queen* (1991) 172 CLR 501.

24. C. Field, 'Taxation Laws Amendment (Superannuation Contributions) Bill 2000', Bills Digest No. 68, Canberra, 2000–01.

25 The Commissioner for Taxation has announced that he will issue new schedules to reflect: A) the changes necessary to implement the income tax threshold reductions announced in last year's 2004-2005 Budget; and: B) the reduction of rates and thresholds as announced in this year's 2005-2006 Budget. Option B will become applicable should the Bill pass through Parliament before 1 July 2005. Australian Tax Office, *Tax office prepares for new withholding tax rates*, media release, NAT2055/29, Canberra, 19 May 2005.

26 In fact, the Commissioner for Taxation has announced that the 'withholding schedules must be tabled in both Houses of Parliament as legislative instruments.' Australian Tax Office, *Tax office prepares for new withholding tax rates*, ibid.

27 Australian Tax Office, Administrative treatment of retrospective legislation, available at http://www.ato.gov.au/taxprofessionals/content.asp?doc=/content/45130.htm&page=1&H1, accessed 13 May 2005.

28 This aspect has been raised as a possible option in M Grattan, op. cit., note 19.

Members, Senators and Parliamentary staff can obtain further information from the Information and Research Services on (02) 6277 2699.