



14 April 2008

Secretary
Senate Economics Committee
PO Box 6100
Parliament House
Canberra ACT 2600

Dear Secretary,

Re: Inquiry into Tax Laws Amendment (Personal Income Tax Reductions) Bill 2008

ACOSS appreciates the opportunity to make a brief submission to this inquiry.

The proposed income tax cuts would raise the second tax threshold, increase the Low Income Tax Offset, and reduce the 40% tax rate to 37%. When fully implemented in 2010-11 they would add \$14 per week to the disposable income of a taxpayer on \$30,000, \$26 to a taxpayer on \$60,000, \$53 to a taxpayer on \$120,000 and \$116 to a taxpayer on \$500,000. In 2010 they are estimated to cost \$13.9 billion per year, or a total of \$30.8 billion over the three years commencing in 2008-09. The proposed tax cuts follow a sequence of five tax cuts implemented over the last 5 years.

Our approach to assessing this and other policies is to ask whether they are the best way to improve the circumstances of low income and disadvantaged people and reduce social exclusion in Australia, and to improve economic efficiency and the sustainability of economic growth.

On this basis, ACOSS has expressed the view that we believe well targeted investment in community services would deliver more cost effective and longer lasting improvements in the living standards of low and middle income Australians than further tax cuts at this time.

We acknowledge that notwithstanding this, the Government has made an election commitment to introduce tax cuts. If the tax cuts proceed, the challenge is how to reduce deficits in community services at the same time.

The main reason for our emphasis on investment in services is the growing gaps between service provision and the community's needs. For example, the Home and Community Care program is chronically under-funded yet by 2019, there will be an increase of almost 50% in the number of people across all age groups who rely on community care services. At least 40% of adult Australians cannot access dental care when they need it. The standard level of funding for Job Network providers to invest in training and other support to improve the job capacity of a jobseeker who has been unemployed for 2 years is approximately \$500. An estimated 30% of low income households pay more than 30% of their income on rent or mortgages in 2003, yet the national waiting list for public and social housing stood at 234,000 in 2006.



Substantial investment in services is especially important for those on the lowest incomes. Last year ACOSS released research conducted by the Social Policy Research Centre for Australia Fair indicating that in 2005, 2,210,000 Australians (11.1% of all Australians), including 412,000 children lived below an internationally accepted poverty line.

ACOSS welcomes the Government's commitments to address 'deficits' in community services, including but not limited to the proposed investments in early childhood education and care in Indigenous communities, funding to help reduce public dental waiting lists, and the 450,000 Vocational Education and Training places for low skilled workers and jobless people. It is vital that this momentum is maintained.

Our emphasis on investment in services is consistent with shifts in public opinion towards public spending and taxing. Recent opinion polls have found that more Australians prefer the Government to raise expenditure on community services such as health and education, instead of reducing income taxes. This reflects a growing awareness that the benefits for low and middle income earners would be more widespread and more sustained if higher public revenues were invested in services instead of tax cuts. For example, over one third of Australian households do not benefit from income tax cuts because their incomes are too low to pay tax.

The situation is complicated by a build up of inflationary pressures in the economy. Inflation has risen slowly but steadily over the past three years and the Reserve Bank has raised interest rates on eight occasions in order to dampen it. Over the year to December 2007, the underlying rate of inflation was 3.6%. At this stage of the business cycle, with high levels of borrowing and labour in short supply, there is a risk that inflation will remain above the Reserve Bank's target zone for some time. Any further increases in interest rates are likely to adversely affect housing affordability and to lead to higher unemployment.

The Government acknowledges this problem and has flagged its intention to reduce expenditure in the 2008 Budget in order to increase the surplus and take pressure off demand for goods and services across the economy. It has set a target of a surplus of at least 1.5 per cent of GDP in 2008-09. In this context, the tax cuts have the effect of increasing the pressure to reduce expenditure. This raises the risk that further action to close the gaps in essential services may be delayed.

One option to offset the fiscal and economic effects of the tax cuts without constraining expenditure on essential services and payments for low and middle income people is to target those expenditures that mainly benefit people with the greatest capacity to pay.

Many of these expenditures are on the taxation side of the Budget ledger. The Treasury estimates that since 1997-98 tax expenditures have grown by 51 per cent in real terms since from \$33.1 billion, to reach \$49.9 billion in 2007-08. Many tax expenditures disproportionately benefit people on higher incomes, including:

- Tax concessions for employer superannuation contributions;
- The concessional tax treatment of large employee termination payments such as 'golden handshakes';
- The concessional treatment of fringe benefits in the form of 'company cars'.



Unlike direct expenditures, tax expenditures are not subject to the rigour of the annual Expenditure Review process. One option to bring them under greater scrutiny would be review tax expenditures along with related portfolio expenses as part of this process.

On the direct expenditure side of the ledger, many payments and rebates extending to people on high incomes could be curbed. Examples include Family Tax Benefits and the Health Insurance Rebate for 'extras' policies.

If the tax cuts proceed, then the most equitable way for the Government to meet its fiscal commitments would be to reduce both tax and direct expenditures that benefit those on higher incomes.

A specific concern that we have about the Bill before the Parliament is that, by locking in three rounds of tax cuts over the next three years, it would greatly limit the Government's future fiscal flexibility. Given divergent views about the economic outlook both here and overseas, if the Parliament decides to proceed with further tax cuts then it would be prudent to legislate separately for each round.

Should you have any inquiries about this submission, please contact me at this address.

Yours sincerely,

Andrew Johnson
Executive Director

Note on sources:

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