

Taxing issues

Why does tax reform matter to the community sector, beyond that it allows sufficient revenue to be raised for programs and services? Australian Council of Social Service (ACOSS) CEO Cassandra Goldie outlines how tax can change the way disadvantage is caused and addressed, and what we can hope for from the Federal Government's National Tax Forum.

Why is ACOSS interested in tax reform – and why is it an issue that the community sector should be fully involved in?

Firstly, we need an adequate revenue base to fund community services and income support payments in future years, which will become more costly as the population ages. The largest and one of the most equitable taxes is the personal income tax, but it will not be capable of funding essential benefits and services in future unless its 'tax base' is repaired by closing off opportunities for people to avoid paying tax at the appropriate marginal rate. The most efficient and fairest way to strengthen public revenue is to tax different forms of income more consistently by closing off tax loopholes and shelters.

Secondly, the distribution of income and resources in the community is very much influenced by the tax system and, of course, the income support system. Despite all the myths around taxation, the present system in Australia actually raises a relatively low level of tax overall – our total tax revenue is in the lowest-third of the 30 OECD countries. But we raise it unfairly. Those on the highest incomes can generally avoid paying tax at 45 cents in the dollar (the highest rate) if they are well advised. At the other end of the income scale, serious anomalies in the income support system mean that single adults on the Newstart Allowance are receiving \$128 less per week than someone on a pension. That's not based on relative need, it's an historical anomaly based on a perception that people on allowance payments are 'less deserving'.

The third reason we're interested in tax reform is that the tax system has an impact on behaviour. We hear all the time about tax having to provide incentives to work, but it also contains a raft of incentives to invest money in one place rather than another. That is a major cause of housing unaffordability in Australia and increases the risk of speculative bubbles in investment in assets that can cause great economic harm, as we have seen recently in the United States and Ireland, for example.

A fourth reason is how the community sector itself is taxed. Currently the tax treatment of charities and community organisations is complex and inequitable, riddled with historical anomalies and inequities. For example, an organisation that provides emergency relief directly to poor people can get the full range of tax concessions for charities, but an organisation that advocates on behalf of poor people cannot.

So ACOSS will be participating in the Federal Government's October tax forum and continuing our long-term work in tax policy with two major goals in mind:

- to seek to resolve the problems identified above, and
- to demonstrate that the community sector's interests aren't confined to the quality of community services or the level of benefit payments enabled by tax, but that we understand that the economic policy issues around tax reform have just as much impact on the lives of the people we're concerned about.

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WHAT DO WE WANT?

The Henry Review – or as it's more formally known, the Australia's Future Tax System report, handed down in 2010 by former Treasury Secretary Ken Henry - was the product of two years of intensive discussion amongst tax and social security experts. It provides a solid framework for reform over the next decade, and includes many proposals that we have long advocated. That now needs to be converted – by both government and community – into a series of viable reform packages.

But we have to be patient and strategic. It is one thing to develop the ideal model of income tax; getting reform through Parliament is tougher. We will focus on four key problems that concern the community, which reform of the tax and income support reform could help resolve:

1. Personal income tax (see breakout on pp8-9)
2. Adequate and equitable retirement incomes
3. Social security reform
4. Distortion of investment decisions



Adequate and equitable retirement incomes

Low and middle income earners approaching retirement are increasingly concerned about having adequate retirement incomes and whether good quality government-funded health, community and aged care services will be available when they need them. Younger generations are increasingly concerned that they will be called upon to meet those costs.

The present superannuation system is poorly designed to meet the retirement income needs of lower and middle income earners because tax breaks for super are skewed heavily towards those in the top tax brackets – fifth of their total value goes to the top 5 per cent of wage earners, and half to the top 20 per cent. Those on the lowest wages do not benefit at all from the tax breaks, and indeed pay tax at a higher rate on super guarantee contributions than on their wages. There is a strong case for restructuring superannuation tax breaks in favour of those on lower incomes – who need the most support to save for retirement and are the least likely to do so without strong incentives (see pp25-27).

While the overall cost to governments of population ageing is relatively low in Australia due to our targeted income support system, future governments will find it hard to fund health and community services, and will increasingly resort to user pays funding models, unless those mature age people with a capacity to pay income tax do so.

Currently less than a quarter of people aged over 65 pay income tax. This is partly because their incomes are often too low but also because those who are relatively well-off can avoid doing so. For example, a 55 year old in a high tax bracket can save considerable tax by churning their earnings through super accounts and taking advantage of age-based tax offsets – thus cutting their tax rates from 30-45 cents in the dollar down to 15 cents or less. People can thus take advantage of tax breaks intended to encourage retirement saving without saving

anything at all! One reason such inequitable and antiquated tax breaks survive is that the system is so complex that only those who can afford professional advice understand it.

Social security reform for people of working age

The present division between 'pension' and 'allowance' payments is based on the old moral notion of the 'deserving' and 'undeserving' poor. Thus, people who are deemed 'able to work' (unemployed people) 'deserve' lower payments than those who have disabilities or caring responsibilities who are therefore 'unable to work'.

These boundaries are increasingly fluid and we no longer assume that parents and people with disabilities are 'unable to work'. Yet the social security system is still lost in a previous era. Unemployed people currently receive \$128 per week less than an age or disability pensioner. This gap is growing every year due to different indexation arrangements. The single age pension rose by \$32 per week in 2009, but unemployed people, sole parents and students were deemed less worthy and missed out.

The differences in social security payments are arbitrary and not based on actual living costs. For example, most research on poverty and deprivation concludes that unemployed people and sole parents on income support face a high risk of financial hardship, yet they receive among the lowest payments. The basis for the increases in single rates of pension that followed the 2009 Pension Review was that the living cost of a single pensioner was typically at least two thirds that of a couple. Yet this relativity was not extended for sole parents or single unemployed people or students.

Over the last decade, the position of those people of working age on pension payments has become less secure, as governments have taken advantage of the gap between pensions and allowances to shift people to the lower allowance payments. The 2006 Welfare to Work policy diverted people deemed able to work at least 15 hours a week from the Disability Support Pension (DSP) to Newstart Allowance, and sole parents whose youngest child was over seven years of age from Parenting Payment to Newstart Allowance. The latest Federal Budget further restricted access to Parenting Payment for many sole parents with older children. Access to disability pensions is increasingly closed off to new entrants and those already on the DSP are subject to vilification in the media over so-called disability 'fraud'.

These anomalies are inequitable, entrench poverty, and are one of the main disincentives for people on pension payments to seek paid work. There is a widespread fear that if people leave the pension system they will not be able to return to it if they need income support in future, and will have to survive on the \$34-a-day Newstart Allowance.

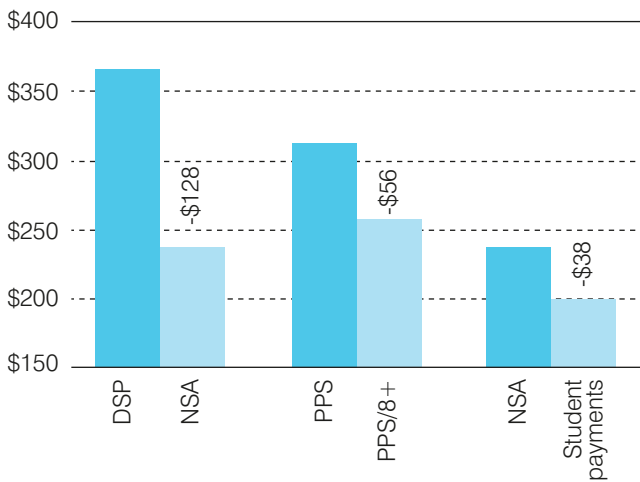
ACOSS is seeking structural reform of working age income support payments that equalises the base rates of payment and supplements this with additional payments for people with

higher living costs, including the costs of a disability and caring for children alone. Similar proposals are being implemented in the UK and New Zealand.

The Henry Review stopped short of major structural reform but did recommend that single people on Allowance payments receive the same increases as pensioners (currently worth around \$50 per week) and that allowances and pensions for people of working age be indexed in the same way, based on wage movements.

We also seek better Rent Assistance to improve housing affordability and the easing of some of the most severe personal income tests to improve work incentives. In particular, the 60 cents in the dollar taper rate for Newstart Allowances discourages many parents and people with disabilities who have part time work requirements from seeking such employment. The latest Federal Budget proposes to ease the Newstart income test for sole parents, but the same argument applies to people with disabilities and partnered parents who are required to seek a part time job.

Rates of payment for singles June 2011 (\$pw)



DSP – Disability Support Pension; NSA – Newstart Allowance; PPS – Parenting Pension (single)

A person who moves from Disability Support to employment and later loses the job can lose \$128 per week if they end up on Newstart.

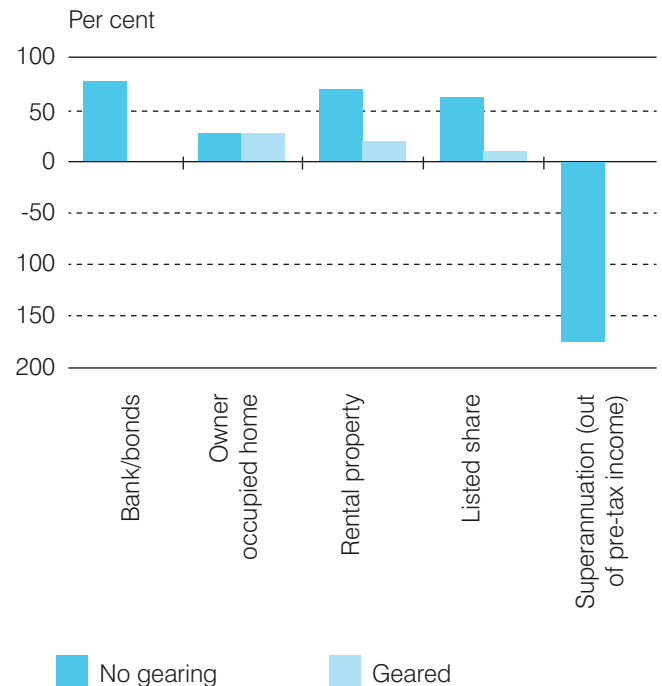
When the youngest child of a sole parent turns eight, the family loses \$56 per week for the same reason, and when an unemployed early school leaver starts to study full time to improve their job prospects, they stand to lose \$38 per week as they move down to a student payment.

Distortion of investment decisions

A further problem that needs attention is the way in which the tax system distorts investment decisions and, as a result, makes housing unaffordable and increases the risk of asset bubbles in the economy, posing a threat to Australia’s economic development.

Over the last decade or so, there has been no shortage of investment in Australia, including from overseas. The argument that Australia is ‘uncompetitive’ as an investment destination because of our income tax rates for individuals and corporations doesn’t hold water. Investment decisions are based on many other factors apart from tax including political stability, sound physical and social infrastructure and a well educated population. The problem is that our tax system encourages inefficient investment. A good example of this is the concessional treatment of capital gains, compared to other forms of investment income like bank interest. Capital gains are only taxed when an asset is sold, and since 2000 has only been taxed at half the normal rate (in the case of individual investors). This encourages people to invest in property and shares and other assets that appreciate in value. Combined with the effects of ‘negative gearing’ – where individuals invest in real estate, agricultural schemes or shares and use their investment losses to offset tax on their other income (especially wages) – this has encouraged an explosion of speculative investment in property, and to a lesser extent shares.

Real effective marginal tax rates on different investments by a high income earner



Losses claimed on rental properties



These biases in the tax system, together with weaknesses in the tax treatment of land and housing (through stamp duties and land tax) by the State and Territory Governments – have contributed to the fact that Australia has among the highest housing prices in the world. (see Saul Eslake on pxxx). A further problem with speculative assets price booms is that they make the economy harder to manage, as the Reserve Bank has pointed out.

WHAT CAN WE EXPECT?

With the mining and carbon taxes already major issues facing the Federal Government, we don't expect a major new tax reform package that addresses disadvantage and inequity to emerge from the Tax Forum. Tax reform is difficult and it takes time to build community support for major change.

A good outcome of the forum itself would be if the issues outlined above got a good airing and attracted some commitment from the Government to consider further reform in these areas and consult with the community.

A bad outcome would be an over-emphasis on issues that are very unlikely to attract consensus for future tax reform such as an increase in the Goods and Services Tax (GST). There also seems little point to further debate initiatives the Government has already announced such as the Clean Energy Future package and the mining tax. And, instead of starting from scratch, the Tax Forum should start with the positive reform proposals advanced by the Henry Report, including:

- Fairer tax treatment of super contributions similar to long-standing ACOSS proposals.
- More consistent tax treatment of investments via a standard 40 per cent discount on personal tax rates for investment income (which would lower taxes on bank interest and raise them on capital gains).
- Curbs on the deductibility of investment expenses.
- An increase in the single rate of Newstart Allowance and a common system of indexation for working age payments.
- Broadening the Land Tax to properties with owner occupied housing and abolishing stamp duties.
- Reducing tax concessions for non-superannuation termination payments (golden handshakes) and for capital gains on small business assets.
- A standard work related deduction in return for curbs on excessive claims.
- Abolition of poorly targeted tax concessions such as the Senior Australians Tax Offset.

These proposals are a good place to start.

Dr Cassandra Goldie is Chief Executive Officer of ACOSS. ACOSS is a member of the Community Tax Forum, which was established in 2008 along with the Australian Council of Trade Unions, Consumers' Federation of Australia and Australian Conservation Foundation. It is convening a meeting in Melbourne on 22 September of representatives of affiliated organisations who will be attending the National Tax Forum. <http://www.taxwatch.org.au/communitytaxforum>