



Parliamentary
Budget Office

Bracket creep and its fiscal impact

Cameron Chisholm

**Presentation to Australian Conference
of Economists, 11 July 2022**

Tax system principles



The diagram consists of three circles arranged horizontally. The leftmost circle is blue and contains the word 'Efficiency'. The middle circle is red and contains the word 'Equity'. The rightmost circle is purple and contains the word 'Sustainability'. All circles have a black outline and are set against a white background.

Efficiency

Equity

Sustainability

Outline

The importance of personal income tax to Australia's fiscal position

A brief history of bracket creep in Australia

Can Australia rely on bracket creep to reduce public debt?

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Can Australia rely on bracket creep to reduce public debt?

Commonwealth tax receipts grew significantly from around 1960 to the mid-1980s



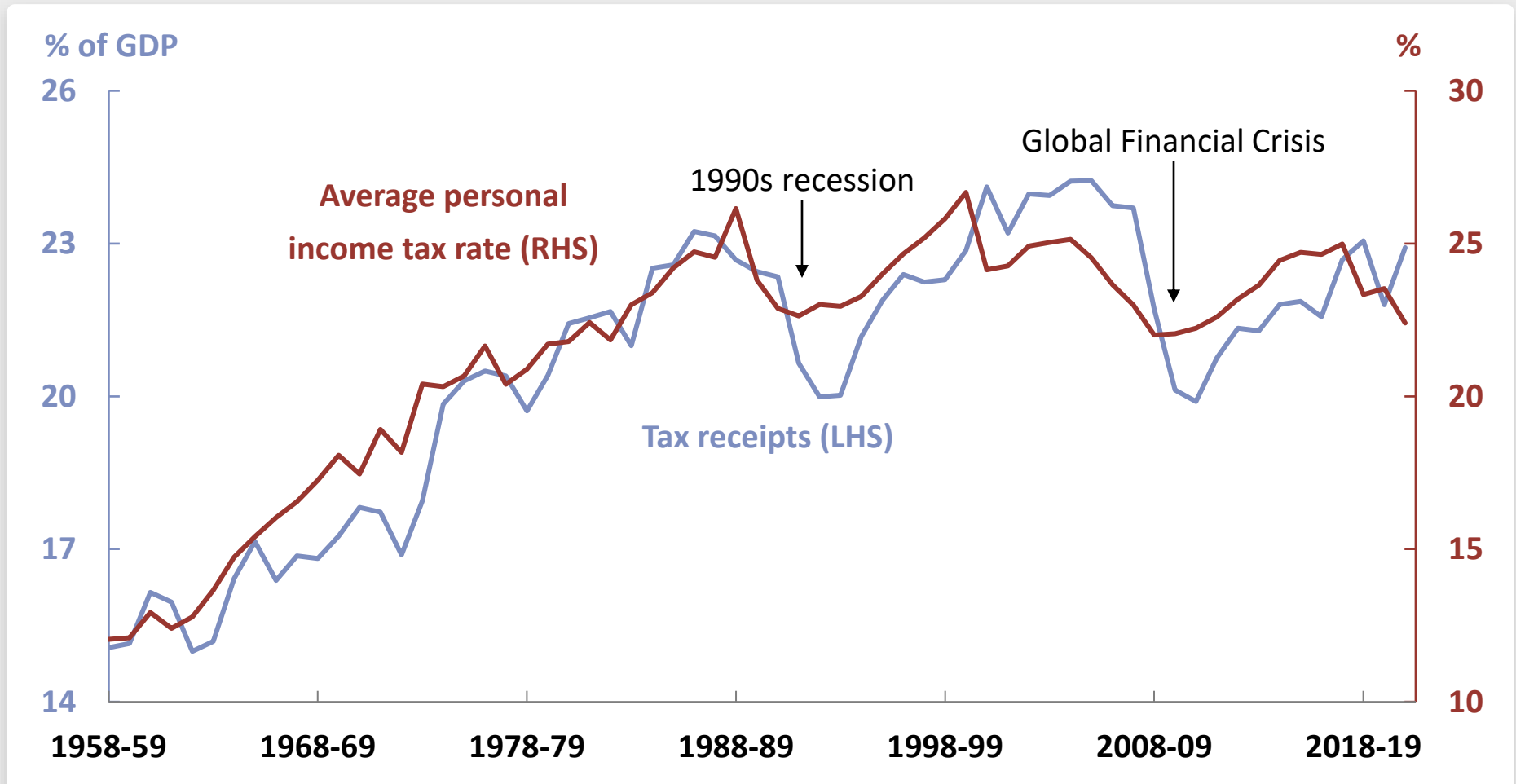
Source: ATO Taxation Statistics, 2022-23 Budget, and PBO analysis

Commonwealth tax receipts grew significantly from around 1960 to the mid-1980s



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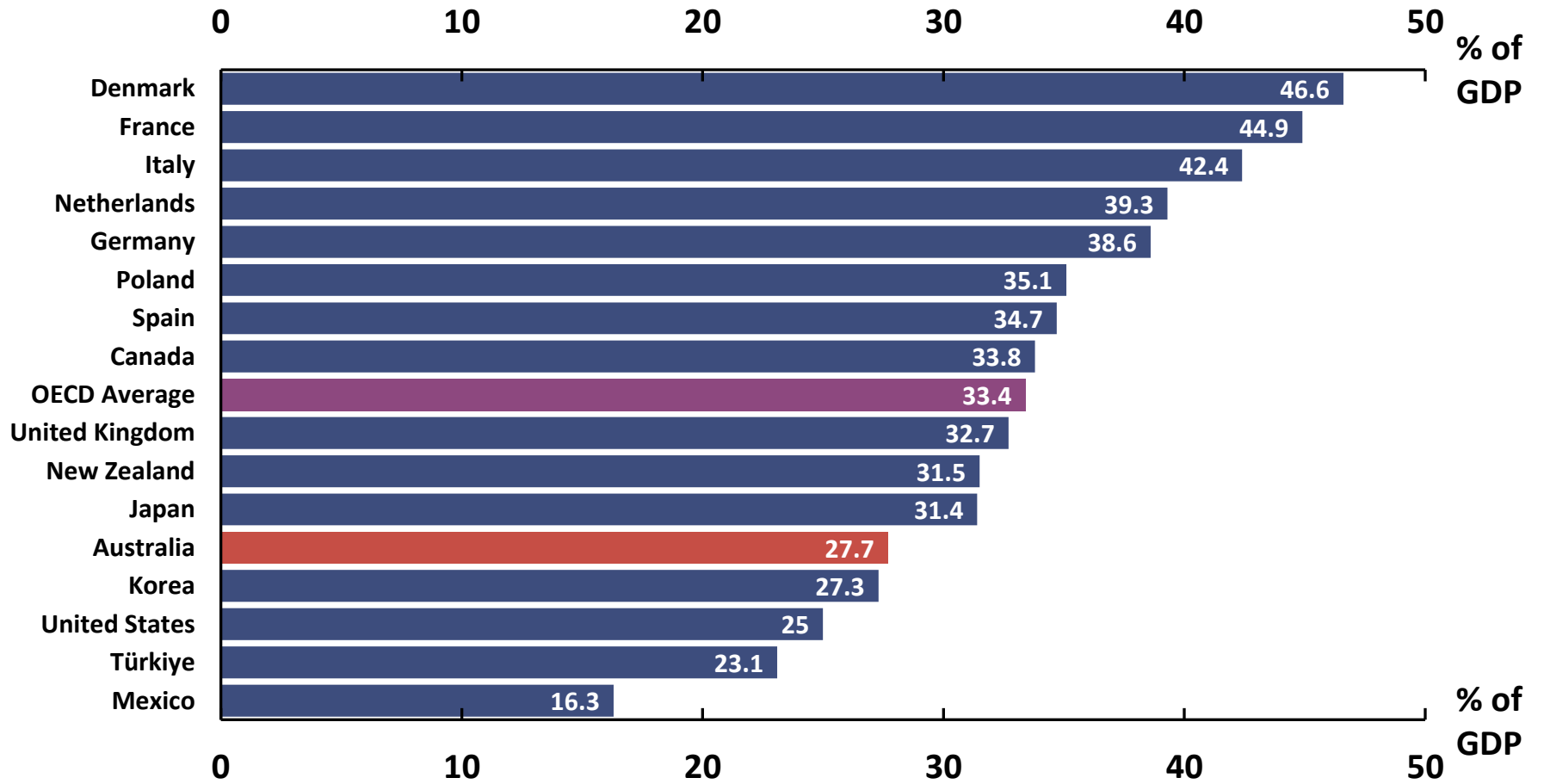
The average rate of tax on personal income has closely tracked tax-to-GDP



Source: ATO Taxation Statistics, 2022-23 Budget, and PBO analysis

Australia's total tax revenue is below the OECD average

Total tax revenue, select OECD countries, 2019

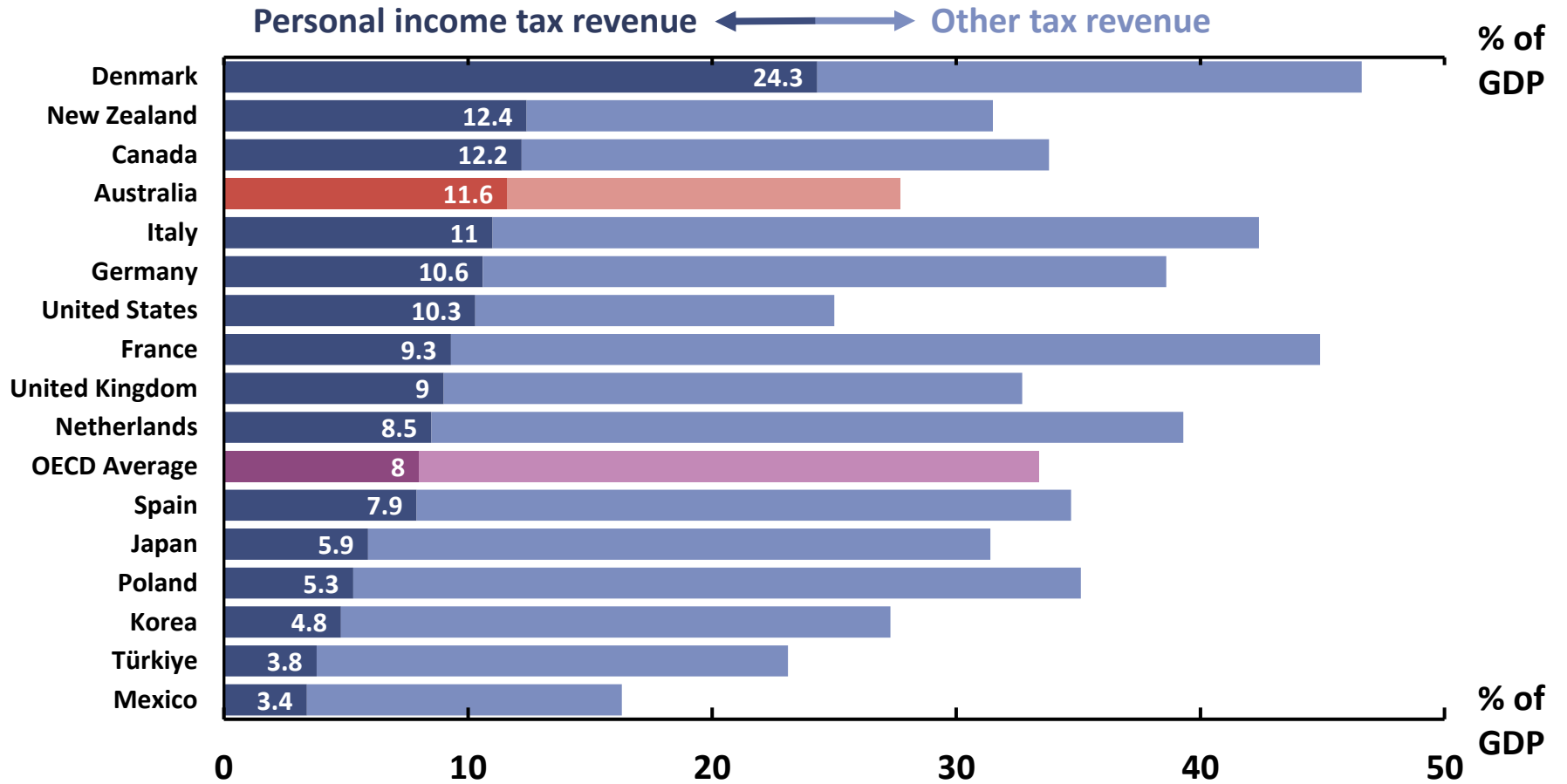


Source: OECD Global Revenue Database, 2022

Note: includes revenue from all sources at all levels of government

But personal tax revenue is above the OECD average

Personal income tax and other tax revenue, select OECD countries, 2019

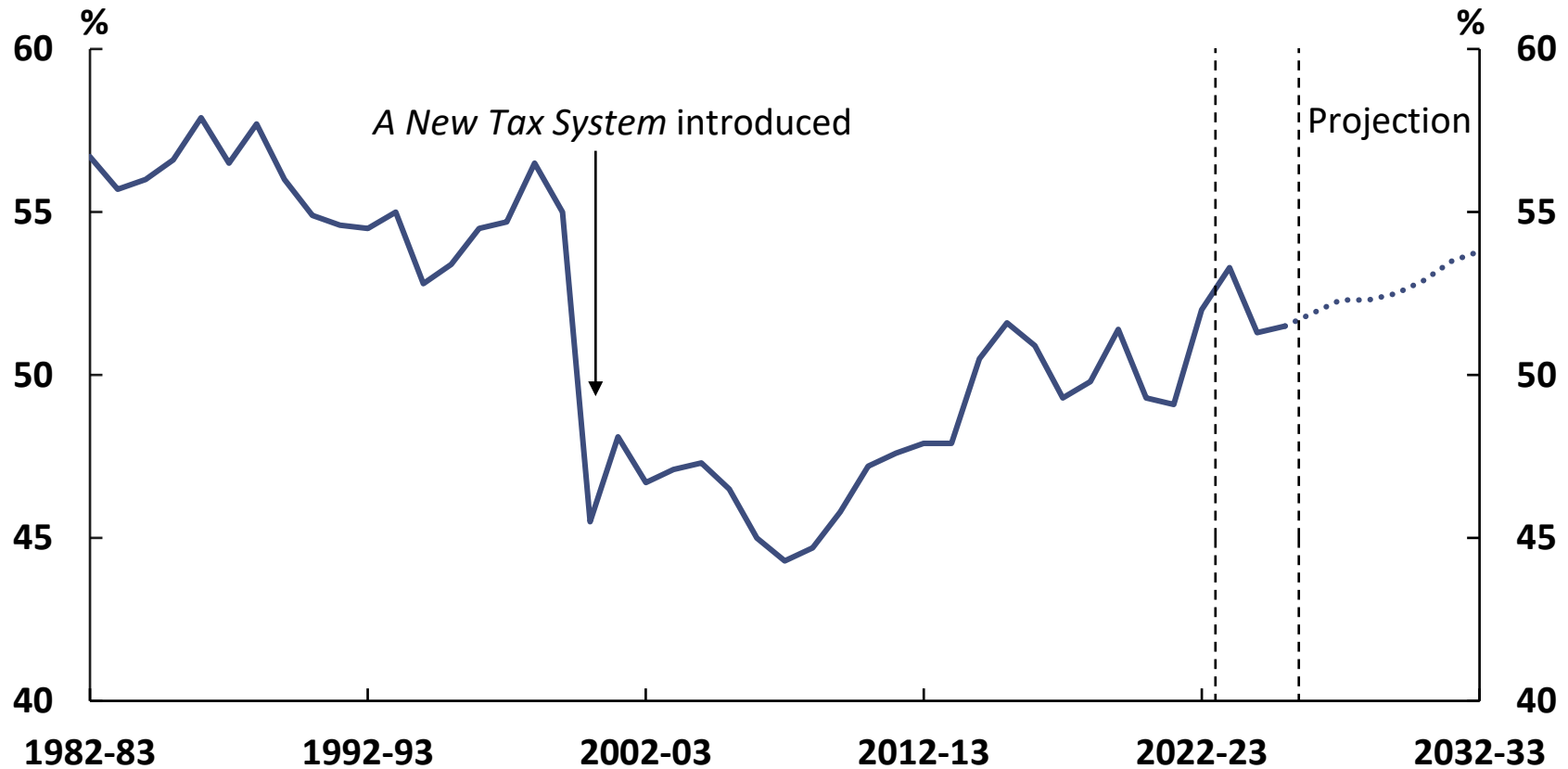


Source: OECD Global Revenue Database, 2022

Note: includes revenue from all sources at all levels of government. 'Personal income tax' revenue includes taxes on income, profits and capital gains of individuals, but does not include social security or superannuation contributions.

Personal tax makes up more than half of all Commonwealth tax receipts

Personal income tax receipts as a percentage of total Commonwealth tax receipts



Source: 2022-23 Budget and PBO analysis

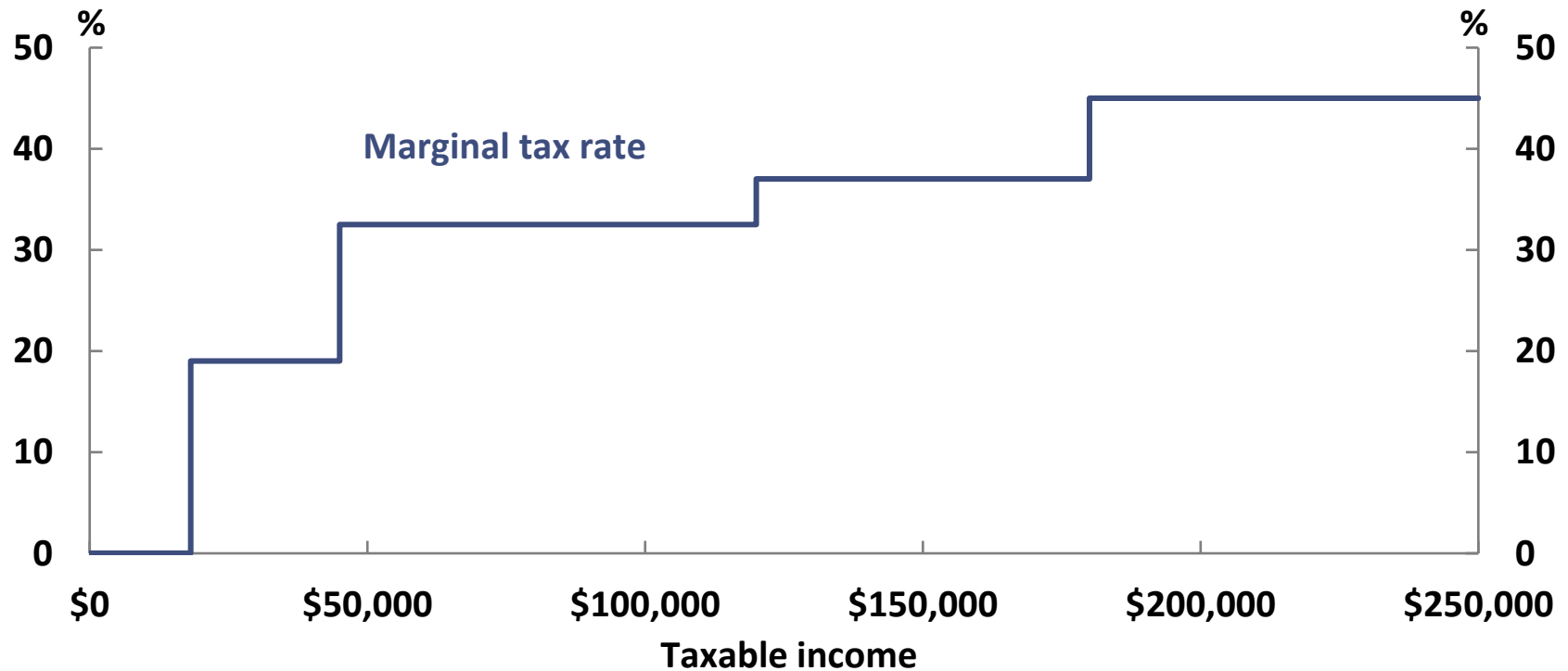
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A brief history of bracket creep in Australia

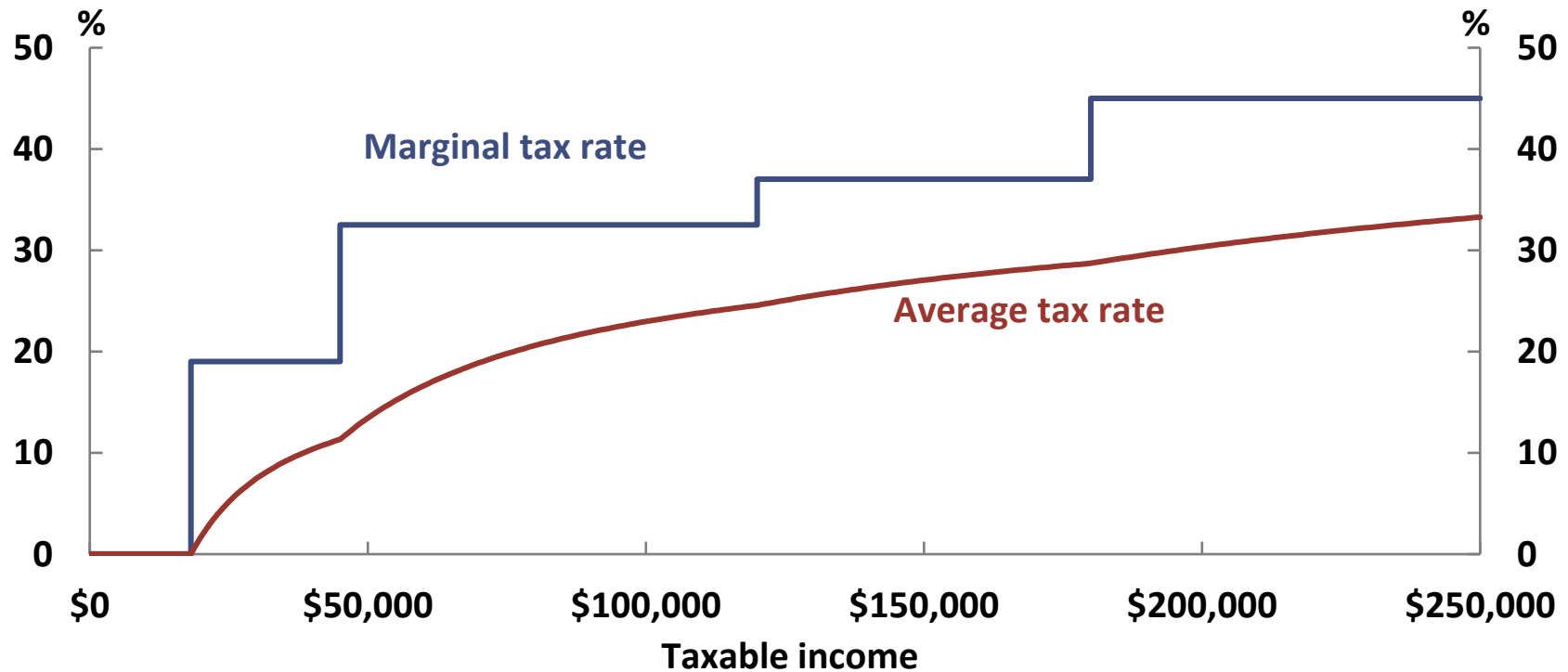
Can Australia rely on bracket creep to reduce public debt?

Bracket creep is a result of marginal tax rates being higher than average tax rates



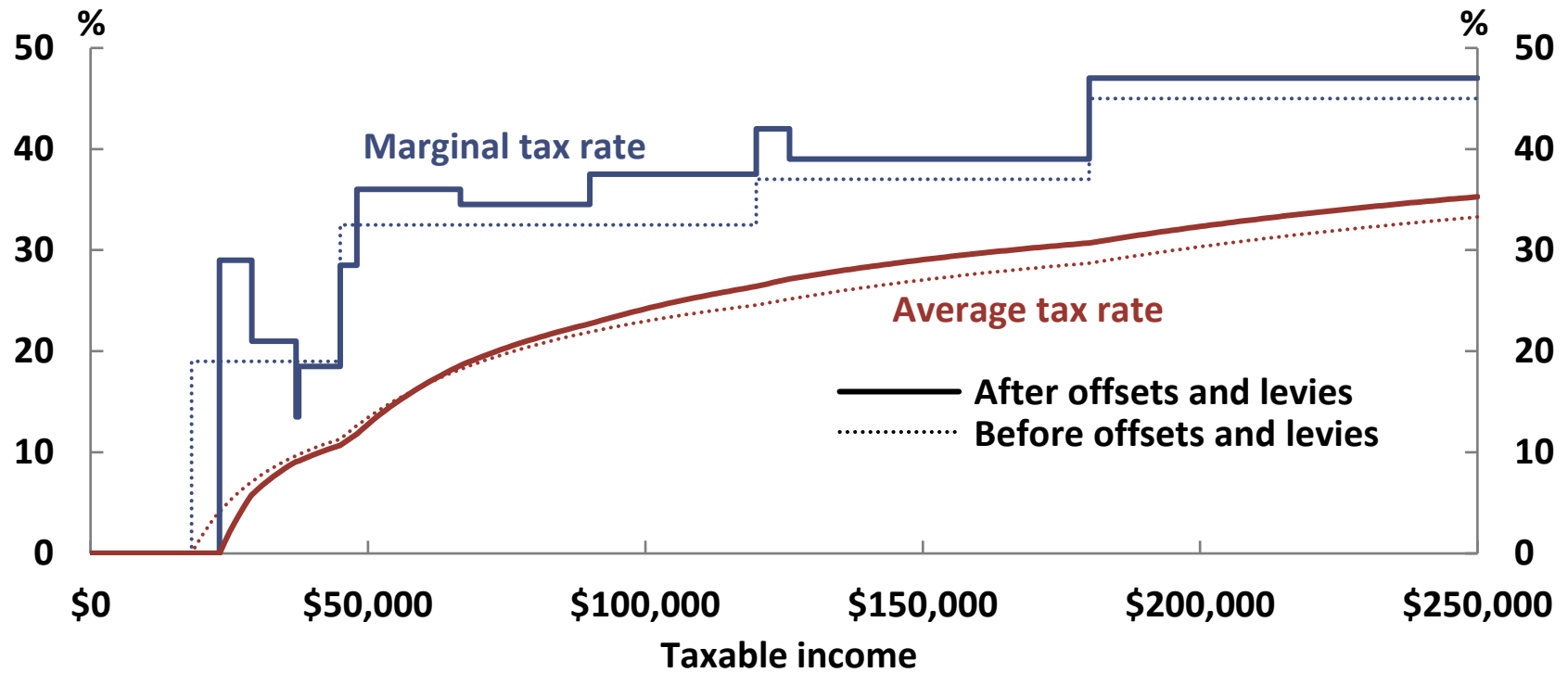
Note: Tax rates from 2021-22

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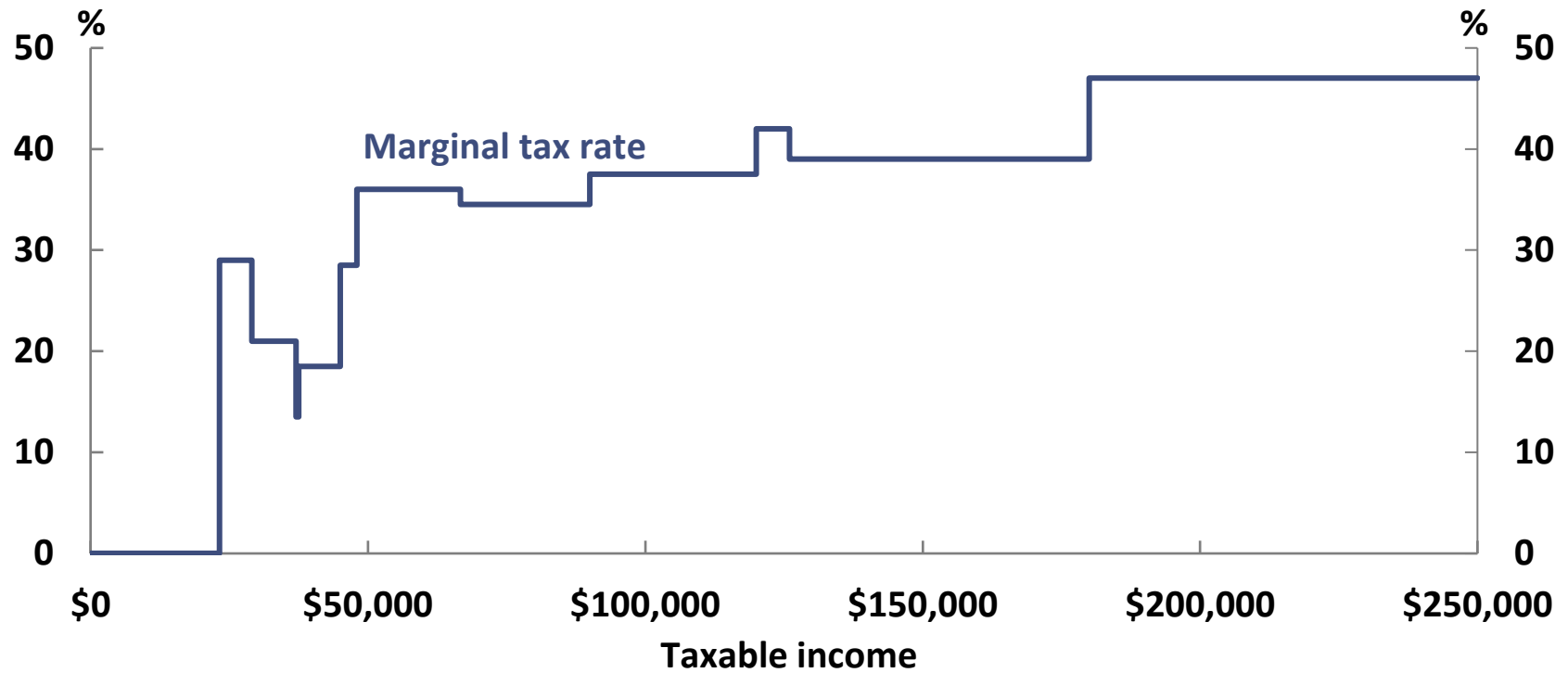
Note: Tax rates from 2021-22

Levies and offsets add complexity



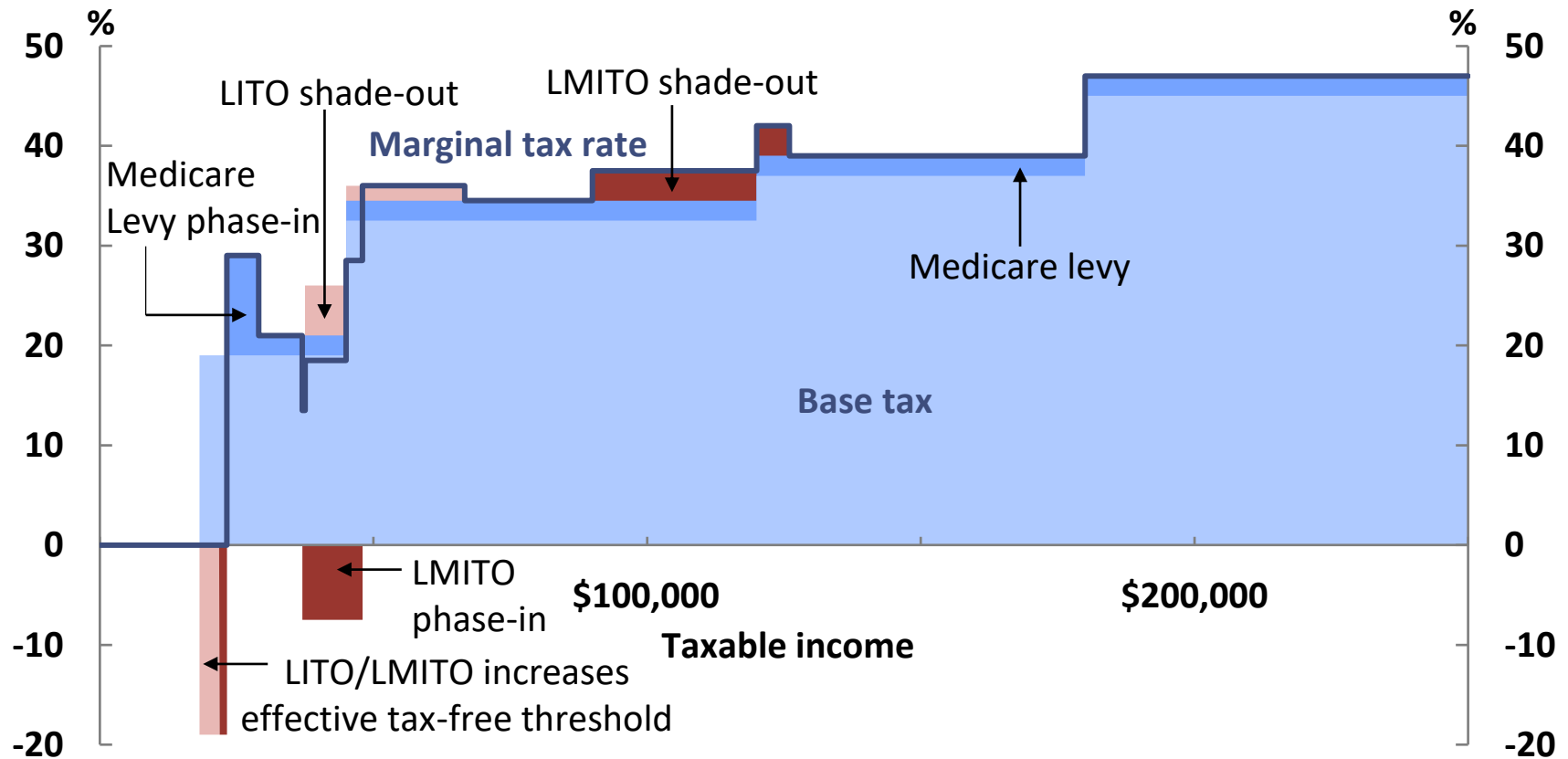
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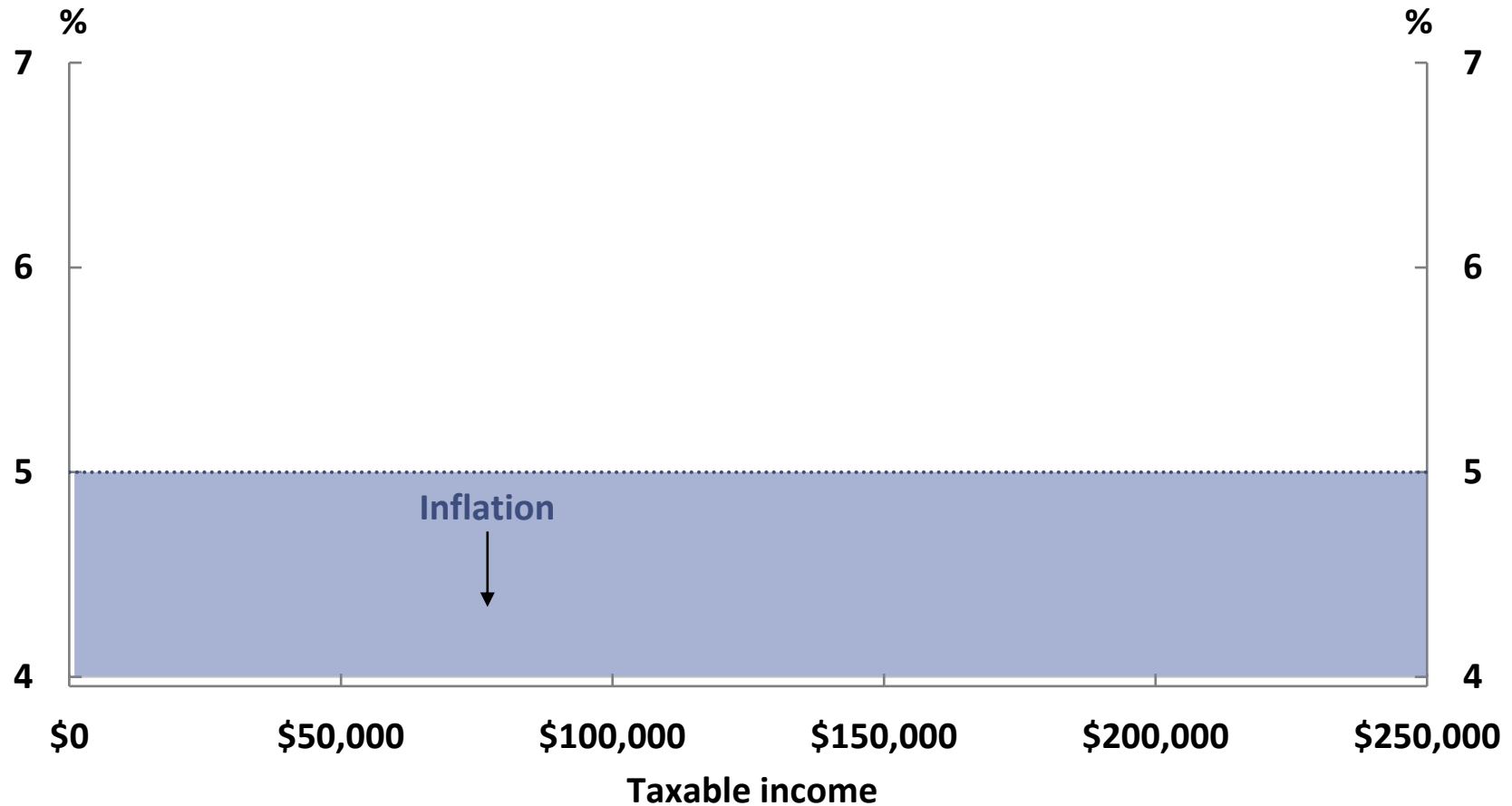
Note: Tax rates from 2021-22

LITO: low income tax offset

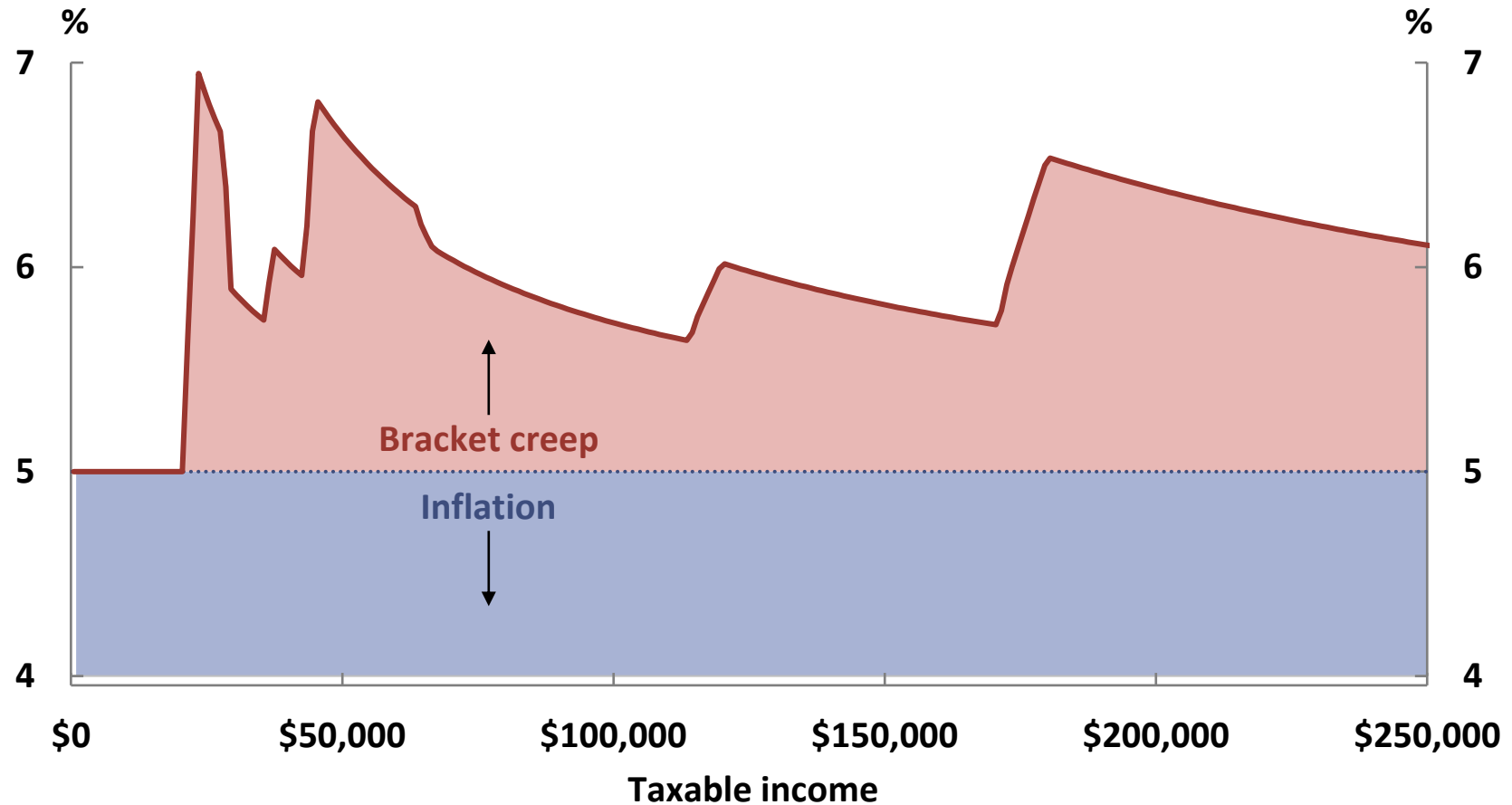
LMITO: low and middle income tax offset (not in place for 2022-23)

How much of a pay rise is required to ‘keep pace with the cost of living’ once taxes are taken into account?

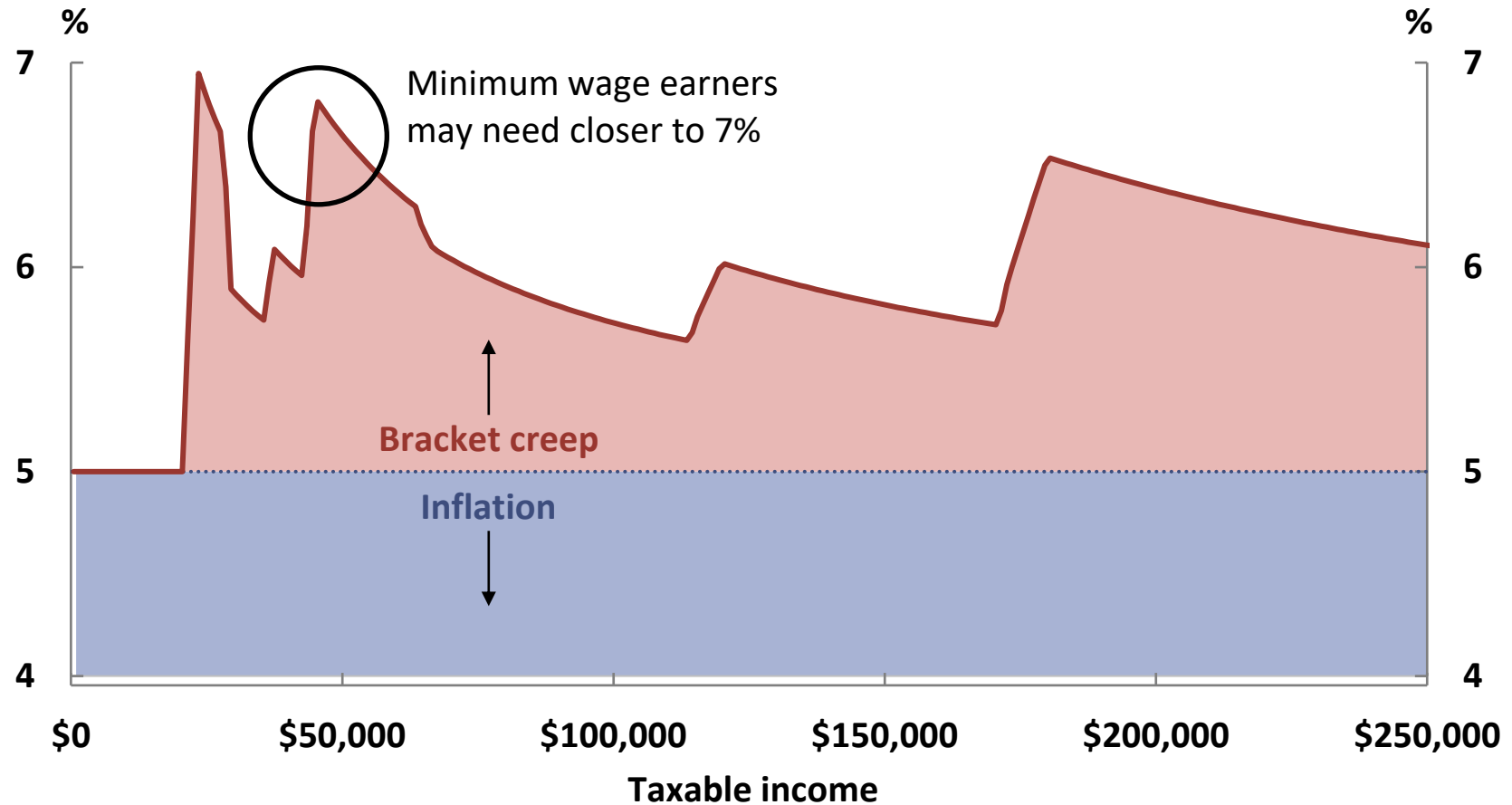
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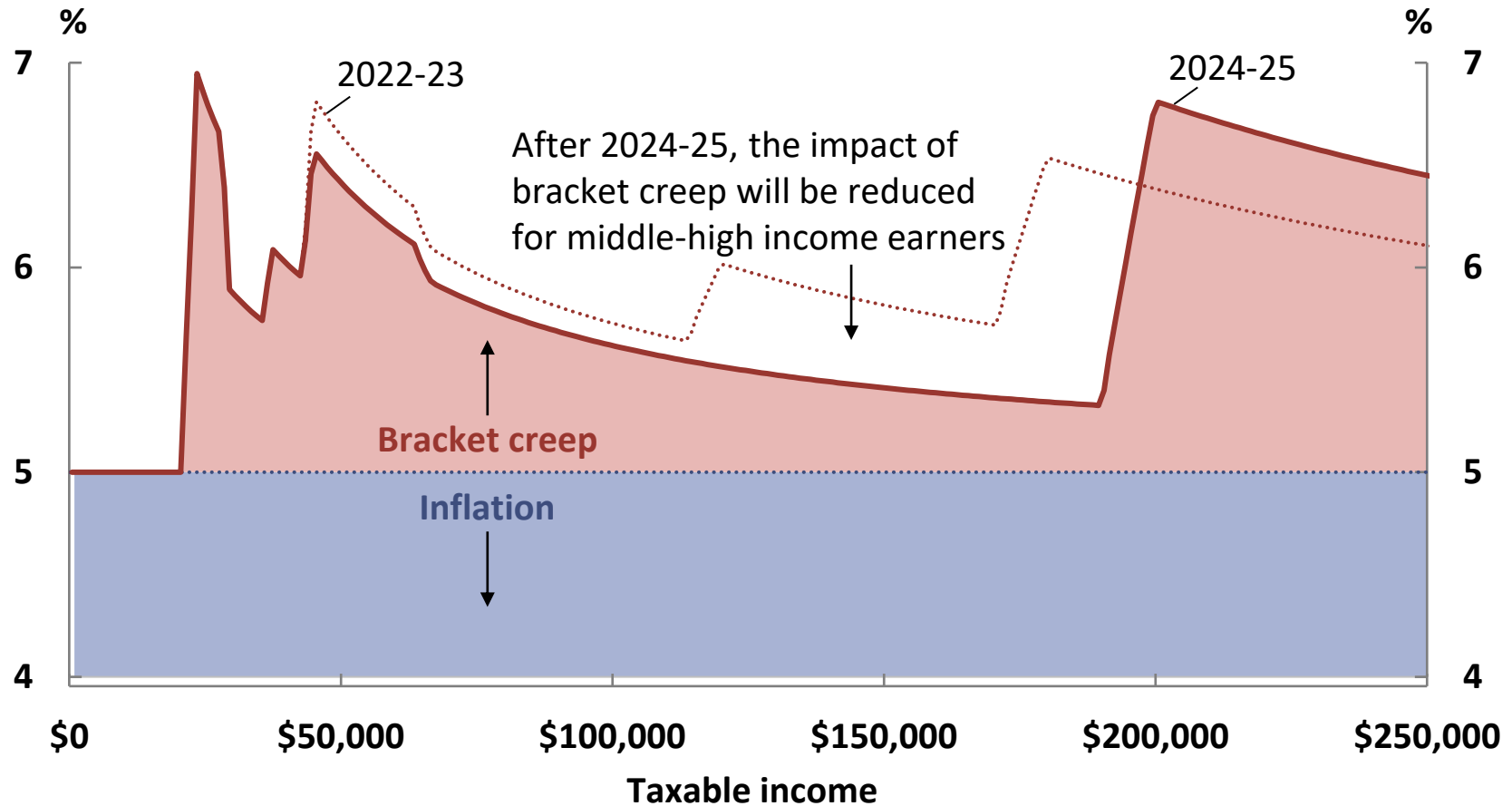
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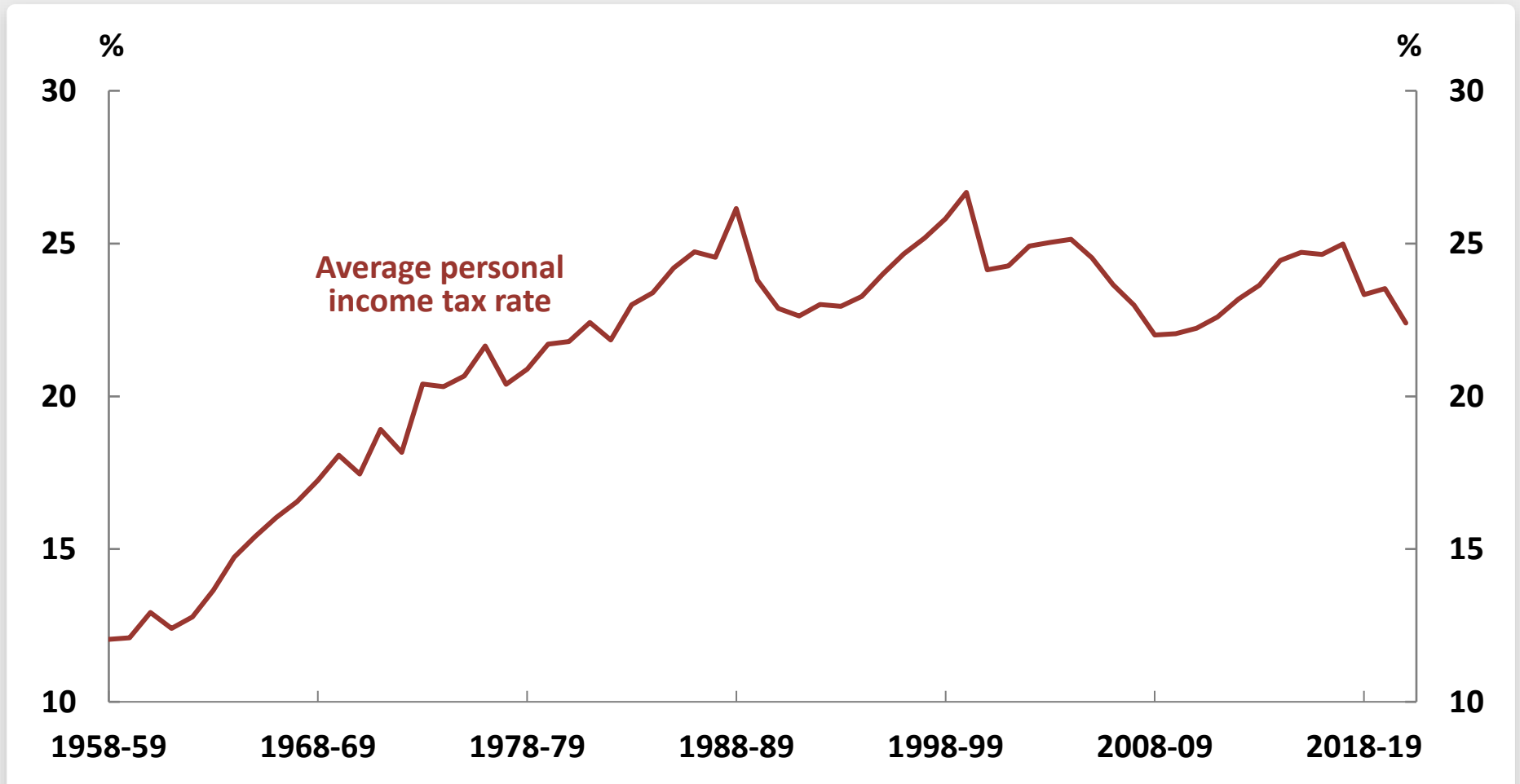
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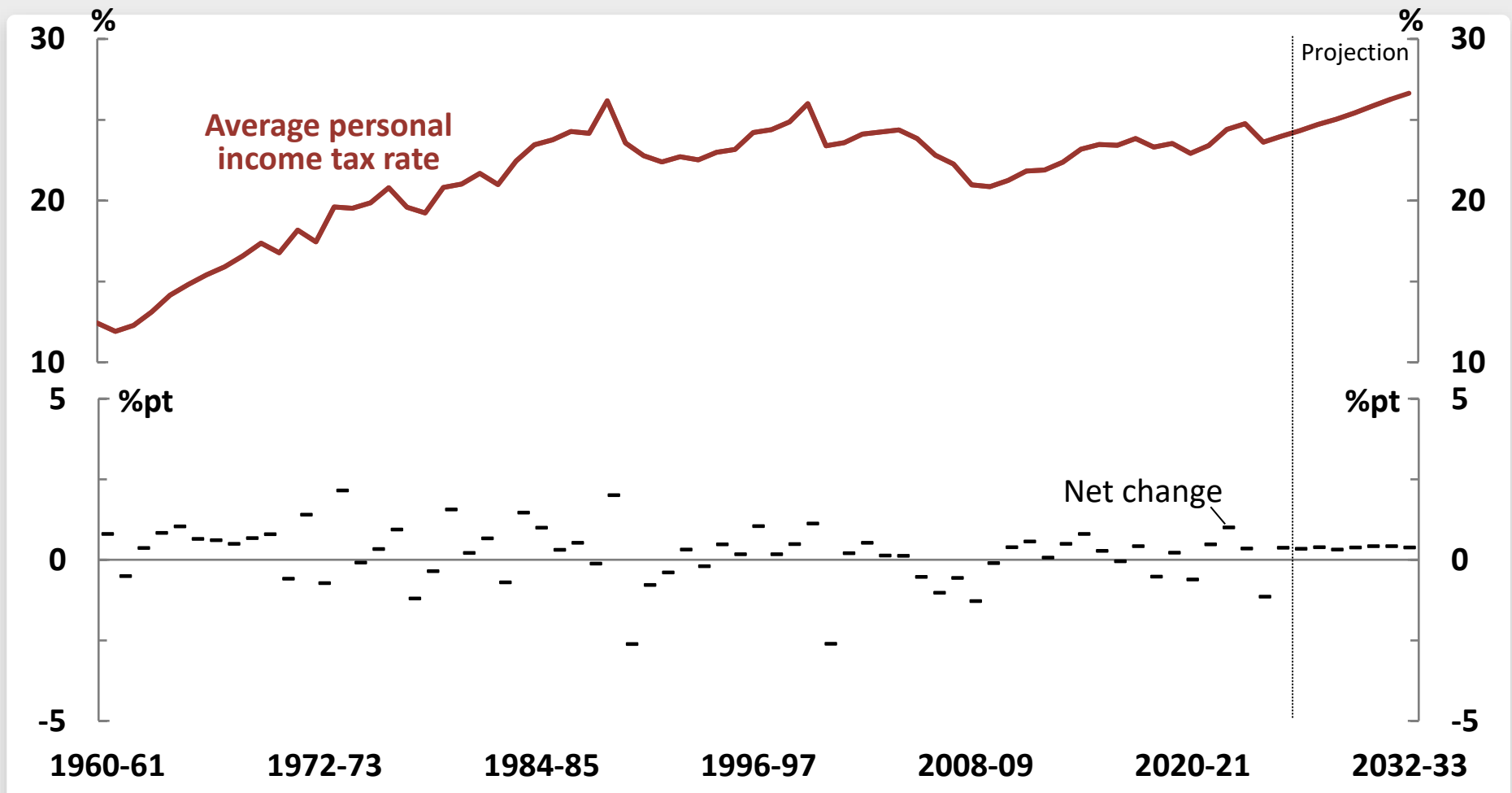


Were increases in the average tax rate driven by explicit policy changes or bracket creep?



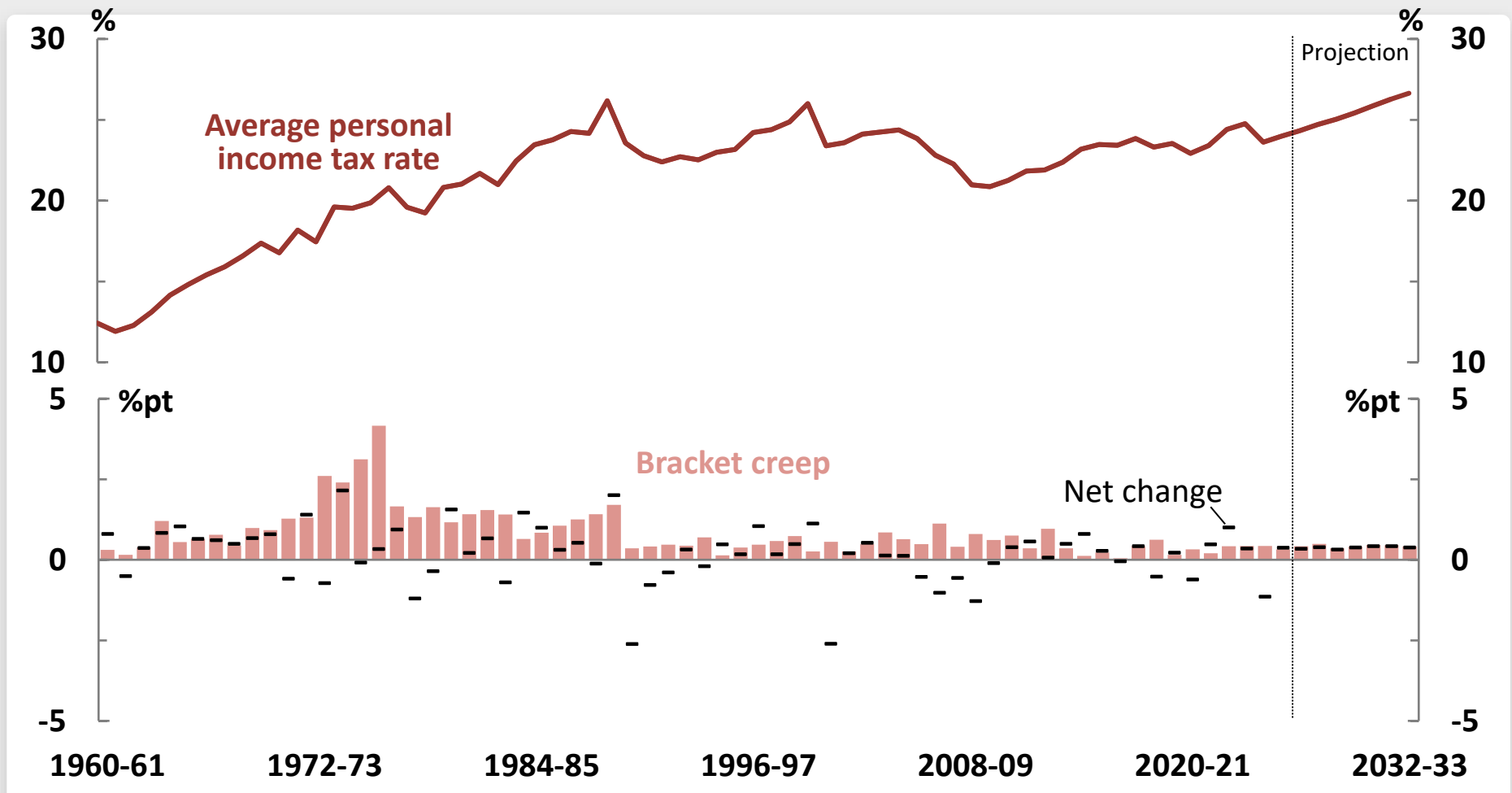
Source: ATO Taxation Statistics and PBO analysis

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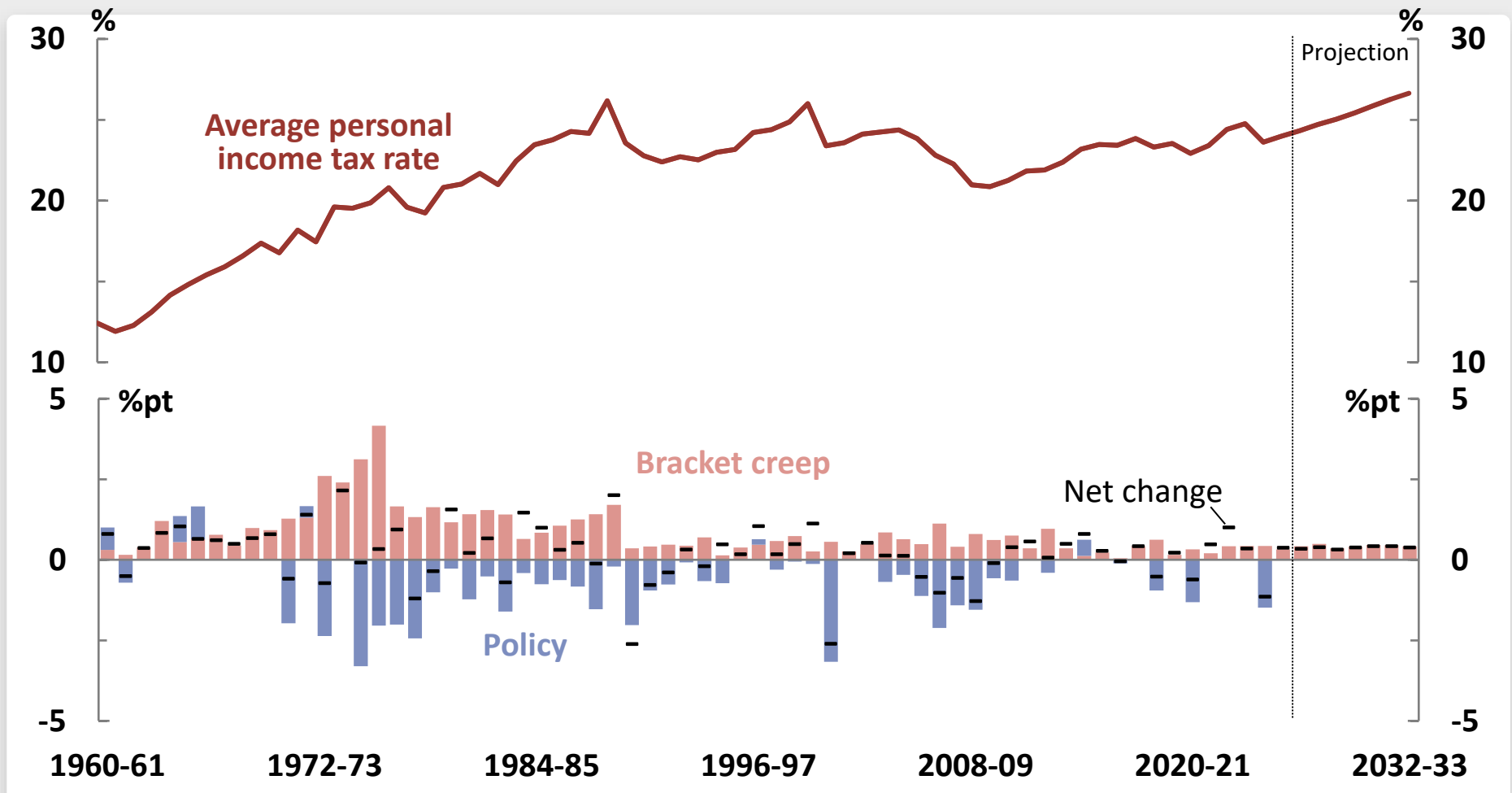
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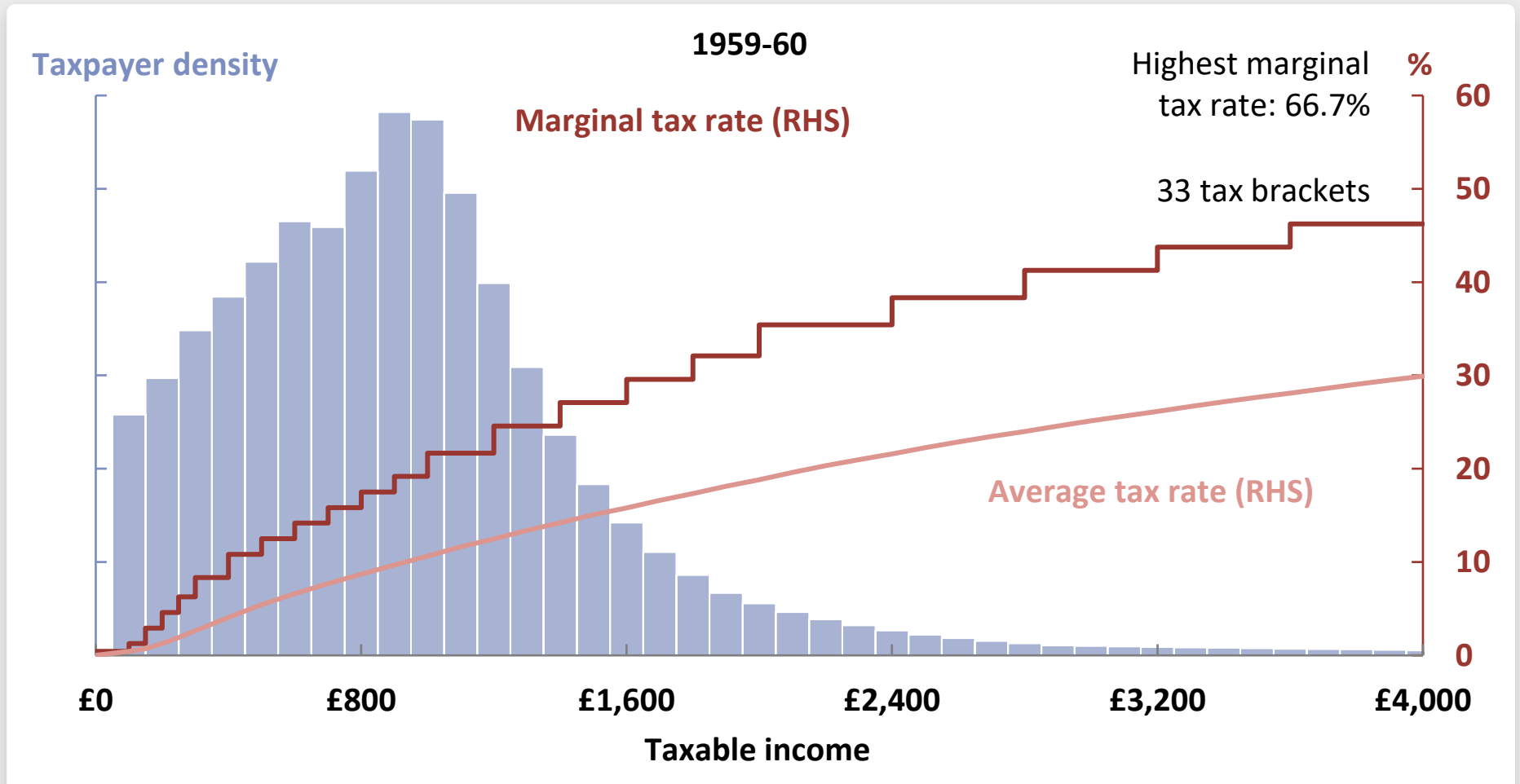
Governments have used bracket creep to increase revenue and to introduce tax cuts



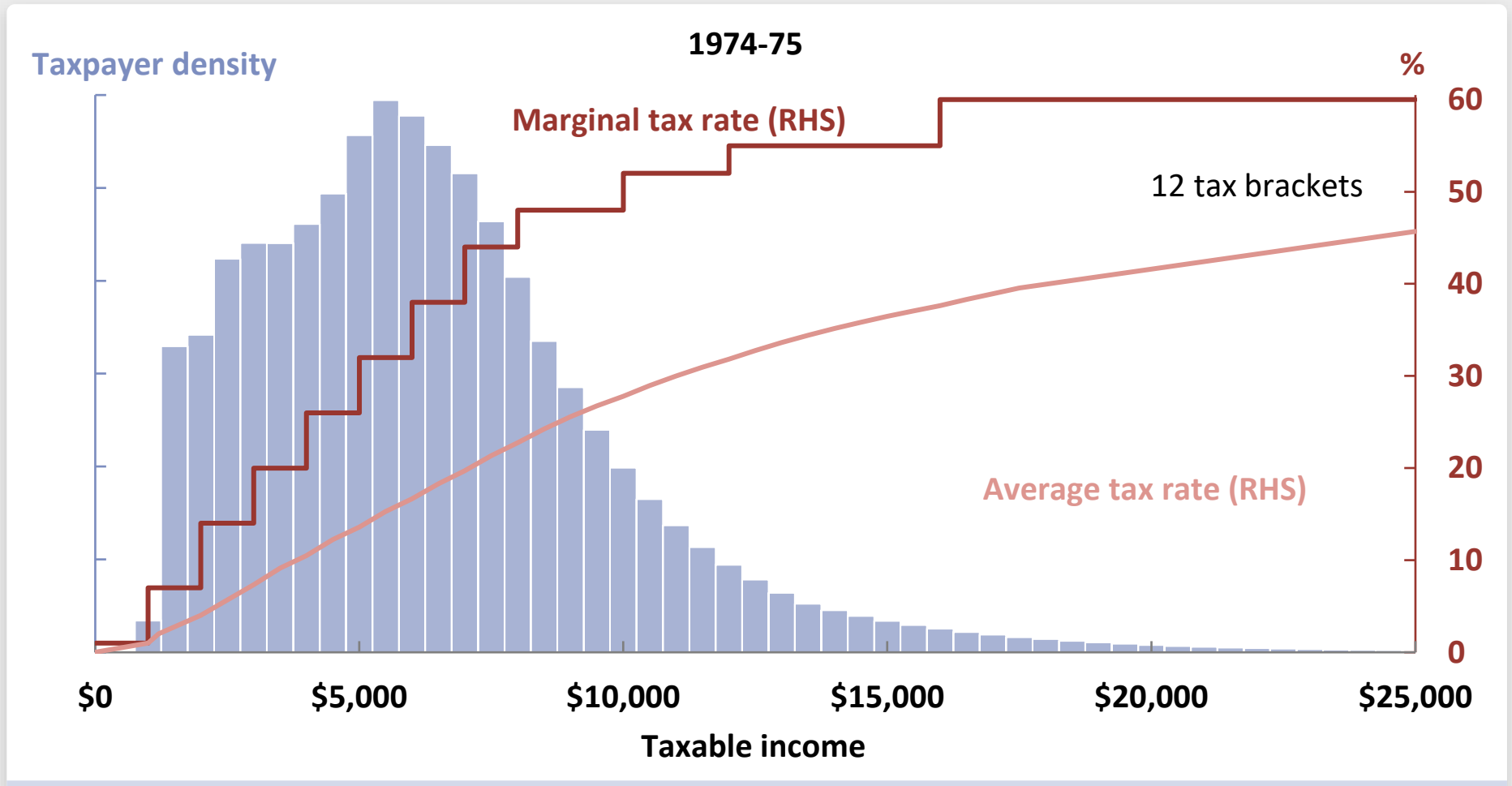
Source: ATO Taxation Statistics and PBO analysis

Note: Net change includes bracket creep, policy and 'other' changes, such as changes to the income distribution

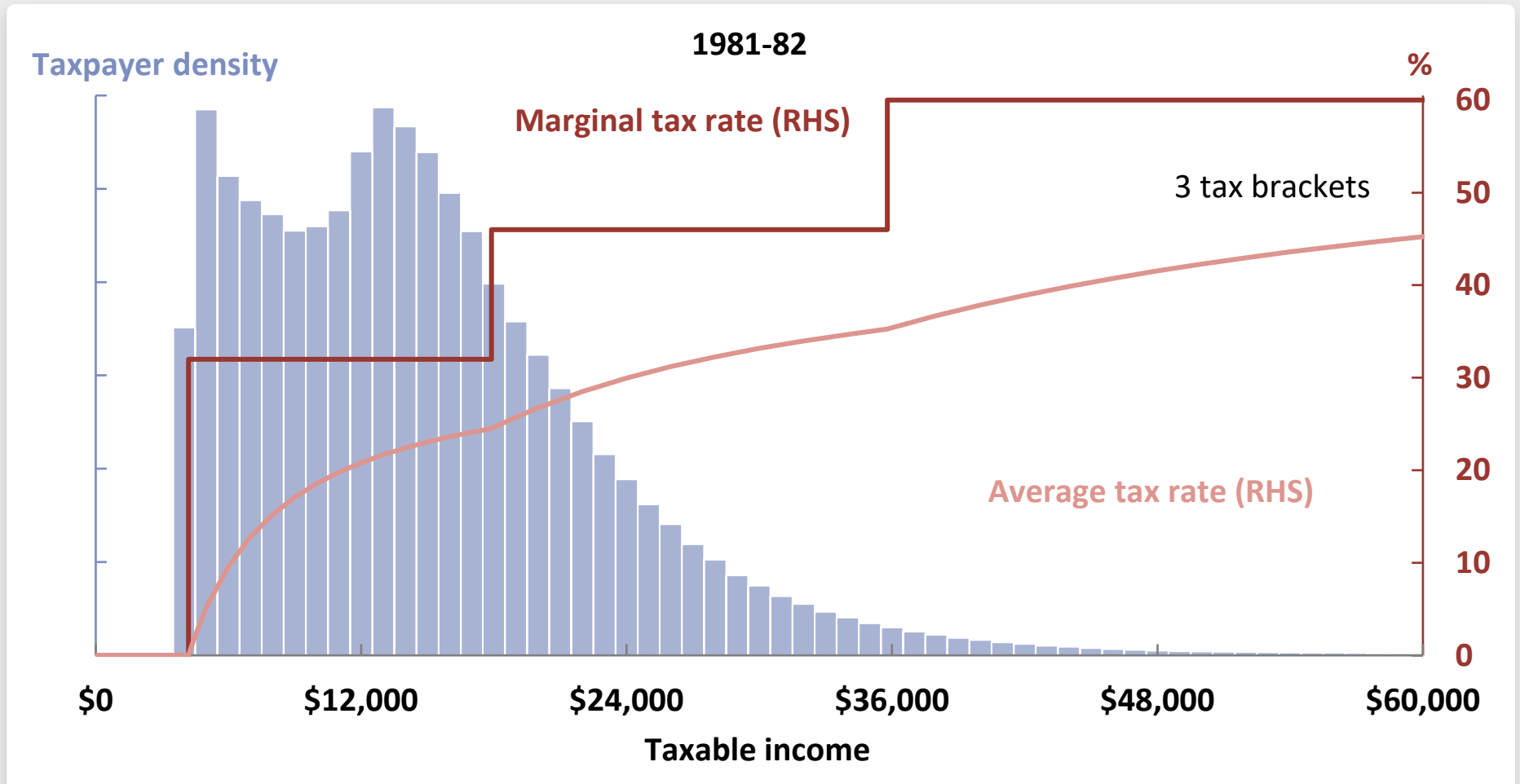
Both the composition of tax rates and the distribution of income have changed significantly



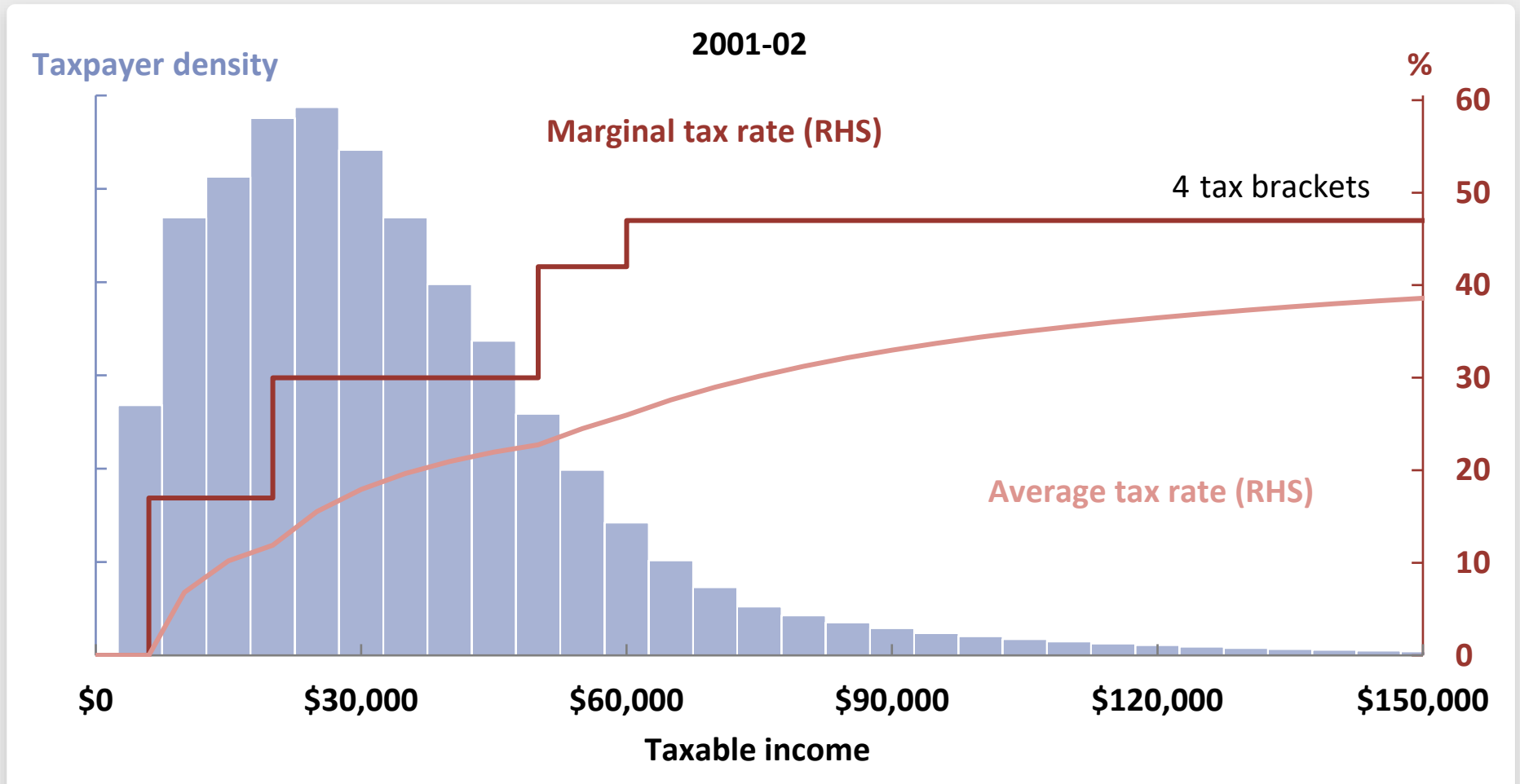
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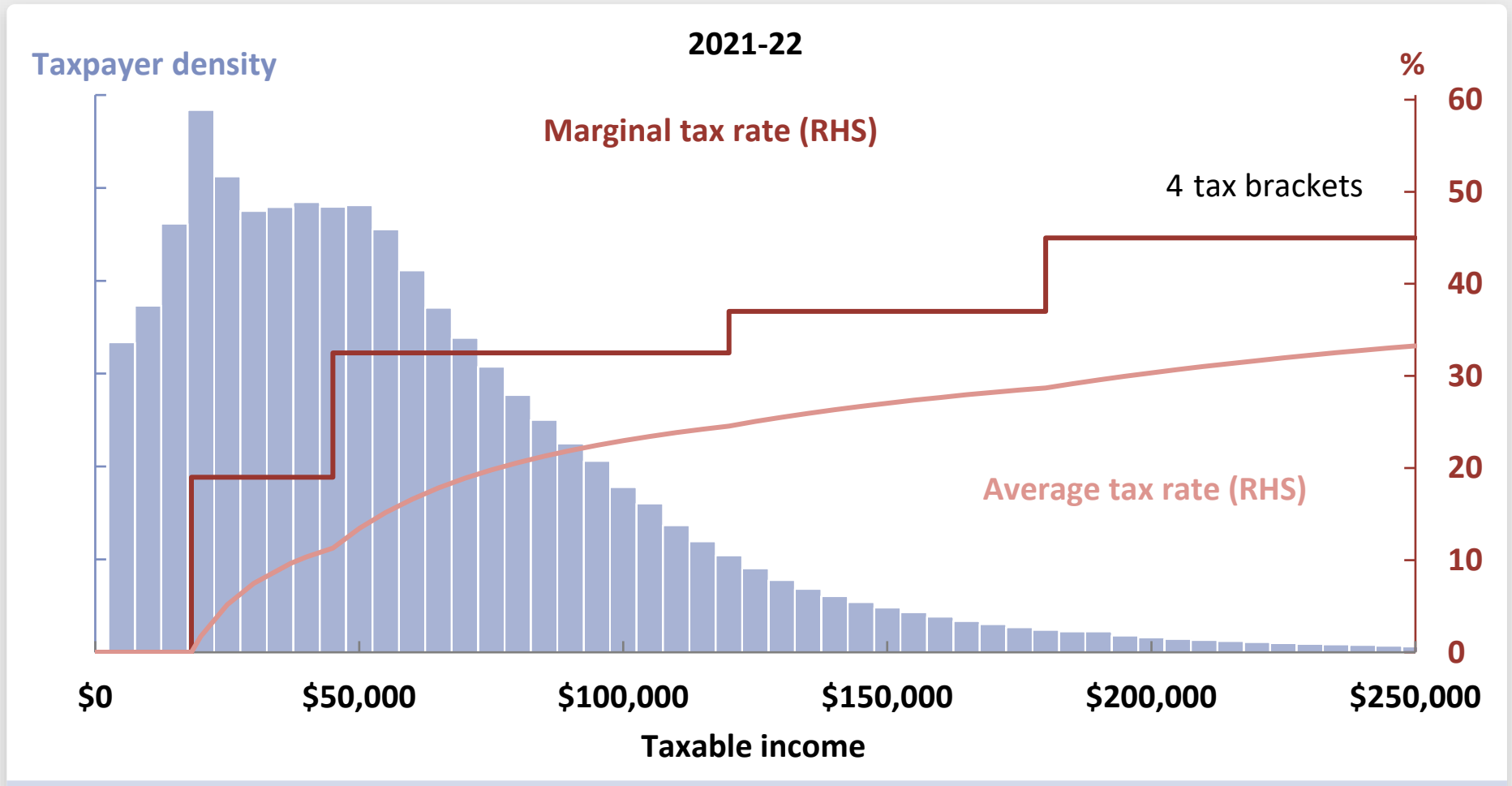
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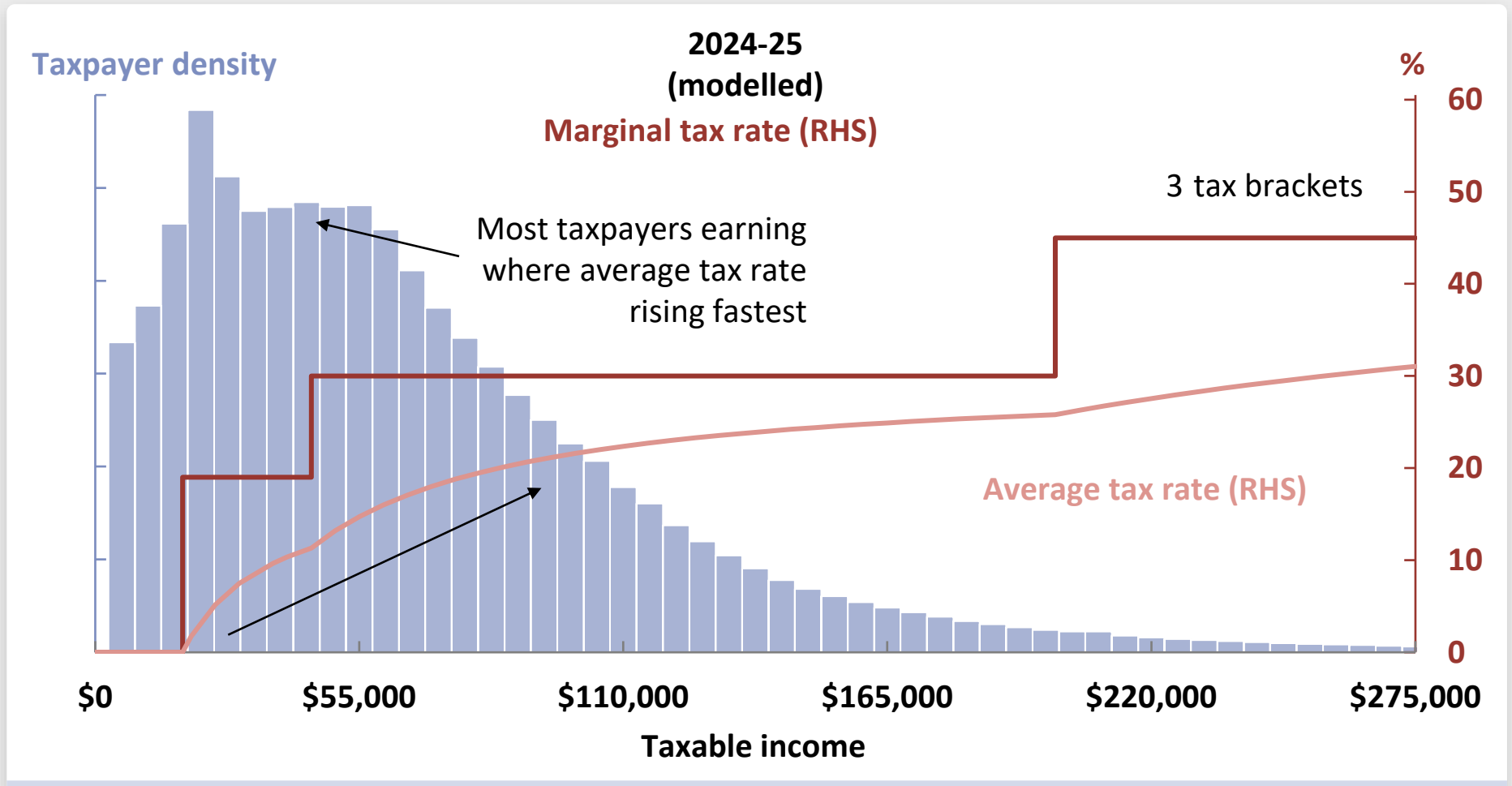


Both the composition of tax rates and the distribution of income have changed significantly



Source: ATO Taxation Statistics, 2022-23 Budget and PBO analysis

The tax system is still progressive after tax cuts in 2024-25



Source: ATO Taxation Statistics, 2022-23 Budget and PBO analysis

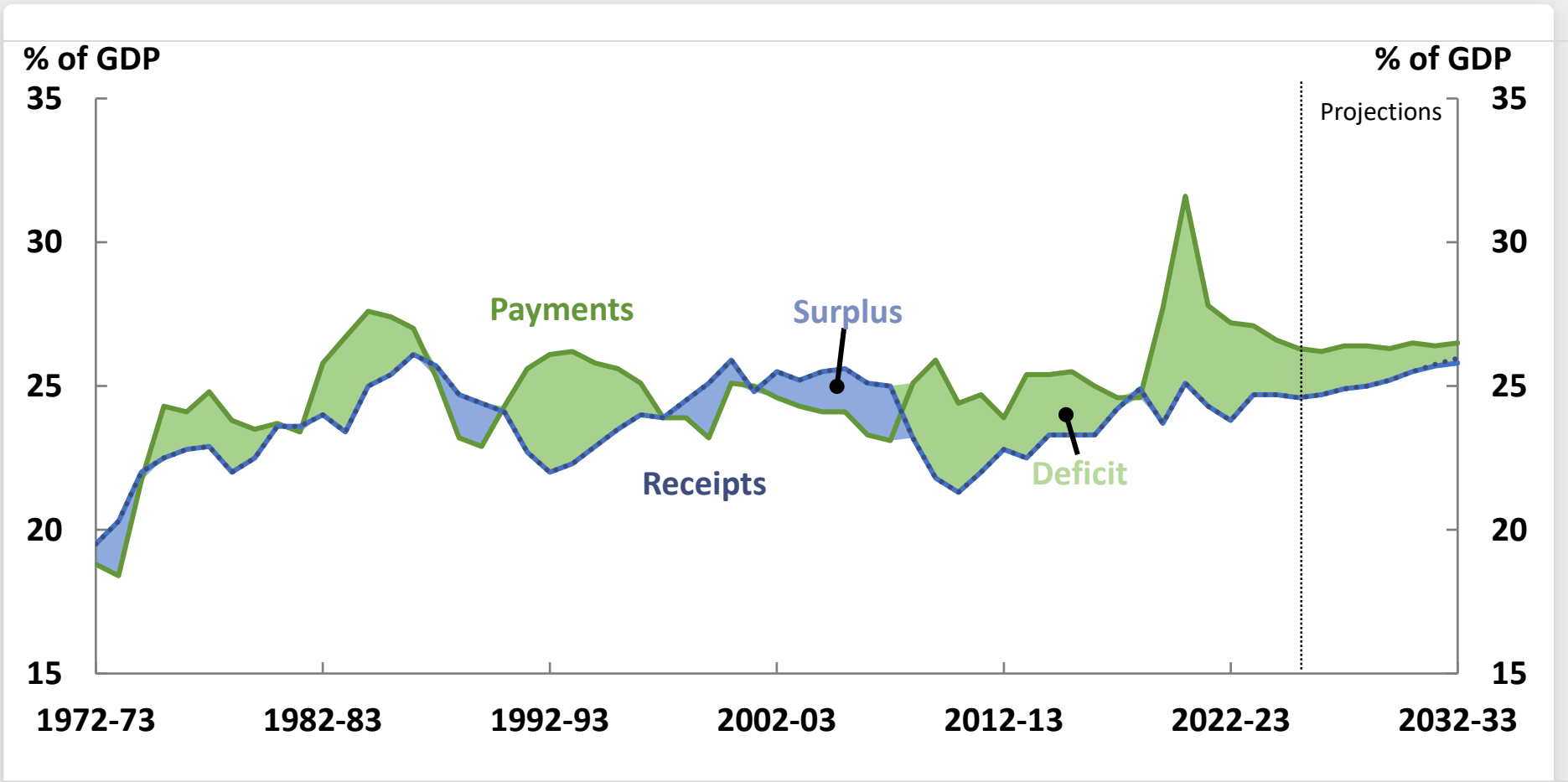
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Can Australia rely on bracket creep to reduce public debt?

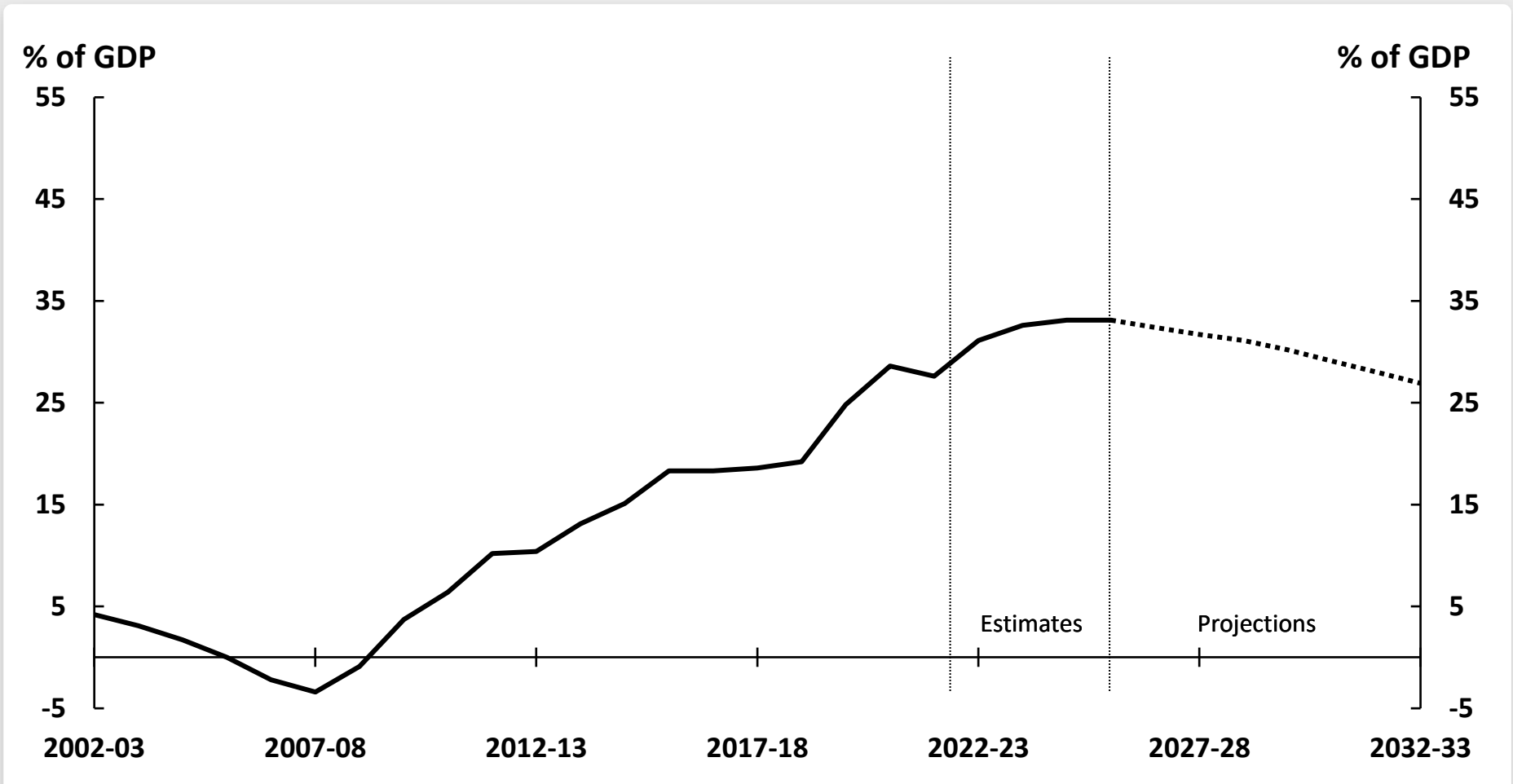
The budget is expected to remain in deficit over the medium term



Source: 2022-23 Budget

Note: The shaded areas broadly correspond to a surplus (blue) or deficit (green) by today's definition of the underlying cash balance. Total receipts includes tax cap of 23.9% from 2031-32.

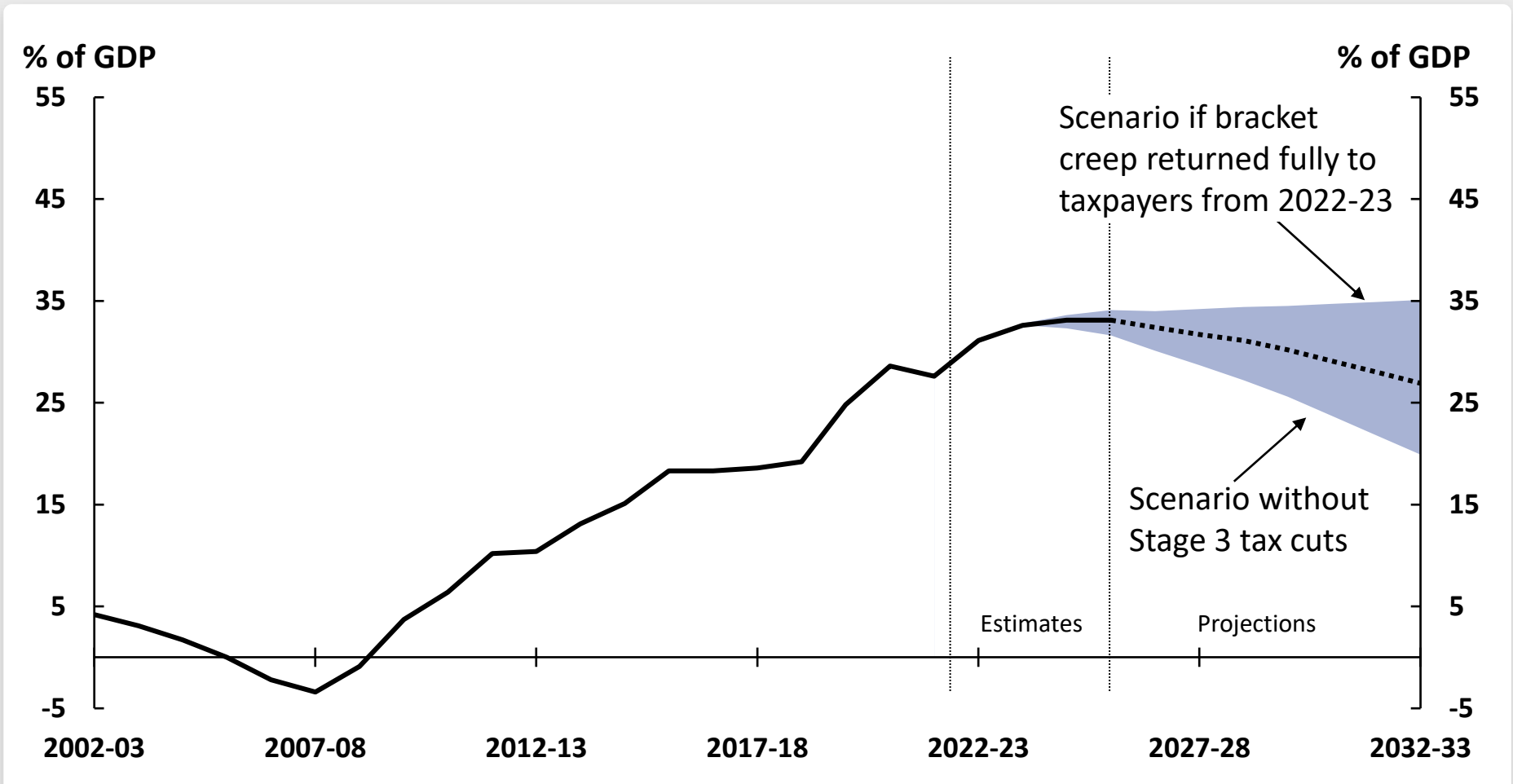
Net debt is projected to decline from around 2026-27



Source: 2022-23 Budget, ATO Taxation Statistics, and PBO analysis.

Note: Scenario where bracket creep is returned assumes thresholds for all tax brackets and offsets are indexed to projected growth in taxable incomes from 2022-23.

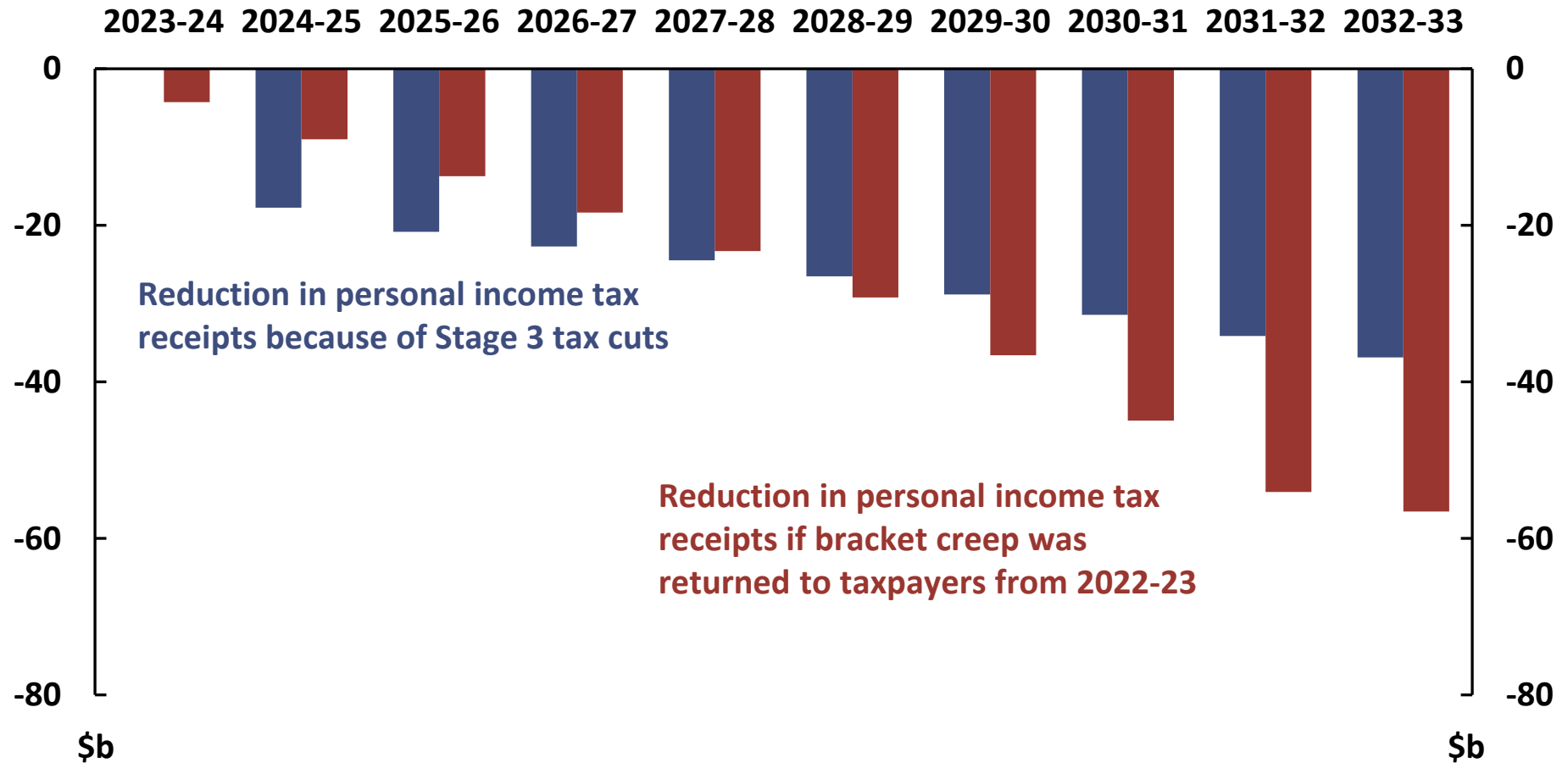
But net debt would continue to increase without bracket creep



Source: 2022-23 Budget, ATO Taxation Statistics, and PBO analysis.

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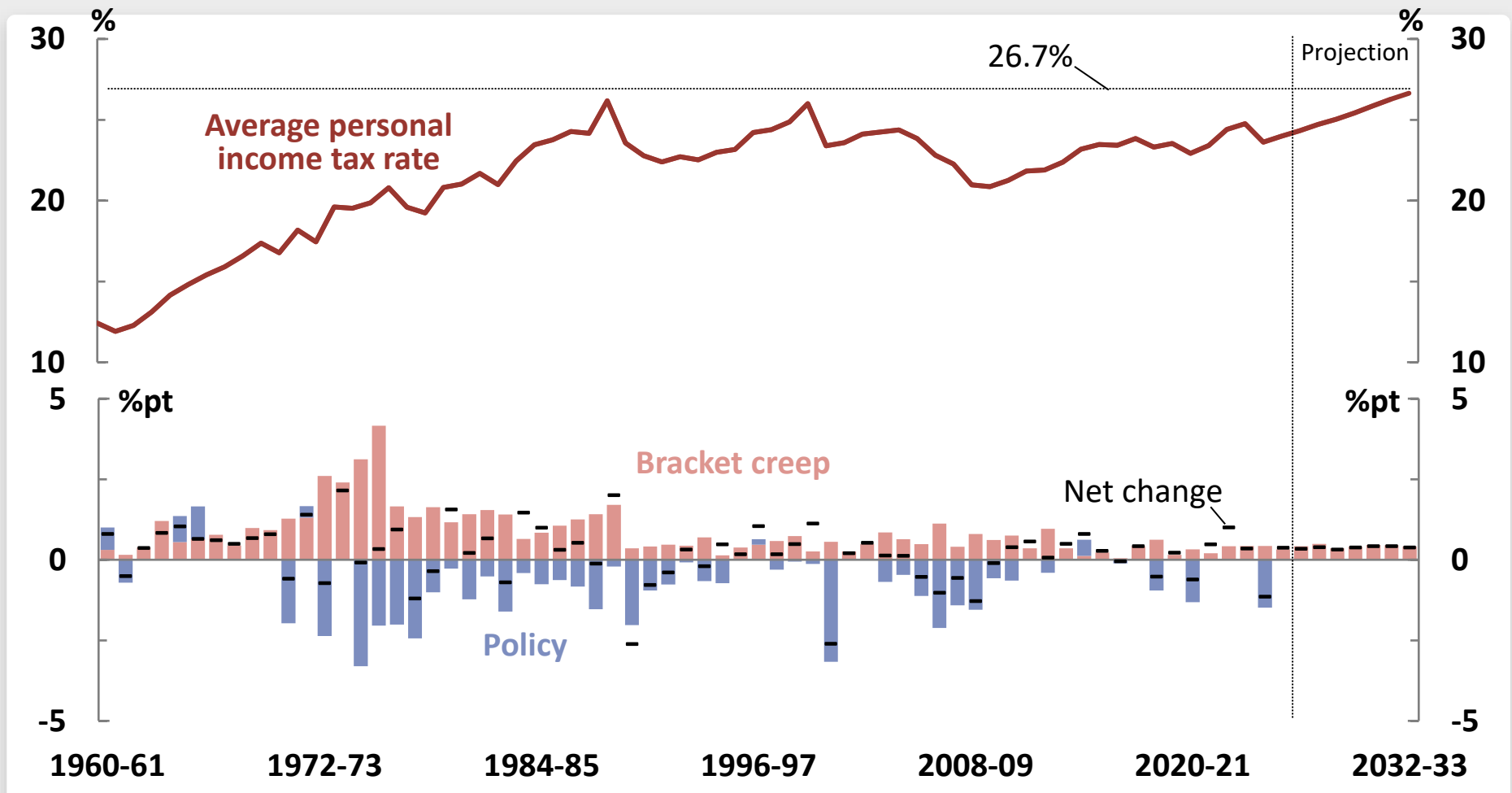
The impact of bracket creep will exceed the cost of the Stage 3 tax cuts by 2028-29



Source: 2022-23 Budget, ATO Taxation Statistics, and PBO analysis.

Note: Scenario where bracket creep is returned assumes thresholds for all tax brackets and offsets are indexed to projected growth in taxable incomes from 2022-23.

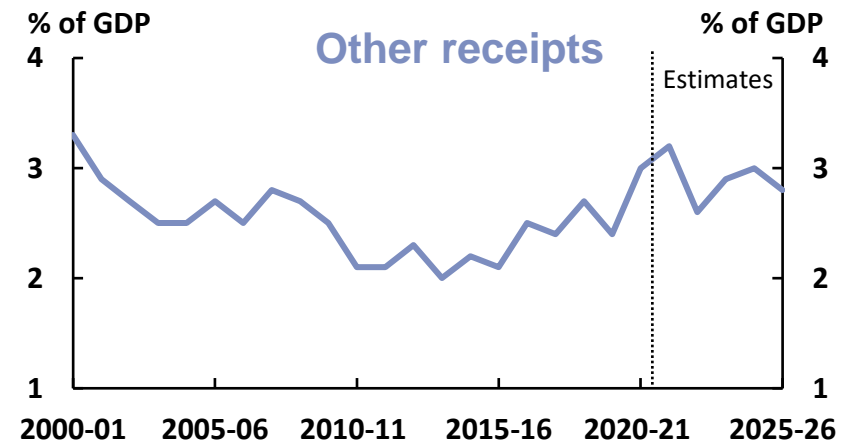
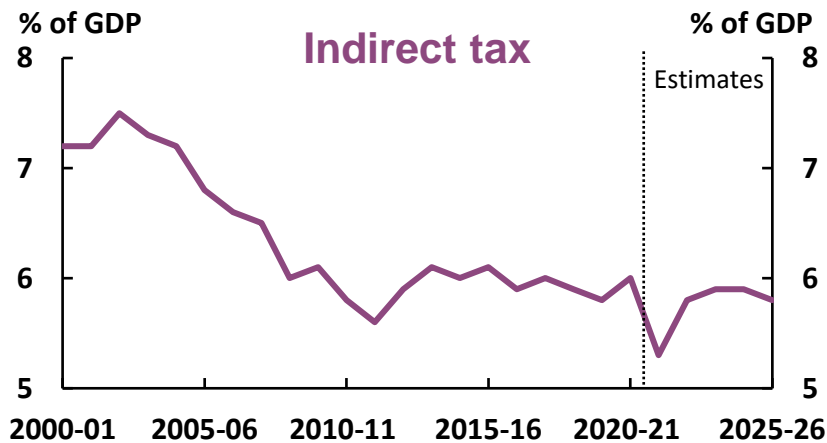
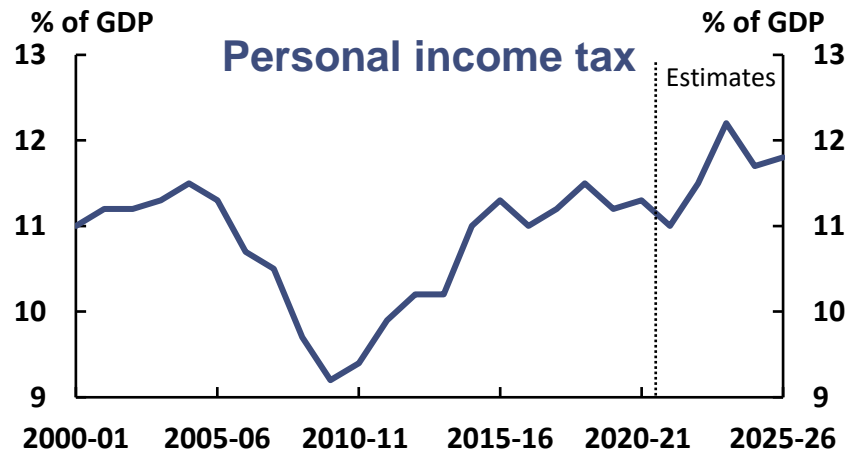
Average tax rates are projected to be higher than they have ever been by 2032-33



Source: ATO Taxation Statistics and PBO analysis

Note: Net change includes bracket creep, policy and 'other' changes, such as changes to the income distribution

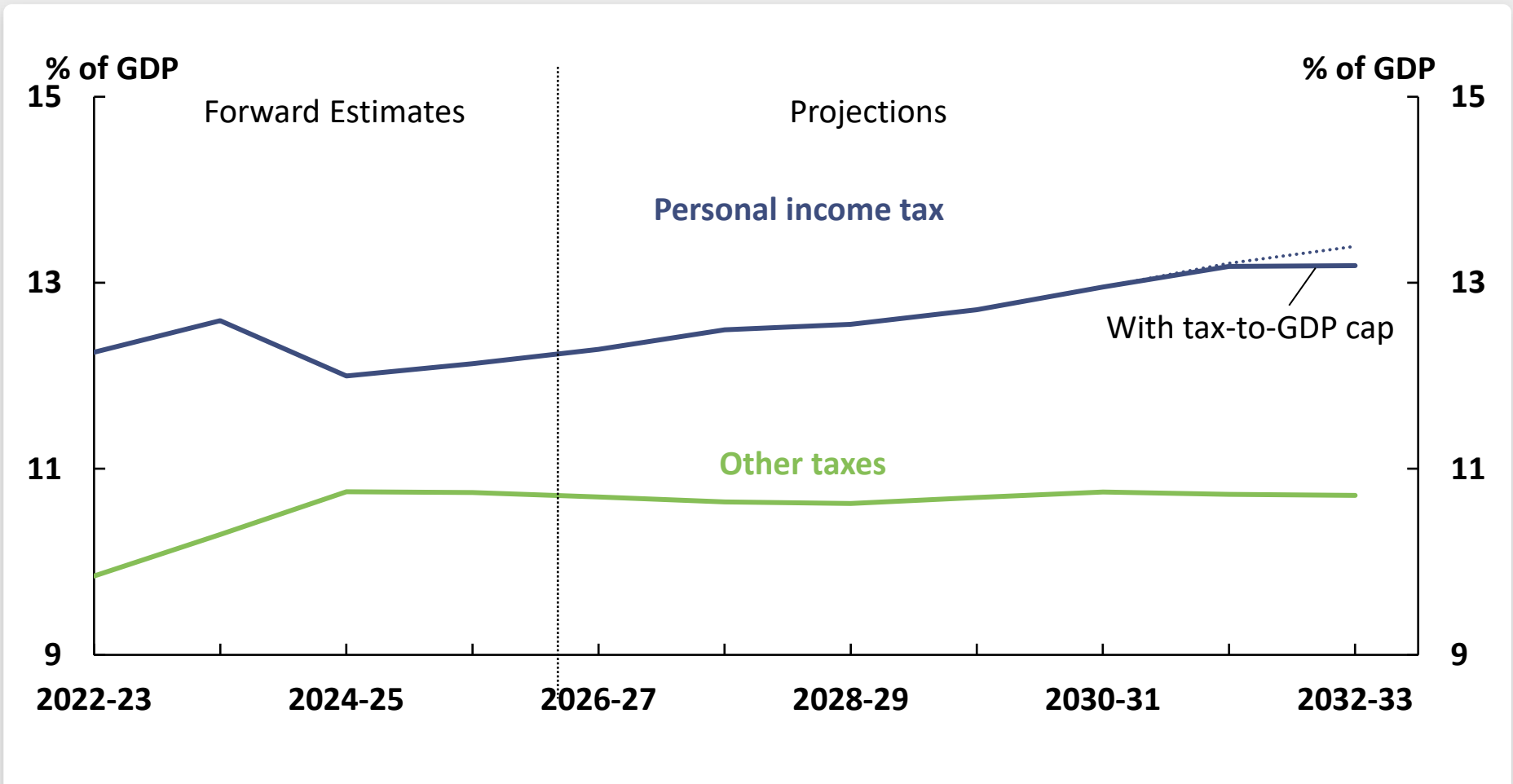
Other receipts are variable or in structural decline



Source: 2022-23 Budget, Budget Paper No. 1, Statement 4 Online Tables

Note: Other receipts includes all other tax and non-tax receipts not related to personal income, company or indirect tax.

Tax receipts are not projected to reach the tax-to-GDP cap of 23.9% until 2031-32



Source: 2022-23 Budget, ATO Taxation Statistics, and PBO analysis.

Note: Receipts projections are sourced from 2022-23 Budget and assume no tax cap. PIT projections from PBO analysis.

Can Australia rely on bracket creep to reduce public debt?

Average personal tax rates could be higher than they were before the GST (26.7%)

Bracket creep is expected to reduce the budget deficit and bring net debt down, even with tax-to-GDP cap

Other taxes in Australia are low by international standards and/or in structural decline

Reform of other taxes may be politically difficult

Bracket creep will make the tax system less progressive over time

Redistributing taxes could increase progressivity without unwinding aggregate bracket creep



Thank you