Budget 2021 – Revenue

Personal taxation overview

The Government has not taken the opportunity to restructure the personal tax plan that was legislated in 2019. Each year since the 2018-19 budget, NFAW has reminded the Government that the stage 3 tax cuts are regressive, with high income earners benefiting the most.

The extension of the Low Middle Income Tax Offset will extend tax relief to middle income earners for another year, but this does not fix the structural flaw in the personal tax rate schedule. Although the Government is claiming that it is delivering a tax cut, it is merely extending the current rates for another year: taxpayers will not see any increase in their pay packets.

Redesigning the stage 3 tax cuts to be more progressive would collect more taxes from those who have the ability to pay to contribute to the cost of funding aged care, childcare and other social infrastructure.

Personal income tax

The Budget

Low Middle Income Tax Offsets

Receipts ($m)

	2020-21	2021-22	2022-23	2023-24	2024-25
Australian Taxation Office	-	-	-7,400.0	-400.0	..

2021-22 Budget Paper No 2, p. 27.

This was the headline personal tax measure for the Government. Although promoted as a tax cut it retains the current tax offset for the 2021-22 income year. The LMITO is a temporary offset to provide tax relief to low and middle income earners prior to the stage 3 tax cuts that are to be introduced in July 2024. The scheduled removal of the LMITO would have resulted in taxpayers earning less than $126,000 paying more tax than in the 2020-21 tax year.

Employee Share Schemes — removing cessation of employment as a taxing point and reducing red tape

Receipts ($m)

	2020-21	2021-22	2022-23	2023-24	2024-25
Australian Taxation Office	-	-	-	-345.0	-205.0

2021-22 Budget Paper No 2, p. 16.

Employee share schemes are used as an incentive by companies wishing to attract and retain staff. They are particularly used by startups and technology companies as well as for high level employees. The Government anticipates that the changes to the Employee Share Schemes (ESS) will assist employers to recruit internationally in high technology and other companies competing in the international market. The Treasurer's speech discussed this measure with other measures to allow Australia to compete globally with technology industries in other countries.

If shares are issued at less than market value, the difference is currently assessed on the earliest of three dates:

- when there is no real risk of forfeiture and the scheme no longer genuinely restricts disposal of the share
- when the employee ceases the employment in respect of which they acquired the share
- 15 years after your employee acquired the share (or seven years if acquired before 1 July 2015).

Employees participating in a ESS may also be eligible for a $1000 discount unless they earn more than $180,000, or salary sacrifice to pay for their shares, in which circumstances they are not eligible for a discount on the market value of the shares. This equity measure does not seem to be affected by the announcement. Employees earning more than $180,000 are still eligible to defer the gain on acquisition for up to 15 years.

The proposed measure defers the point at which the bonus shares will be liable to tax. Currently the value of the shares when issued to the employee is taxed if an employee leaves the company. This taxing point will be removed, but tax will still be payable after all conditions are removed or after 15 years. There is also capital gains tax payable on Employee Shares when sold, after taking account of the amount already included.

There are also measures to simplify the paperwork that the employer is required to complete. The reporting requirements were introduced in 2009. The simplification is targeted to ensure that large transactions will still be identified.

Compliance and Simplification Measures

- *Reducing compliance costs for individuals claiming self-education expense deductions*

The Government will remove the exclusion of the first $250 of deductions for prescribed courses of education. The first $250 of a prescribed course of education expense is currently not deductible. Removing the $250 exclusion for prescribed courses of education will reduce compliance costs for individuals claiming self-education expense deductions. This measure will have negligible effect on revenue collections (2021-22 Budget Paper No 2, p. 26).

- *Modernising the individual tax residency rules*

The Government will replace the individual tax residency rules with a new, modernised framework. This measure follows a report of the Board of Taxation. The primary test will be a simple objective test — a person who is physically present in Australia for 183 days or more in any income year will be an Australian tax resident. Individuals who do not meet the primary test will be subject to secondary tests that depend on a combination of physical presence and measurable, objective criteria. The measure will take effect from the first income year after the date of Royal Assent of the enabling legislation. It will have an unquantified effect on revenue collections, with $1m allocated to the ATO to administer the change (2021-22 Budget Paper No 2, p. 21).

- *Personal Income Tax — increasing the Medicare levy low-income thresholds*

The Government will increase the Medicare levy low-income thresholds for singles, families, and seniors and pensioners from 1 July 2020 to take account of recent movements in the CPI so that low-income taxpayers generally continue to be exempt from paying the Medicare levy. This is a routine adjustment (2021-22 Budget Paper No 2, p. 24).

Philanthropy — updates to the list of specifically listed deductible gift recipients

Since the 2020-21 MYEFO, a number of organisations have been granted deductible gift recipient status or extensions to that status. These organisations are listed in the budget papers, with an estimated cost of $7.5m over the forward estimates (2021-22 Budget Paper No 2, p. 25).

Gender implications

Why is this an issue for women?

As we stated in the 2020 Gender Lens on the Budget, a reduction in the higher tax rates will benefit more men than women. Tax rates and systems are gender blind: they do not take account of gender. The gendered effect of tax cuts is a consequence of the gender pay gap that results in women being underrepresented in the higher income brackets.

Labour market participation rates are highly dependent on effective marginal tax rates which are based on the interaction between tax rates and transfer payments such as Family Tax Benefits (Kalb, 2017). In deciding whether to take on additional work the taxpayer will take into account the effective marginal tax rate and additional child care costs to decide whether it is worth taking on the extra hours of work. This year there are no substantive changes to tax rates. The childcare reforms (see Early Childhood Education and Care) will benefit families that have two children under six in care or where the combined family income is more than $189,390.

The tax data show that women represent a far smaller proportion than men in the highest tax brackets, with 27 per cent of taxpayers earning more than $120,000 being women. While the difference is smaller in the middle tax rate of 32.5 per cent, women, who submit fewer than half as many tax returns, make up 57 per cent of people returning incomes under $45,000.
Extracted from Taxation Statistics 2017-18, Individuals Table 3A (accessed 15 May 2021) Data.gov.au

Therefore when designing changes to the tax system, changes that benefit lower income earners will assist women more than men. It will increase the financial incentive to participate in the workforce as well as putting more cash in the purses of low income earners.

Women are also more likely to support, and benefit from, government spending on public goods, including health and the age pension. ABS Fiscal Incidence Studies show that single parent families and people over the age of 65 receive more in social transfers than they pay in taxes (ABS 2016), and both of these demographic groups are predominantly female (DSS, 2021). Taxes are the primary form of collection of revenue to fund these services.

What are the 2021 Budget impacts on women?

As stated in our analysis of the 2018-19 Budget, the stage 3 tax cuts that are scheduled to take effect from 1 July 2024 give the most significant tax cuts to the highest earning taxpayers. The LMITO was introduced to give temporary tax relief to taxpayers earning less than $120,000. The effect of the tax cuts brought forward to 2020 as a COVID relief measure was that low income earners would have faced an increase in taxes. Accordingly the Government extended the LMITO in 2020. The 2021 "tax cuts" are an extension of this policy, and the effect will be to prevent the tax increase that would otherwise take effect from the 2021-22 income tax year. Note that this will not be paid until after people have lodged their income tax return; ie after June 2022.

The impacts of the personal income tax system on women arise because women are more likely to be lower income earners. The most recent tax data, for the year ended 30 June 2018 shows that although about 48 per cent of taxpayers who earn less than $120,000 are women, among taxpayer earning more than $120,000 that figure drops to 47 per cent.

Analysis undertaken by Bankwest Curtin Economics Centre prior to the 2021-22 budget indicates that when stage 3 of the tax cut plan is introduced men will, on average, receive tax cuts of $2,989 whereas women will receive cuts of $637 (at p. 5). The extension of the LMITO will mitigate this, however the stage 3 tax cuts remain regressive.

We also noted in 2018 that the offset mechanism is 'a retrograde piece of policy design that adds complexity to the system' (Irvine, 2018). As a result of the phase out over higher incomes, the LMITO increases disincentives to work, particularly for part time working women." (Irvine, 2018)

The extension is necessary, but it perpetuates bad tax design, as it is a disincentive to increased workforce participation, and it increases the effective marginal tax rates for low-middle income workers.

One of the justifications that the Government put forward in 2018-19 for legislating a long term tax plan was to address “bracket creep”: as workers earn more they are pushed into higher tax brackets and pay a higher average rate of tax on their income. This argument has not withstood the changes in economic circumstances, with wage growth at record low levels since the 2018-19 budget. The Budget Papers note that wages will remain below 2 per cent until June 2023. (Budget Paper No 1, p. 62, 2021-22)

We note that internationally there are moves to increase the progressivity of tax systems: the Biden Tax Plan proposes an increase in personal income tax rates and capital gains tax for the highest income earners.

The inequitable tax plan must be reviewed, with the stage 3 tax cuts repealed or restructured. The uncertainty of extending the LMITO in the annual budget must be reviewed, and the tax offset should be paid through the PAYG system, instead of eligible taxpayers being forced to wait until they lodge their income tax return after the end of the financial year.

The tax data does not show the number of women who have benefited from Employee Share Schemes, or the income range of those who benefited from the schemes. We would recommend that high income earners be excluded from the relaxation of the deferred taxing point. We note that ESS offers over $30,000 per employee must still be reported to the ATO, ensuring that these arrangements can be traced; but would recommend that this value is set at a lower level. The tax statistics note that the average value of all reported ESS data is considerably higher than the median value. We would recommend that the value be lowered to $10,000, which would be higher than the median but lower than the average value of transactions in all categories (extracted from *Taxation Statistics 2017-18, Individuals Table 1B, accessed 15 May 2021)*.

There are several welcome changes to reduce the complexity of lodging income tax returns. Specifically the removal of the $250 exclusion of some self-education expenses will simplify the process of determining the amount that is deductible where the self-education expenses are related to earning assessable income. Similarly the clarification of the residency rule will make it easier to apply the tests to determine whether a person is taxed as an Australian resident. Neither of these measures will have a significant effect on revenue collection.

The usual annual housekeeping measures relating to new Deductible Gift Recipients and the indexation of the Medicare Levy Threshold have also been reported in the budget papers.

Recommendations

- The inequitable tax plan must be reviewed, with the stage 3 tax cuts repealed or restructured to ensure that the tax rates and thresholds are more progressive.

- The uncertainty of extending the LMITO in the annual budget must be reviewed, and the tax offset should be paid through the PAYG system, instead of eligible taxpayers being forced to wait until they lodge their income tax return after the end of the financial year.

- The reduced reporting threshold for Employee Share Schemes should be set at $10,000.