



Reform of income tax in Australia: A long- term agenda

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ABSTRACT

Income tax reform has been at the centre of the policy agenda in recent years. In particular, there is concern about whether tax rates are dampening work incentives at all levels of the income distribution. In this paper, we examine the potential for reform of the Australian income tax system. We explore three scenarios: one which maximises the tax-free income threshold while keeping existing marginal tax rates constant, a second which adjusts the relationship between the average tax rate and the company tax rate, and a third which maximises the tax-free threshold subject to a flat marginal tax rate of 35 per cent. We demonstrate that it would be

possible over a decade to increase the tax-free threshold above the single adult rate of Newstart Allowance (the main unemployment benefit) and to reduce the gap between the company tax rate and average income tax rates to less than five percentage points over a wide range of incomes. Our modelling is contingent upon a continuation of increases in real earnings. The models demonstrate how benefits from continued increases in productivity can be distributed between the government and taxpayers in a way that promotes work incentives, achieves a gain in vertical equity, and allows the government's revenue to continue