

Shifting the tax burden to middle-income earners will undermine jobs and growth

Written by The Conversation

The government's idea of raising the Medicare levy, while also removing the 2% budget deficit levy on incomes above A\$180,000, is less "transformational" and more signature Liberal policy. It shifts the tax burden towards middle income earners, as opposed to Labor's plan to direct higher tax rates towards higher income earners.

Rather than introducing a simple flat rate rise of 0.5% in the marginal tax rate across all taxpayers, the government has chosen to increase the Medicare levy. The reason lies in the fact that the levy contains the equivalent of a low-income tax offset due to the [phasing out of the low-income exemption](#).

For example, in the current financial year, the thresholds for the phasing out of the Medicare levy exemption is A\$21,665 for singles and A\$36,541 (plus A\$3,356 for each dependent child/student) for families. At these thresholds, tax rates rise by the rate of the withdrawal of the exemption, which works out to be 8% (calculated as 10% less the 2% Medicare levy rate).

In the case of a two-child family, this means an 8% rise in the marginal tax rate at an income from A\$43,253, to an upper income limit of A\$51,803. If a Medicare levy increase of 0.5% were introduced in the current tax year, the upper income limit for the higher marginal tax rate would rise to A\$54,066.

In combining a rise in the Medicare levy with the removal of the budget deficit levy, the government is therefore proposing a rise in marginal tax rates across a wide band of middle incomes and a marginal tax rate cut for the top.

This direction of tax reform is a continuation of the incremental shift in the overall tax burden towards middle income earners over recent decades. And because the threshold for the Medicare levy exemption is based on family income, the reform will reinforce the move towards higher effective tax rates on low income second earners in a family.

This shift in the tax burden from top to middle income earners, and to middle income families, will undermine aggregate demand and, in turn, "jobs and growth" in the future.

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In contrast to the government's policy, Labor's policy limits the rise in the Medicare levy to incomes above the top two bracket points and retains the budget deficit levy. Raising taxes on top incomes is not only a fairer policy, but a more efficient one in the conventional economic sense.

The impact of taxes on hours worked declines as earnings get higher, and has close to no effect on [the hours worked by those with top incomes](#) . And by avoiding higher taxes on second family earners, Labor's policy should have a less negative effect on second earner hours of work and therefore the tax base.

The government's and Labor's tax reforms therefore represent very different policies.

Patricia Apps has previously received ARC grants.

Read more <http://theconversation.com/shifting-the-tax-burden-to-middle-income-earners-will-undermine-jobs-and-growth-77706>