
About this paper

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Tax Cuts for Growth: The impact of marginal tax rates on Australia's labour supply

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About the author

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Summary

The Australians facing the strongest disincentives to work are mostly on

The context for personal tax reduction

Australia is currently debating the issue of whether and how to cut personal income tax. The purpose of this paper is to explore what income tax reductions would do most to encourage economic growth. The paper does this by assessing the existing literature on tax and tax cuts in Australia and overseas, as well as examining recent Australian economic modelling work.

The paper assumes that a substantial amount of revenue from the Federal Government's projected surplus and/or base broadening will be foregone to fund reductions in personal tax. It does not examine the question of whether that revenue could be applied to other purposes – to new government spending or debt reduction. And it does not explore which

Australia's supply of labour

Compared with other English-speaking countries, Australia has relatively low labour market participation – that is, a relatively low fraction of the population is working or looking for work. In particular, a relatively low

Understanding effective marginal tax rates

Where people receive family payments and face tax on their earnings, the

Responses to rates

Once we have established who faces what effective tax rates, the second

The conclusion above – that Australian high-income earners are less responsive to tax cuts – is not without

4.

If, for instance, we cut the bottom rate of ta

Cutting tax for higher income earners

It seems that, with the possible exception of second income earners, tax cuts for higher income earners will produce less additional labour supply than applying the same quantity of revenue foregone to cutting tax lower down the income scale.⁸ This is hardly surprising given that unemployment rates are so much lower among those able to earn high incomes and that a disproportionate number of them already work relatively long hours.

ABS figures disclose that 30 per cent of full time employees work 50 hours a week or more, with 56 per cent of managers working very long hours, and 11 per cent working more than 70 per cent a week (ABS 2003). The incidence of long hours has risen from a low point in the early 1980s though the debate in Australia has generally focused on the role of changing institutional arrangements and the bargaining power between workers and managers in explaining these

For these people, in so far as the tax system is relevant to their decision,

TABLE 6: THE COSTS OF LOWERING THE TOP RATE COMPARED WITH LIFTING THE SECOND TOP THRESHOLD

Measure	Cost (\$b)	Proportion of total (%)
Cut top rate	2.3	100

Company tax and the top marginal rate: should they be aligned?

The idea of aligning th

Appendix 3

Modelling the interactions: The MITTS model

The Melbourne Institute Tax and Transfer Simulator (MITTS) is a microsimulation model of the Australian economy with detailed information about Australia's tax and transfer system. [Technical description, 2015-16 update](#)

Appendix 4

References

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