Australian Council of Social Service

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Senator Siewert
Chair
Senate Standing Committee on Community Affairs
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Parliament House
Canberra ACT 2600
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Dear Senator Siewert,

Thank you for the opportunity to provide a submission to the 'Inquiry into the extent of income inequality in Australia'. ACOSS is a national voice for people affected by poverty, disadvantage and inequality. Our vision is for a fair, inclusive and sustainable Australia where all individuals and communities have the opportunities and resources they need to participate in and benefit from social and economic life. This vision underpins all of our policy and advocacy, and enclosed for the committee's consideration are a number of key publications that propose strategies to reduce inequality.

Australia has enjoyed unbroken economic growth for more than two decades. Yet the benefits of this growth have not been enjoyed by all. Too many members of our community remain in poverty, with 2.2 million people including 1 in 6 children living below the poverty line in Australia. At the lower end of the income distribution many people lack access to the opportunities that would allow them to share the benefits of our national prosperity.

The level of income inequality in Australia sits above the OECD average, and it has risen over the past two decades. An OECD report published in 2014 shows that over the last 15 years, Australia has become a less equal society, with the income share of those at the bottom and in the middle falling, and those at the top rising. The Productivity Commission identified that in the 2000's inequality in Australia grew faster than most other OECD countries, with the rate of increases the third fastest in the OECD, ahead of both the UK and the US. Furthermore, Professor Peter Whiteford finds that while both GDP and inequality have increased since the early 1980s, the more rapid period of increase in inequality occurred concurrent with periods of high economic growth after the mid-1990s.

There is nothing inevitable about the inequality experienced by a society. The nature and extent of inequality is influenced by social and economic policy decisions, both directly through the redistribution of resources and the provision of services, and indirectly through the influence of policy settings on individual and institutional behaviour. Australia is fortunate to have many policy settings that ameliorate inequality. Significant amongst these in terms of impacts on income inequality are our tax and transfer system and our employment and labour market structures.

The tax and transfer systems have been important mechanisms by which Australian governments have offset rising inequality in market incomes. However analysis by Professor Peter Whiteford shows that from the mid-1990s the extent of re-distribution made through the tax and transfer system has fallen, and that the more rapid rise in disposable income inequality since the 1990s results substantially from reduced government re-distribution. This is due in part to falling unemployment (leading to less reliance on social security) but also to policy changes in the tax-transfer system.

I would like to draw the Committee's attention to the growing body of research, including a 2012 OECD report 'Income Inequality and Growth: The role of taxes and transfers', which finds that many redistributive policies have a positive impact on economic growth. Consistent with these findings, ACOSS considers that well-designed taxes and expenditures (education and training, health, social security, social services, housing and transport infrastructure) underpin productivity and economic growth.

Australia needs a system of economic growth that is inclusive. This should draw on work already undertaken by the OECD and the C20 steering committee which has focussed on human capital development, promoting entrepreneurship, local strategies (affordable housing and physical and social infrastructure), and collaborative leadership across Government, community and business.

Among the key public policies that directly influence the level of income inequality and who is affected by it are:

- The adequacy and targeting of social security system and its effectiveness in connecting people with employment opportunities, where appropriate;
- Education and skills policies, especially those affecting the quality and accessibility of early childhood education and schooling in disadvantaged communities;
- Investment in employment assistance for those who are disadvantaged in the labour market;
- Labour market regulation including minimum wages and employment security;
- Policies to remove barriers to employment and career progression for women, who comprise the majority of low paid workers; and
- The tax system, especially the overall balance between progressive and regressive taxes, and the extent of opportunities for people on high incomes to avoid paying tax at statutory rates.

The strong increase in employment and decline in unemployment from the early 1990s to mid-2000s, together with higher workforce participation especially among women, has provided a solid foundation for public policies to reduce income inequality. Strong and sustained employment growth is obviously vital and it is likely that the recent slow-down in jobs growth has contributed to an increase in inequality since the global downturn.

It is also vital that those who are disadvantaged in the labour market, especially those whose unemployment is prolonged, have equitable access to the jobs that are created across the economy. For example, the Government's investment in public infrastructure should yield job opportunities for people who are unemployed long-term as well as improvements in public amenity and productivity. Australia invests half as much as the OECD average in labour market assistance for unemployed people, and this is false economy. Our submission to last year's the review of employment services is attached and available online.

ACOSS, the BCA and the ACTU have been working together on policies to improve access to employment for people disadvantaged in the labour market. Our joint statement proposing a partnership model of employment assistance is attached and available online.

A key factor working against a reduction in income inequality between the early 1990s and mid-2000s was the increase in wage inequality among those who were employed. Wage inequality has increased over the past three decades, with modest wage increases at the bottom of the earnings distribution and much greater increases at the top. Structural changes in the labour market favouring more skilled employment have contributed to this, along with changes in workplace regulation and a lack of effective constraints (whether market based or legislative) on wages growth at the top end of the distribution. I refer the Committee to our submission to the Annual Wage Review which is attached and online.

Effective public investment in education and training can help lift the skills of those who would otherwise face a career of low paid employment or lengthy periods of unemployment. Policy priorities include ensuring that children have access to early education regardless of the labour market status of their parents, and extending funding commitments under the new national schools funding regime so that fair access to quality schooling is assured for families in disadvantaged communities.

The main weakness of our social security safety net is the inadequacy of 'allowance' payments for unemployed people, single parents and students. Recent increases in pensions for older people have sharply reduced poverty but these were not extended to allowance recipients and the gap in payments between pensions and allowances is now $166 per week for a single adult. Policy makers should end the pretence that employment and activation policies alone can prevent poverty among people of working age. This has not happened in any OECD country. Clearly the social security system needs to carry its share of the load, starting with implementation of the 'Henry Report' proposal to extend recent pension increases to those on the lower allowance payments.

The system of indexation of social security payments also makes a big difference to income inequality over the long term. The decision to stop indexing family payments to wage movements in 2009, and the recent Budget proposal to remove indexation of pensions to wages guarantee that the majority of households at the bottom of the income distribution will fall behind income growth across the broader community. This is already the experience of unemployed people on the lower allowance payments, which have not increased in real terms for 20 years. All social security payments for those with low incomes should be indexed to wage movements as well as consumer price movements.

The tax system plays a crucial role in reducing income inequality, both by raising the revenue needed to finance social expenditures and by imposing higher average rates of tax on those with greater capacity to pay. The personal income tax system is the main 'equalising factor' within the tax system since it taxes investment income as well as earnings from employment, and does so at progressive rates. Taxes on land are also progressive to the extent that they apply to owner-occupied housing as well as business and investment property. On the other hand, taxes on consumption and business inputs (to the extent that these flow through to consumers) are regressive since they do not tax that part of incomes that are saved and invested, and there is limited scope to 'discount' consumption taxes to benefit households on low incomes (the GST exemption for uncooked foods is one example of this). Taken together, Australian taxes on income and consumption and business inputs are close to proportional in their overall incidence. That is, the progressive impact of taxes on income is almost offset by the regressive impact of taxes on consumption and business inputs so that households pay roughly the same overall rate of tax on their income across the income distribution.

While the progressive personal income tax rate scale is clearly progressive, people on higher incomes can easily avoid paying tax at their marginal rate through tax shelters and loopholes such as superannuation, negatively geared investment in assets, the preferential tax treatment of capital gains, and the use of private trusts. For example, the top 20% of wage earners receive the majority of the benefits from tax breaks for superannuation, even though they are unlikely to have to rely on age pensions when they retire. The top 10% of male wage earners receive more in superannuation tax concessions over their lives than they would if they received the full rate of the age pension.

To ensure that tax policies reduce income inequality rather than increase it, access to these and other tax shelters which make no positive contribution to economic growth and productivity should be restricted. It is also vital that policy makers avoid any major shift in the incidence of taxation from income to consumption as this would greatly increase inequality of spending power by raising taxes on people on the lowest incomes and reducing them on high income households.

ACOSS recognises that Australia faces a challenge in meeting the growing gap between the community's reasonable expectations and available resources to meet those expectations. This was exacerbated by fiscal policy during the 'boom years', on both the expenditure and revenue sides of the Budget.

Government expenditure in Australia is low compared to other OECD nations. We are the third lowest spending nation and the fifth lowest taxing nation. The main reason for this is that we have one of the most tightly targeted social security systems in the OECD, spending just 8% of our GDP on social security compared to an OECD average of 12%. However, the targeting of some payments was loosened in recent years, with family payments and pensions extending to households that arguably do not need them including retired couples with over $1 million in financial assets apart from their homes.

Yet the source of Australian Government's fiscal problems lies mainly on the revenue side. While budget deficits have only emerged since the onset of the global financial crisis, the budget has been in structural decline since the early 2000s. This is largely due to Governments decisions to 'spend' the revenue windfall from the housing and mining booms of the 2000s on eight successive income tax cuts and on increasing a range of tax concessions. From 1999 to 2010, personal income tax takings shrank from 12% to 10% of GDP (2010) while at the same time the cost of tax expenditures rose from 4% to 8% of GDP, including a rise from 2 to 5% of GDP for superannuation tax expenditures. Tax 'bracket creep' is slowly restoring revenue from personal income tax but this cannot be sustained indefinitely. A fairer and more economically efficient way to restore revenue from income tax is to broaden this tax base by reducing the impact of the shelters and loopholes referred to previously.

Clearly, there is a need for revenue and expenditure to be considered together, and ACOSS supported a comprehensive review of direct expenditures and tax expenditures through the National Commission of Audit process. Unfortunately the Commission (unlike the previous Audit process in 2006) was unable to properly consider the cost efficiency of tax expenditures. I attached for the Committee's consideration our submission to the Commission which identifies what we consider the role of Government to be, and highlighting areas where changes could be made over the short and medium term to government taxation and expenditure that would improve the equity and efficiency of the tax and transfer system.

Also attached is the ACOSS 2014-15 Budget Submission, highlighting immediate changes that would improve the fairness of government fiscal activity. The submission calls for effective and targeted expenditure on housing, income support and community services. Critical amongst these is a proposed $50 per week increase in social security 'allowance' payments.

The 2014-15 budget represented a missed opportunity – focusing too much on spending and too little on where the bigger problem lies – falling revenue. Our analysis of the budget has highlights that by focusing on expenditure savings, and targeting within those savings measures many people on the lowest incomes, the budget proposals would disproportionately affect people with the least capacity to pay and increase income inequality.

To reform the social security and tax systems, improve the effectiveness of our economic and social infrastructure, and to restore inclusive and sustainable growth, Governments need to work collaboratively with the community as well as business. The first step is to start a dialogue across the community to forge a consensus on the nature of challenges we face. The growing gaps between the 'haves' and 'have nots', and between those who are fortunate enough to have high paying jobs and substantial income from investments and the rest of the community are among the key challenges we face as a nation. We cannot effectively resolve our other economic and social problems unless we deal with the inequality challenge at the same time.

Yours sincerely,

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CEO, ACOSS