Does the U.S Experience Offer Any Lessons for Tax Reform in Australia?
Remarks for Australia National University's COVID-19 National Tax Summit
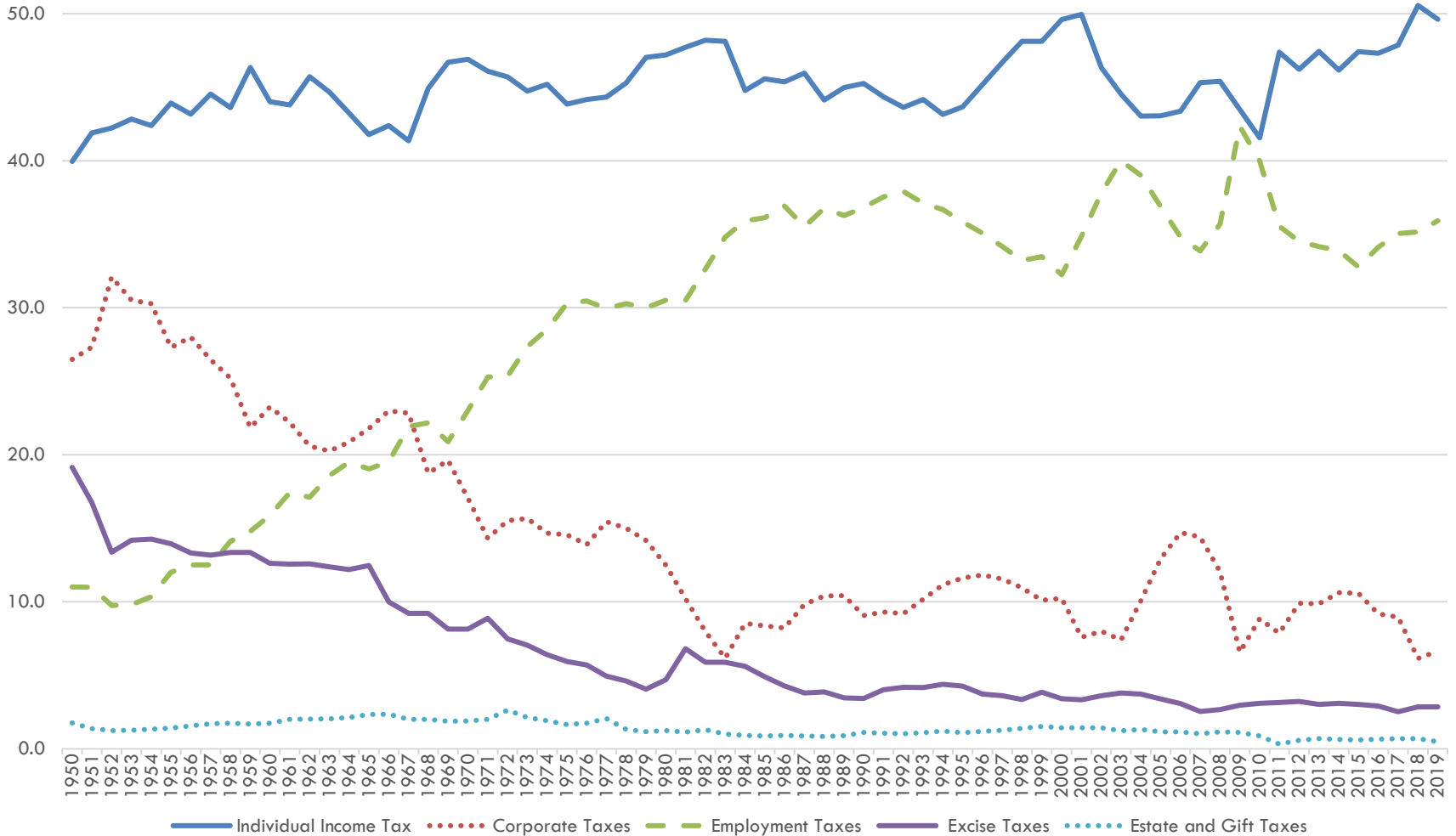

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Some Background on the U.S. Federal Tax System

❑ The U. S. federal government is more reliant on direct taxes on individuals and households than is Australia

  ■ Income and payroll taxes account for more than 80% of government revenue

  ■ Unlike Australia, no national GST

Figure A-1.−Federal Receipts by Source as Share of Total Receipts, 1950-2019

Legend: Individual Income Tax — Corporate Taxes — Employment Taxes — Excise Taxes — Estate and Gift Taxes

Sources: Office of Management and Budget, Historical Tables, Fiscal Year 2020; Final Monthly Treasury Statement Fiscal Year 2019; Joint Committee on Taxation calculations.

Some Background on the U.S. Federal Tax System

❑ Overall, the Federal tax system is progressive

  ■ The dominant component producing the progressivity is the individual income tax

  ■ Because of ownership of business assets, the corporate income tax also contributes to the overall progressivity

Distribution of Taxpayers and Average Tax Rates

Table A-6.–Distribution of Income and Taxes, and Average Tax Rates in 2019 (Projected)

Income Category [1]	Number of Returns [2] (Thousands)	Share of Returns	Income ($ Millions)	Share of Income	Combined Income, Employment, and Excise Taxes Under Present Law [3]			Individual Income Taxes			Employment Taxes		
					$ Billions	Percent share	Average Tax Rate	$ Billions	Percent share	Average Tax Rate	$ Billions	Percent share	Average Tax Rate
Less than $10,000......................	17,173	9.9%	57,690	0.4%	2.2	0.1%	3.8%	-8.6	-0.6%	-14.9%	6.8	0.6%	11.8%
$10,000 to $20,000......................	17,566	10.1%	267,657	1.7%	-2.8	-0.1%	-1.0%	-38.6	-2.6%	-14.4%	29.2	2.4%	10.9%
$20,000 to $30,000.....................	19,631	11.3%	489,231	3.1%	19.8	0.7%	4.0%	-34.3	-2.3%	-7.0%	45.1	3.8%	9.2%
$30,000 to $40,000.....................	16,513	9.5%	575,313	3.7%	43.7	1.5%	7.6%	-16.9	-1.1%	-2.9%	50.8	4.3%	8.8%
$40,000 to $50,000.....................	14,349	8.3%	644,389	4.1%	62.9	2.1%	9.8%	-3.9	-0.3%	-0.6%	56.5	4.7%	8.8%
$50,000 to $75,000.....................	27,832	16.0%	1,708,410	10.9%	215.9	7.3%	12.6%	41.4	2.8%	2.4%	146.4	12.3%	8.6%
$75,000 to $100,000..................	17,251	9.9%	1,496,621	9.6%	226.1	7.6%	15.1%	73.7	4.9%	4.9%	127.2	10.7%	8.5%
$100,000 to $200,000..................	31,090	17.9%	4,294,090	27.5%	810.2	27.3%	18.9%	330.1	22.1%	7.7%	403.3	33.8%	9.4%
$200,000 to $500,000..................	10,290	5.9%	2,876,976	18.4%	678.9	22.9%	23.6%	381.7	25.5%	13.3%	239.8	20.1%	8.3%
$500,000 to $1,000,000..............	1,348	0.8%	902,823	5.8%	250.3	8.4%	27.7%	187.0	12.5%	20.7%	45.1	3.8%	5.0%
$1,000,000 and over...................	689	0.4%	2,290,307	14.7%	662.9	22.3%	28.9%	582.9	39.0%	25.4%	43.3	3.6%	1.9%
Total, All Taxpayers.................	173,732	100.0%	15,603,507	100.0%	2,970.1	100.0%	19.0%	1,494.6	100.0%	9.6%	1,193.6	100.0%	7.6%

[1] The income concept used to place tax returns into income categories is adjusted gross income (AGI) plus: (1) tax-exempt interest,
    (2) employer contributions for health plans and life insurance, (3) employer share of FICA tax, (4) worker's compensation,
    (5) nontaxable Social Security benefits, (6) insurance value of Medicare benefits, (7) alternative minimum tax preference items,
    (8) individual share of business taxes, and (9) excluded income of U.S. citizens living abroad. Categories are measured at 2019 levels.

[2] Includes nonfilers, excludes dependent filers and returns with negative income.

[3] Federal taxes are equal to individual income tax (including the outlay portion of refundable credits), employment tax (attributed to employees),
    excise taxes (attributed to consumers), and corporate income taxes. The estimates of Federal taxes are preliminary and subject to change.
    Individuals who are dependents of other taxpayers and taxpayers with negative income are excluded from the analysis.
    Does not include indirect effects.

[4] The average tax rate is equal to Federal taxes described in footnote [3] divided by income described in footnote [1].

Source: Joint Committee on Taxation staff estimates.

Some Background on the U.S. Federal Tax System

❑ The individual income tax operates as a negative income tax

❑ Negative, refundable tax liabilities are created by refundable tax credits which are based on family size and earned income

❑ Many low-income households have no income tax liability and receive a refundable credit that exceeds the household's payroll tax liability

Table 2.--Distribution by Income Class of All Returns, Taxable Returns, Itemized Returns, and Tax Liability
at 2019 Rates, 2019 Law, and 2019 Income Levels [1]

[Money amounts in millions of dollars, returns in thousands]

Income Class [2]	All Returns [3]	Taxable Returns	Itemized Returns	Tax Liability [4]
Below $10,000	17,173	5,738	63	-$8,322
$10,000 to $20,000	17,566	6,386	127	-37,619
$20,000 to $30,000	19,631	9,273	197	-32,262
$30,000 to $40,000	16,513	9,743	341	-13,917
$40,000 to $50,000	14,349	9,673	504	-152
$50,000 to $75,000	27,832	22,118	1,876	54,215
$75,000 to $100,000	17,251	15,920	2,197	87,660
$100,000 to $200,000	31,090	30,719	6,422	380,674
$200,000 and over	12,327	12,316	5,958	1,246,505
Total	173,732	121,886	17,685	$1,676,781

[1] Tax law as in effect on July 1, 2019. Income categories are measured at 2019 levels.

[2] The income concept used to place tax returns into classes is adjusted gross income ("AGI") plus: (a) tax-exempt interest, (b) employer contributions for health plans and life insurance, (c) employer share of FICA tax, (d) workers' compensation, (e) nontaxable Social Security benefits, (f) insurance value of Medicare benefits, (g) alternative minimum tax preference items, (h) excluded income of U.S. citizens living abroad, and (i) individuals' share of business taxes.

[3] Includes filing and non-filing units. Filing units include all taxable and nontaxable returns. Non-filing units include individuals with income that is exempt from Federal income taxation (e.g., transfer payments, interest from tax-exempt bonds, etc.). Excludes individuals who are dependents of other taxpayers and taxpayers with negative income.

[4] Individual income tax and individuals' share of business taxes.

NOTE--Details may not add to totals due to rounding.

Source: Joint Committee on Taxation

Some Background on the U.S. Federal Tax System

❑ Two-thirds of taxpayers pay more in payroll taxes than income taxes

Distribution of Taxpayers by Income Tax and Employment Taxes

Table A-7.—Tax Returns with Inocme or Employment Taxes in 2019 (Projected)

Income Category [1]	Number of Returns [2] (Millions)	Individual Income Taxes [3]	Employment Taxes [3]	Employment Taxes Less than Income Taxes [3]	Employment Taxes Greater than Income Taxes [3]	
		$ Billions	$ Billions	Returns (Millions)	Returns (Millions)	Fraction of Total
Less than $10,000.........................	17.2	-8.6	6.8	[4]	9.2	53.6%
$10,000 to $20,000........................	17.6	-38.6	29.2	0.1	14.5	82.8%
$20,000 to $30,000........................	19.6	-34.3	45.1	0.2	14.4	73.3%
$30,000 to $40,000........................	16.5	-16.9	50.8	0.4	12.4	75.1%
$40,000 to $50,000........................	14.3	-3.9	56.5	1.1	10.7	74.9%
$50,000 to $75,000........................	27.8	41.4	146.4	3.9	20.6	74.2%
$75,000 to $100,000......................	17.3	73.7	127.2	4.2	12.3	71.6%
$100,000 to $200,000.....................	31.1	330.1	403.3	10.2	20.8	66.9%
$200,000 to $500,000.....................	10.3	381.7	239.8	7.5	2.7	26.7%
$500,000 to $1,000,000..................	1.3	187.0	45.1	1.3	[4]	1.5%
$1,000,000 and over......................	0.7	582.9	43.3	0.7	[4]	1.3%
Total, All Taxpayers....................	173.7	1494.6	1193.6	29.7	117.8	67.8%

[1] The income concept used to place tax returns into income categories is adjusted gross income (AGI) plus: (1) tax-exempt interest,
    (2) employer contributions for health plans and life insurance, (3) employer share of FICA tax, (4) worker's compensation,
    (5) nontaxable Social Security benefits, (6) insurance value of Medicare benefits, (7) alternative minimum tax preference items,
    (8) individual share of business taxes, and (9) excluded income of U.S. citizens living abroad. Categories are measured at 2019 levels.

[2] Includes nonfilers, excludes dependent filers and returns with negative income.

[3] The estimates of individual income tax (including the outlay portion of refundable credits) and employment tax (attributed to employees)
    are preliminary and subject to change. Individuals who are dependents of other taxpayers and taxpayers with negative income are
    excluded from the analysis. Does not include indirect effects.

[4] Less than 50,000.

Source: Joint Committee on Taxation staff estimates.

Some Background on the U.S. Federal Tax System

❑ The combination of payroll taxes with the individual income tax and its refundable credits results in generally progressive taxation of labor income

Average Marginal Tax Rates on Labor Income

Table A-8.—Marginal Tax Rates on Labor and Long-Term Capital Gains, by Income Category in 2019 (Projected)

Income Category [1]	Labor Income			Long-Term Capital Gains Income
	Average Marginal Income Tax Rate [2]	Average Marginal Employment Tax Rate [2]	Average Combined Marginal Income and Employment Tax Rate [2]	Average Marginal Capital Gains Tax Rate [2]
Less than $10,000........................	-8.0%	14.2%	6.3%	3.7%
$10,000 to $20,000......................	-2.6%	14.2%	11.6%	2.5%
$20,000 to $30,000......................	7.0%	14.2%	21.2%	2.3%
$30,000 to $40,000......................	10.8%	14.2%	25.0%	2.7%
$40,000 to $50,000......................	12.8%	14.2%	27.0%	3.1%
$50,000 to $75,000......................	14.7%	14.2%	28.9%	6.1%
$75,000 to $100,000....................	15.4%	14.2%	29.6%	9.3%
$100,000 to $200,000..................	18.1%	13.5%	31.6%	12.7%
$200,000 to $500,000..................	23.6%	10.0%	33.6%	18.1%
$500,000 to $1,000,000...............	33.6%	7.2%	40.7%	22.6%
$1,000,000 and over....................	34.5%	6.9%	41.4%	23.5%
Total, All Taxpayers.................	13.0%	13.5%	26.6%	21.5%

[1] The income concept used to place tax returns into income categories is adjusted gross income (AGI) plus: (1) tax-exempt interest, (2) employer contributions for health plans and life insurance, (3) employer share of FICA tax, (4) worker's compensation, (5) nontaxable Social Security benefits, (6) insurance value of Medicare benefits, (7) alternative minimum tax preference items, (8) individual share of business taxes, and (9) excluded income of U.S. citizens living abroad. Categories are measured at 2019 levels.

[2] For individual income and employment taxes, the average marginal tax rate is equal to the change in taxes from an additional $100 of wages to each spouse with positive wages. For long-term capital gain, the average marginal tax rate equals the change in taxes from an additional 1% increase in long-term capital gains to each taxpayer with positive long-term capital gains. Effective marginal rates may be higher or lower than statutory marginal rates due to certain provisions in the Code including the phasein and phaseout of certain exemptions or credits.

Source: Joint Committee on Taxation staff estimates.

Does the United States Experience Offer Any Lessons?

- Major tax legislation in the United States over the past 35 years
    - 1986 – the Tax Reform Act of 1986
    - 1997 – the Tax Reform Act of 1997
    - 2001 – the Economic Growth and Tax Relief Reconciliation Act of 2001
    - 2017 – Public Law 115-97

Lesson #1

❑ Common to the enactment of each of these pieces of legislation was active engagement by the President

❑ In the United States, the legislature cannot do be sweeping change on its own

What is the Goal?

❑ The President helped build a consensus around a clearly articulated goal

- 1986 – Ronald Reagan and his campaign promise to lower rates and simplify
- 1997 – Bill Clinton as part of ending welfare "as we knew it"
- 2001 – George W. Bush and his campaign promise to return the projected budget surplus to the American taxpayer
- 2017 – Donald Trump and his promise of pro-growth policies

Lesson #2

❑ Build a consensus around a clearly articulated goal

Multiple Policy Goals

❑ How many problems will you attempt to solve?

❑ In the United States, policy makers have identified several policy targets as motivation for tax reform

■ Stronger economic growth

■ International competition

■ Complexity of the tax system and related compliance issues

■ Income and wealth inequality

■ Climate change

■ Infrastructure finance

■ The temporary structure of many provisions of tax law

Lesson # 2.5

- ❏ In 2017 the Congress and the President emphasized two targets
  - ▪ Economic growth
  - ▪ International competition

- ❏ This is not to say that the other goals were not worthy, but there was bipartisan consensus on these two

- ❏ Lesson #2.5 – To have a successful consensus you probably cannot solve all the problems at once

Lesson #3

❑ Remember there are always tradeoffs in policy design

- ■ Efficiency vs. Equity
- ■ Simplicity vs. Efficiency
- ■ Equity vs. Growth

Lesson #3 (cont'd)

❑ A fundamental axiom is that to "solve" a policy problem you need at least as many policy tools as policy targets

❑ Within the broad goal of 2017 to provide incentives for business growth the policymakers had several sub-targets.
  - Weigh the benefits to domestic only business compared to MNCs
  - Weigh the benefits to corporations compared to businesses operated as pass through entities
  - Weight the benefits of domestically headquartered MNCs compared to foreign headquartered MNC

❑ The tools chosen led to trade-offs between equity, efficiency, simplicity, and growth

Lesson #4

❑ There is always a budget constraint

❑ And budget constraints re-enforce lesson #3 – there are always tradeoffs

- The budget constraint in 1986
- The budget constraint in 2001
- The budget constraint in 2017

Do the People Understand Economics?
Do Economists Understand the People?

❑ Do we as policy analysts communicate clearly, enabling policy makers and the public to make reasoned decisions?

■ In public debate, it appears that often the anecdote prevails over data analysis

■ The anecdote often is drawn from one tail of the distribution of outcomes

■ Do we design policy for the tail or for the mean or median

Do People Understand Economics?
Do Economists Understand the People?

❑ Does poor communication of policy analysis constrain policy design?

■ Statutory incidence vs. economic incidence

❑ Good economics may not make good public policy

■ 1990 – Margaret Thatcher and the poll tax

■ This is, in part, lesson #3 again

Lesson #5

❑ Good reform need not be perfect reform

❑ Because reform requires consensus, the reform policy needs to be consistent with the public's understanding

Thank You!

❑ Good luck addressing the challenges before your country