Sharing the Budget pain

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In his Budget speech last week, the Treasurer again stated that the age of entitlement is over, and noted that "it is time, for all of us, to contribute and build" and "it is only fair that everyone makes a contribution".

In assessing proposed budget changes, it is standard practice to determine whether a change is **progressive**, **regressive** or distributionally **neutral**. A change is regarded as progressive if it either increases the incomes of lower income groups by a higher percentage than for high income groups or reduces the income of high income groups more than those of low income groups; a change is regressive if it has the opposite effects; while a change is distributionally neutral if it affects the incomes of all groups by the same proportional change.

A small group of high income earners – Members of Parliament and senior public servants will have their salaries frozen for one year. A wider group of high-income earners will contribute through a Temporary Budget Repair Levy that increases the top marginal tax rate by two percentage points, for people earning more than $180,000 a year. The levy is estimated to collect about $1.2 billion at its peak in 2016-17. Both of these changes could be expected to be progressive in their impact, but limited by their temporary character.

The majority of the population will contribute through a new charge of $7 per visit for a standard GP consultation, with a limit of charges for 10 services for concessional patients and children under 16 while pharmaceutical co-payments will be increased. In total this will save about $1.7 billion in the 2017-18 year. These changes could be expected to be regressive, offset to some extent by a range of safety net measures. Their distributional impact is also affected by the extent of need for medical services in different groups in the community.

Most households will also contribute through the reintroduction of fuel excise indexation that is projected to raise $990 million by 2017-18. This change could be expected to be mildly regressive among households who drive motor vehicles.

Many of the changes however, were in the social security system, with significant changes to Family Tax Benefits, including the freezing of family assistance rates for two years, the freezing of income rest thresholds, the abolition of higher income-test thresholds for larger families as well as other changes. Families will no longer be eligible for Family Tax Benefit Part B if the main earner's income is $100,000 and the payment that will no longer be available when a family's youngest child turns six and is at school.

Overall, these changes cut to family benefits are estimated to save about $3.2 billion in 2017-18, making reduction in assistance for families the second largest contributor to savings, after changes in the foreign aid budget.

The lowering of the Family Tax Benefit Part B threshold is likely to be progressive, but most of the other changes in the Family Payment system could be expected to be regressive. For example, freezing payment rates is regressive, since proportionately the cuts are higher for lower income families.

From next year, unemployed people under 25 will get Youth Allowance, not Newstart and people under 30 will wait up to six months before getting unemployment benefits, and then will have to participate in Work for the Dole, to be eligible for income support, saving about $330 million in 2017-18. These changes could be expected to be regressive because the unemployed are disproportionately low income.

Assessing how fair everyone's contribution to the important medium to long-term task of moving to budget surplus is complicated by the fact that the Budget papers do not give any estimate of what the cumulative effects of these proposed changes are on households at different income levels.

The absence of estimates of distributional impacts is striking, given that since 2004-05, [the Budget Overview] has each year contained an Appendix showing how much different types of households have gained from policy changes announced in the Budget or over the course of the period of government. Showing losses is not as politically attractive as showing increases in disposable income, however.

Given this lack of information we decided to replicate the methodologies used in previous edition of the Budget Overview and calculate what the impact on households at different income levels could be. This is not straightforward, partly because different initiatives start at different times, and involves a range of assumptions, but as noted, as far as possible we used the same approach as previous Budget Papers and we use the estimates from the most recent Budget for future wage and price increases.

Using the projections set out in the Budget, we have replicated the methodology used in earlier Budget papers, comparing the impact on disposable incomes in 2016–17, when all of the measures have come into effect.

Essentially we calculate what the disposable incomes – after taxes and benefits - of households in different specified family situations and income levels and compare what these incomes would be in 2016-17 with and without the proposed Budget changes. In the table, we then deflate these differences to current (2014) dollars and also show them as a percentage of the projected disposable income of the household, which is the basis for determining whether the impact is likely to be regressive or progressive.

We only look at changes in income tax including the Medicare Levy and cash benefits and do not include the impact of changes in health charges, increases in fuel excise or other changes to the education system.

We find that people on benefits do the heaviest lifting. An unemployed 23-year-old loses $47 per week or 18 per cent of their disposable income. An unemployed lone parent with one 8-year-old child loses $54 per week or 12 per cent.

Lone parents earning around two-thirds of the average wage lose between 5.6 to 7 per cent of their disposable income. A single-income couple with two school-age children and average earnings loses $82 per week or 6 per cent of their disposable income.

Compare this to the $24, or less than 1 per cent of disposable income paid through the Deficit Levy by an individual on three times the average wage – close to $250,000 by 2016–17. High-income couples could together bring in up to $360,000 per year and not contribute an extra cent.

These calculations are conservative. They do not take into account the proposed abolition of the Schoolkids Bonus as this is not a new Budget initiative. They do not deduct rent or child care. As noted, nor do they include increased costs of health care and fuel or changes to education.

Households stand to save $550 per year if power prices fall due to the abolition of the carbon tax. This is likely to have a mildly progressive effect but would offset less than one-fifth of the losses of those who are unemployed or in low paid work.

Our conclusion is that the Budget proposals mean that the Budget pain is not being evenly shared but will be heaviest for many working-age people at the lowest income levels.

Projected difference in real disposable incomes (2014 $ pw) of different household types in 2017, as result of 2014-15 Budget changes

2016-17	Disposable Income 2014 $pw		Difference	
Type	1. Current policy	2. Budget Change	3. 2014 $ pw	%
Single person on Newstart, 23 years	259	211	47	-18.3
Lone parent, one child aged 3, Parenting Payment Single	553	540	13	-2.4
Lone parent, 1 child aged 3, (67% AWOTE)	1,013	999	15	-1.5
Lone parent, one child aged 6, Parenting Payment Single	530	476	54	-10.2
Lone parent, one child aged 6 (67% AWOTE)	990	935	56	-5.6
Lone parent, 1 child aged 8, Newstart	446	392	54	-12.2
Lone parent, one child aged 8, (67% AWOTE)	957	889	67	-7.0
Single income couple with two children, 3 and 6 years (100% AWOTE)	1,310	1,282	28	-2.1
Single income couple with two children, 6 and 9 years (100% AWOTE)	1,287	1,205	82	-6.4
Dual income couple with two children, 3 and 6 years (100% and 33% AWOTE)	1,658	1,590	69	-4.2
Dual income couple with three children, 3 ,6 and 9 years (100% and 33% AWOTE)	1,723	1,656	67	-3.9
Single person (300% AWOTE)	2,847	2,823	24	-0.9
Couple, no children (150% and 100% AWOTE)	2,712	2,712	0	0.0

Note: Results are estimate for the 2016-17 year, but are deflated to 2014 $. Differences per week (3) may not precisely equal Current policy (1) less Budget change (2) due to rounding.

Explanatory notes

Average weekly ordinary time earnings (AWOTE) for full-time employees is projected to be $ 1,583.30 pw in 2016-17. Disposable income is the sum of private income and government cash transfers less net tax paid. Inclusive of the clean energy supplements which are paid to assist households with the impact of the carbon price. Families with incomes exceeding the Medicare surcharge thresholds hold Private Health Insurance cover.

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