



Australian Social Trends

2008

**Article: Government benefits,
taxes and household income**

AUSTRALIAN BUREAU OF STATISTICS

EMBARGO: 11.30AM (CANBERRA TIME) WED 23 JUL 2008

Government benefits, taxes and household income

In 2003–04, people in the bottom 20% of private household incomes in Australia received less than 1% of the total of such income, but after government benefits and taxes their share of final income was 13%.

One of the aims of the system of government benefits and taxes is to assist members of the community who most need financial support. In addition to paying pensions, benefits and allowances, governments provide a range of goods, services and infrastructure for use by households. This article looks at the effects of the tax and transfer system on the distribution of income among households in Australia.

Income and the tax and transfer system

While income is usually received by individuals, it is normally shared between partners in a couple relationship, with dependent children, and to a lesser extent, with other members of the household. A restricted concept of household income is private income. Private income includes the gross incomes, before tax, received in the form of: wages and salaries; profit or loss from own unincorporated business operations; income from property and financial investments; income from superannuation and annuities; and private inter-household transfers.

Adding social assistance benefits (government cash benefits and allowances) to private income gives a measure of gross household income. While gross household income is a useful concept for some analyses, it does not give a complete picture of the current income resources available to households to meet their daily needs. Disposable household income, derived by subtracting income taxes

Data sources and definitions

The major data sources used in this article are the 2003–04 ABS Household Expenditure Survey, ABS Government Finance Statistics, and Input-Output tables from the Australian System of National Accounts.

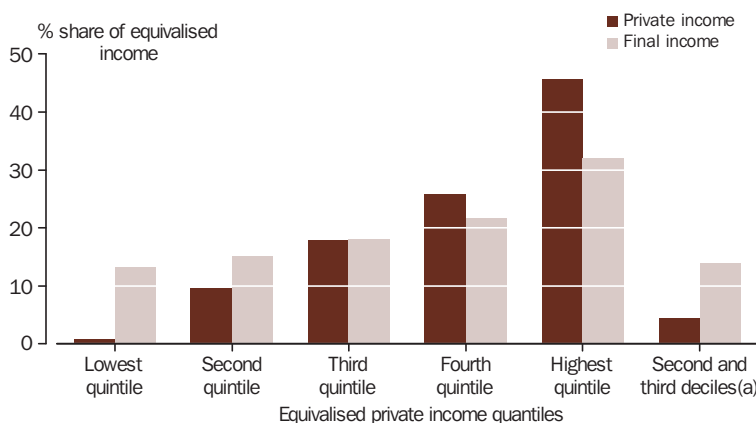
All quintile groups in this article are based on the distribution of equivalised private income. *Equivalising* takes account of differing household sizes and composition and is used to give a relative comparison of living standards. Larger households normally require a greater level of income to maintain the same material standard of living as smaller households, and the material needs of adults are normally greater than the needs of children. Therefore, income estimates are adjusted (by equivalence factors) to standardise the income estimates with respect to household size and composition, while taking into account the economies of scale that arise from the sharing of dwellings. For a more detailed explanation see Appendix 2 of *Government Benefits, Taxes and Household Income, Australia, 2003–04* (ABS cat. no. 6537.0).

and the Medicare levy from gross income, is a more complete income measure for understanding the material wellbeing of households.

An even more extensive measure of a household's command over economic resources to satisfy its needs and wants can be obtained by also taking account of the goods and services received from local, state/territory and federal governments (e.g. medical care, schooling, child care, aged care, disability services and public housing). While health, education, child care, housing and other services can be obtained entirely in the private market, many households receive some of these services either free of charge or subsidised to some extent by governments. The value of some of these services can be determined and allocated to households (based on the characteristics of each household). Adding that value (referred to as 'social transfers in kind') to the disposable income of households provides a wider picture of the resources available to and used by households to support their material standard of living.

Finally, understanding the distributive effects on households of the whole tax and transfer system needs to take account of taxes paid by households not only directly, as income tax, but also indirectly as taxes on production that are passed on to households in the prices that

Effect of taxes and benefits on household income — 2003–04



(a) Low income households are defined as those in the second and third deciles of equivalised income.

Source: *Government Benefits, Taxes and Household Income, Australia, 2003–04* (ABS cat. no. 6537.0)

Intra-household transfers

While income is usually received by individuals, it is normally shared between partners in a couple relationship and with dependent children. To a lesser degree, there may be sharing with other members of the household. Even when there is no transfer of income between members of a household, nor provision of free or cheap accommodation, members are still likely to benefit from the economies of scale that arise from the sharing of dwellings. The income measures used in the analysis of income distribution and material wellbeing therefore generally relate to household income.

Inter-household transfers

Private transfers are one form of income redistribution between households, and for some households, communities and even economies they can be very significant. In Australia, in aggregate, private transfers between households are relatively small. As with most research into income distribution, this article does not separately analyse private incomes before inter-household transfers are made.

they pay, such as the goods and services tax and the excise taxes on products such as alcohol and tobacco. Deducting these taxes from the sum of disposable income and social transfers in kind provides a more comprehensive income measure, referred to as final income.

...magnitude of income redistribution

In 2003–04, the net effect of the system of government benefits and taxes was to redistribute substantial economic resources from people with relatively high private incomes to people with lower private incomes. In 2003–04, people in the bottom 20% of equivalised private household incomes in Australia received less than 1% of such income. Their share of final income rose to 13% after being adjusted for government benefits and taxes. Conversely, the share of income for the top 20% of households was 46% of private incomes, falling to 32% of final incomes.

The differences in income distribution initially observed in private incomes narrow for disposable household income (when Australian government pensions, allowances and family tax benefit are added, and income tax and the Medicare levy are deducted). They narrow further when social transfers in kind are added and indirect taxes on production are removed. As a result of income redistribution through the tax and transfer system, the average final income of households in the lowest quintile of equivalised private income was about 40% of

average final income of households in the highest quintile. In contrast, the average private income of households in the lowest quintile of equivalised private income was 2% of that of households in the highest quintile.

...low and middle incomes

The extent to which the system of government taxation and benefit allocation raises the living standards of people in low income households is of fundamental interest to policy makers and the wider community.

Some households in the bottom income decile (i.e. the 10% of households with the lowest income) have disproportionately high levels of consumption expenditure and/or wealth relative to their incomes. Incomes alone therefore do not accurately reflect the economic wellbeing of the average household in the bottom decile. Thus, in summary analysis, households in the second and third lowest income deciles combined are often used in preference to households in the bottom quintile (i.e. bottom and second deciles) to better represent those with relatively low consumption possibilities. The income share of these 'low' private income households was 4% of all private incomes, rising to 14% of final income after the effects of government benefits and taxes were taken into account.

The system of government benefits and taxes gave middle income households (those in the fifth and sixth equivalised private income deciles) a marginal increase in their share of income, from 18% of all private income to a 19% share of all final income.

Life course stages

People's private incomes may change over the life course as their circumstances change. The extent to which they, on balance, contribute to or benefit from the system of government benefits and taxes is influenced by a range of factors which may also change throughout their lives. For example, the presence and number of people in a household, their ages, whether they are employed, and whether or not they have children benefiting from subsidised services in the education and health systems, will affect the extent to which a household is a net beneficiary of the government system of household-based benefits and tax.

...young singles and couples

Young people (aged less than 35 years) living alone or as a couple without children tend to contribute more on average in taxes than they

Modelling benefits and taxes

Information reported in the ABS 2003–04 Household Expenditure Survey (HES) formed the basis for the modelling of benefits and taxes which underpins some of the data presented in this article. The HES established the composition of households, the characteristics of their members, the level and sources of their gross income, and their expenditure patterns. Income tax was then imputed using tax legislation in force in 2003–04. Government non-cash benefits were also imputed, according to the characteristics of household members and their expenditure patterns, using estimates of expenditure at all levels of government. Indirect taxes were imputed from survey expenditure data using Input-Output tables from the Australian System of National Accounts.

Only benefits and taxes conceptually and practically relatable to individual households were allocated to households. For example, government revenue from capital gains tax and company tax has not been allocated. Nor has government spending on defence, public order and safety, transport and communications. Overall, 59% of the taxation revenue of all levels of government (net of subsidies) and 51% of total government expenditure has been allocated to individual households for the purpose of calculating their final income. The value of government services received includes related research and program administration costs.

There are several ways to analyse the effects of taxation and government expenditure on the distribution of income among private households in Australia. The extent of change to data sources and methods for the analysis of 2003–04 data means that it is not comparable with the analyses undertaken for 1984, 1988–89, 1993–94 and 1998–99 and published by the ABS.

For a more detailed explanation of these technical matters see the explanatory notes and Appendices 4–5 of *Government Benefits, Taxes and Household Income, Australia, 2003–04* (ABS cat. no. 6537.0).

receive in benefits. In 2003–04, young singles contributed on average \$258 a week in taxes and received \$87 a week in benefits, while young couple households paid \$534 a week and received \$109 a week in benefits. The net contributor state for these two life course groups largely reflects their comparatively high employment levels and their relative youth, which means they tend to be in good health and therefore use fewer health services than other groups. The absence of children in these households also means that they receive relatively few education benefits and no health benefits associated with the early years of life.

...couples with young children

The net effect of government benefits and taxes changes with the arrival of children. Before any of their children reach school age, couples whose eldest child is under 5 years of

age still paid more in taxes (\$450 a week) than they received in benefits (\$282 a week). The average net contribution to the tax and transfer system (\$167 a week) of these households was much less than that of young childless couples (\$425 a week), partly because households with children have fewer employed people and pay less income tax, but also because they receive a range of benefits targeted at families with children, such as the family tax benefit, parenting payment and subsidised child care. They also receive more subsidised health services such as hospital care, 'well baby' clinics, community dental health services, immunisation, and screening for childhood diseases.

...couples with older children

Couples whose eldest child is aged between 5 and 14 years gained slightly overall from the system of government benefits and taxes, largely reflecting both the value of schooling (\$219 a week) that they received and the higher family tax benefit (\$81 a week on average).

...couples aged 55–64 years

Couple only households with reference person aged 55–64 years were net contributors through the tax and transfer system, paying an average of \$64 a week more in taxes than they received in benefits. As the average number of employed people in these households was relatively small (0.9), their private income (\$861 a week on average) was much lower than that of younger couple only households (\$1,577 a week) who had more employed people per household (1.8 on average). The 55–64 year old couple households, however, received much more in government pensions and allowances (\$113 a week) than couples aged under 35 years (\$12), and much more in health benefits (\$115 a week compared with \$60 for younger couples).

...older people

On average, people aged 65 years and over without children benefit substantially from the system of government benefits and taxes. During 2003–04, older couple only households (reference person aged 65 years and over) were allocated \$586 a week on average in benefits and paid \$148 in taxes. People aged 65 years and over living alone received a similar boost (\$361 in benefits less \$84 in taxes).

Because fewer members of these older households were employed than in younger households, they had lower private incomes on average and therefore paid less income tax. In contrast, during 2003–04, government pensions and allowances (largely the Age

Effect of taxes and benefits on the household income of selected life course groups — 2003–04(a)

Selected life course groups	Benefits				Taxes	Final	Net effect of taxes and benefits
	Private	Income payments	Social transfers	Total			
	\$	\$	\$	\$	\$	\$	\$
Lone person aged under 35 years	710	32	55	87	258	539	-171
Couple only, reference person aged under 35 years	1 577	12	96	109	534	1 152	-425
Couple with dependent children only, eldest child aged 0–4 years	1 262	82	200	282	450	1 094	-167
Couple with dependent children only, eldest child aged 5–14 years	1 356	118	405	523	495	1 384	**28
Couple with dependent children only, eldest child aged 15–24 years	1 643	101	481	583	578	1 648	**5
Couple with dependent and non-dependent children only	1 785	134	468	602	612	1 775	**10
Couple with non-dependent children only	1 582	157	213	370	542	1 410	-172
Couple only, reference person aged 55 to 64 years	861	113	149	261	325	797	*64
Couple only, reference person aged 65 and over	335	285	302	586	148	774	438
Lone person aged 65 and over	195	185	175	361	84	471	277
All households	992	136	238	375	360	1 007	*15

(a) Average weekly value.

Source: *Government Benefits, Taxes and Household Income, Australia, 2003–04* (ABS cat. no. 6537.0).

pension and to a much lesser extent the Veterans Affairs pension) comprised the principal source of gross income for 68% of older couple only households and 75% of older people living alone.

The final incomes of these older households were also considerably boosted by the allocated value of publicly-funded health benefits (\$240 a week for couples and \$138 a week for singles). Compared with younger households, older couple only households and older people living alone received much more acute care in institutions such as hospitals and hospices. During 2003–04, government spending on pharmaceuticals, medical aids and appliances was also greater for these older groups.

Patterns of income redistribution from young adults to people of pensionable age underpin concerns about the fiscal pressures that could potentially accompany the projected continual ageing of the Australian population. Such concerns have prompted a range of policies over recent decades encouraging people to have more children, to delay retirement, and to accumulate sufficient superannuation assets to be able to self-fund their retirement years.

Other population groups of special interest

Some population groups, such as couple families with no employed parent and lone parents, are of interest because of the risks of disadvantage that their circumstances raise.

Allocating the effects of taxes and transfers aids understanding of the overall impact of the tax and transfer system on these groups.

...lone parents

One-parent family households with dependent children received substantial income support, predominantly in the form of the family tax benefit and parenting payment. They also benefited from government spending on pre-school, primary and secondary education, and student transportation.

In 2003–04, the average value of social assistance benefits in cash received by these lone parent households was \$293 a week compared with \$136 a week for all households. Social transfers in kind were also relatively high because of high use of education services (average value of \$383 a week compared with \$238 a week for all households).

Taxes on income and taxes on production are low for sole parents, since their incomes and expenditures are relatively low. Taxes on income for this group averaged \$95 a week compared with \$213 a week for all households. Taxes on production averaged \$108 a week compared with \$147 a week for all households.

The average weekly equivalised private income of lone parent households was 46% of the average weekly equivalised private income of all households. Due to the higher net benefits they received, however, the average equivalised final income of this group was a much higher proportion of average equivalised final income of all households (93%).

...couple families with children and no employed parent

Couple family households with dependent children and with no employed parent received relatively high amounts of government cash benefits (\$439 a week), most notably family tax benefit, parenting payment, student and unemployment allowances and disability support pension.

There was a marked difference between the amount of tax paid by couple family households with dependent children with one or two or more persons employed (\$436 and \$581 a week respectively) and such families with no one employed (\$118 a week). The total tax paid by families with no employed person was relatively low because of both the lower level of income tax paid, and the lower indirect taxes due to the constraints on their consumption of market supplied goods and services. They also received more government non-cash benefits than other couple family households with dependent children.

...public housing tenants

Many public housing tenants belong to population groups discussed above in terms of the effects of the system of benefits and taxes. These include low income households, lone parents and households where no parent is employed. In 2003–04, households renting from a state or territory housing

authority received on average a relatively low private income of \$152 a week. However, they received a net transfer of \$551 a week after the allocation of government benefits and taxes, largely reflecting the high cash benefits they received on average (\$288 a week), high housing benefits (\$71 a week) and sizeable school education and health transfers in kind.

Changes since 2003–04

There have been numerous changes to the system of government benefits and taxes since 30 June 2004 which would alter the extent to which income is currently being redistributed. For example, individual income tax rates have changed each year. In 2003–04, the highest marginal tax rate (47%) applied to annual income above \$62,500, whereas by 2007–08, the highest rate had reduced to 45% and was not payable until annual income had reached \$150,000. Eligibility to receive the baby bonus commenced on 1 July 2004, and there have also been changes to the Family Tax Benefit, child care funding and the taxation of superannuation payments.

The next ABS Household Expenditure Survey (currently scheduled for 2009–10) will provide the basis for the next opportunity to measure final income redistribution in Australia.

Effect of taxes and benefits on the household income of selected population groups — 2003–04(a)

Selected household types	Benefits				Taxes	Net effect of taxes and benefits	
	Private	Income payments	Social transfers	Total		Final	
	\$	\$	\$	\$	\$	\$	\$
One parent family households with dependent children							
with one dependent child	559	243	263	506	221	844	285
with two dependent children	448	305	440	744	194	998	550
with three or more dependent children	326	432	657	1 090	159	1 257	931
Couple family households with dependent children							
no person employed	117	439	512	951	118	950	833
one person employed	1 091	157	370	527	436	1 182	91
two or more persons employed	1 707	68	391	459	581	1 584	-122
Gross income principally government pensions and allowances							
50% to less than 90%	154	351	302	653	105	701	547
90% and over	12	334	273	607	69	550	537
Households renting from a state/territory housing authority	152	288	343	631	80	703	551
All households	992	136	238	375	360	1 007	*15

(a) Average weekly value.

Source: Government Benefits, Taxes and Household Income, Australia, 2003–04 (ABS cat. no. 6537.0).

FOR MORE INFORMATION . . .

INTERNET **www.abs.gov.au** the ABS website is the best place for data from our publications and information about the ABS.

INFORMATION AND REFERRAL SERVICE

Our consultants can help you access the full range of information published by the ABS that is available free of charge from our website. Information tailored to your needs can also be requested as a 'user pays' service. Specialists are on hand to help you with analytical or methodological advice.

PHONE 1300 135 070

EMAIL client.services@abs.gov.au

FAX 1300 135 211

POST Client Services, ABS, GPO Box 796, Sydney NSW 2001

FREE ACCESS TO STATISTICS

All statistics on the ABS website can be downloaded free of charge.

WEB ADDRESS www.abs.gov.au