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Inquiry into Balancing Work and Family

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Australia now ranks as having one of the least "friendly" work and family environments among comparable OECD countries. Among the policy areas that have contributed to this outcome are the following:

The tax and family benefit systems: Over the last two decades Australia has shifted towards a less progressive income tax (including the Medicare Levy), towards a family tax benefit system highly targeted on joint income and on the income of the second earner, and towards regressive indirect taxation. These reforms have had two effects. First, they have shifted the overall tax burden away from families in which there is at least one high income earner to those on low to average earnings. Second, they have increased the effective tax rates on the second earner in families at the lower end and across the middle of the wage distribution, to create a "tax-wedge" for working mothers that is the highest among comparable OECD member countries.

Costly and limited access to child care: Successive Australian Governments have failed to address the problems of market failure that are pervasive in the private provision of child care. Instead, these problems have been exacerbated by support for the expansion of privatised, for profit, child care. The limitations of this policy direction become clear when we compare the cost (government and private) of the first year of primary school with the last year of fully privatized child care. If the first year of primary school were to be treated in the same way as child care, few parents would be able to afford the cost, the female participation rate would fall, and so would fertility.

Misdirected reforms that increase labour market inefficiencies: Examples include labour market reforms that expand the proportion of "working poor" families and, in turn, necessitate the expansion of the family benefit system. Reforms of this kind represent the use of the family benefit system as a policy instrument for subsidising inefficient industries.

The above problems are analysed in detail in the attached paper:
"The High Taxation of Working Families", *Australian Review of Public Affairs*, 5, 1-24.

Key policy recommendations are:

- Development of a high quality, efficient public sector child care system. Empirical research identifies this as the most efficient and effective policy measure for reducing losses to the economy caused by the distortionary effects of an imperfect capital market, together with wage uncertainty.

- A return to a progressive individual income tax system. This implies a reversal of the trend of recent decades towards joint taxation and an inverted U-shaped effective tax rate scale. Empirical studies show that reforms supporting individual taxation at progressive rates lead to an increase in female labour supply and, in turn, in the tax base required for funding child care and the age pension.

- Elimination of Family Tax Benefit Part B. This would help to reduce the "tax wedge" and therefore to achieve a more "neutral" treatment of single and two-earner families.

- Introduction of measures to broaden the income tax base, including in particular the elimination of opportunities for tax minimisation, through the use of negative gearing, trusts, etc.

Consistent with the findings of theoretical and empirical studies for OECD countries, reforms of these kinds can be expected to increase fertility, female labour supply and GDP, and to improve the overall efficiency and fairness of the Australian economy.

Additional References:

Apps, PF and R Rees (2003) "Time Allocation and Saving in an Imperfect Capital Market", NBER Summer Institute: *Aggregate Implications of Microeconomic Consumption Behavior*, Boston, July 21-25. (Downloadable on www.iza.org)

Apps, PF (2002), "Why an Earned Income Tax Credit Program is a Mistake for Australia", *Australian Journal of Labour Economics* 5, 549-568.

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