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Economist urges scrapping of annual income tax returns

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ABOLISHING income tax returns could save the economy \$3 billion in lost productivity and give most people the equivalent of an extra public holiday a year.

Australian National University economist Andrew Leigh has called for PAYE taxpayers to be freed from filing tax returns, arguing that Australia's tax rules are behind those of international competitors such as Britain and New Zealand.

"Reduced work incentives are not the only deadweight cost of taxation," Dr Leigh writes in the most recent instalment in Labor's Progressive Essays series.

"Another deadweight cost of taxation is the administrative burden. Getting your receipts in order and ploughing through the Tax Pack takes time that could be spent doing more productive activities."

Two-thirds of Australian adults filed a tax return in 2002-03. By contrast, just one in five British adults now file tax returns, Dr Leigh says.

He estimates the cost of tax compliance today is \$300 per person after a 1995 survey found that Australian taxpayers spend 8.5 hours a year on their tax affairs.

"We can make life easier for Australian taxpayers," he says, proposing that taxpayers who do not want to claim deductions should be free not to file a return.

Also in his essay, Dr Leigh says Australia should cut taxes for the poor and provide low-income families with an "earned-income tax credit".

And he argues that cutting the top marginal tax rate of 47 per cent is "misguided". "Instead of cutting tax rates for the rich, we should focus on making the tax system simpler for ordinary Australians," he said.

Tax barrister and federal Nationals president David Russell QC yesterday agreed that compulsory tax returns should be scrapped. But he said the move - which would involve giving up deductions and "copping the withholding" - would be more attractive alongside a cut in the top marginal tax rate.

Grant Samuel tax expert Louise McBride called for an overhaul of the income tax act, with annual compulsory income tax returns scrapped.

"Why we still insist on making individuals lodge tax returns is beyond me - the UK and Asia don't do it, they use a simple system of withholding," she said.

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DEBATE ON TAX CUTS BARKING UP WRONG TREE

Scrapping annual tax returns for many Australians and providing relief for low-income earners should be the focus of the tax debate rather than more tax cuts for the rich, according to a paper released today by ANU economist Dr Andrew Leigh.

"Three Ideas On Tax Reform" points out although that the tax cuts announced in the May 2005 budget were particularly generous to the rich, much recent tax debate has been cutting tax for the rich even further.

"Those who advocate lowering top tax rates are out of step with the views of most Australians." Dr Leigh said. "Polled on whether they would prefer lower taxes or more social spending, more people say they prefer social spending than tax cuts."

"One reason why sections of the commentariat may be out of step with popular opinion is a misunderstanding of what the typical Australian earns. The taxation rates that apply to most politicians, journalists, business executives and think-tank staffers are not those that apply to the average voter.

"Contrary to figures that are often reported, the income of the average Australian is \$26,000 per year, which is near the bottom of the 30 percent tax bracket."

Instead, Dr Leigh argues that we should simplify our tax filing system by allowing most people the option of not filing a return.

"The Australian tax system presently requires two-thirds of adults to file a return. On average, tax filing takes 8½ hours. This means that the cost to taxpayers of complying with the personal income taxation system is \$3 billion per year.

"But only three in ten New Zealand taxpayers now file tax returns. We should follow the example of the Kiwis, and remove the requirement for Australians with straightforward income to file a tax return. Doing so would be the equivalent of an extra public holiday a year for many Australians."

Dr Leigh also argues that we should reduce effective marginal tax rates at the bottom, where the rates are highest, and the problem of joblessness most acute.

"Rather than focusing on tax rates faced by the rich, a more productive national tax debate would target attention where it is needed most – to reducing the marginal tax rates faced by the poor.

"While the highest marginal tax rate faced by the rich is 47 percent, those seeking to move from welfare to work can often face marginal tax rates of 60 percent or more. Countries such as Belgium, Finland, Germany, Ireland, the Netherlands, the UK and the US offer earned income tax credits to make work more attractive. In Australia, earned income tax credits should be on the policy menu of all forward-thinking politicians."

Dr Leigh is available for comment on 0431 706 600.

For a copy of the report: <http://econrsss.anu.edu.au/~aleigh/>.