Bracket creep and its fiscal impact – abstract

Cameron Chisholm[1], Jordan King[1], Izaac Phillips[1], Lynette Yap[1]

1 Parliamentary Budget Office

Bracket creep is generally associated with the experience of individuals paying higher tax rates rather than the implications for how governments manage their finances. In Australia, bracket creep has played an important role in repairing the budget after a major downturn, as well as increasing Commonwealth tax revenue over time. For instance, the average tax rate steadily rose from around 12% in 1960 to more than 25% before 1990, and increased from less than 40% of total government revenue to 56%. The structure of the personal tax system has also changed significantly over time, as we have moved from 28 tax thresholds to only 4, soon to be 3. This paper explores how bracket creep affects both different individuals and the government budget, applying both a historical and forward-looking perspective.

With Australia's net debt expected to peak at 33% of GDP ($865 billion) by the end of 2025-26, personal income tax receipts, driven by bracket creep, are likely to be a major driver in reducing the debt-to-GDP ratio over the medium and long term, particularly as some other sources of revenue are in structural decline. Even with significant personal income tax cuts between 2018-19 and 2024-25, the average tax rate on personal income is expected to be above 25% by 2030-31, a level not seen since just before the large tax cuts associated with the introduction of the GST in 2000. Governments will face a trade-off between returning bracket creep and allowing bracket creep to reduce debt faster.

Key words

Bracket creep, fiscal policy, personal income tax,

The Parliamentary Budget Office's budget explainer, *Bracket creep and its fiscal impact*, is available here.