Parliament of Australia
Parliamentary Budget Office

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Senator Christine Milne
Leader of the Australian Greens
Parliament House
CANBERRA ACT 2600

Dear Senator Milne

Please find attached a response to your costing request, *A better Paid Parental Leave scheme* (letter of 14 August 2013).

The response to this request will be released on the PBO website (www.aph.gov.au/pbo).

If you have any queries about this costing, please do not hesitate to contact Colin Brown on (02) 6277 9530.

Yours sincerely

Phil Bowen
20 August 2013

COSTING – ELECTION CARETAKER PERIOD

Name of proposal to be costed:	**A better Paid Parental Leave scheme**
Summary of proposal:	The proposal would replace the current Paid Parental Leave (PPL) scheme with the following elements: Part 1: Provide 26 weeks PPL, to be paid at the greater of the National Minimum Wage (NMW) or the primary carer's replacement wage (capped at a maximum salary of $100,000 per annum). The scheme would also include superannuation contributions at the superannuation guarantee rate. For partnered parents, an additional two weeks would be available as paid partner leave at the greater of the NMW or 100 per cent of the partner's replacement wage (capped at a maximum salary of $100,000 per annum). Payments would be made through the Family Assistance Office. Part 2: Impose a 1.5 per cent levy on that part of company taxable income over $5 million. This levy would generate franking credits. The proposal would have effect from 1 July 2014.
Person/party requesting costing:	Senator Christine Milne, Australian Greens
Date costing request received:	14 August 2013
Date costing completed:	20 August 2013
Date of public release of policy:	23 July 2013
Agencies from which information was obtained:	• Department of Families, Housing, Community Services and Indigenous Affairs (FaHCSIA) • Department of Human Services (DHS) • The Treasury

Costing overview

The proposal is estimated to decrease the underlying cash balance by $2.215 billion over the 2013-14 Budget forward estimates period. Over the same period, this proposal is expected to decrease the fiscal balance by $2.185 billion.

Table 1: Financial implications (outturn prices)[(a)]

Impact on	2013-14	2014-15	2015-16	2016-17
Underlying cash balance ($m)	190	-1,595	-535	-275
Fiscal balance ($m)	190	-1,575	-525	-275

(a) A positive number for the fiscal balance indicates an increase in revenue or a decrease in expenses in accrual terms. A positive number for the underlying cash balance indicates an increase in receipts or a decrease in payments in cash terms. A negative number for the fiscal balance indicates a decrease in revenue or an increase in expenses in accrual terms. A negative number for the underlying cash balance indicates a decrease in receipts or an increase in payments in cash terms.

The financial impact of the proposal in the forward estimates period is not indicative of its longer term ongoing impact as it is significantly affected by the timing of collections of the levy on company taxable incomes in the initial period of operation.

This proposal will have an ongoing impact that extends beyond the forward estimates period.

Part 1: Paid Parental Leave.

The proposed extension to the PPL program is expected to decrease the underlying cash balance by $6.915 billion and decrease the fiscal balance by $6.885 billion over the 2013-14 Budget forward estimates period.

The underlying cash balance impact of this part reflects an increase in cash expenditure of $9.415 billion and an increase in cash receipts of $2.5 billion over the 2013-14 forward estimates period. The fiscal balance impact reflects an increase in expenses of $9.385 billion and an increase in revenue of $2.5 billion over this period. A further disaggregation of Part 1 of the costing can be found at Attachment A.

These impacts will be ongoing beyond the 2013-14 forward estimates period.

The proposed PPL scheme would result in increased expenses for the PPL program, primarily reflecting the higher level of payments under the scheme, but also because more families will choose to receive PPL in preference to the alternative Family Tax Benefit (FTB) supplement. This increased expense will be partially offset by a reduction in payments of FTB Parts A and B.

As PPL payments are taxable, the increased expense of the scheme will also be partially offset by increased personal income tax revenue. Contributions tax will also be collected on the superannuation payments made under the scheme. The inclusion of superannuation in the PPL scheme will also result in increased expenses due to additional Low Income Superannuation Contribution (LISC) payments made in respect to these contributions.

Part 1 of the costing includes departmental costs of $35 million over the 2013-14 forward estimates period. This estimate reflects a number of factors: an information campaign, IT changes to make systems compatible with paying PPL at a rate proportional to the recipients' replacement wage, additional upfront costs to clarify a person's replacement wage when they apply for PPL, additional transactional costs associated with paying PPL for 26 weeks rather than 18 and also making payments to superannuation funds. These estimates have been based on consultation with the Department of Human Services and expenditure on advertising for recent changes to family payments, such as the Schoolkids Bonus and the Clean Energy Future Household Assistance Package.

The underlying cash balance impact of this proposal differs from the fiscal balance impact due to the FTB supplement and lump sum FTB payments, along with LISC payments being made in the year following the liability being accrued.

The cost of the proposal is lower in the first year as some recipients of the payment who have their child in 2014-15 will not receive their entire 26 weeks' worth of payments in this financial year. The estimated saving from the current PPL scheme in 2014-15 is less than the current expense estimate for the program in that year. This reflects the fact that some families who have a child in 2013-14 would still complete their PPL period under the old scheme in 2014-15.

The costing estimate for Part 1 is considered to be of low to medium reliability, as the costing is based on heavily aggregated data and reliant on several assumptions. The estimates in this costing will be sensitive to changes in the National Minimum Wage, fertility rates, the participation of women in the labour market, and the wages primary carers (and their partners) earn.

The estimates for Part 1 of the costing differ only slightly from those provided by the applicant in their request. This difference reflects updated economic parameters, that the base data used in the costing has been updated from 2011-12 to 2012-13 and that the PBO has consulted with DHS on the likely departmental expenses of a similar scheme.

<u>Part 2: 1.5 per cent levy on that part of company taxable income over $5 million – levy generates franking credits</u>

Imposing a 1.5 per cent levy on that part of a company's taxable income over $5 million with the levy generating franking credits would increase both the underlying cash and fiscal balances by $4.7 billion over the 2013-14 Budget forward estimates period. This impact is entirely due to an increase in revenue. Detailed financial implications for Part 2 are included at <u>Attachment B.</u>

These impacts will be ongoing beyond the 2013-14 forward estimates period.

Departmental expenses are expected to be minimal for Part 2 of this proposal and have not been included in this costing.

The costing of Part 2 is considered to be of medium reliability as modelling is based on historical tax data and several assumptions. Possible behavioural responses to this part of the proposal are uncertain.

The costing of Part 2 varies from that provided in the applicant's request due to revised company tax collections reported in the 2013 Pre-Election Economic and Fiscal Outlook.

Key assumptions

The PBO has made the following assumptions regarding this costing.

<u>Part 1: PPL</u>

General assumptions

- The grouped data approach used to model the policy cannot capture the full level of diversity in the population. The model works under the assumption that the outcome for an average person in each group represents the average outcome for the group.
- The transaction costs for making PPL payments through employers are assumed to be equivalent to those incurred by paying PPL through the Family Assistance Office.

Income distribution of PPL recipients

- The income distribution of new mothers has been based on aggregated data on the distribution of adjusted taxable incomes of PPL recipients in the first eleven months of 2012-13.
- These incomes have been grown in line with average weekly earnings.
- An assumption has been made about the proportion of eligible families that have partnered parents as well the average incomes of the partners. These assumptions have been made based on analysis of unit record data from the 2009-10 Survey of Income and Housing.
- Assumptions have also been made regarding the amount of time primary carers spend working outside the PPL period during the year of birth.

Take up of Secondary Carer Payment

- Not all secondary carers currently take up Dad and Partner Pay. Under the proposed scheme, all secondary carers are assumed to take up the payment, as there would be no loss in income from choosing to do so. When paid paternity leave is not paid, the secondary carer is expected to continue to work. Thus, the income from the more generous paid paternity leave payment is not expected to result in a significant increase in personal income tax collections.

Child care assistance

- The effect of the proposal on child care assistance payments is expected to be minimal and has not been included in the costing.

Transitional arrangements

- It has also been assumed that those who have a child in 2013-14, but do not complete their PPL period by the end of the financial year, will continue to receive their payments under the current scheme until their 18 week period expires.

<u>Part 2: Company Tax Levy</u>

General assumptions

- Superannuation funds and the superannuation business of life insurance companies would continue to be taxed at the 15 per cent rate.
- Growth rates are based on company gross operating surplus (GOS), adjusted to take into account the effects of many companies having substituted accounting periods.
- Estimates have been rounded to the nearest $100 million.

Behavioural 'bring forward' assumption

- With a start date of 1 July 2014 and announcement of the proposal in 2013, the PBO considers that there is sufficient time for companies to take steps to change the timing of their deductions and income in the financial year prior to the start date in order to benefit from the introduction of the levy. Having a long lead time increases the likelihood of a behavioural response that would increase the cost of transition to the proposal and decrease revenue.
  - The PBO has assumed that around 0.375 per cent of company taxable income over $5 million would be brought forward around the commencement of this proposal in order to avoid an announced levy on company income in excess of $5 million.

Impact of the imputation system

- As specified by the applicant, the 1.5 per cent levy on company taxable income in excess of $5 million would be creditable for dividend imputation purposes and flows through into the rate at which dividends are franked. This means a proportion of the increased tax paid at the company level will flow through to resident shareholders as imputation credits which they can then use to reduce their own tax liabilities.
- The PBO has assumed that companies with taxable income less than $5 million would also be required to frank their dividends at the same rate as companies with taxable income in excess of $5 million.
- With regard to company dividends and imputation, the PBO has assumed that the impact of the levy would be absorbed by companies and would not impact on the level of cash dividends paid.

Timing assumptions

The PBO has assumed that the levy is collected via the company pay as you go (PAYG) instalment system. This means the levy would have the same timing as general company tax collections. This costing assumes that the Australian Taxation Office (ATO) will not vary company instalment calculations in response to the company levy. Instalment rates are calculated by the ATO based on the amount of tax paid by a company in the previous year and are not based on the statutory company rate.

The assumption in relation to instalments mainly impacts on the profile of company tax collections as instalments adjust to the new company rate and does not affect the cost of the proposal once instalments assimilate the company levy. If the ATO were to vary instalments to take account of the impact of the company levy, the cost of the proposal would be larger in the first year following the date of effect than in this costing, with this difference unwound over the next three years.

Data sources

The costing estimate for Part 1 relied on aggregated data on the incomes of PPL recipients in 2012-13 along with forward estimates of expenses and recipient numbers for both Parental Leave Pay and Dad and Partner Pay, which were provided by FaHCSIA.

The Treasury was also consulted on the effect the PPL scheme including the impact superannuation contributions would have on contributions tax and the LISC.

The Australian Bureau of Statistics' Survey of Income and Housing confidentialised unit record files and their publication *Survey of Pregnancy and Employment Transitions* were also analysed to help inform assumptions used in the costing.

Data sources for Part 2 include ATO tax return data for companies, individuals and the superannuation business of life insurance companies up to the 2010-11 financial year. The data includes entities that are taxed as companies.

ATTACHMENT A

This attachment provides a disaggregation of the costing of Part 1 of the proposal.

Table A1 provides estimates on an underlying cash balance basis. A positive number for expenditure reflects an increase in cash paid by the Commonwealth, while a positive number for receipts reflects an increase in cash collected by the Commonwealth. The effect on the underlying cash balance is the change in receipts less the change in expenditure.

Table A1. Disaggregation of PPL Costing – Cash Basis

($m)	2013-14	2014-15	2015-16	2016-17	Total
Expenditure					
Paid Parental Leave	-	2,410	3,570	3,780	9,760
Consisting of:					
New Primary Carer Scheme (including SG)	-	*3,750*	*5,180*	*5,450*	*14,380*
Existing Parental Leave Pay	-	*-1,530*	*-1,860*	*-1,920*	*-5,310*
New Secondary Carer Scheme (including SG)	-	*250*	*330*	*340*	*920*
Existing Dad and Partner Pay	-	*-60*	*-80*	*-90*	*-230*
Family Assistance Payments	-	-90	-150	-160	-400
Low Income Super Contribution	-	-	10	10	20
Total Administered Expenditure	**-**	**2,320**	**3,430**	**3,630**	**9,380**
Departmental Expenditure	**10**	**15**	**5**	**5**	**35**
Receipts					
Personal Income Tax	-	590	830	880	2,300
Superannuation Contributions Tax	-	50	70	80	200
Total Receipts	**-**	**640**	**900**	**960**	**2,500**
Effect on Underlying Cash Balance	**-10**	**-1,695**	**-2,535**	**-2,675**	**-6,915**

Table A2 provides estimates on a fiscal balance basis. A positive number for expenses reflects an increased liability incurred by the Commonwealth, while a positive number for revenue reflects an increase in money owed to the Commonwealth. The effect on the fiscal balance is the change in revenue less the change in expenses.

Table A2. Disaggregation of PPL Costing – Fiscal Balance Basis

($m)	2013-14	2014-15	2015-16	2016-17	Total
Expenses					
Paid Parental Leave	-	2,410	3,570	3,780	9,760
Consisting of:					
New Primary Carer Scheme (including SG)	-	*3,750*	*5,180*	*5,450*	*14,380*
Existing Parental Leave Pay	-	*-1,530*	*-1,860*	*-1,920*	*-5,310*
New Secondary Carer Scheme (including SG)	-	*250*	*330*	*340*	*920*
Existing Dad and Partner Pay	-	*-60*	*-80*	*-90*	*-230*
Family Assistance Payments	-	-120	-160	-160	-440
Low Income Super Contribution	-	10	10	10	30
Total Administered Expenses	**-**	**2,300**	**3,420**	**3,630**	**9,350**
Departmental Expenses	**10**	**15**	**5**	**5**	**35**
Revenue					
Personal Income Tax	-	590	830	880	2,300
Superannuation Contributions Tax	-	50	70	80	200
Total Revenue	**-**	**640**	**900**	**960**	**2,500**
Effect on Fiscal Balance	**-10**	**-1,675**	**-2,525**	**-2,675**	**-6,885**

ATTACHMENT B

This attachment provides a disaggregation of the costing of Part 2 of the proposal.

Table B1: Revenue impact of the Company Levy – Cash and Fiscal Balance Basis[(a)]

($m)	2013-14	2014-15	2015-16	2016-17	Total
Revenue					
Company Tax	200	300	3,400	4,000	7,900
Personal Income Tax	-	-200	-1,400	-1,600	-3,200
Total Revenue	**200**	**100**	**2,000**	**2,400**	**4,700**
Effect on Cash and Fiscal Balance	**200**	**100**	**2,000**	**2,400**	**4,700**

(a) A positive number for the fiscal balance indicates an increase in revenue in accrual terms. A positive number for the underlying cash balance indicates an increase in receipts in cash terms. A negative number for the fiscal balance indicates a decrease in revenue in accrual terms. A negative number for the underlying cash balance indicates a decrease in receipts in cash terms.