

# Pre-Budget Report Briefing

Institute for Fiscal Studies

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# Tax credits and childcare

Mike Brewer

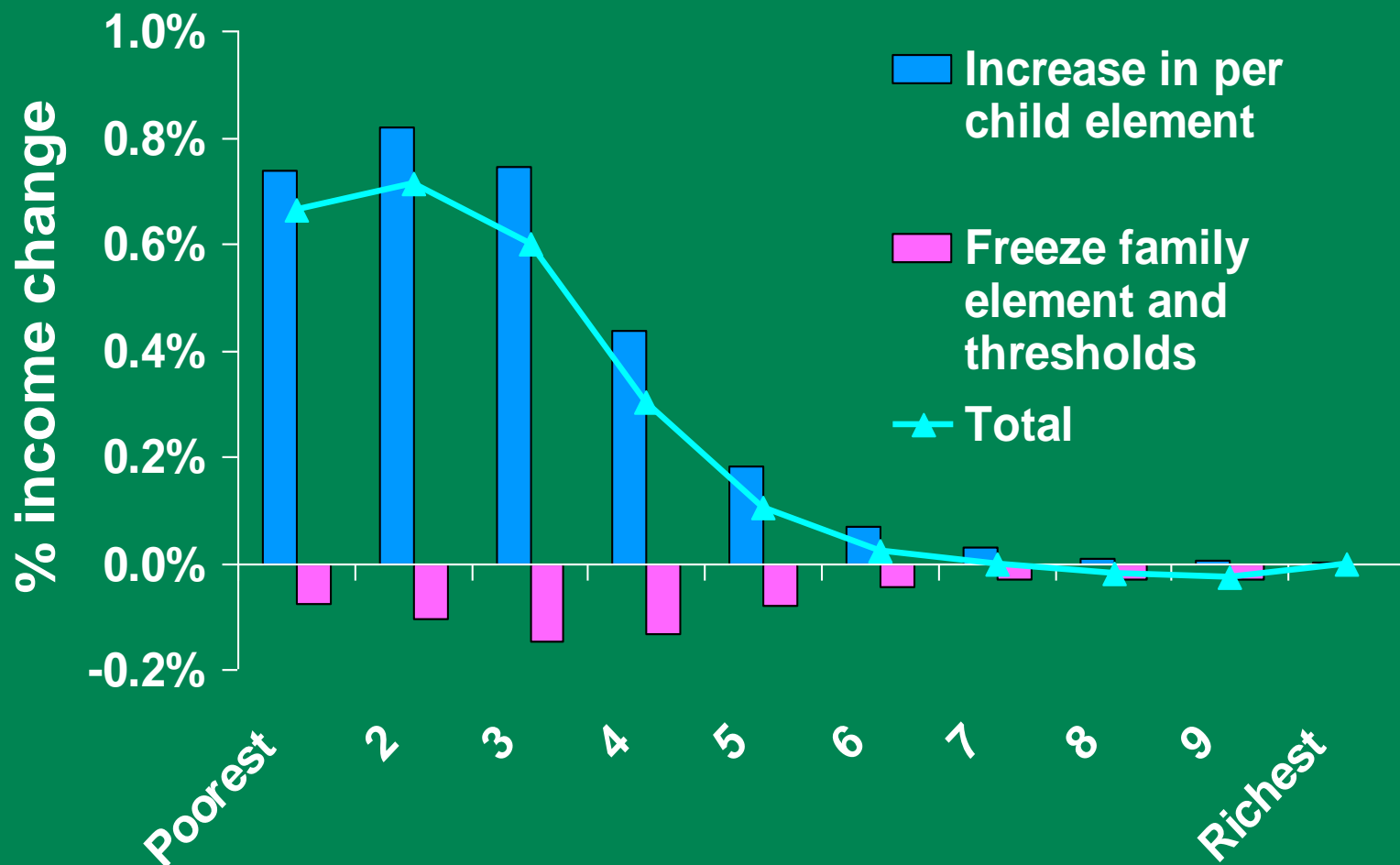
# Main changes

- Tax credits
  - Per child element up by £180 (cost £885m)
  - Working tax credit rates indexed
  - Some tax credit rates and thresholds frozen (save £240m)
- Tax exemption for employer-funded childcare (cost £25m)
- Other
  - Confirmed pension credit and pensioners tax allowance rise with earnings
  - Personal allowance and NI thresholds indexed
  - Higher-rate threshold for April 2004 not announced

## Tax credits: winners and losers compared to indexation

- Poorest 3.7m families gain £165 per child
- All families lose £15 because family element frozen
- All families on WTC or taper of CTC lose £52 because 1<sup>st</sup> threshold frozen
- Families between £50-58,000 lose £93 because 2<sup>nd</sup> threshold frozen

# Tax credit changes: distributional impact



## Tax credit: thoughts

- Might just hit poverty target
- “Spot the freeze in tax credits”
  - See Budget 2003, Appendix A2, “Explaining the Costings”
- Tax credit freeze assumed indefinitely
  - Reduces and redistributes tax credit spend
  - By 2008/9, will be saving £1.2bn/year, and have reduced child tax credit by 13% for better off

# Employers and childcare

- Tax exemption for employer-supported childcare
  - Currently affect around 60,000 employees, but tax break will increase the appeal
  - Cost implies low take-up
- Confusing for low-income parents
  - employer-funded, tax-free, childcare or self-funded, childcare-tax-credit-subsidised, childcare?
- Should employers have a role?
  - What happens if parents lose their jobs? or change employers?

# The Public Finances

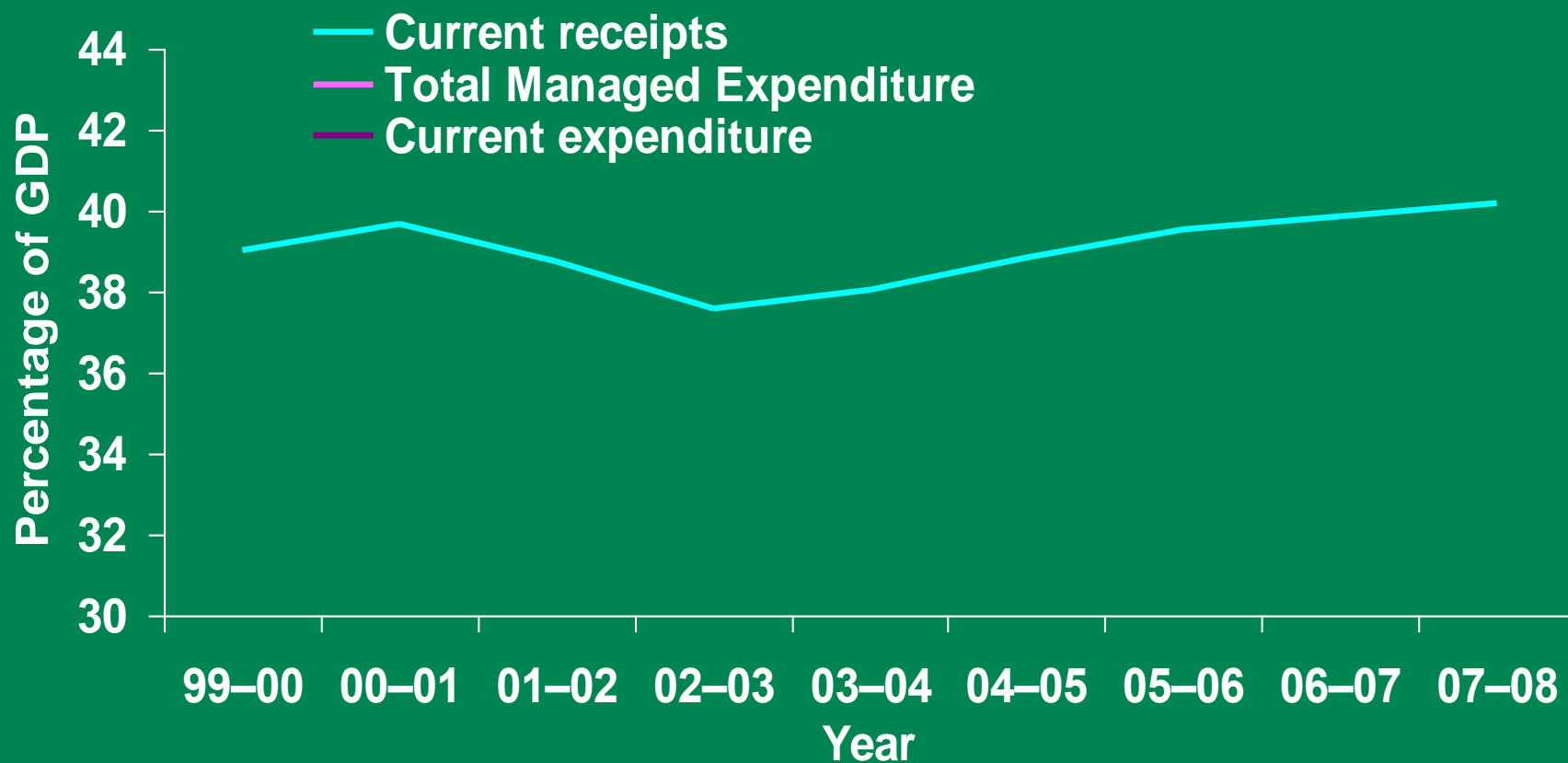
Christine Frayne



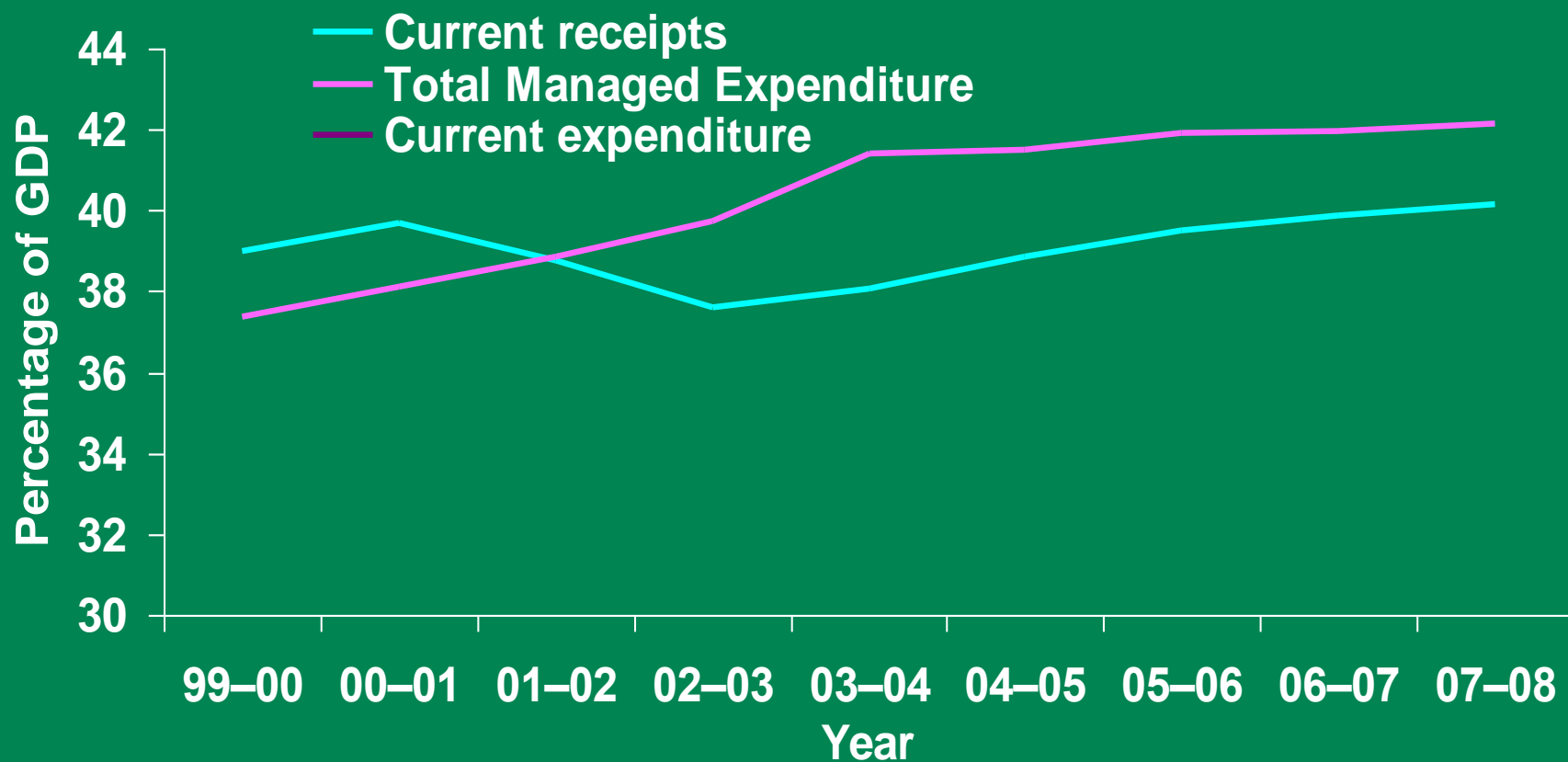
# The famous fiscal rules

- Golden rule: only borrow to invest
  - Receipts cover current spending
  - Surplus on current budget
- Judged over the economic cycle
- Sustainable investment rule: debt at a 'stable and prudent' level,  $\leq 40\%$  of national income

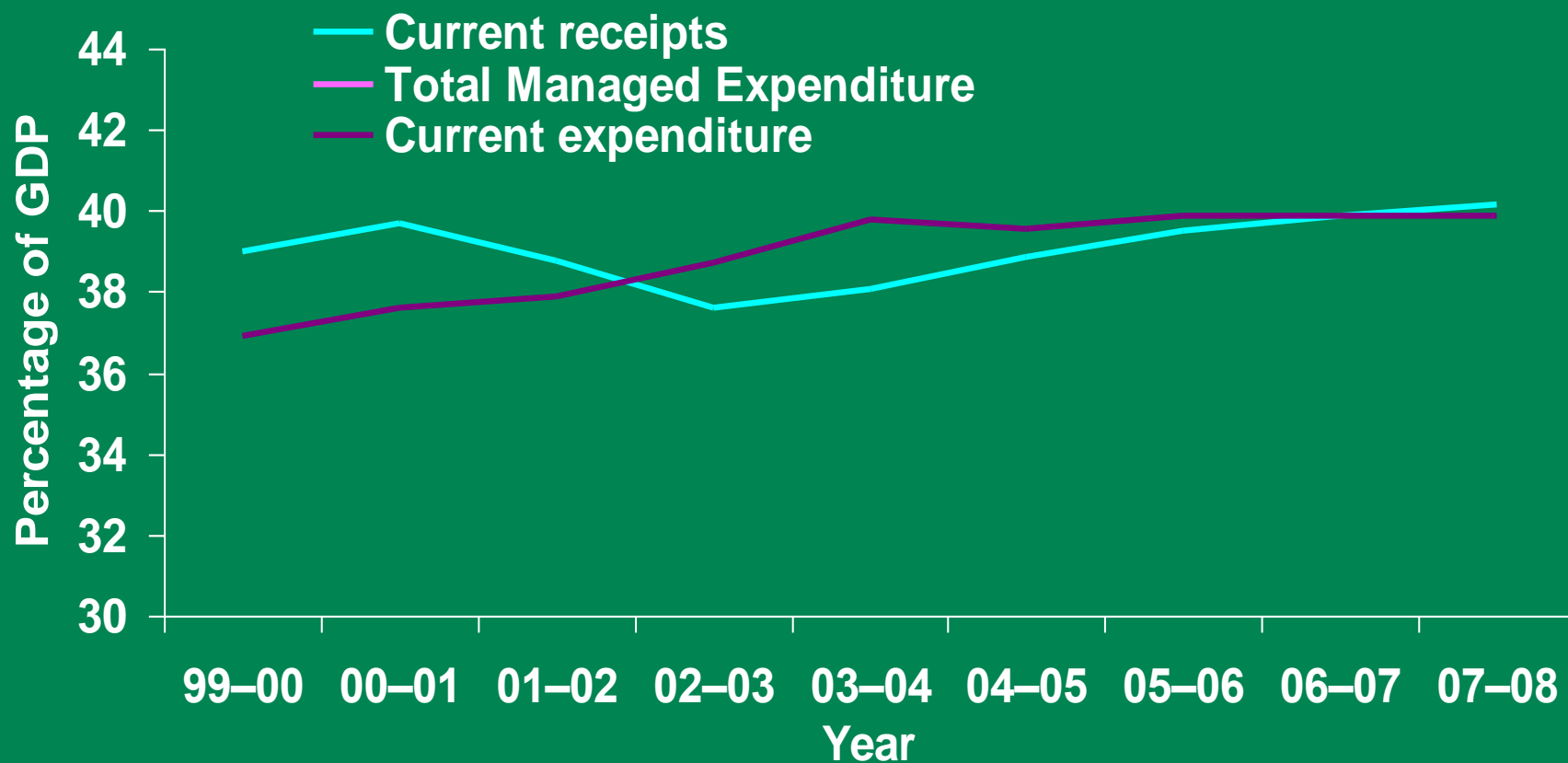
# Revenues and spending



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# Surplus on current budget – yesterday's changes

	2003-04	2004-05	2005-06	2006-07	2007-08
Budget 2003	-8.4	-1	2	6	9

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Pre-Budget Report 2003	-19.3	-8	-5	0	4
<b>Change</b>	<b>-10.9</b>	<b>-7</b>	<b>-7</b>	<b>-6</b>	<b>-5</b>

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Pre-Budget Report 2003	-19.3	-8	-5	0	4
Change	-10.9	-7	-7	-6	-5
Pre-Budget Report measures	-2.5	-1	-1	0	0

# Discretionary PBR measures

£ million	2003-04	2004-05	2005-06
International commitments	-£2,500	-£300	0
Increase in Child Tax Credit	0	-£855	-£925
Productivity measures	0	-£120	-£215
Protecting revenues	0	£370	£560
Fairer society	-£20	-£35	-£75
<b>TOTAL</b>	<b>-£2,520</b>	<b>-£970</b>	<b>-£655</b>



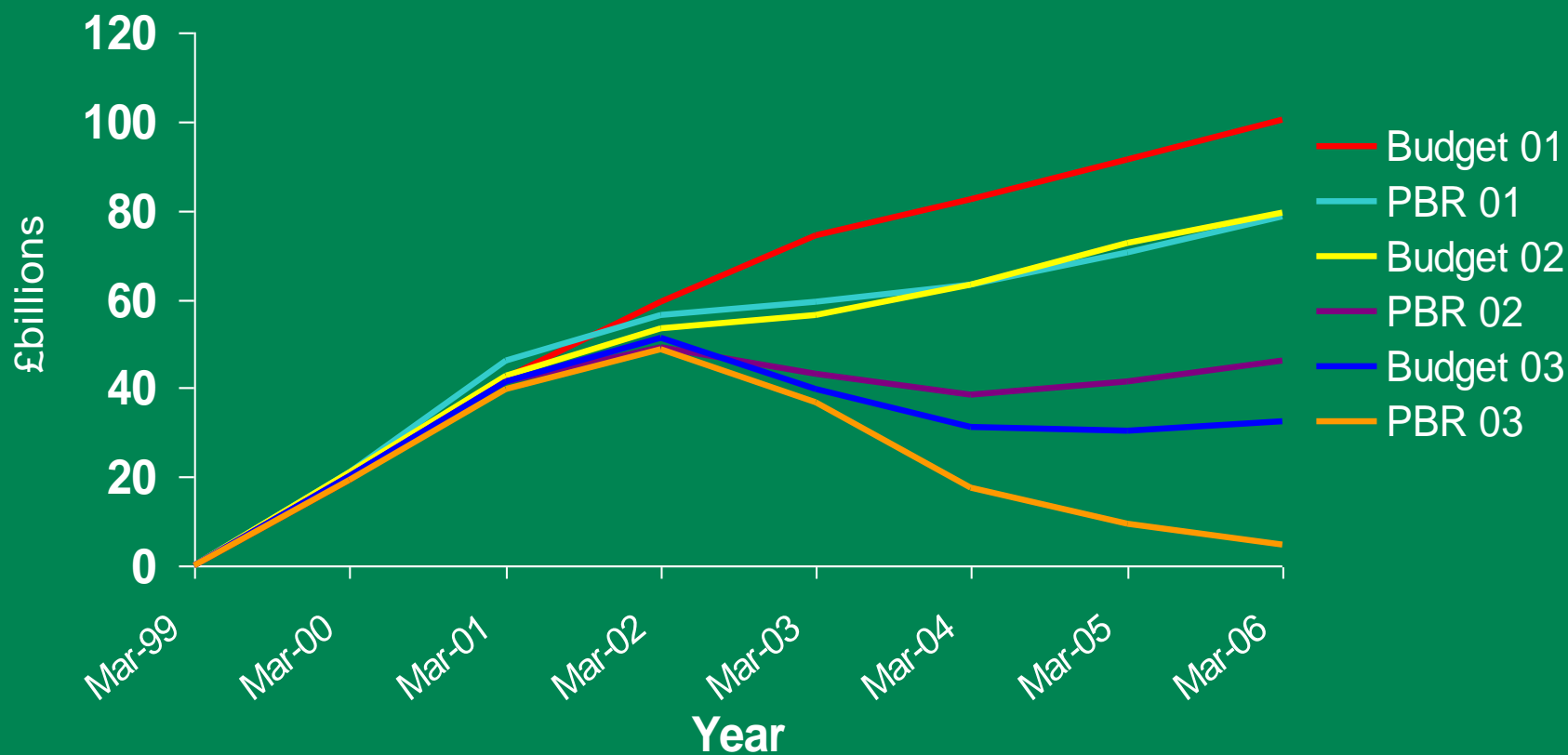
# Non-discretionary spending: £2bn to £3bn a year higher

- Child Tax Credit & Working Tax Credit
  - higher than expected take-up
  - more scored as spending than negative tax
- Social security benefits
  - higher RPI inflation
  - (offset partially by lower unemployment)
- Higher interest payments
  - higher borrowing
  - higher RPI inflation
- Other technical accounting adjustments

# Non-discretionary receipts changes

	2003-04	2004-05	2005-06	2006-07	2007-08
Equity price assumption	$\frac{1}{2}$	1	$1\frac{1}{2}$	$1\frac{1}{2}$	$1\frac{1}{2}$
<i>GDP components:</i>					
<i>Wages and salaries</i>	$-3\frac{1}{2}$	-4	-4	$-3\frac{1}{2}$	-3
<i>Consumers' exp.</i>	$-\frac{1}{2}$	$-\frac{1}{2}$	-1	-1	$-\frac{1}{2}$
Other	-2	$-\frac{1}{2}$	-1	0	1
Total	-5.5	-4	-4	-3	-1

# Cumulative current budget



## Room to manoeuvre?

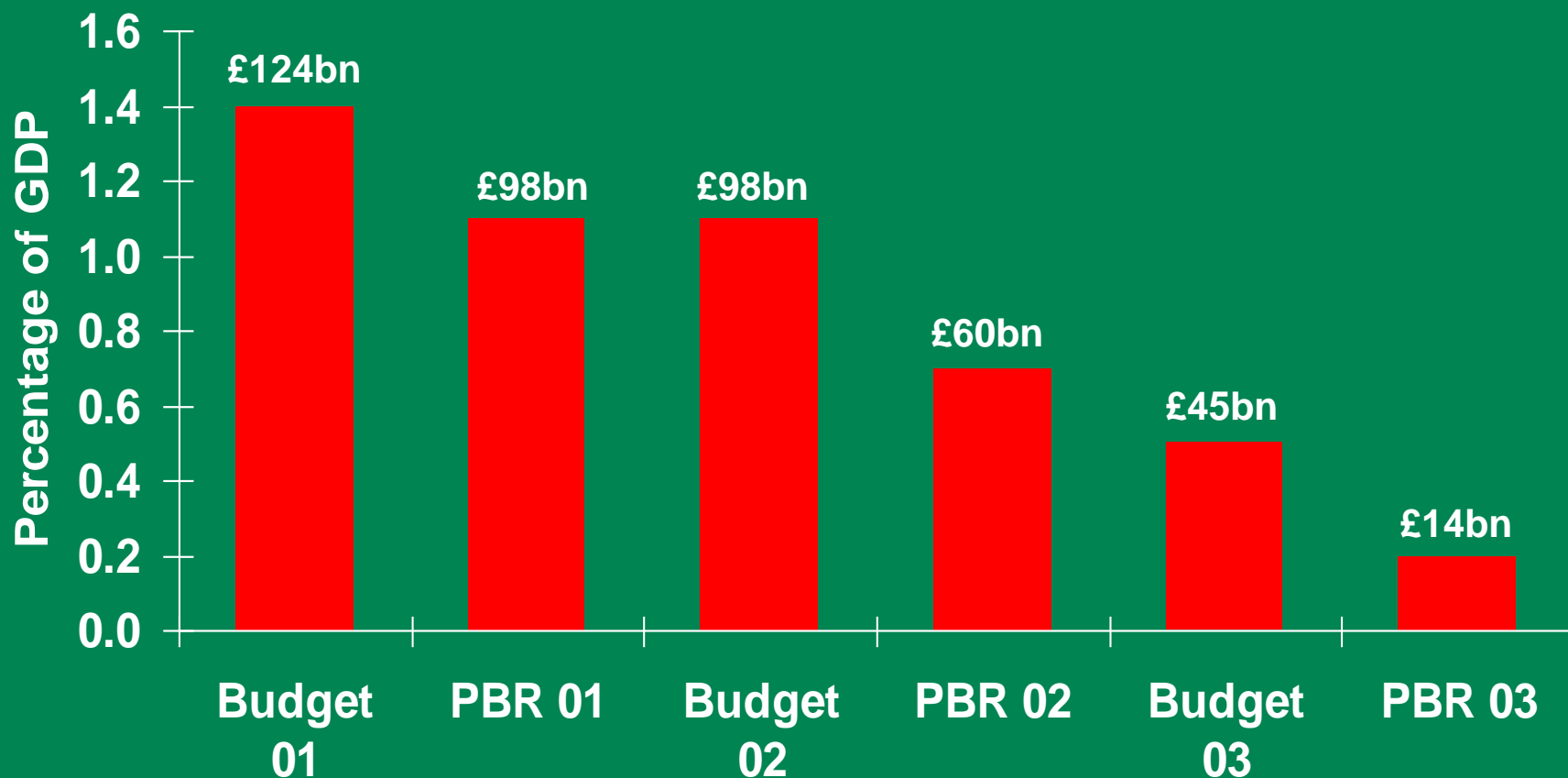
“By 2005-06, when the current cycle ends under the assumptions used in these projections, the accumulated total surplus over the economic cycle will be £4½ billion.” (Para B37, 2003 PBR)

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“.... we have an average annual surplus over the whole cycle of around 0.2 per cent of GDP - meeting our first rule in this cycle by a margin of £14 billion.” (Gordon Brown, 2003 PBR Speech)

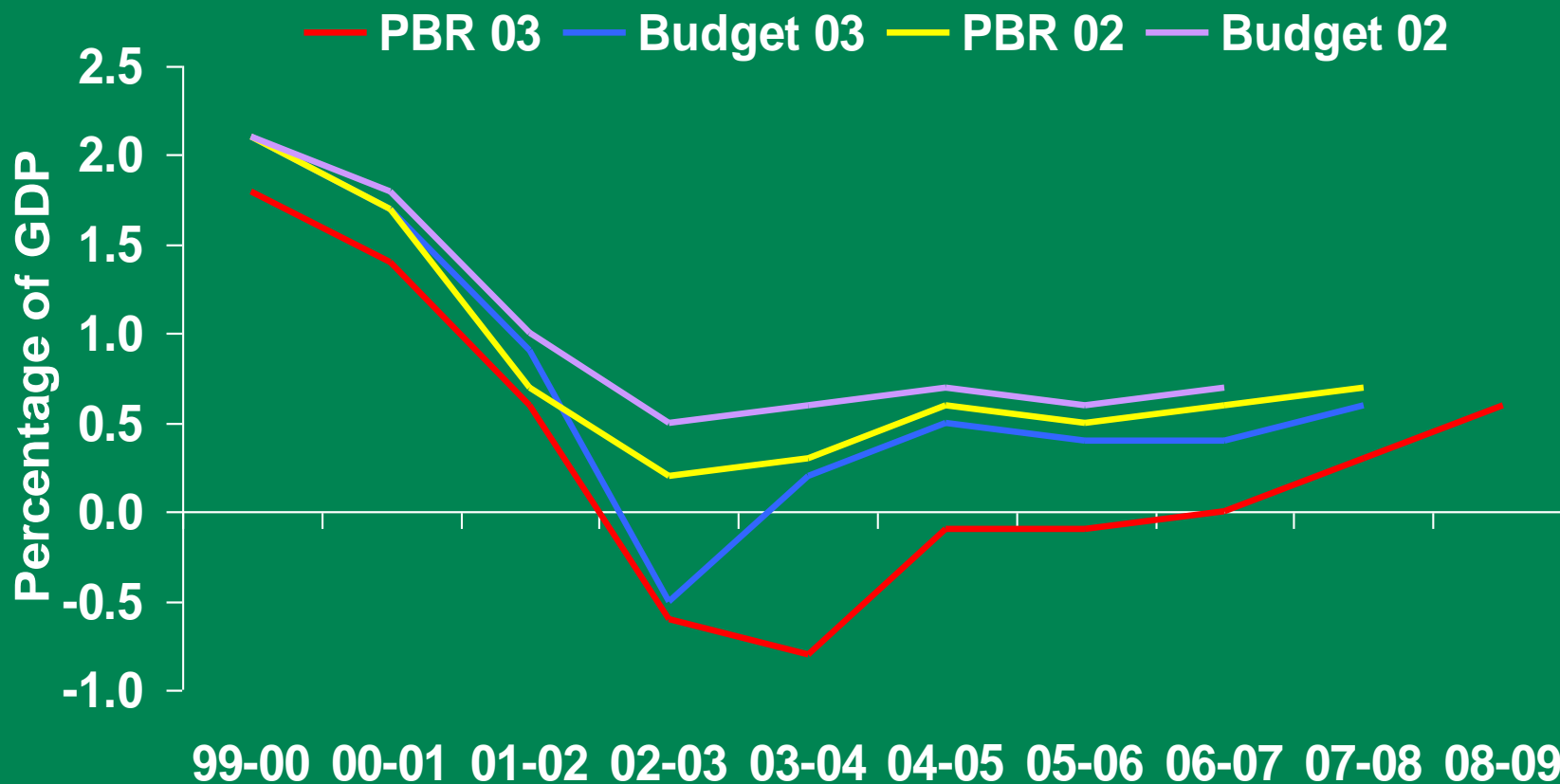
# How the Treasury got £14bn



# AME margin £ billion

	2003-04	2004-05	2005-06	<i>Funds needed?</i>
Budget 2003	1.0	2.0	3.0	
Pre-Budget Report 2003	0.3	0.0	0.0	
<i>Budget 2004?</i>	<i>0.0</i>	<i>1.0</i>	<i>2.0</i>	
<i>Difference?</i>	<i>-0.3</i>	<i>+1.0</i>	<i>+2.0</i>	<i>+2.7</i>

# Cyclically-adjusted current budget





# Companies and Productivity

- New pilot Enterprise Capital Funds
- Changes to R&D tax credit definition
- Extension of Employer Training Pilots
  
- Transfer pricing legislation extended to domestic transactions
- Doubling of asset and turnover thresholds for SMEs

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