

# Tax and benefit changes and distributional analysis

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## A lot of changes had been pencilled in for April 2009

- Temporary measures for 2008 disappearing
  - £600 increase in Income Tax Personal Allowance
  - £50 (£100) increase in Winter Fuel payment for 60+ (80+)
- Higher rate threshold in Income Tax increased by £800 and UEL increased to that level
  
- £50/year increase in the per-child element of the Child Tax Credit
- Child benefit increased to £20/week for the first child
  - But only a 25p/week real increase because inflation so high this September
- Child benefit not counted as income in Housing Benefit and Council Tax Benefit
- Amount of child maintenance not counted as income for means tested benefits increased
  
- Alcohol duties increased by 2% in real terms
- Fuel duty increase of 3.84p (2p postponed from April, 1.84p already pencilled in for 2009)

# Income tax and NI changes

## Income tax

- 10p saga led to £600 rise in personal allowance in May 2008 as “compensation”: this is now permanent
- Extra £130 rise in personal allowance for April 2009 and April 2010 only
- Basic-rate limit frozen in April 2011
  - small real-terms cut in point at which pay higher-rate tax

## National insurance

- Confirmed real-terms rise in UEL in April 2009 (announced in Budget 2007)
  - Means higher-earners and self-employed pay more NI
  - Aligns UEL with HRT
- Real-terms rise in Primary Threshold in April 2011
  - Means all working-age employees pay less NI
  - Re-aligns with personal allowance but decouples from employer threshold
- Rise in all NI rates of 0.5ppts
  - Means all working-age employees, employers and self-employed pay more NI

# Income tax changes for the very rich

From April 2010, value of personal allowance will be reduced for incomes above £100,000. Affects 0.8 million (<2% adults) (HMT)

- Personal allowance in 2010/11 is £6,475, but its value depends on marginal income tax rate
  - Would be worth £1,295 to basic-rate taxpayer & £2,590 to higher-rate taxpayer
- Reform means:
  - Income between £106,475 to £140,000: value of personal allowance same as for basic-rate taxpayer
  - Income above £146,475: no personal allowance
- Phase-outs equivalent to creating 2 short income ranges where marginal income tax rate is 60%
  - Very few people will be affected
  - People will presumably make private pension contributions or charitable donations to lower their taxable income to the point where a phase-out begins.

From April 2011, 45% income tax rate on income above £150,000

- Affects 0.4 million (<1% adults)

Real-terms cut in amount of pension contributions that can be made free of income tax (raises £0.4bn in 2011/12, but more by 2016/7) (HMT)

- Sensible change to make when increasing income tax rate for very rich

# Benefits and tax credits

## Families with children

- Child benefit increased slightly in January-March 2009
- £75 increase in CTC above indexation in April 2009
  - £50 had already been announced, other £25 is brought forward from April 2010
- Nothing specific for child poverty in 2010/11
  - “Govt will take stock of progress...in the Budget” (para 5.13)
  - IFS currently revising its assessment of likely progress by 2010 in light of recession

## Pensioners

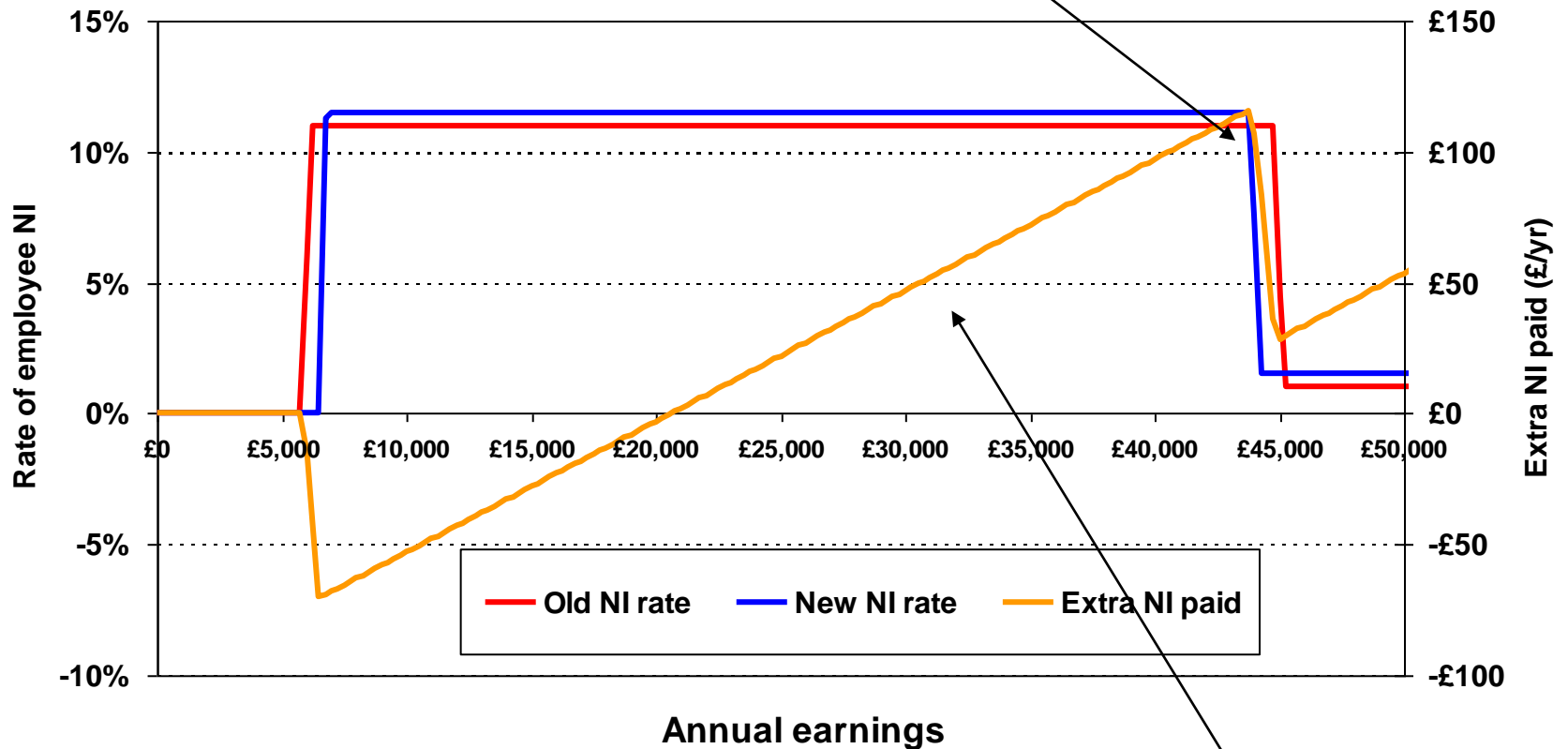
- £60 per pensioner (and some other benefit recipients) in January 2009
- So-called “above indexation increase” in pension credit in April 2009
  - Rise is greater than average earnings, but equal to inflation
- But higher winter fuel payments in winter 2008 NOT (yet) repeated in winter 2009

## Other

- Commitment not to cut benefits and tax credits in cash terms in April 2010 when RPI to be negative.
- Small increase in support for out-of-work home-owners (on top of rise since Budget 2008)

# NI change for those of working-age (April 2011)

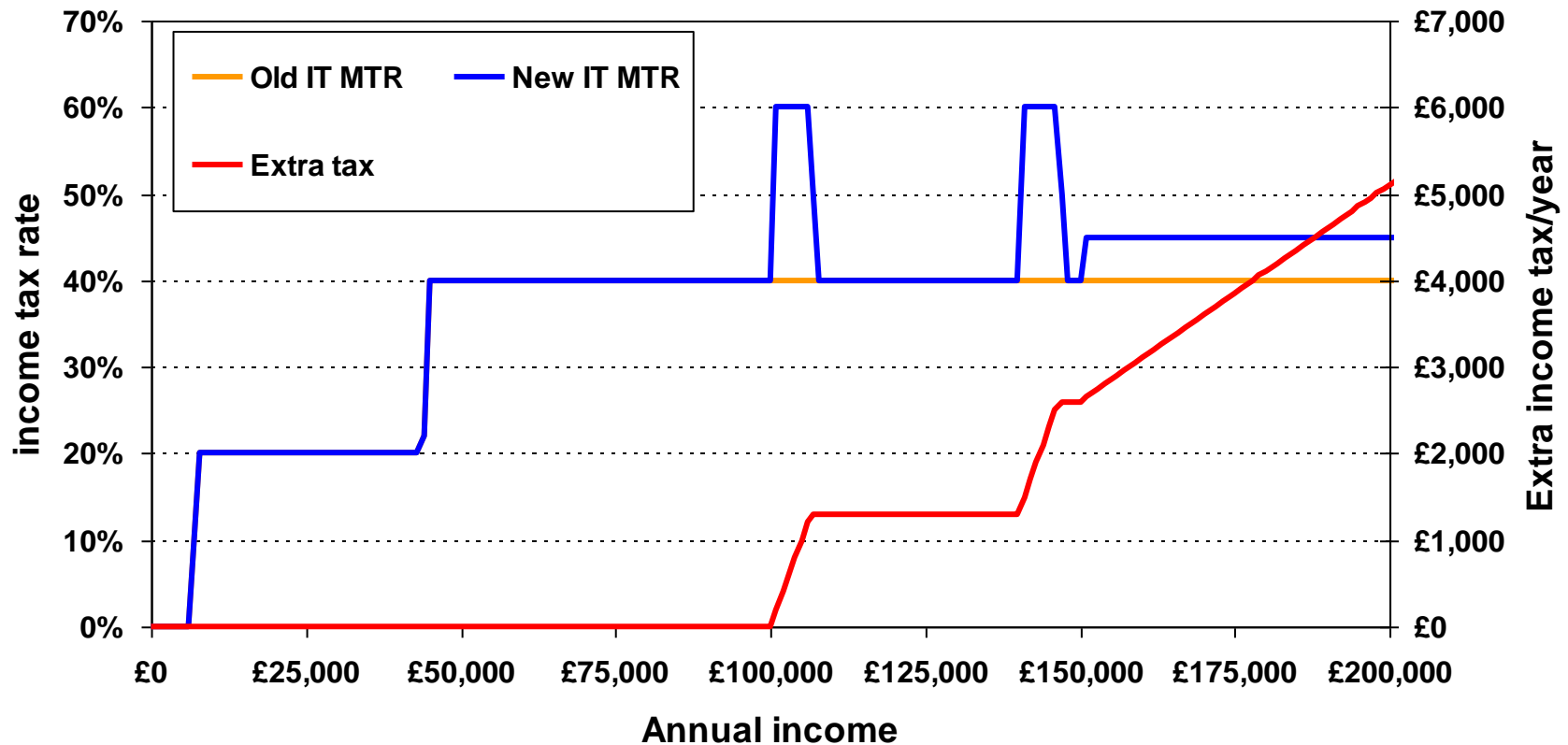
Assumes UEL follows BRT in April 2010



Ignores employer NI, which also rises by 0.5 pts

Will pay more NI if earn > £20K. HMT argue £600 rise in PA compensates those on £20-£40K

# Income tax changes for those above £100K (April 2011)



“Like the side view of Battersea power station” (an anonymous IFS researcher)

## Will tax rises for the very rich raise any money?

- HMT estimate personal allowance phase-out and new 45% rate each raise £1.6bn a year (full-year effect)
- But 45% income tax rate in addition to 0.5% on employee and employer NICs, so marginal rate on top earnings to be
  - 46.5% with income tax and employee NI
  - 52.8% including employer NI
  - 59.8% including consumption taxes
- Revenue-maximising top rate estimated to be 56.6%. If true, 45% rate will raise approximately nothing, and HMT would raise more with, eg, 44% rate. However
  - Estimated elasticities based on reforms in 1980s
  - Estimated elasticities very uncertain, and revenue-maximising top rate could be higher (or lower, even than current top rate)
- HMT have allowed for some behavioural change, but not clear how much
  - If reform raises no money, then only achievement is to lower inequality

Brewer, Saez, Shephard (2008), “Means-testing and tax rates on earnings”,  
[http://www.ifs.org.uk/mirrleesreview/press\\_docs/rates.pdf](http://www.ifs.org.uk/mirrleesreview/press_docs/rates.pdf)



# Distributional analysis of PBR measures

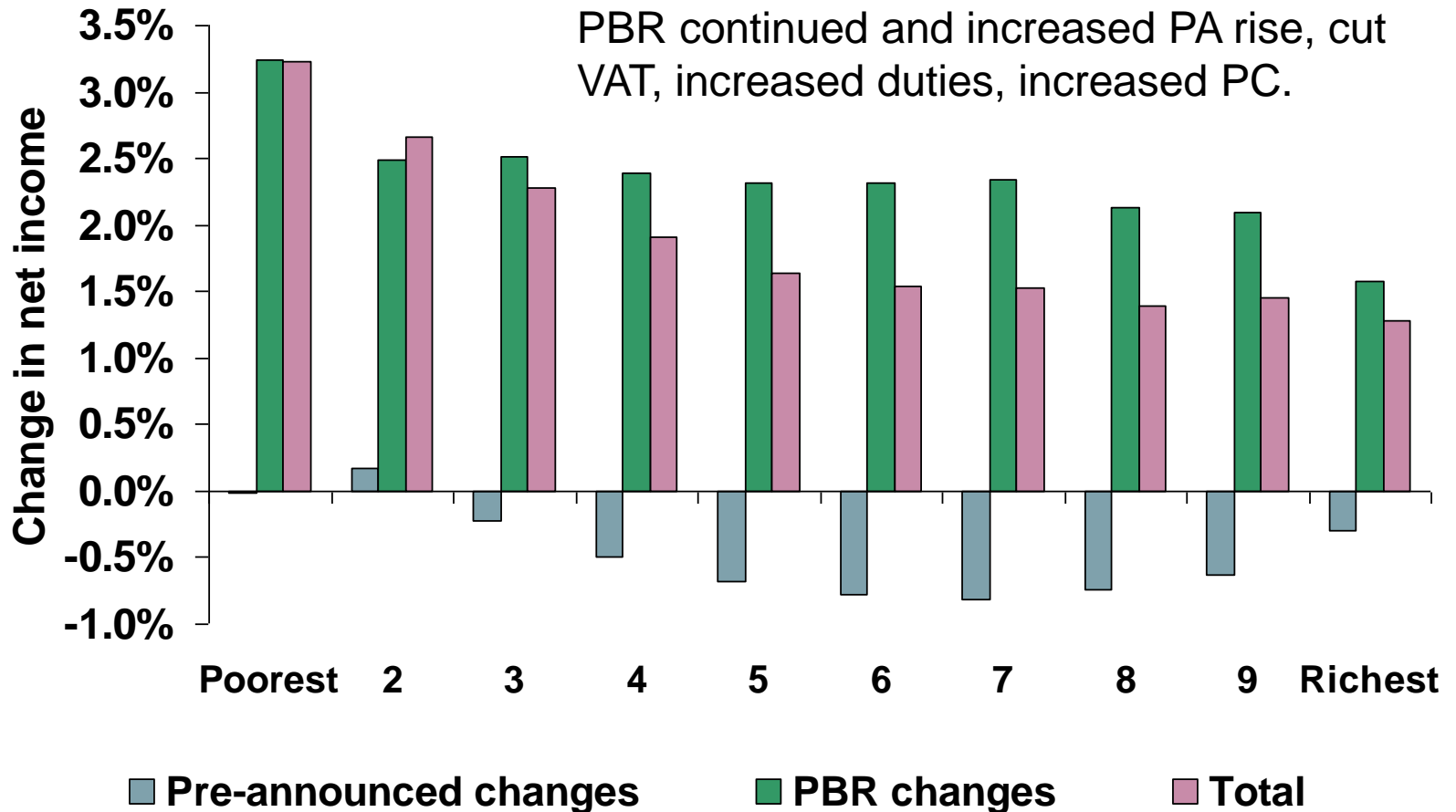
1. In April 2009
2. In April 2011.

Will not show impact of changes this year, nor of changes affecting very rich, nor of employer NI

# Distributional effects of reforms for April 2009

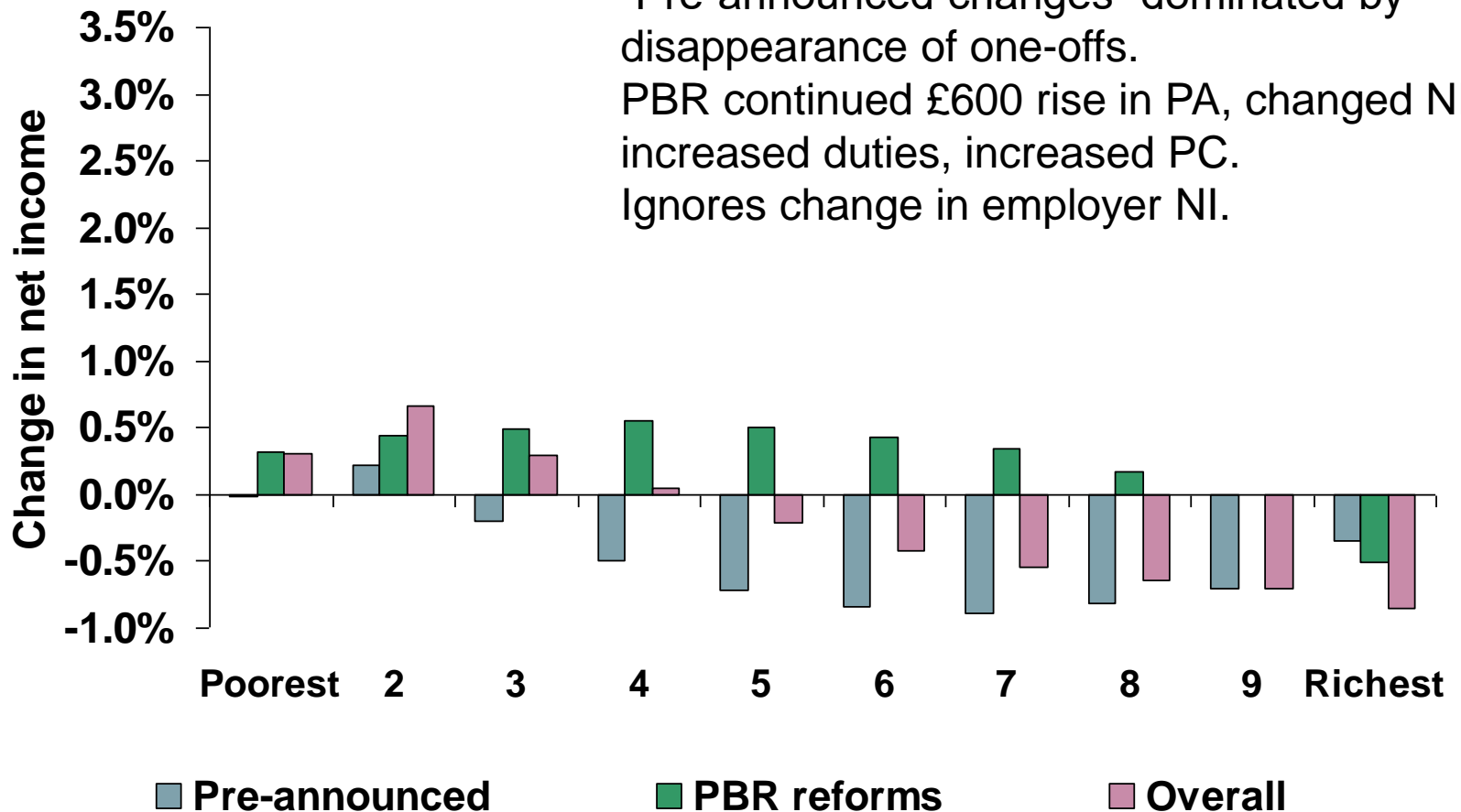
“Pre-announced changes” dominated by disappearance of one-offs.

PBR continued and increased PA rise, cut VAT, increased duties, increased PC.



# Distributional effects of reforms for April 2011 (excludes income tax changes for very rich)

“Pre-announced changes” dominated by disappearance of one-offs.  
 PBR continued £600 rise in PA, changed NI, increased duties, increased PC.  
 Ignores change in employer NI.

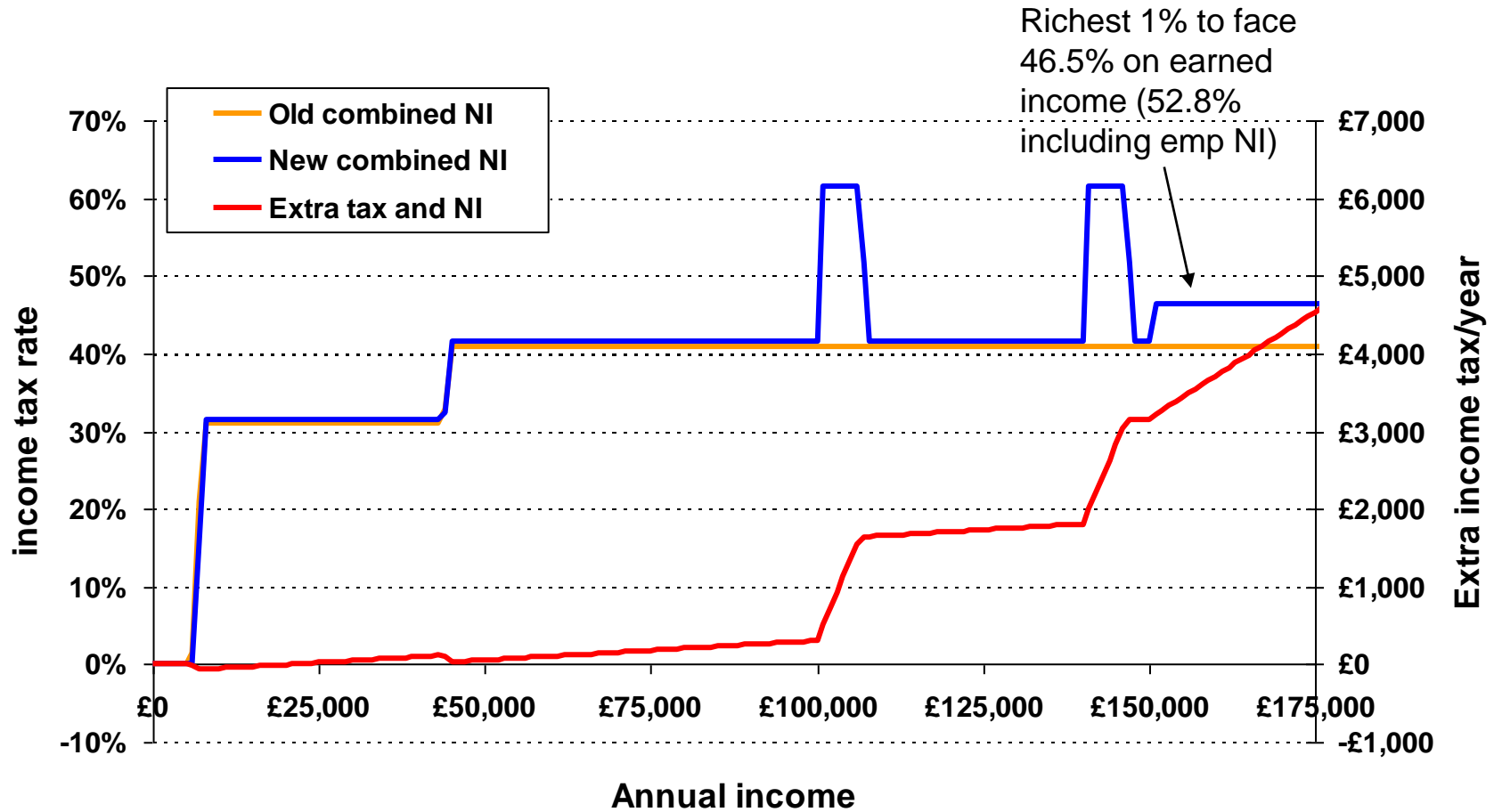


# So where does this leave us?

- Number of “10p losers” reduced to just 0.5m (HMT). How?
  - £600 rise in PA made permanent
  - Extra £130 on PA for 2 years then rise in NI threshold
- HMT: “The measures [in PBR 08] mean that people with incomes below £40,000 will not pay more income tax and NICs in April 2011 than in April 2008 (para 5.9)
  - True if strictly comparing April 2008 (ie BEFORE £600 rise in PA) with April 2011
  - Not true if comparing the 2008/9 tax system (ie WITH £600 rise in PA) with the 2011/12 tax system
    - Depends on how treat £600 rise in PA
    - Might be better to count winners and losers compared with April 2007?
- Pensioners still set to lose extra winter fuel allowance in Winter 2009

**End**

# All income tax and NI changes (April 2011)



Assumes contracted in and ignores employer NI, which also rises by 0.5 ppts

## Distributional effects of reforms for January 2009

Child Benefit increase brought forward  
 Extra payment of £60 for all pensioners  
 VAT cut and duty changes  
 Assumes full-year effect

