What don't we know? (Yet)

Taxing Top Incomes

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The challenge of studying top incomes

- Improved access to tax data has led to huge progress in understanding over recent years

- But much work still to do:

  - (Individual) tax records still only a partial picture

    - More work needed to link tax data with other sources

  - Analysing behaviours of top earners/investors is hard, even with good data

    - Their tax affairs are complicated; needs input from tax lawyers/accountants as well as economists

(1) Measurement

Most existing research is based on *taxable income…*
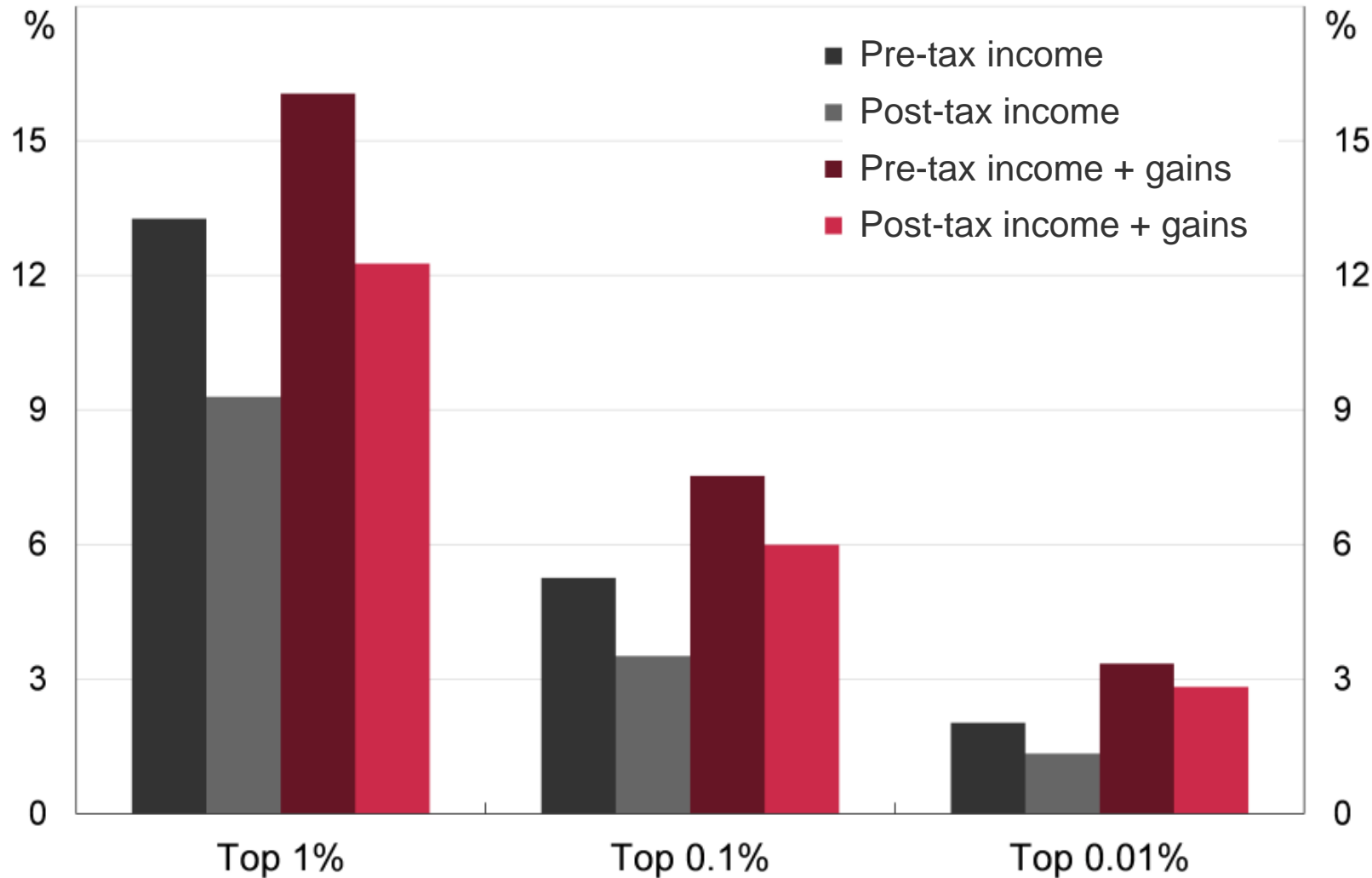
But this misses:
- Capital gains (taxable and non-taxable)
- Unremitted foreign income of non-doms
- Tax-exempt investment returns (e.g. ISAs, VCTs)
- Inheritances and gifts
- Underreporting from non-compliance (incl evasion)

Also misses unless/until paid out:
- Retained corporate profits
- Returns on pension savings
- Returns retained in (some) trusts
  (not assigned to beneficiaries)

Example: capital gains

Legend:
- Pre-tax income
- Post-tax income
- Pre-tax income + gains
- Post-tax income + gains

Chart categories: Top 1%, Top 0.1%, Top 0.01%

- Pre-tax inequality is higher including (taxable) gains

- Smaller difference between pre- and post- tax (measure of redistribution)

Advani & Summers (2020), Capital Gains & UK Inequality

(2) Behavioural responses

- Various ways people can respond to taxes:

  - How much to work; when to retire; whether to migrate; how much to save/invest, etc (**"real" responses**)

  - Timing of payments e.g. dividends, bonuses; income vs gains; income-shifting within the household, etc (**"paper" responses**)

- Non-tax specialists (media, politicians etc) tend to focus on or assume real responses, but paper responses are also important, especially at the top

Example: 50p reform

- Increase in top Income Tax rate from 40p to 50p (April 2010), then back down to 45p (April 2013)

  - "Strolling across the summit of the Laffer curve?" (Robert Chote, then Chairman of OBR)

- Difficulties estimating underlying response (and revenue effect) due to dividend forestalling (Browne & Phillips 2017)

- Lack of evidence on magnitude of specific responses

  - e.g. migration, pension savings, retirement, shifting from income to gains

- Distinguishing responses matters because some have easier policy solutions than others (e.g. don't pre-announce!)

(3) Economic impacts

- If taxes cause top earners / investors to leave the UK, work less, invest less etc, what are the wider effects on the UK economy?

- How effective (/ value for money) are tax reliefs aimed at incentivising additional investment?

  - Lack of evidence even on who uses investment reliefs (and their target investments), let alone downstream impacts on innovation, employment, productivity etc

- Requires linking individual tax records with firm-level data (from taxes and other sources), plus suitable policy variation

Ongoing research

- Major programme of work over next 3-4yrs, funded by ESRC & Nuffield
- Economists working in collaboration with tax lawyers and practitioners
- Mainly using data accessed via HMRC Datalab
- Focus on top 1%, and within that top 0.1% ('super-rich')
- Aim to generate new evidence that can be used to inform policymaking
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