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Top incomes and tax policy



Economic
and Social
Research Council



The top 1% and their income

- *Fiscal Income* - from HMRC tax records - captures income from:
 - **employment** (inc taxable employment benefits, net of tax-deductible employment-related expenses); **profits from sole trading** (net of capital allowances and losses); **partnership income**; **dividends**; **property**; **investments** (inc from interest, trusts, settlements and estates); **private pensions**
- Doesn't capture some incomes, including:
 - Capital gains
 - Some forms of foreign income
 - Tax evasion
 - Inheritances and lifetime gifts

Income is highly skewed

In 2018-19 and as % of UK adults:

- **Top 10%: around 5m people** with annual income > **£44,000**
 - **42% of pre-tax fiscal income**
- **Top 1%: around 0.5m people** with annual income > **£130,000**
 - **15% of pre-tax fiscal income**
 - More than bottom half of income distribution
- **Top 0.1%: around 50,000 people** with annual income > **£500,000**
 - **6% of pre-tax fiscal income**
 - 60 times greater than their share of the population

Top income shares were rising from early 1980s to financial crisis

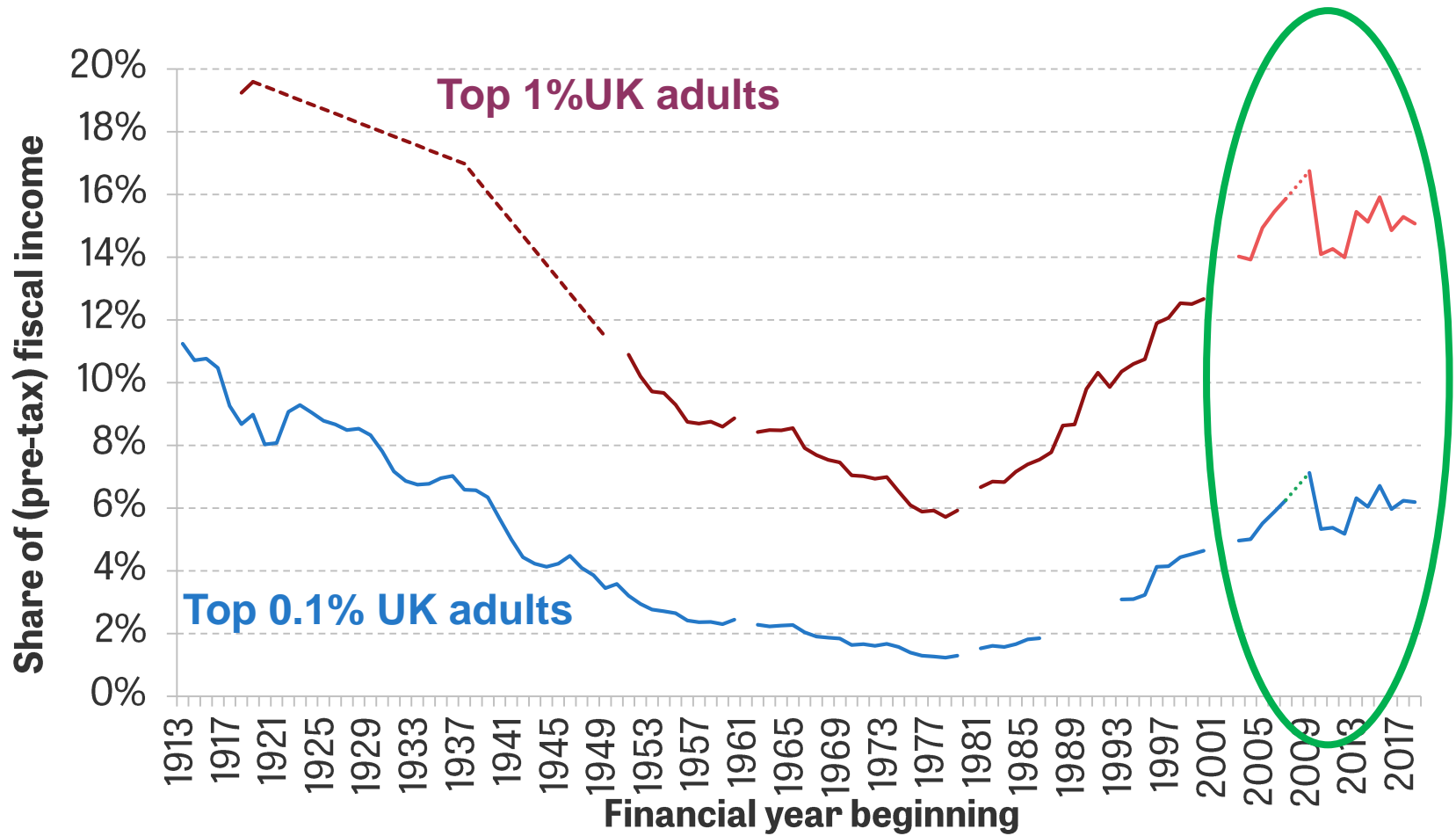


Figure 2, Delestre, I., Kopczuk, W., Miller, H. and Smith, K. (2022), 'Top income inequality and tax policy', IFS Deaton Review of Inequalities

Business income is more important at the top

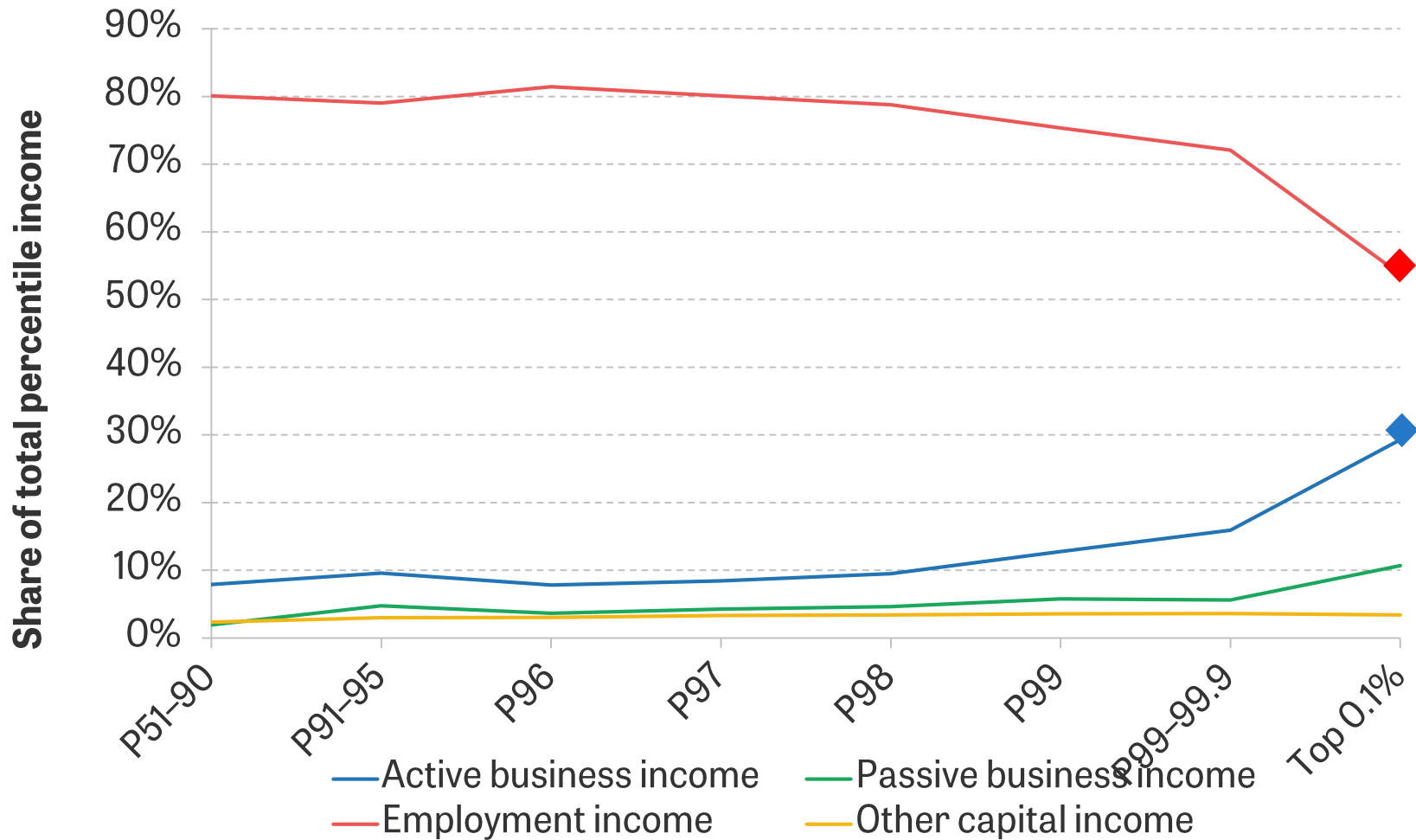


Figure 3, Delestre et al (2022)

More self-employed and company owner-managers at the top

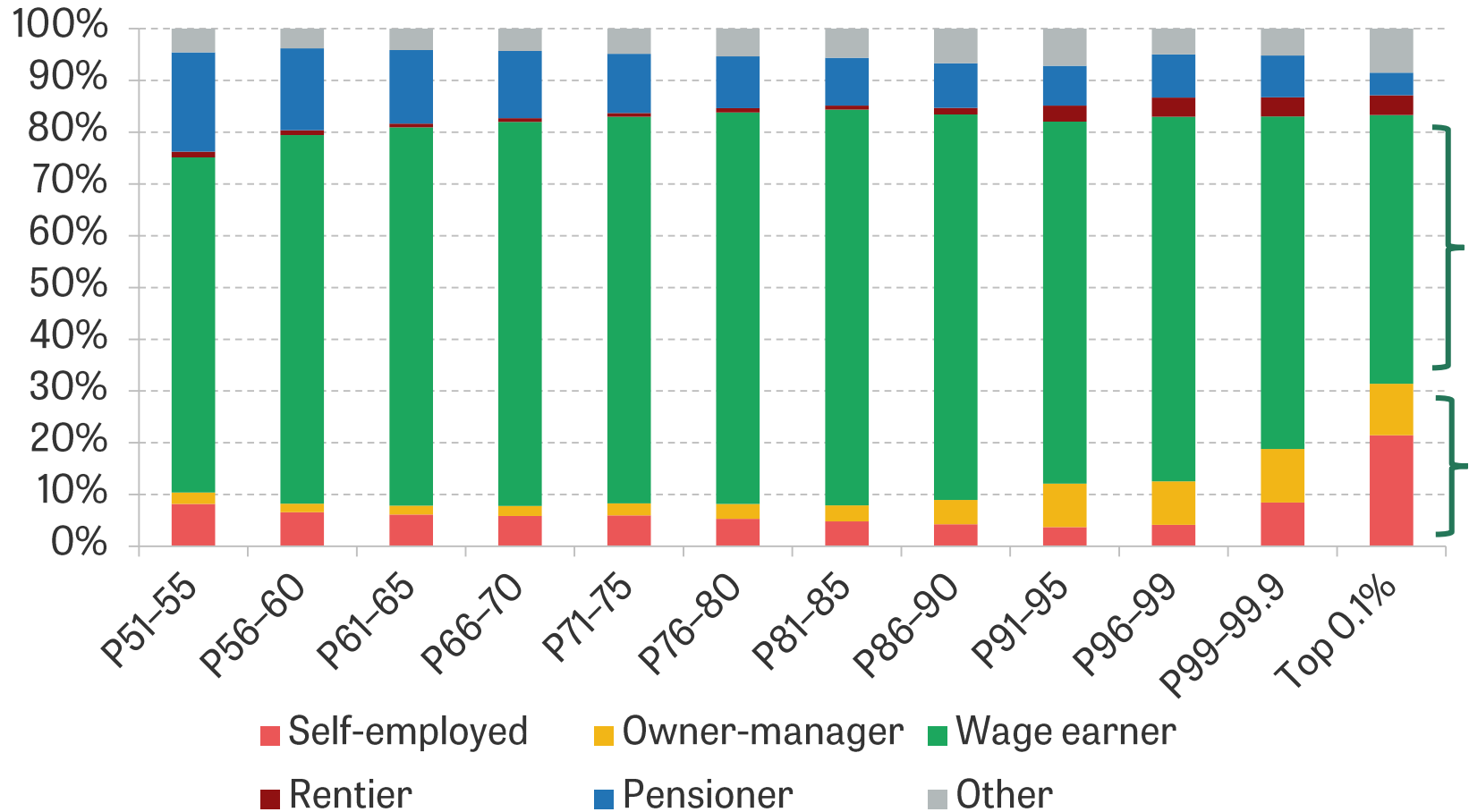


Figure 4a, Delestre et al (2022)

Company owner-managers are more varied

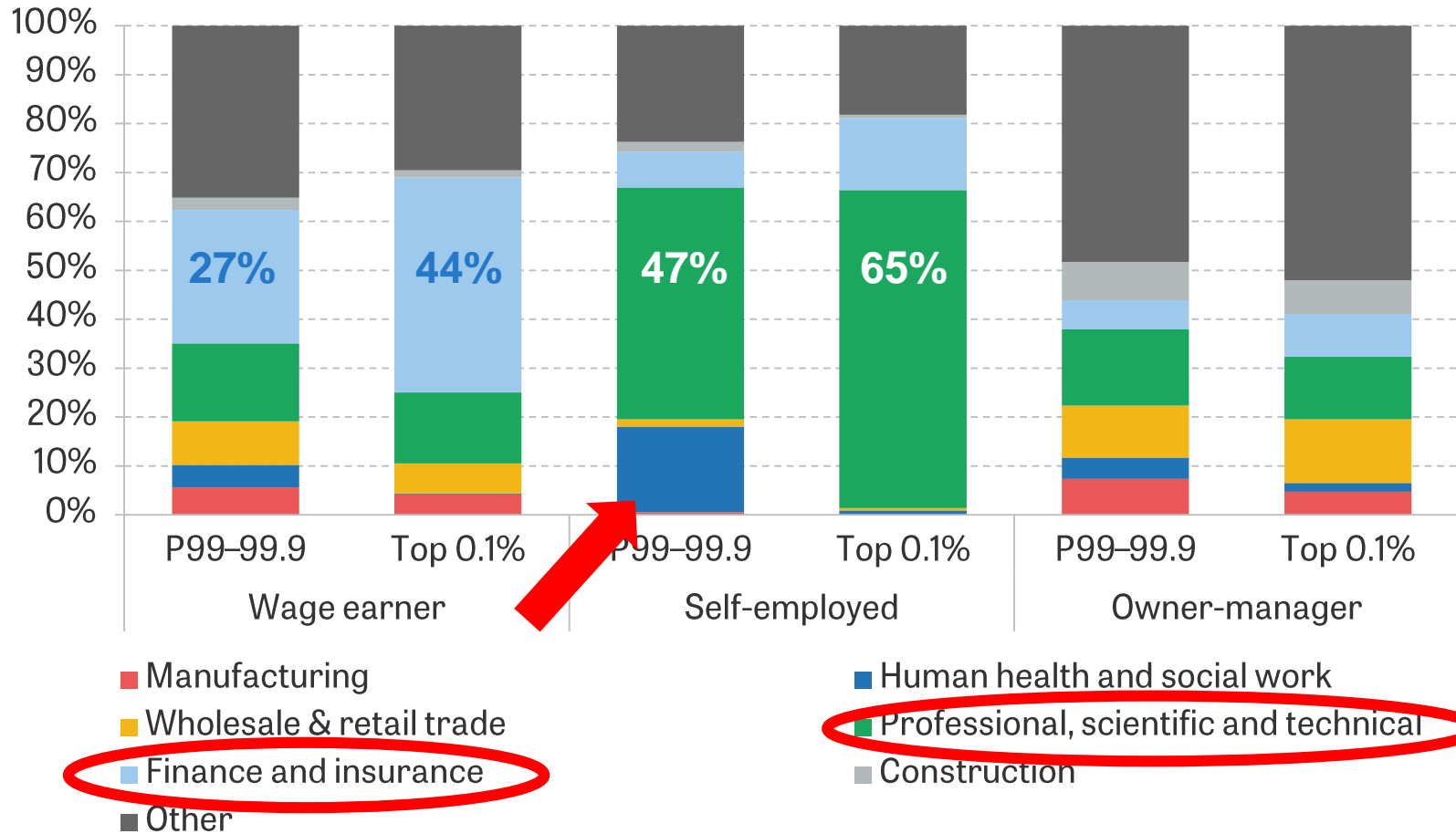


Figure 4b, Delestre et al (2022)

Male, middle aged, Londoners

| | P99–99.9 | Top 0.1% | All UK adults |
|------------------|----------|----------|---------------|
| Male | 79% | 87% | 49% |
| Age: | | | |
| 35–44 | 27% | 22% | 16% |
| 45–54 | 36% | 43% | 17% |
| 55–64 | 21% | 23% | 16% |
| Region: | | | |
| London | 33% | 46% | 13% |
| South East | 22% | 21% | 14% |
| North of England | 10% | 6% | 22% |

24% of top 1% are migrants

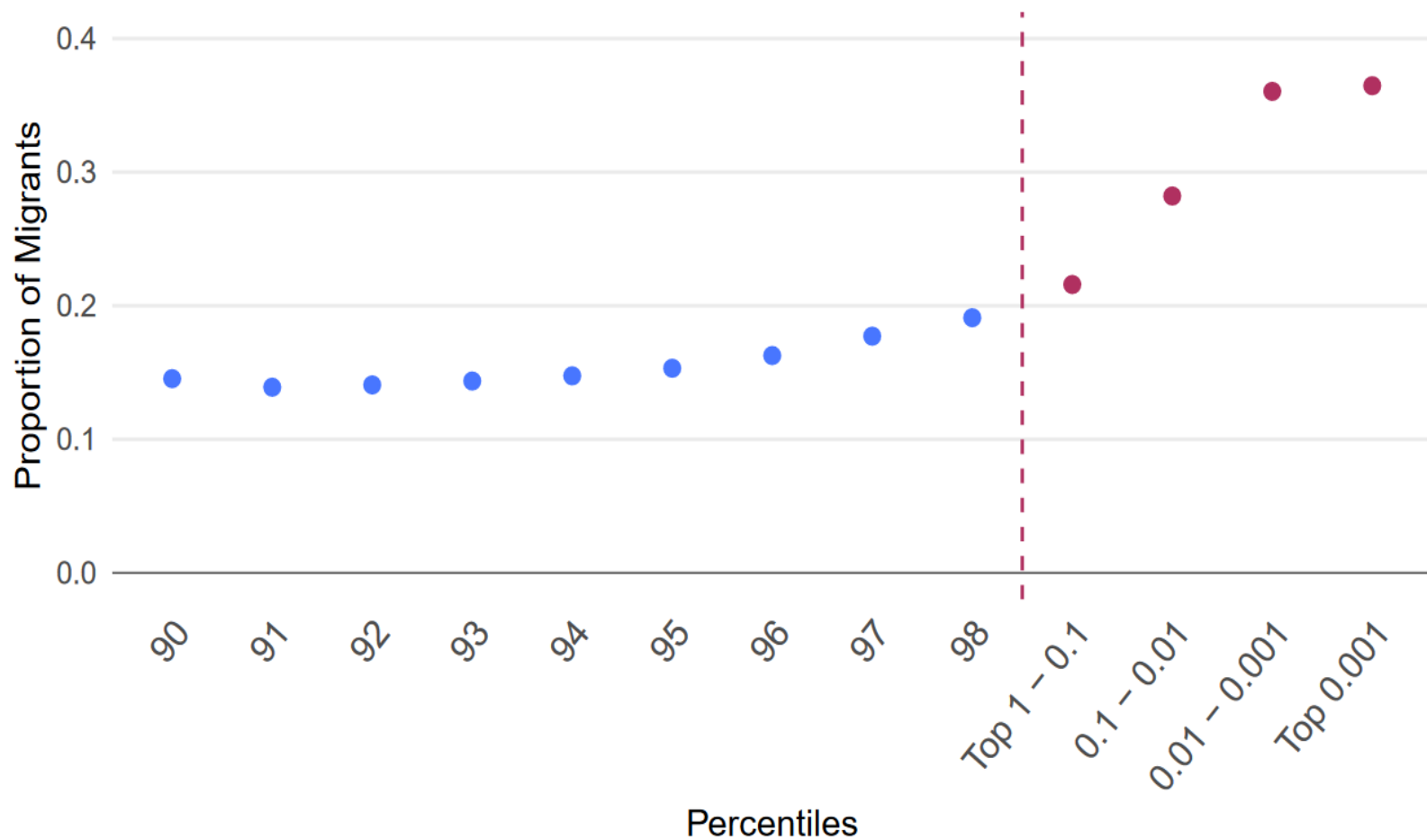


Figure 1b, Proportion of migrants within the top decile, [Advani et al \(2023\)](#), Immigration and the top 1%

Capital gains

- Most gains aren't taxable
 - Large capital gains related to housing -- much more equally distributed than taxable gains

In 2018–19 (based on HMRC statistics):

- UK taxpayers received a total of **£64 billion in taxable capital gains** (compared to £1.1 trillion of fiscal income)
 - half of gains from the sale of business stock not listed on the LSE
- Gains flowed to just 281,000 taxpayers – **average gains of £228,000**
 - enough to put an individual in the top 1% based on gains alone
 - most people getting gains were already in top 1% - 42% of taxable gains went to people with fiscal income >£150,000
 - reflects income accrued over many years

Taxable capital gains are very concentrated at the top

Within the **top 10%** of taxpayers:

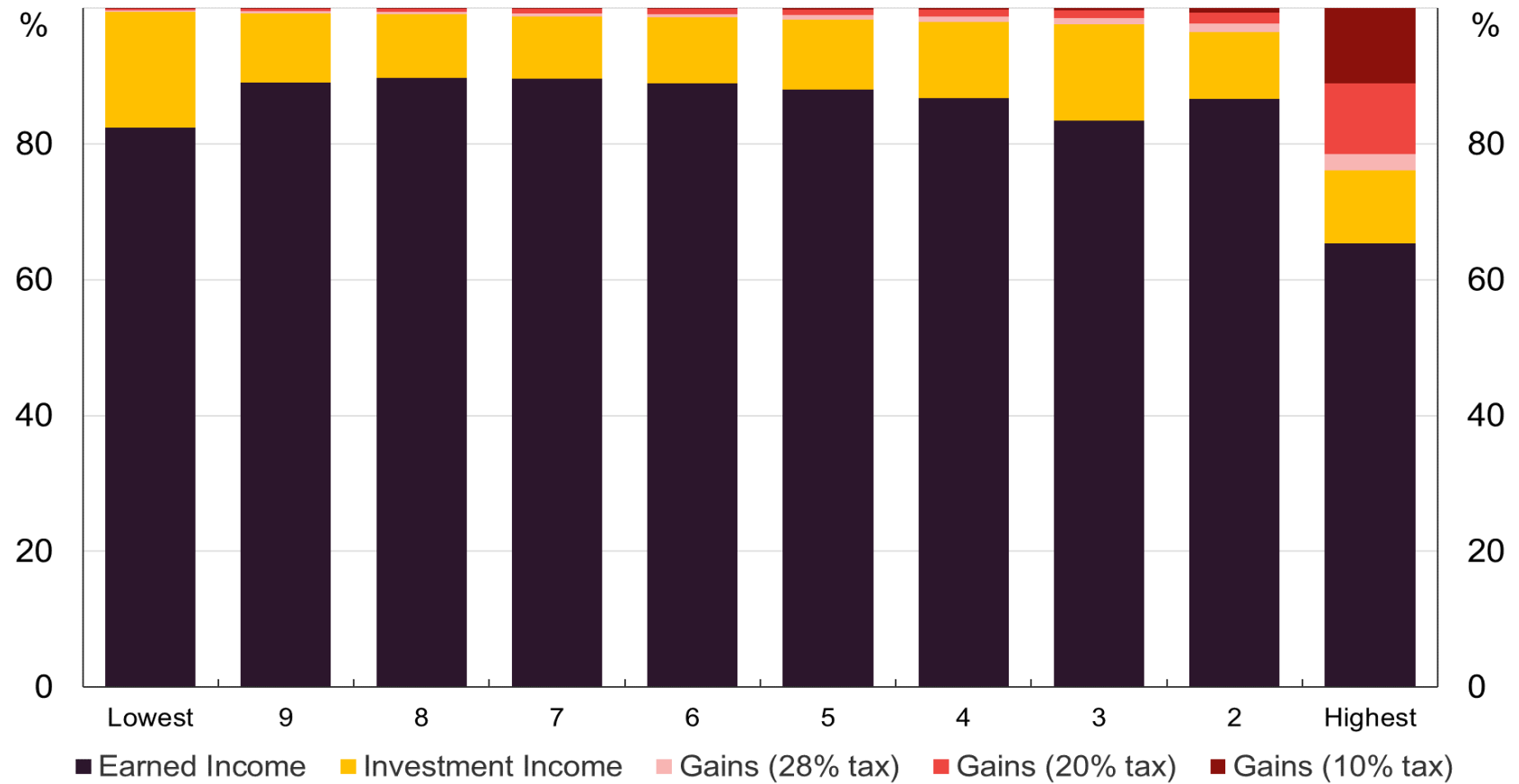


Figure 4, [Advani and Summers \(2023\)](#). Share of total remuneration (including gains) taxed at different rates, by level of total remuneration

Taxable capital gains are very concentrated at the very top

Within the top 1% of taxpayers:

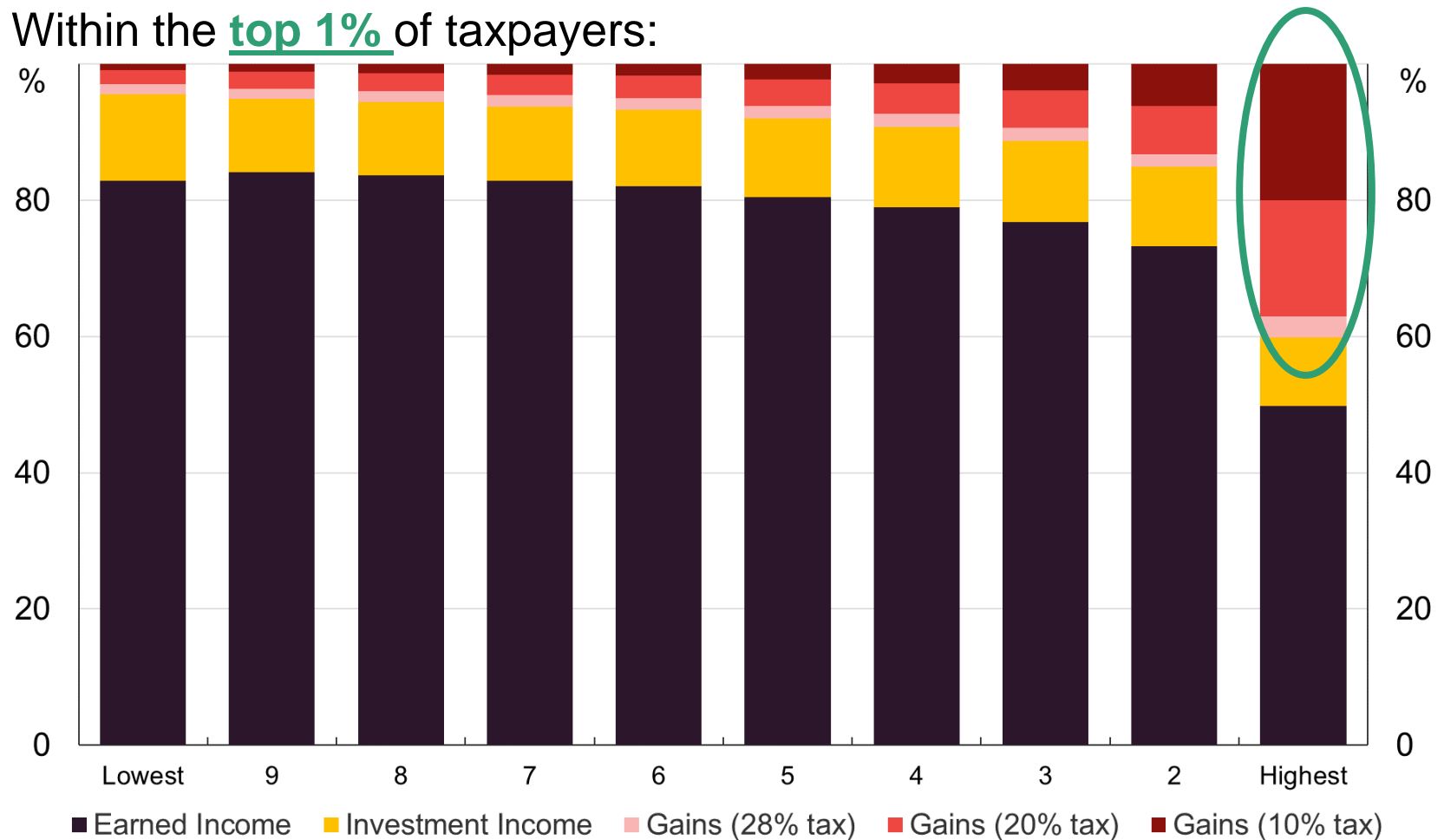


Figure 4, Advani and Summers (2023). Share of total remuneration (including gains) taxed at different rates, by level of total remuneration

Business owners retain a lot of profits in their companies

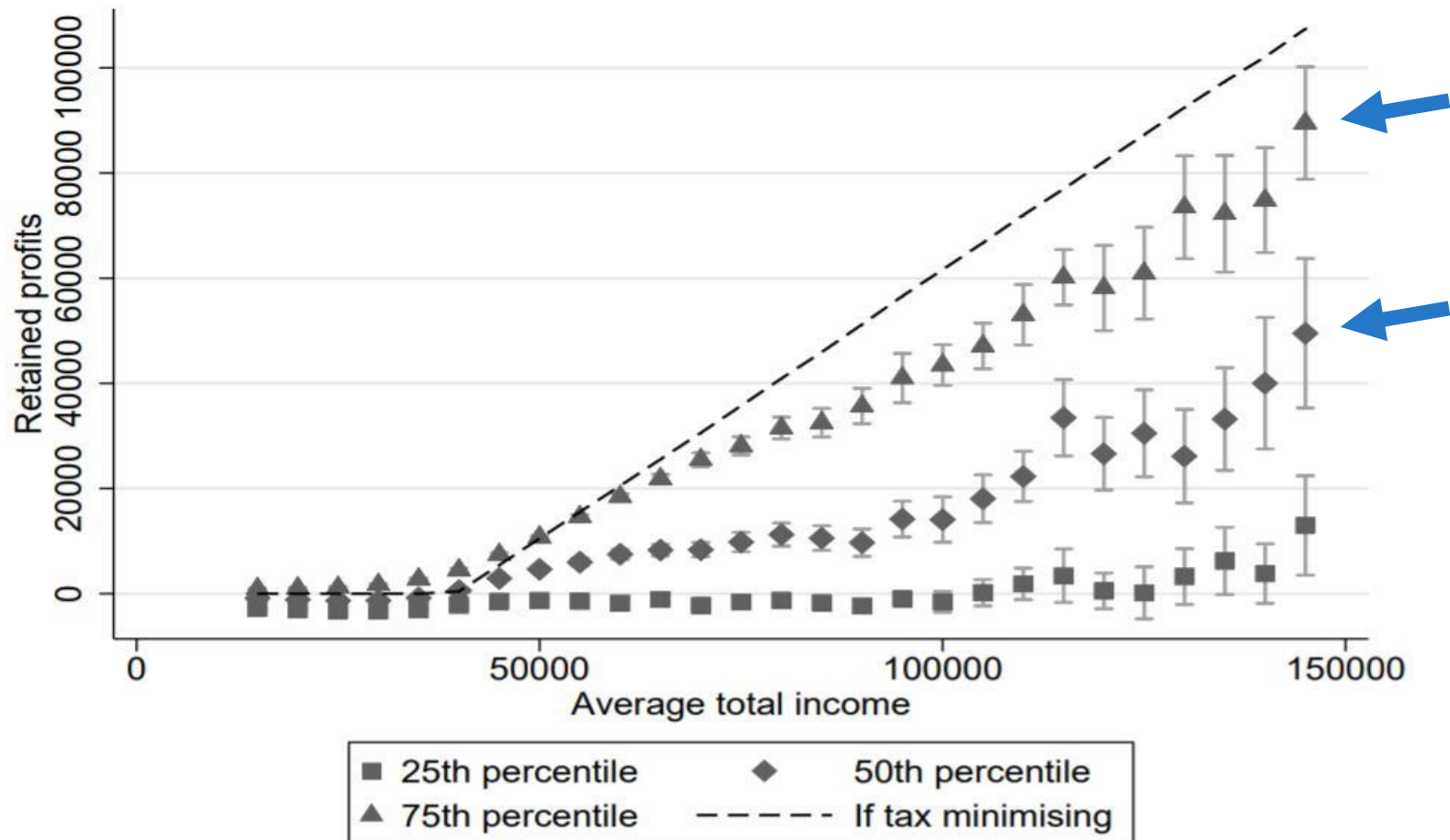


Figure 4.5 (for 2013-15), Miller et al (2023) [Intertemporal income shifting and the taxation of business owner-managers](#), *Review of Economics and Statistics*



Taxes paid at the top

Income tax revenues are skewed to the top

Share of total tax revenue paid by fiscal income percentile of UK adults, 2018–19

| | <P90 | P90–99 | Top 1% |
|---|------|--------|--------|
| Total fiscal income | 58% | 27% | 15% |
| Income tax | 32% | 34% | 34% |
| Income tax & NICs (excluding employer) | 39% | 33% | 28% |

- Share of tax paid by the top has been rising
 - In 2003-04: top 1% paid **20%** of income tax and NICs (exc employer NICs)
 - Partly the effect of rising incomes. Partly the effect of higher top taxes since 2010

Top taxes have been rising & reduced post-tax income shares

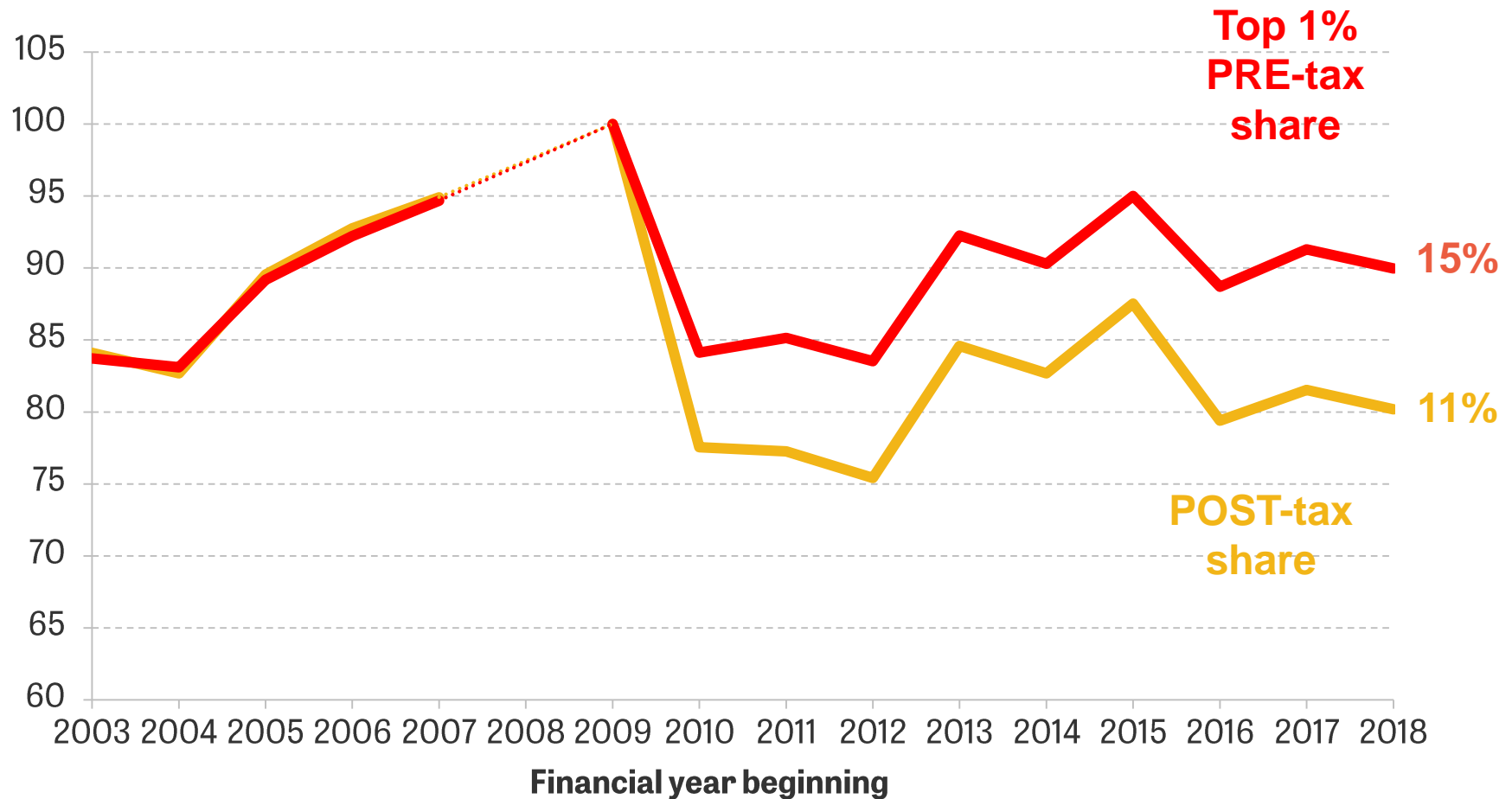


Figure 10, Delestre et al (2022). Indexed to 100 in 2009.

Tax rates vary by income source

Overall top marginal statutory tax rates

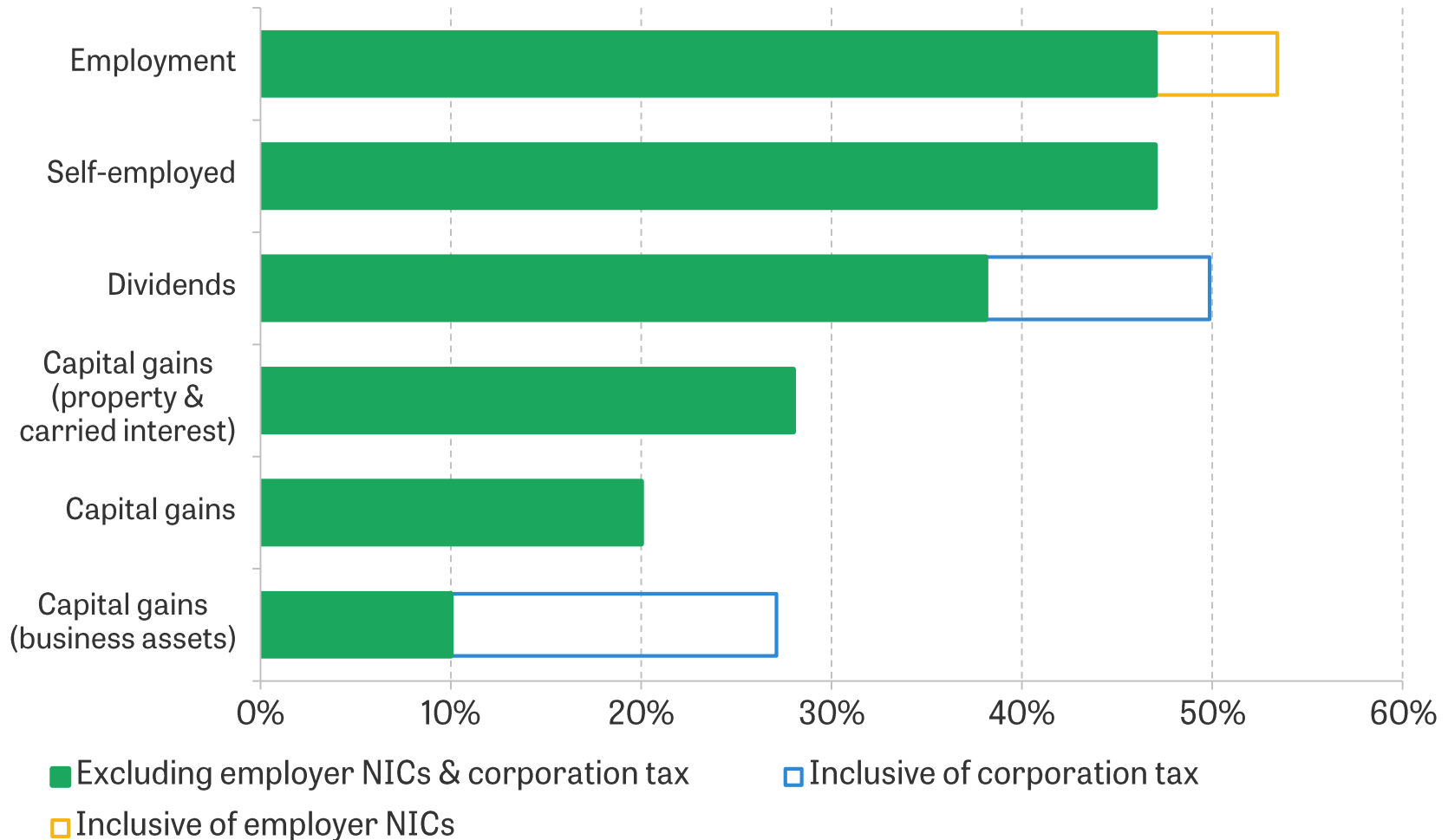


Figure 8, Delestre et al (2022)

Taxes vary by income source

Mean average tax rate by type of individual within the top 1% of UK adults, 2018–19

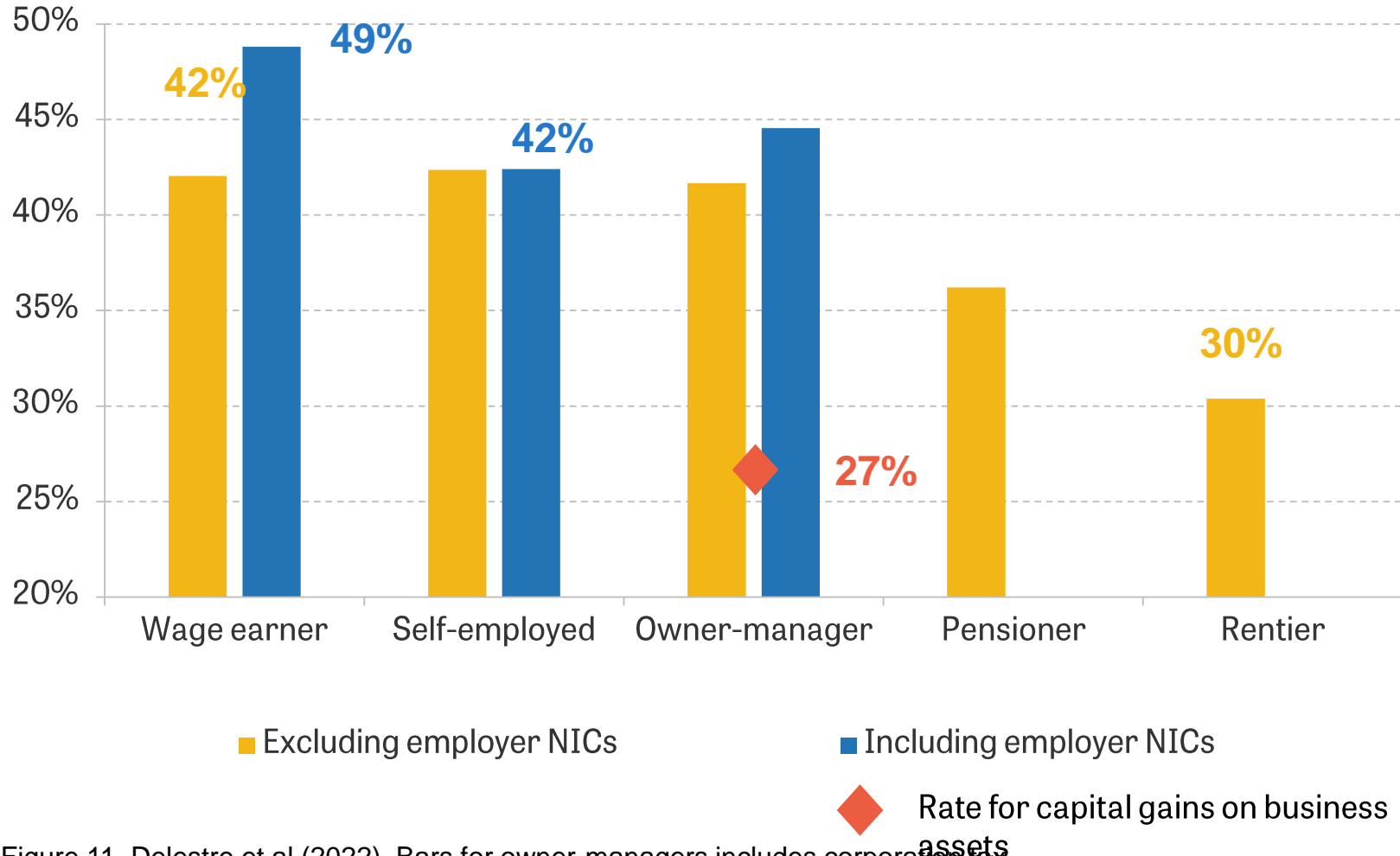


Figure 11, Delestre et al (2022). Bars for owner-managers includes corporation tax.



Tax policy and the top

Setting top tax rates

- How high should top tax rates be?
 - depends in part of political preferences – not a *right* answer
- The design of top taxes affects how people would respond to higher top rates
- Official forecasts predict a higher **additional rate of income tax** would raise little additional revenue (albeit with large uncertainty)
 - High-income people are responsive to taxes
 - There are a variety of responses that will differ across people
 - Includes shifting across tax bases

Setting capital tax rates come with trade-offs

- Large differences across types of income are problematic
 - Efficiency costs from tax motivated income shifting (across time and tax bases) & changes in legal form
 - Horizontally inequitable (where people are doing similar work)
- Lower tax rates on capital income reduce discouragement to investment

How to design taxes at the top

- What is the aim of a preferential rate / regime?
 - To reduce the extent to which tax discourages some activities?
 - -> *aim for a neutral tax system*
 - To actively encourage some activities?
 - -> *aim for tax to change behaviour*

- What is the role of the tax base vs tax rates?

Summary

- **There's a lot of income at the top** – and a lot of associated tax revenue
 - Still some income we don't know enough about
- **Employment income is always the single most important source of income**
 - Important trends in migrants and the financial sector
- **Business income (including capital gains) much more important at the top**
 - Business owners sit between personal income taxes and corporate taxes
- **There is a lot of variation across people**
 - Broad brush stereotype: the top 1% are middle aged, men living in London who are bankers, lawyers or accountants or who run their own businesses