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## Conservative and Labour tax proposals

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# What's coming up

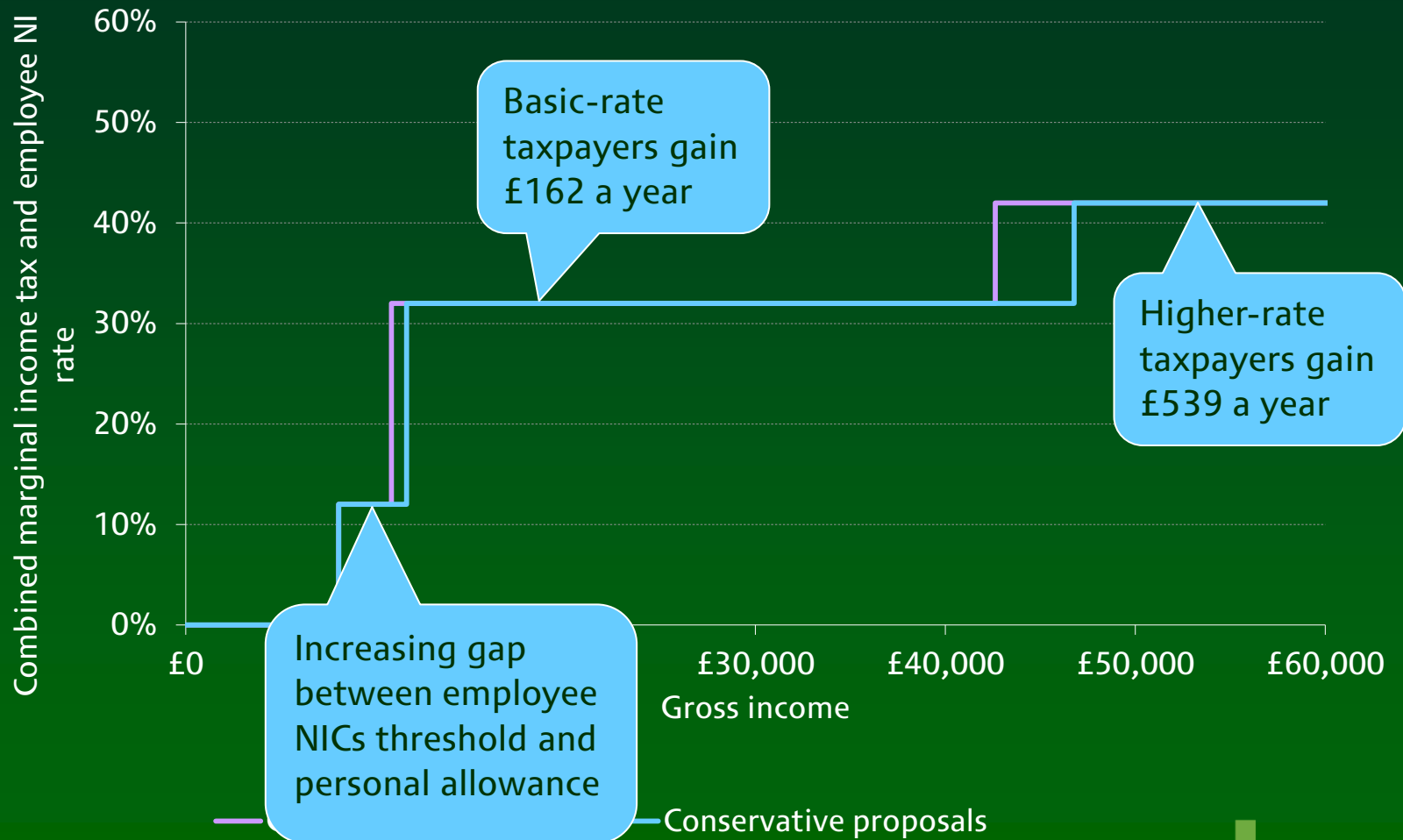
- Discuss Conservative and Labour proposals on:
  - Income tax
  - Pensions tax relief
  - Taxation of housing
  - Tax avoidance
- Analyse policies as if in place in 2015–16, assuming all measures announced up to and including Budget 2015 already in place
- In each case, look at:
  - Winners and losers
  - Impact on incentives
  - Simplicity and efficiency
- Full report also looks at Liberal Democrat proposals

# Income tax proposals

- Conservatives:
  - Increase personal allowance to £12,500 and higher-rate threshold to £50,000 by 2020–21. Overall cost: **£5.9 billion** per year
- Labour:
  - Abolish transferable personal allowance for married couples and introduce 10% income tax band. **Revenue-neutral**
  - Increase 45% additional rate of income tax to 50%. Yield: HMRC estimate **£110 million** per year, but highly uncertain

# Conservative income tax proposals

2020–21 system in current prices



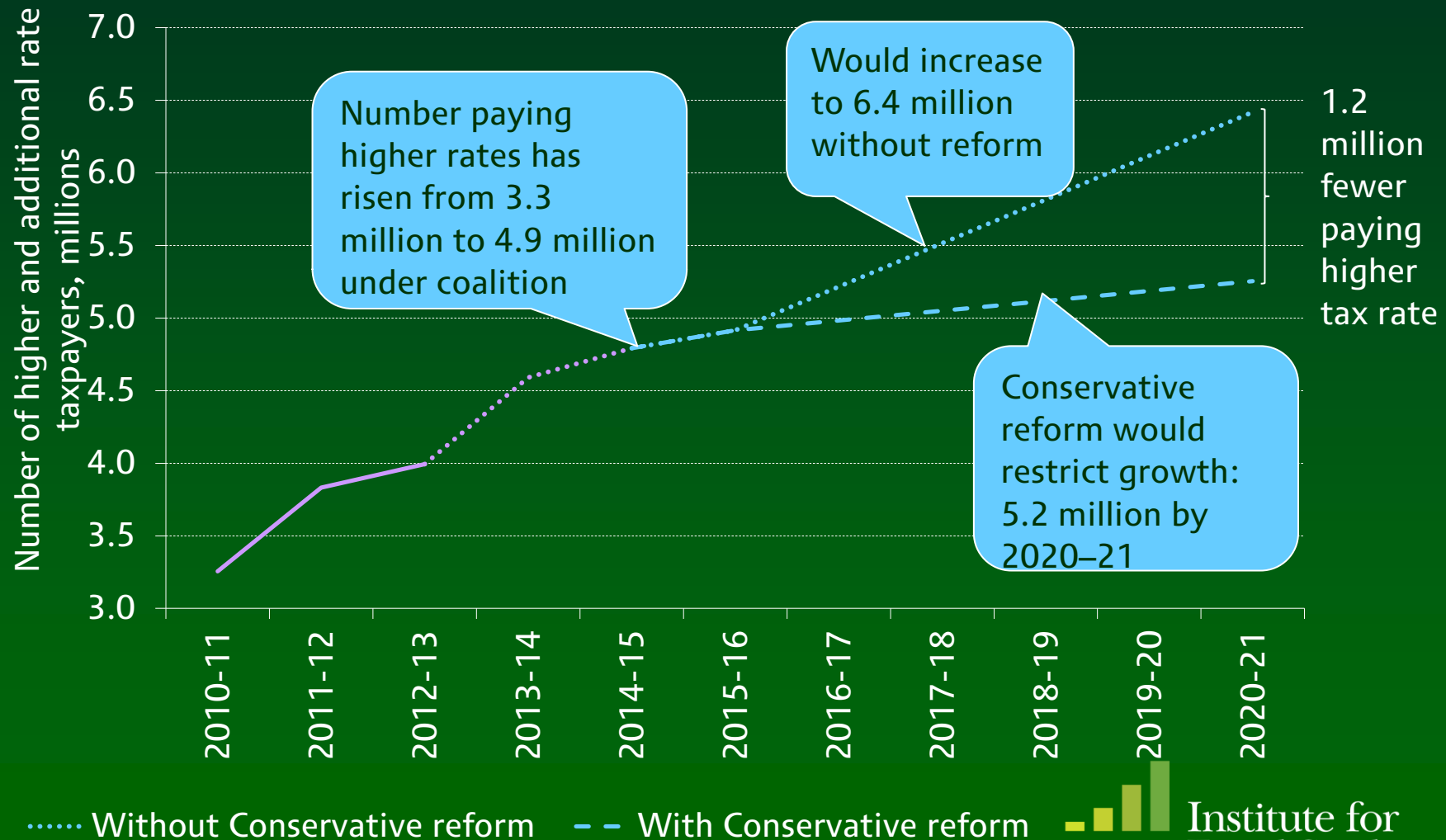
Note: assumes all income from employment, no pension contributions



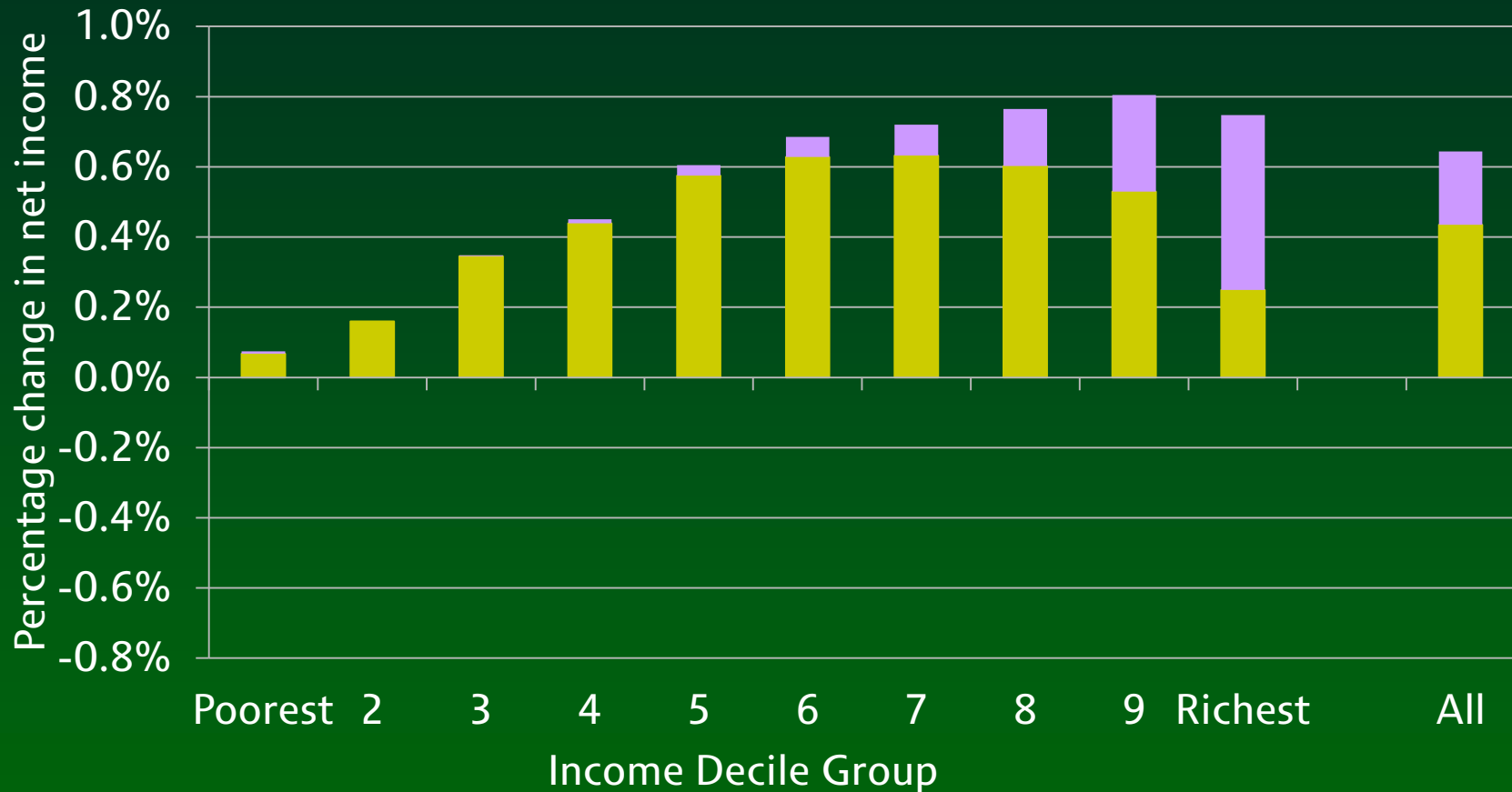
# Personal allowance increase

- Both Conservatives and Liberal Democrats want to increase the personal allowance to £12,500 by 2020–21
- Biggest tax cut proposed by any of the three parties: **£4bn**
  - Follows £8 billion giveaway during last Parliament
  - Conservatives want to link personal allowance to minimum wage, which would increase the cost in the long run
- 44% of adults don't pay income tax, so wouldn't benefit
  - Up from 39% in 2010–11
  - Most taxpaying pensioners would benefit, unlike previous increases

# Increasing higher-rate threshold: Cost £1.9bn

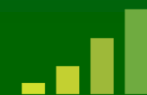


# Distributional impact of the Conservative Party's income tax proposals



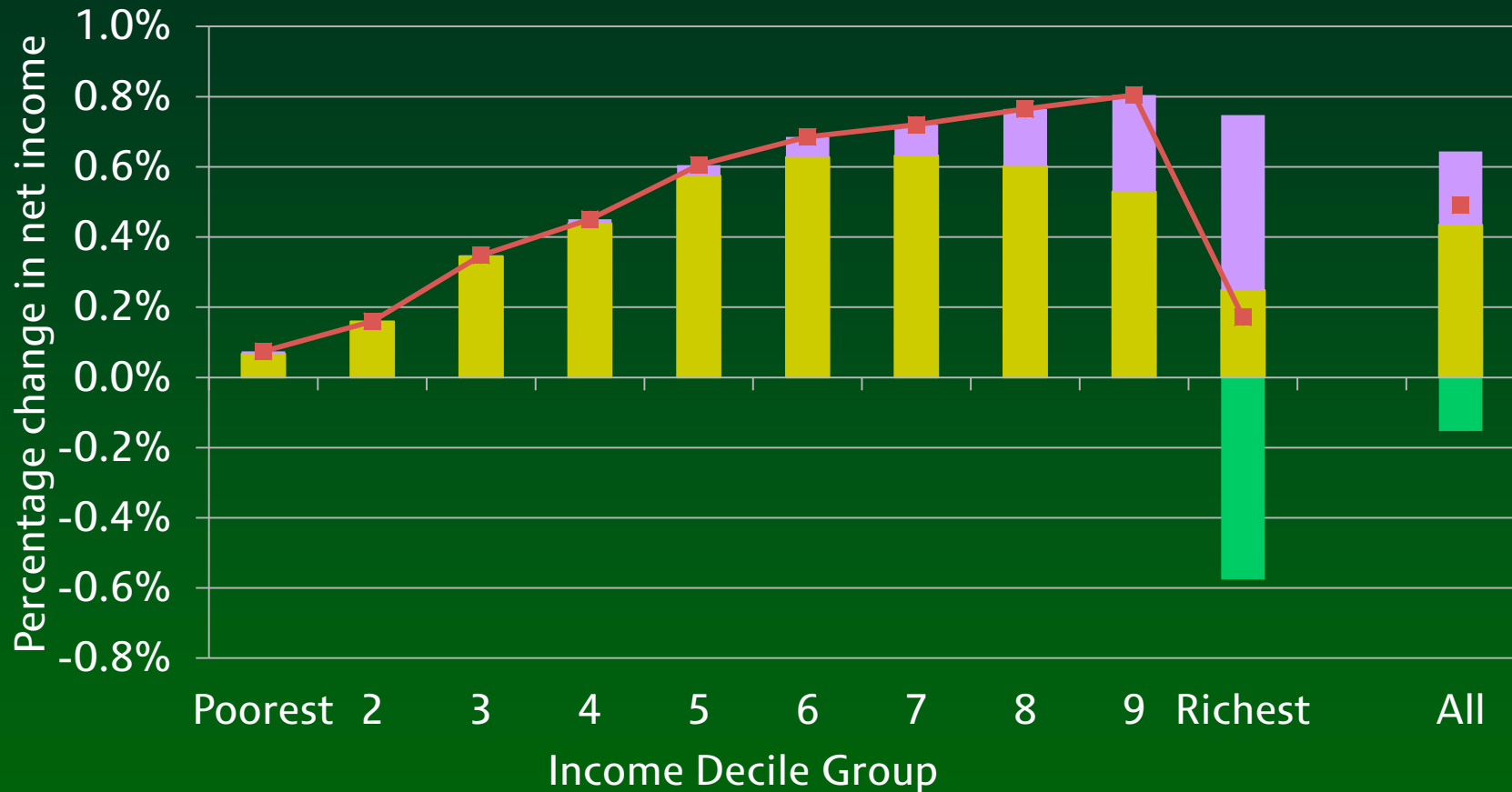
■ Higher rate threshold

■ Personal allowance



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# Distributional impact of the Conservative Party's income tax proposals



■ Restriction of pensions annual allowance
 ■ Higher rate threshold
 ■ Personal allowance
 —■ Total



# Labour: abolish transferable personal allowance, reintroduce 10% income tax rate

- Transferable personal allowance allows a non-taxpayer to transfer part of their personal allowance to their spouse, if they are a basic-rate taxpayer
  - One third of married couples benefit by up to £212 a year from this
  - Single-earner couples and pensioners: tend to be in lower-middle of income distribution
  - Costs £675 million a year
- Would allow a 10% tax rate to apply to the first £260 of taxable income: all with incomes more than £11k gain £26/year
  - Tiny range: why not increase personal allowance?
- Both policies very small: replacing one complication of income tax system with another

# Distributional impact of abolishing transferable personal allowance and Labour's 10p income tax rate



# Labour: increase additional rate of income tax to 50%

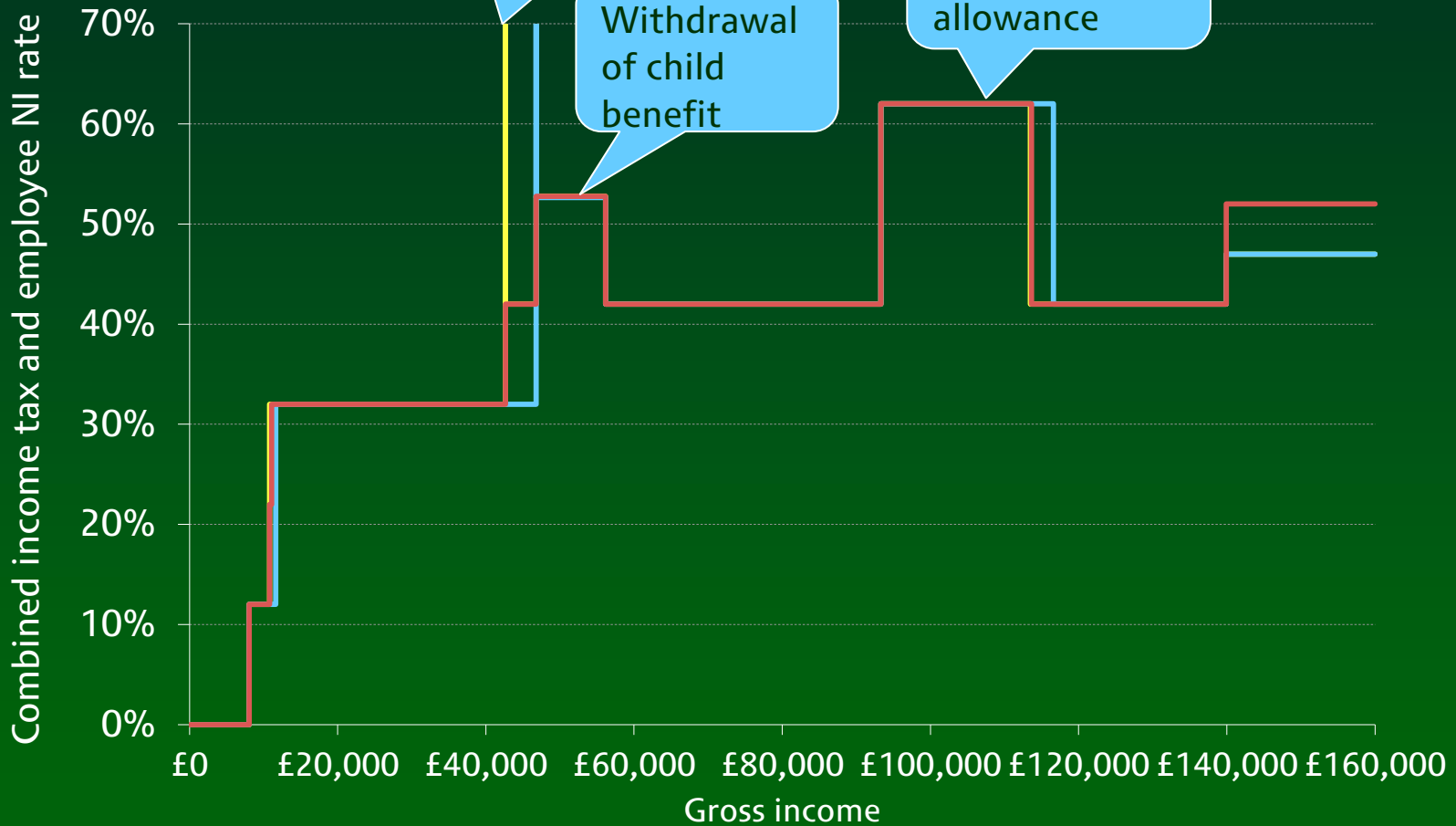
- Labour (and SNP) would increase the additional rate of income tax that applies above £150,000 to 50%
  - Affects highest-income 313,000 adults
- Would raise £3.6 billion a year if no behavioural change
- But big behavioural response likely
  - HMRC estimated that cut from 50% to 45% would cost just £110 million a year (though much uncertainty)
- Previous evidence has shown much of response increased use of tax deductions and shelters
  - Labour's anti-avoidance measures and restriction on tax relief on pension contributions may increase yield from this tax rise
- Even so, cannot rely on significant additional revenues from this

# The tax 2020-21 system

## 2020-21 system

### 20-21

#### le-earner couple



— Current plans    — Conservative proposals    — Labour proposals

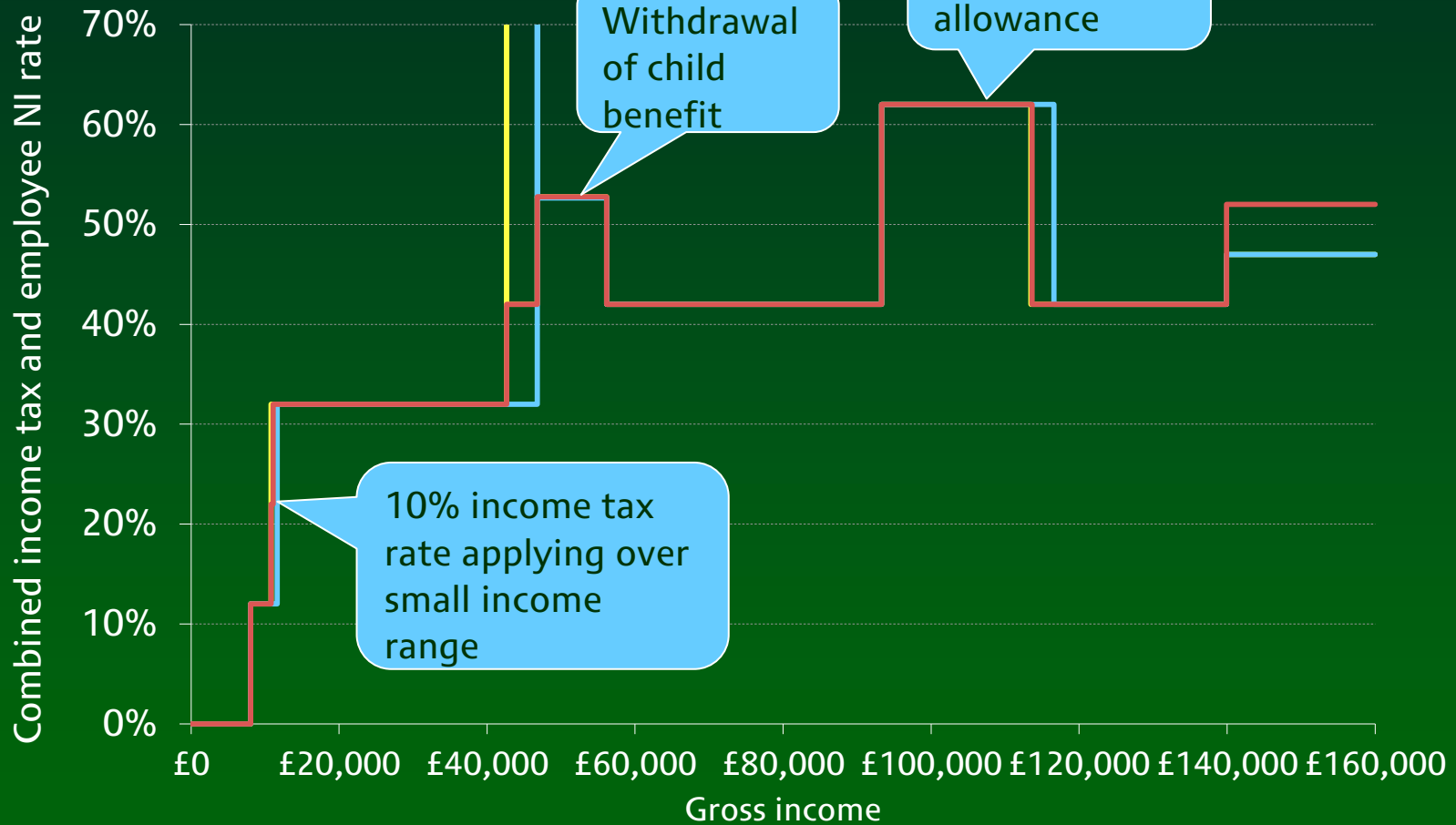
Note: assumes all income from employment, no pension contributions



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# The tax schedule in 2020–21

2020–21 system in current prices, single-earner married couple with one child



— Current plans    — Conservative proposals    — Labour proposals

Note: assumes all income from employment, no pension contributions



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# Restricting tax relief on pension contributions

- Much instability over last five years
- Would continue under both Conservatives and Labour
- Conservatives: reduce amount of contributions that attract income tax relief for those with incomes above £150,000
  - Sliding scale from £40,000 at £150,000 to £10,000 at £210,000
  - Expect this to yield £1.4 billion a year
- Labour: reduce annual allowance to £30,000 and give relief at 20% rather than marginal rate for those with high incomes
  - Income above £130,000 and incomes + employer pension contributions of more than £150,000
  - Together expected to yield £2.3 billion a year

# Problems with Conservative and Labour proposals on pensions tax relief

- Moving away from sensible system
  - Tax relief on contributions, returns untaxed, pay tax on withdrawals
- Conservative proposal would create strong disincentive for those with incomes £150-£210k to increase earnings
  - Why allow £40k of contributions at £150k but only £10k at £210k?
- Labour proposal creates ‘cliff-edge’ at £130,000
  - Why is relief at marginal rate ‘fair’ for 40%, but not 50%, rate taxpayers?
- Are better alternatives: remove genuine subsidies that exist in the current system:
  - Tax free lump sum: get up to £250,000 tax-free
  - Employer contributions not subject to NICs at any point: £14 billion a year exchequer cost

# Taxation of housing: Conservatives' inheritance tax proposal

- New transferable £175,000 main residence allowance in IHT
- Increases effective IHT threshold to £1 million for married couples
  - If main residence worth at least £350k
- Gradually withdrawn from estates worth more than £2 million, creating effective 60% IHT band
- Leaked HMT advice said 'not strong economic arguments' for this policy
  - Creates incentive to hold wealth in main home rather than downsize
  - Tax system already favours owner occupation



# Taxation of housing: 'Mansion tax'

- Labour: 'Mansion tax' on properties worth more than £2 million
  - Lib Dems and SNP have similar policy
- Banded structure similar to council tax
- Annual charge of £3,000 for properties worth £2 million-£3 million
- Revenue target of £1.2 billion will determine liabilities above that
- No one knows how many properties would be affected
- If 95,000 between £2 million and £3 million and 55,000 above £3 million, those above £3 million would pay £16,600 each on average
- Basic-rate and non-taxpayers will be able to defer payment (with interest) until sale or death

# Taxation of housing: 'Mansion tax'

- Strong case that high-value properties under-taxed at present
  - Council tax does not rise proportionally to property values
- Mansion tax at best only partly corrects for this
- But falls far short of solving all problems with property taxation
  - Council tax still based on 1991 values in England & Scotland
  - Better to solve problems with council tax than introduce new tax

# Anti-avoidance measures

- All three main parties rely on raising significant revenues from reducing tax evasion and avoidance
  - Conservatives £5bn, Labour £7bn, Lib Dems £10bn
- Some detail from parties, e.g.
  - Strengthened General Anti-Abuse Rule, OECD's BEPS proposals, non-dom taxation, ending 'shares for rights'
- But nowhere near enough to meet targets

## Other Labour policies

- Increase corporation tax from 20% to 21%. Yield: £1.0 billion
- Cut business rates by 3.8%. Cost: £0.2 billion
- Levy on tobacco firms. Yield: £0.2 billion
- Increase bank levy. Yield: £0.8 billion
- Stamp duty holiday for first time buyers. Cost: £0.2 billion
- Reintroduce stamp duty on collective investment schemes. Yield: £0.2 billion
- One-off bankers' bonus tax. Expected yield: £1.5-£2 billion
- One-off tax rebate to firms who raise all employees' wages to the 'Living Wage'

# Summary

- Conservatives propose small overall tax cut
  - Income tax & IHT giveaways just offset ‘takeaways’ from pensions tax relief and (unspecified) anti-avoidance measures
  - Biggest winners those with incomes between £50,000 and £150,000
- Labour propose £12.2 billion tax rise
  - More than half of this from unspecified anti-avoidance measures
  - Most of the rest from ‘the rich’ and companies
- Neither would do much to deal with fundamental problems of tax system and some measures would complicate further
- Both relying on anti-avoidance numbers plucked from thin air