Broad shoulders and tight belts: Options for taxing the better-off

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Background

• Income vs wealth
  – 10% of households receive 32% of pre-tax income
  – A different 10% of households (mostly aged 45-64) own 44% of wealth
  – Which of these groups (if either) does the government want to target?
• Tax payments very concentrated among high-income households
Cumulative shares of tax liability

Note: excludes corporation tax, business rates, stamp duties, CGT and IHT.
Source: Figure 9.4
Cumulative shares of tax liability

Cumulative percentage paid vs. Percentage of households

- % of tax-minus-benefits paid by highest-income households
- % of tax paid by highest-income households

Note: excludes corporation tax, business rates, stamp duties, CGT and IHT.
Source: Figure 9.4
Background

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  – Which of these groups (if either) does the government want to target?

• Tax payments very concentrated among high-income households
  – Highest-income 20% provide nearly half of the tax revenue we model
  – and provide over 80% of tax-minus-benefits

• Highest-income households hit more by fiscal consolidation to date than bottom half
  – Though the remainder of the top half haven’t
  – See Chapter 7

• *IF* wanted to raise more from the well-off, what are the options?
Distributional impact of 1p income tax rise
Assuming no behavioural response

Source: Figure 9.5
Distributional impact of 1p income tax rise
Assuming no behavioural response

Yield after some behavioural response:
- £1.1bn
- £5.7bn

Percentage of net income

Income Decile Group
- Poorest
- 2
- 3
- 4
- 5
- 6
- 7
- 8
- 9
- Richest
- All

Higher rate
All rates

Source: Figures 9.5 and 9.6
Capital gains tax

• Raises £3.7bn in 2012-13
  – Half comes from 3,000 people realising gains >£1m

• Simplest options: increase rates or reduce allowance
  – Each percentage point on higher rate raises £80m

• But there are better options
  – Merge income tax and CGT allowances
  – ‘Forgiveness’ of CGT on death costs £490m
  – Entrepreneur’s relief costs £1.7bn (ignoring behavioural response)
Taxation of private pensions

• Currently give income tax relief on pension contributions, up to limits
  – Tax pension income instead (but can take 25% as tax-free lump sum)

• One option: reduce limits on contributions
  – Coalition is already reducing annual limit from £255,000 to £40,000 and lifetime limit from £1.8m to £1.25m – could go further

• There are worse options
  – Restricting tax relief to the basic rate would be a bad idea

• But there are better options too
  – Cap tax-free lump sum (from April 2014, up to £312,500 can be tax-free)
  – Change NICs treatment of employer pension contributions (costs £13bn)
Inheritance tax

• Raises £3.1bn in 2012-13
  – Two-thirds comes from 3,500 estates worth >£1m

• Simplest options: increase rate or reduce threshold
  – Each percentage point on rate raises £80m

• But there are better options available
  – Abolish relief for business assets and agricultural land (cost £700m)
  – Tax gifts made >7 years before death
Taxation of housing

- Stamp duty land tax is a bad tax
  - Why impose heavier tax on properties that change hands more often?
  - Properties should be owned by the people who value them most
  - Should be abolished, not increased

- Taxing property values makes more sense
  - But council tax should be proportional to up-to-date property values
  - Minimally, could increase council tax rates on high-band properties
Distributional impact of doubling high-band council tax

<table>
<thead>
<tr>
<th>Income Decile Group</th>
<th>Band H (0.6% of dwellings)</th>
<th>Band G (3.5% of dwellings)</th>
<th>Band F (5.0% of dwellings)</th>
<th>Band E (9.4% of dwellings)</th>
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<tbody>
<tr>
<td>Poorest</td>
<td>-0.2%</td>
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<tr>
<td>Richest</td>
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</tr>
<tr>
<td>All</td>
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<td>-0.6%</td>
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</tr>
</tbody>
</table>

Source: Figure 9.9
Conclusions

- Government should be clear who (if anyone) they want to target
  - High income or high wealth?
  - Top half? Top 10%? Top 1%?
- Simplest way to target better-off is to increase rates of IT, NICs, VAT
- There are many unattractive options
  - Wealth tax, SDLT, restricting tax relief on pension contributions
- But also many more attractive options
  - CGT on death, entrepreneur’s relief, merge CGT & income tax allowances
  - Pensions lump-sum and NICs treatment of employer contributions
  - IHT on business and agricultural property and >7 years before death
  - Council tax proportional to up-to-date values
- Improve existing taxes before thinking about new ones