



Institute for
Fiscal Studies

Tax measures

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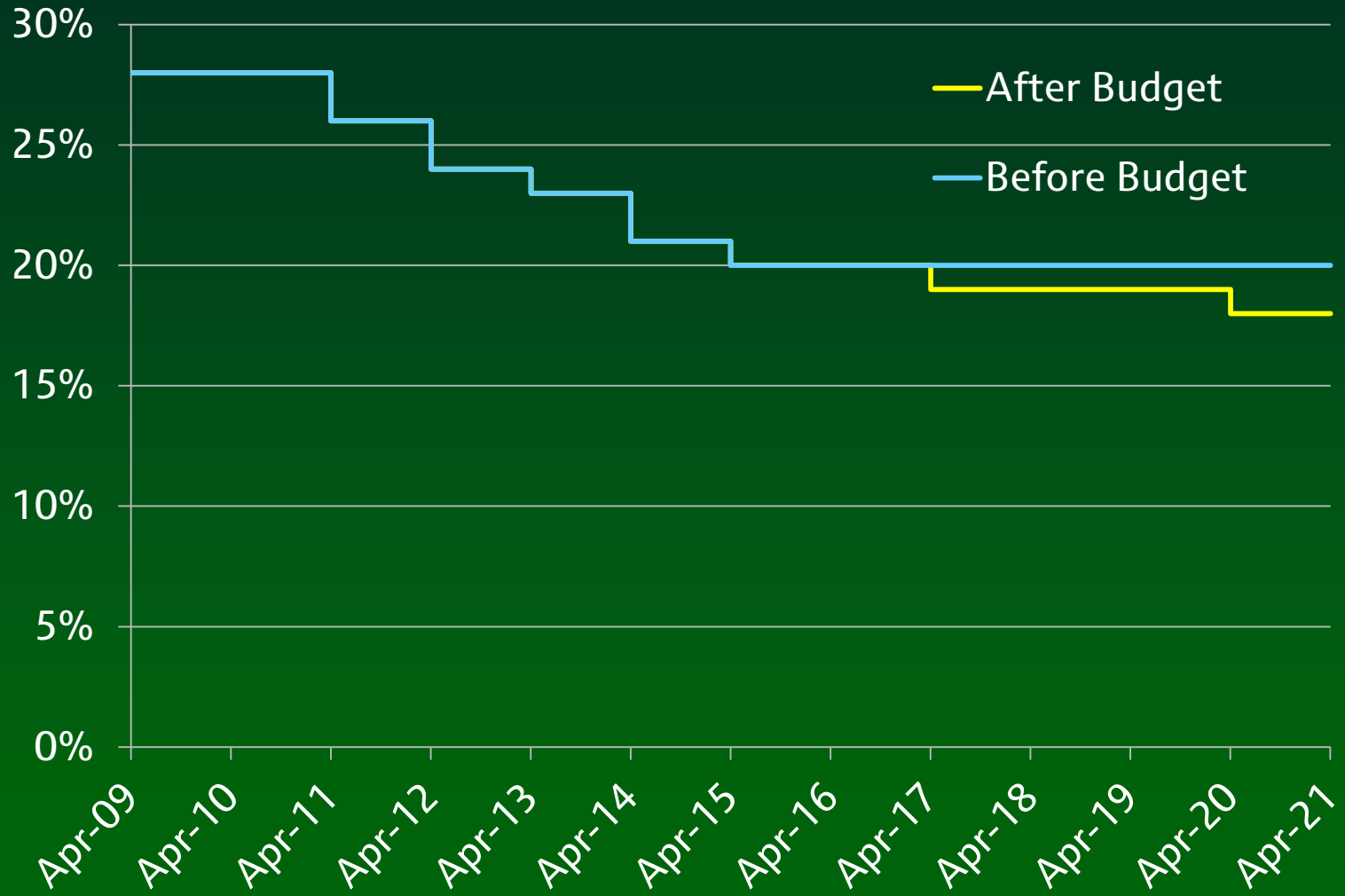


Personal allowance and higher rate threshold

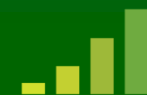
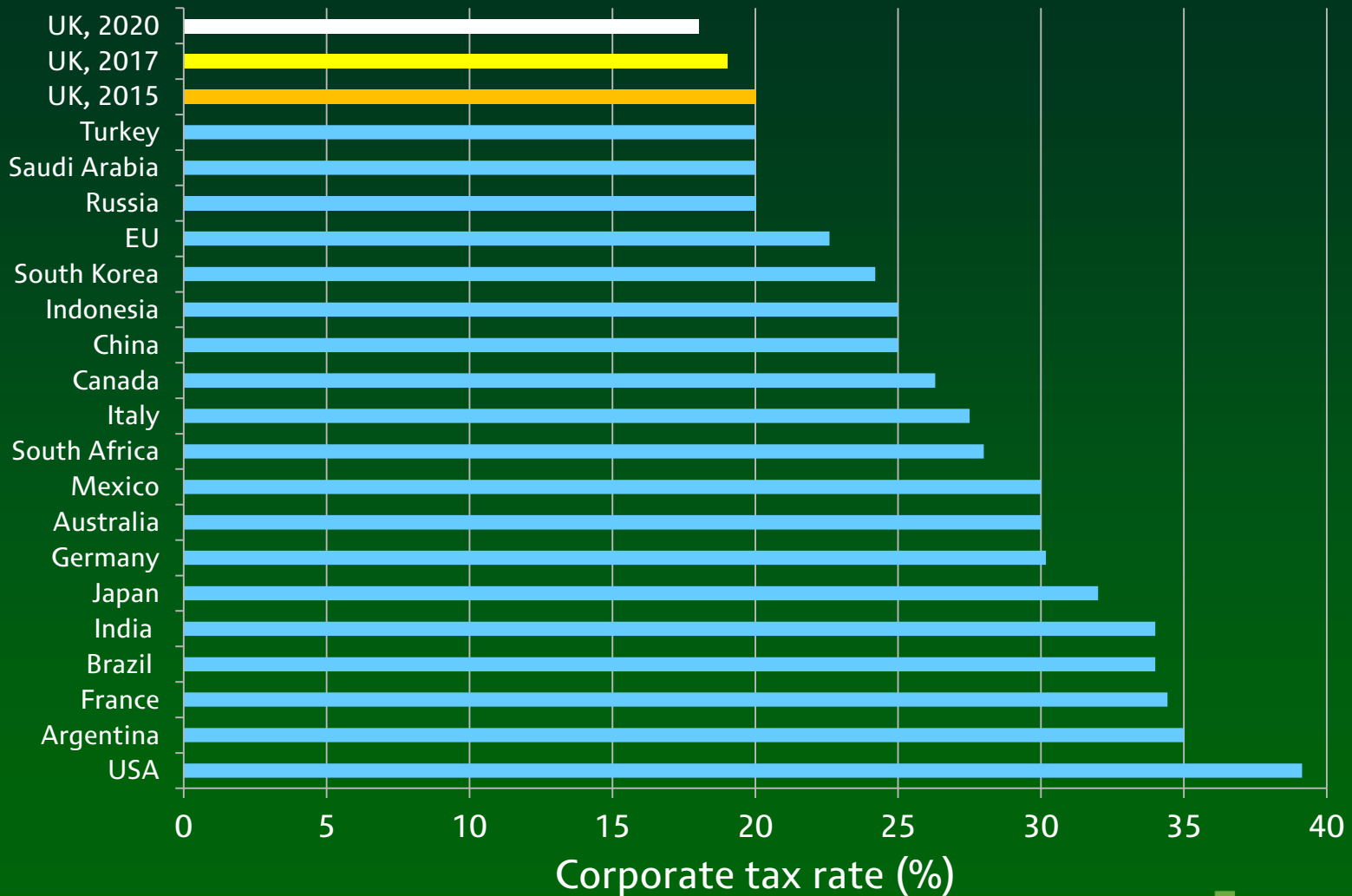
- Income tax personal allowance to continue to increase faster than inflation, to £11,000 in 2016–17 and £11,200 in 2017–18
 - Had previously said would increase to £10,800 in 2016–17 and £11,000 in 2017–18
 - Costs £1.2bn in 2017–18
 - Basic rate taxpayers £40 a year better off
- Higher rate threshold will increase to £43,000 in 2016–17
 - Costs £0.2bn in 2017–18
 - Higher rate taxpayers with incomes less than £122,000 gain £70 a year from combination of two policies
- Total cost of changes to personal allowance and higher rate threshold between 2010–11 and 2017–18 will be about £11bn
 - Basic rate taxpayers will be £597 a year better off in 2017–18 as a result of these changes
 - Higher rate taxpayers will be £442 a year worse off



UK headline corporation tax rate



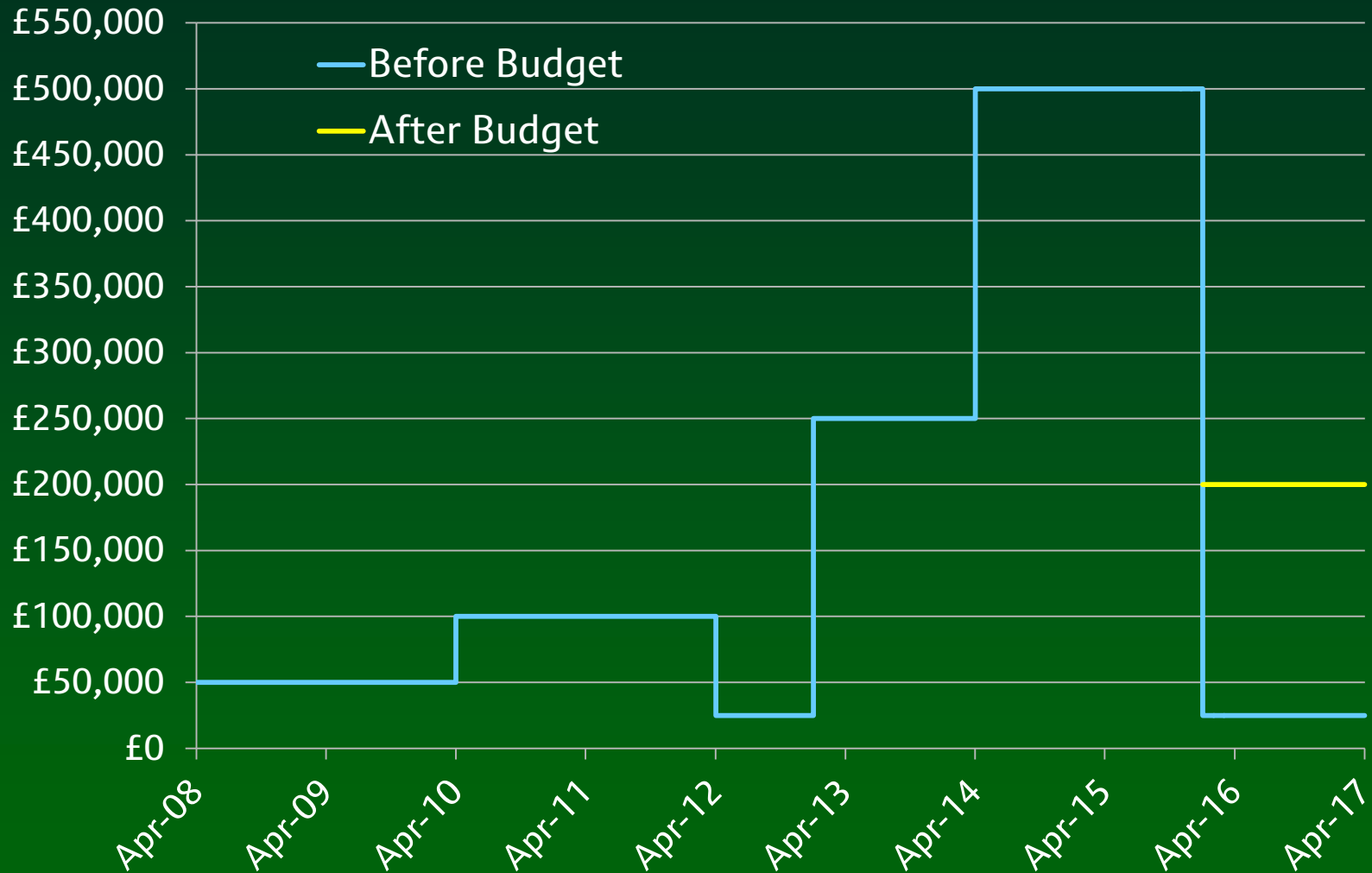
Statutory corporate tax rates in the G20, 2015



Corporation tax changes

- Rate cut from 20% to 19% in April 2017 and 18% in April 2020
 - Costs £2.5bn in 2020-21, but will be nearer £4bn thereafter
- Annual investment allowance set at £200,000 from January 2016
 - Costs £0.8bn

Annual investment allowance



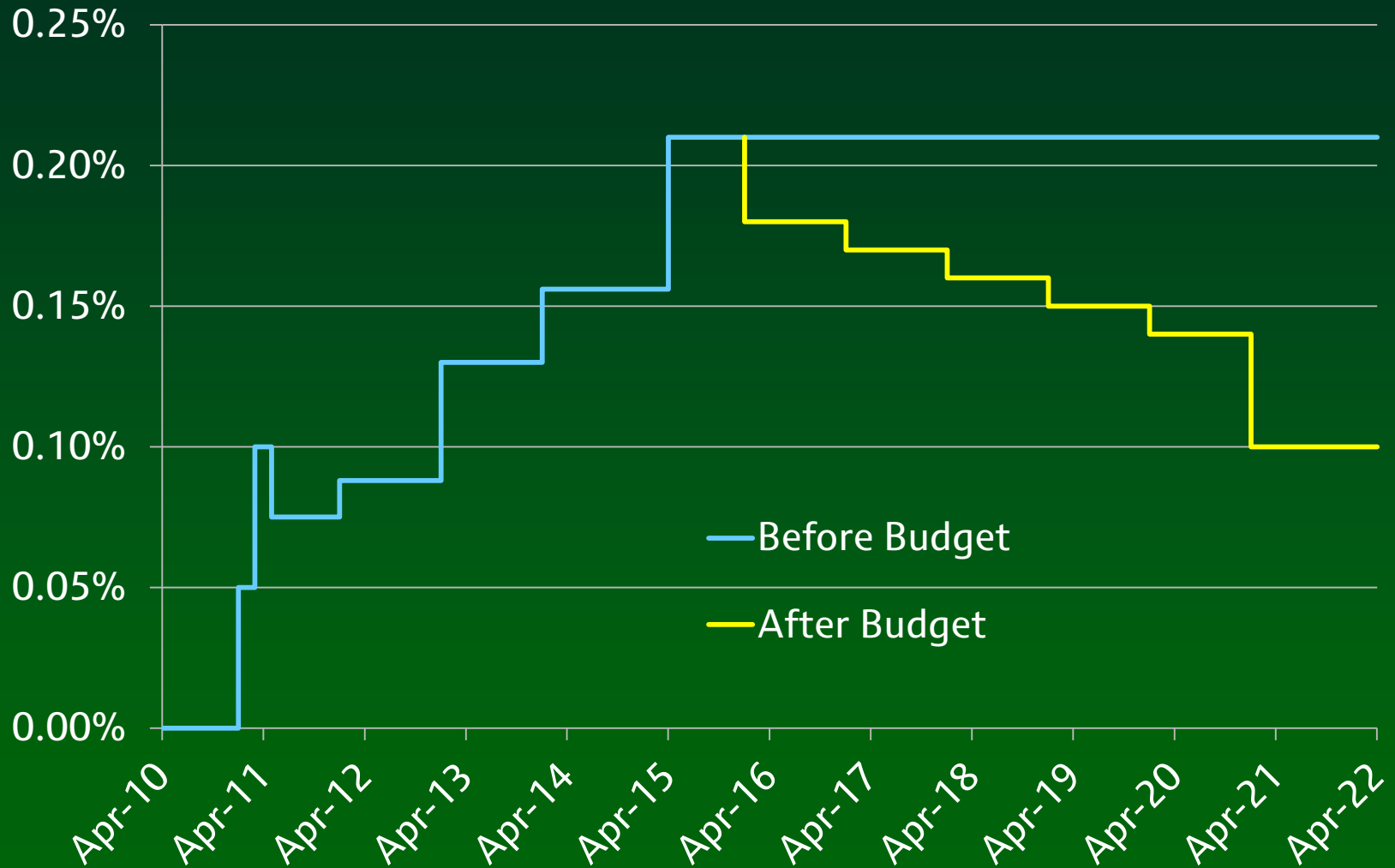
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 - Costs £2.5bn in 2020-21, but will be nearer £4bn thereafter
- Annual investment allowance set at £200,000 from January 2016
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- Companies making profits \geq £20m must pay tax 3 months earlier
 - Raises one-off £7.8bn

Taxing banks

- Bank levy gradually reduced from 0.21% to 0.10% by January 2021
 - By 2021 there will have been 13 tax rates in 10 years

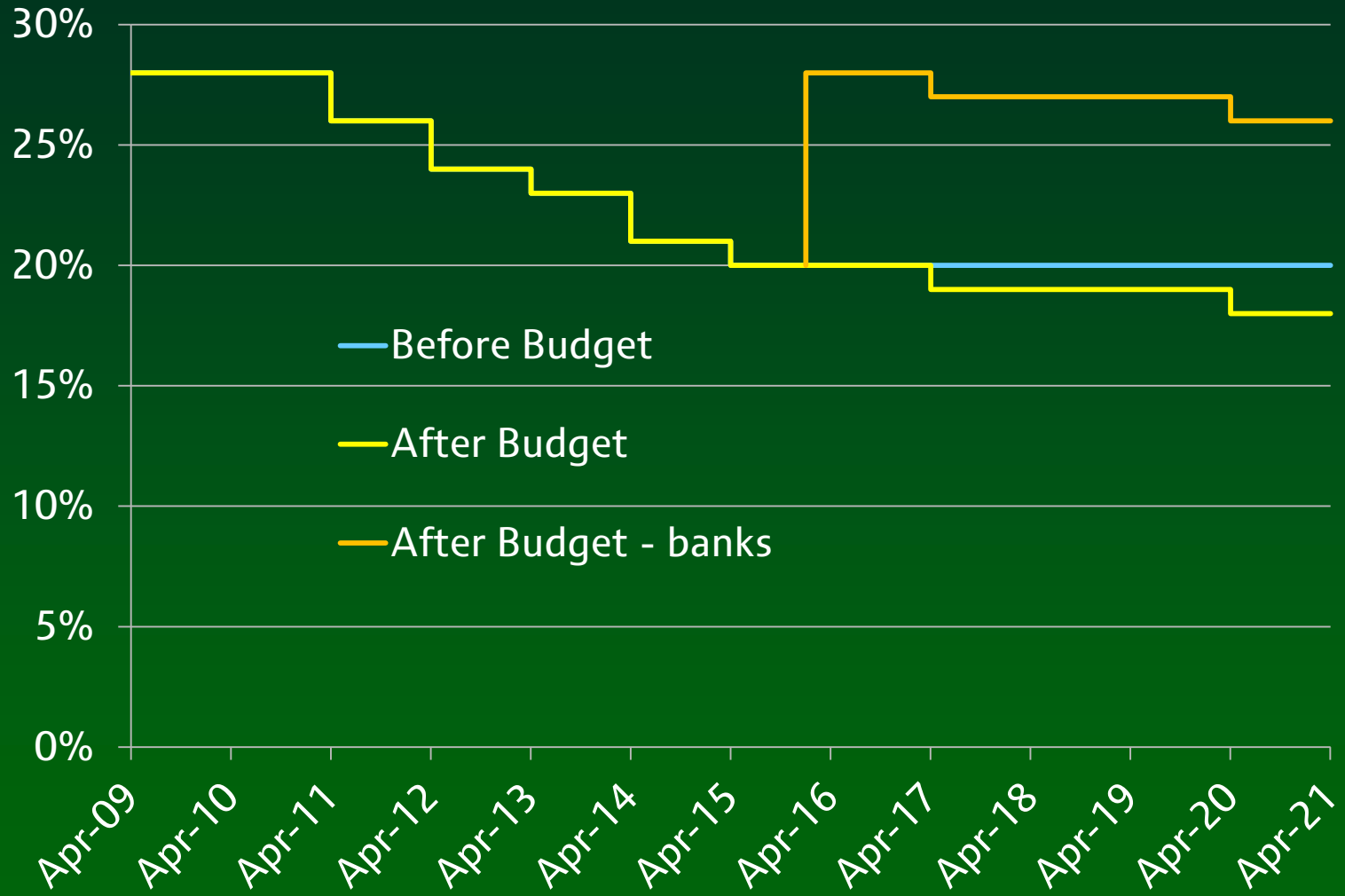
The bank levy



Taxing banks

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 - By 2021 there will have been 13 tax rates in 10 years
 - Costs £1.8bn from 2021-22
- UK banks taxed only on liabilities in the UK, not worldwide, from 2021
 - Significant giveaway, a large slice to HSBC
- 8% corporation tax surcharge on bank profits from January 2016
 - Raises £1.3bn

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- 8% corporation tax surcharge on bank profits from January 2016
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- What is the rationale for a higher corporation tax rate for banks?
 - Bank levy designed to discourage risky leverage (with mixed success)
 - But corporation tax just discourages declaring UK profits
 - Future profits not a good proxy for cost of past bail-outs, future risk posed, implicit insurance provided,...
 - Maybe profits less responsive (e.g. internationally mobile) than profits of other companies?

Dividend tax changes (1/3)

- Dividends outside pensions and ISAs subject to income tax
 - In 2012–13, 4.6m taxpayers received £45bn of taxable dividends
 - Mixture of portfolio investors and company owner-managers
- Effective tax rates currently 0% (basic), 25% (higher), 30.6% (additional)
 - Lower than ordinary income tax rates
 - Partly reflects corporation tax already paid: combined rates 20%, 40%, 44%
 - But no NICs on dividends → incentive to set up company and take dividends
 - Lighter taxation of dividends also reduces disincentive to invest
- Budget announced significant reform
 - Effective tax rates all increased by 7.5 percentage points from April 2016
 - But first £5,000 of dividend income to be tax-free
 - Raises £2.5bn

Dividend tax changes (2/3)

- **Winners:**
 - Higher-rate taxpayers receiving dividends of less than £21,667
 - Additional-rate taxpayers receiving dividends of less than £25,250
- **Losers:**
 - Higher- and additional-rate taxpayers receiving dividends above those levels
 - Basic-rate taxpayers receiving dividends of more than £5,000
- **Unaffected:**
 - Basic-rate taxpayers receiving dividends <£5,000
 - People holding shares within pensions or ISAs

Dividend tax changes (3/3)

- Less (more) incentive to set up as a company if would be a loser (winner)
 - Government thinks this reduces cost by £0.6bn
- Less incentive to take dividends (above £5,000) rather than salary
- Disincentive to save heavily in shares (outside pensions and ISAs) and to generate profits and dividends
 - Government thinks this increases cost by £1.0bn
- These incentives partly offset by cut in corporation tax rate
- Now separate tax-free allowances for savings income, dividend income and capital gains as well as the basic income tax allowance
 - If use all of them, can receive over £28,000 a year free of income tax/CGT
 - Why favour people who receive money in a variety of forms?

Restricting mortgage interest relief for landlords

- Mortgage interest payments currently tax-deductible for landlords
- Budget announced restriction of tax relief to the basic rate
 - To be phased in over 4 years from April 2017
 - Raises £0.7bn from high-income landlords
- Budget speech: ‘landlords have a huge advantage in the market as they can offset their mortgage interest payments against their income, whereas homebuyers cannot.’
- Nonsense
 - Landlords taxed on rental income and capital gains
 - Owner-occupiers not taxed on (implicit) rental income and capital gains
 - Deduction of costs is appropriate counterpart to tax on returns
- Exacerbates tax bias towards owner-occupation

Inheritance tax

- New transferable main residence allowance
 - £100k in 2017–18, rising by £25k a year until reaches £175k in 2020–21
 - Increases effective IHT threshold to £1m for married couples (if main residence worth at least £350k)
- Also £325,000 threshold to be frozen in cash terms until March 2021
 - already frozen from April 2009 to March 2019
- Overall cost of both policies £940m in 2020–21

New transferable main residence allowance

- Similar to policy discussed in Treasury document leaked to Guardian (published 17 March 2015):
- *‘There are not strong economic arguments for introducing an inheritance tax exemption specifically related to main residences’*
- *‘Some commentators, including the IFS, are very likely to make these points and be critical’*
 - Increases bias towards buying owner-occupied housing over other assets
 - Pushes up house prices
 - Inequitable that some smaller estates attract more IHT than larger ones simply because a smaller proportion is held in property

Reducing pension annual allowance for high earners

- Maximum tax-relieved contribution reduced for those with incomes (including employer contributions) above £150k from April 2016
 - Sliding scale from £40k at £150k to £10k at £210k
 - Expected to raise £0.9bn in 2018–19
- Continues instability of last five years
- Moving away from sensible system
 - tax relief on contributions, returns untaxed, pay tax on withdrawals
- Why allow £40k of contributions at £150k but only £10k at £210k?
- Strong disincentive to increase income between £150k and £210k

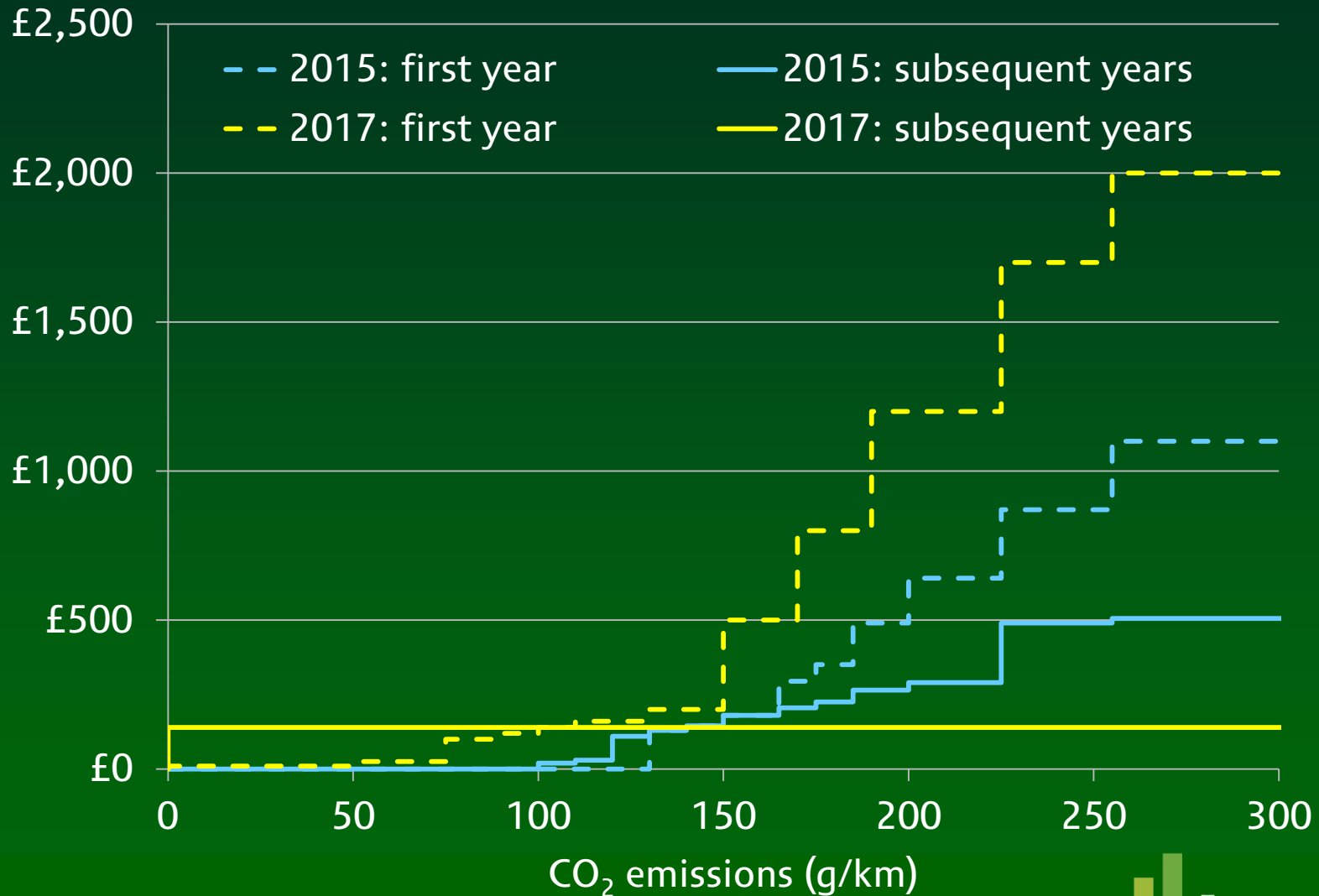
- ‘we will not propose any further changes to the system during the next Parliament’ – Conservatives, 12 April 2015. But now...

Consultation on pensions taxation

- Government to consult on whether to keep current approach or move to something more like ISAs
 - potentially with a government top-up
- Big difference is that tax would be collected up front
 - bad: individuals would not be able to ‘tax-rate smooth’
 - bad: above-normal returns would not be subject to tax
 - good: top-up could improve on existing subsidies
- In 2013–14 income tax and NICs revenues would have been flattered by up to £41bn
 - much would represent revenues simply being brought forward rather than a true strengthening in the public finances
 - could we trust successive governments to run appropriately stronger headline fiscal position?
 - could we trust future governments not to tax pensions twice over?



VED for new cars to raise £1.4bn in 2020-21



Other indirect tax rises

- Climate change levy exemption for renewables ended
 - Raises £0.9bn
 - Why tax business use of renewable-sourced electricity?
 - Should be aiming for consistent pricing of carbon emissions
- Insurance premium tax increased from 6% to 9.5% from Nov 2015
 - Raises £1.6bn
 - Why tax business use of insurance?
 - Should be aiming to apply VAT to insurance instead

Other notable tax announcements

- NICs employment allowance increased from £2,000 to £3,000
 - But abolished for firms with a single employee
 - Raises £0.6bn
- Broadly sensible reform to taxation of ‘non-doms’
 - Raises £0.5bn
- Lots of anti-avoidance and -evasion measures
 - £2.8bn a year from tackling evasion would be a huge return on investment in HMRC
- Lots of consultations and reviews
- Confirmed intention to legislate to ‘prevent’ increases in headline rates of income tax, NICs or VAT
 - Can’t bind future selves – and why should they need to?

Summary: winners and losers

Winners:

- Most income tax payers, a bit
- Wealthy home-owners and their descendents
- High-income people receiving modest dividends
- Most companies (i.e. their customers/employees/shareholders)

Losers:

- High-income people saving a lot in a pension or renting out property
- People receiving large dividends
- UK-born / long-term resident non-doms
- People buying insurance or (after 2017) new cars
- Firms using insurance or renewable-source electricity
- Highly profitable, low-leverage banks
- Tax evaders

Conclusions

- Huge number of major reforms
- Hard to discern a theme or strategy
- Several of the changes make no economic sense
 - Buy-to-let mortgage relief, VED hypothecation, CCL on renewables, IHT main residence relief, pension annual allowance withdrawal
- Announcing paths for future tax rates raises hopes of future stability
 - Rates of corporation tax, annual investment allowance and bank levy as well as income tax, NICs and VAT
- The more uncertain costings are almost all revenue-raisers