The fiscal squeeze and tax and welfare changes affecting low-earning individuals

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Presentation to Low Pay Commission, London
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The cure (December 2013): 11.1% national income consolidation over 10 years (£209bn)

Dec 2014: 8.8% national income (£165bn) hole in public finances

Sources: HM Treasury; OBR; Author’s calculations.
Impact of tax and benefit reforms
January 2010 - April 2015 inclusive

Change in net income

-14% -12% -10% -8% -6% -4% -2% 0% 2% 4%

Income decile group

Poorest 2 3 4 5 6 7 8 9 Richest All

- Households with children
- Pensioner households
- Working-age without children

Source: Browne and Elming (2014). Assumes full take-up of means-tested benefits and tax credits.
Income tax allowance changes in April 2015

• Main personal allowance up £480 in real terms to £10,600 – annual real gain of up to £96
  – Brings real increase over this parliament to £2,835 (gain of £567 per year for basic rate income taxpayers)
  – (Even) less targeted on lowest earners now that PA is much higher
  – For those on low incomes, 65% of gains can be lost via reduced housing benefit; typically around 20% via reduced council tax support (depends on local taper rate)

• Transferable allowance of £1,060 introduced for married couples
  – Gain of up to £212 per year for basic rate taxpayers whose spouse is not a taxpayer (1/3 of married couples benefit)
  – Take-up assumed to be 70-75% initially, growing to above 85% within a few years
Cuts to employer NICs for young workers

• Employer NICs abolished on earnings below £815 p/w for workers under 21, from April 2015
  – Would otherwise have been 13.8% on earnings above £153 p/w
  – So affects only full time workers if on minimum wage: those on the 18-20 /under 18 rates working at least 30/40 hours p/w

• Typically would expect employer NICs cuts to be (at least partly) passed on to workers as higher wages

• Where minimum wage binds we would expect less pass-through to wages (and higher employment or profits or lower prices instead)

• A given minimum wage for under-21s will be less binding than before for many full-timers
  – ...and less binding than before relative to the main minimum wage (possible substitution between employees just under and just over 21?)
Benefit entitlements

- Continuation of 3-year policy: most benefits/tax credits increased by 1% in April 2013, 2014 and 2015
  - Pensioners and more severely disabled largely protected
  - Given the fall in inflation this now looks like being a very small real cut (at most) in 2015-16

- NB maximum Housing Benefit entitlements for private sector renters included in 1% rule – bigger impact in areas with higher rent growth
  - And after 2015 these entitlements will be CPI-indexed (not rent-indexed)

- Affects in-work and out-of-work benefits
  - Mixed impacts on work incentives
More Universal credit delays

• Further delays to UC have been announced this year

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<thead>
<tr>
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<th>Original plan</th>
<th>Current plan</th>
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<tbody>
<tr>
<td>Roll-out started everywhere</td>
<td>October 2013</td>
<td>March 2016</td>
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<tr>
<td>All new claims are to UC</td>
<td>April 2014</td>
<td>December 2017</td>
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<td>All existing claims migrated</td>
<td>December 2017</td>
<td>Most by December 2019</td>
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• In addition OBR now assuming that current plans won’t be delivered on time, reflecting past “optimism bias” in rollout plans

• Current OBR assumption involves 2.9m fewer UC claimants in 2017-18 than it assumed one year ago
Vintages of the universal credit roll-out assumption

Source: Chart D in OBR Economic and Fiscal Outlook, December 2014.