

Institute for
Fiscal Studies



The distributional impact of tax and benefit reforms by region

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What's coming up

- Methodology
- Average losses from tax and benefit reforms for each region
- Drill down further for London:
 - Examine average losses by income quintile
 - And for different types of family

What are we trying to measure?

- Direct impact of tax and benefit measures on household incomes
 - As if they were implemented overnight
- This means that we assume that there is no behavioural response, and that reforms do not change pre-tax prices in the economy
 - More plausible in some cases than others (e.g. VAT, Housing Benefit)
- Obtain an average cash loss for households in each region, and express this as a percentage of the average household income for each region
- Tax and benefit system and reforms apply (almost) equally across the country
- Any differences between regions reflect differences in distribution of income, demographics, rent levels etc rather than deliberate policy decisions

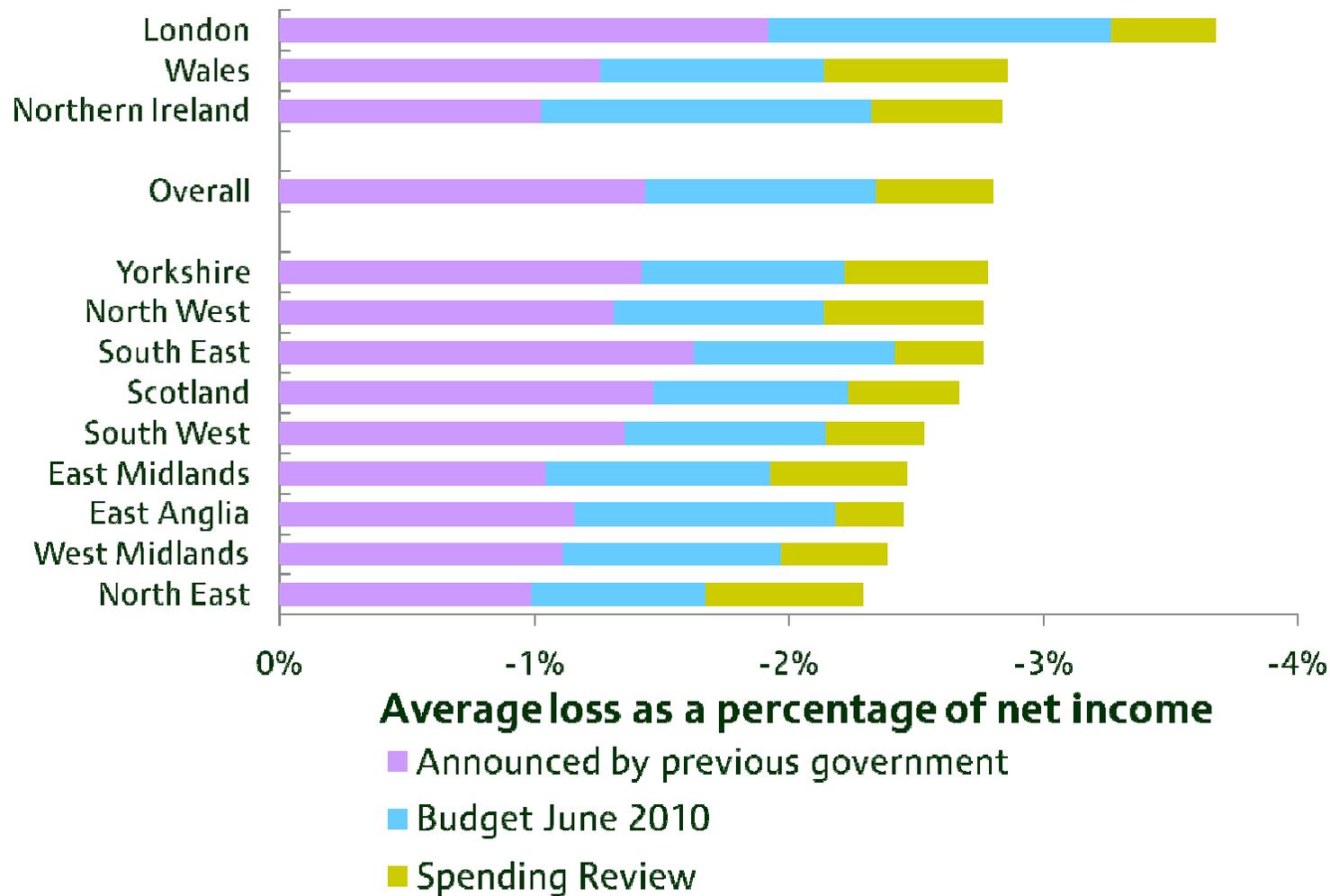
What are the tax and benefit changes under consideration?

- All personal tax and benefit changes to be introduced between April 2010 and April 2014
- Key tax changes are
 - 1ppt increase in all NI rates (from April 2011)
 - Reduction in real value of higher rate threshold
 - Restriction of tax relief on pension contributions
- Key benefit changes are
 - Use of CPI rather than RPI/Rossi index to uprate benefits
 - Withdrawal of child benefit from higher-rate taxpayers
 - More aggressive means-testing of tax credits
 - Cuts to housing benefit
 - Time-limiting contributory ESA for work-related activity group
 - New disability test for DLA recipients

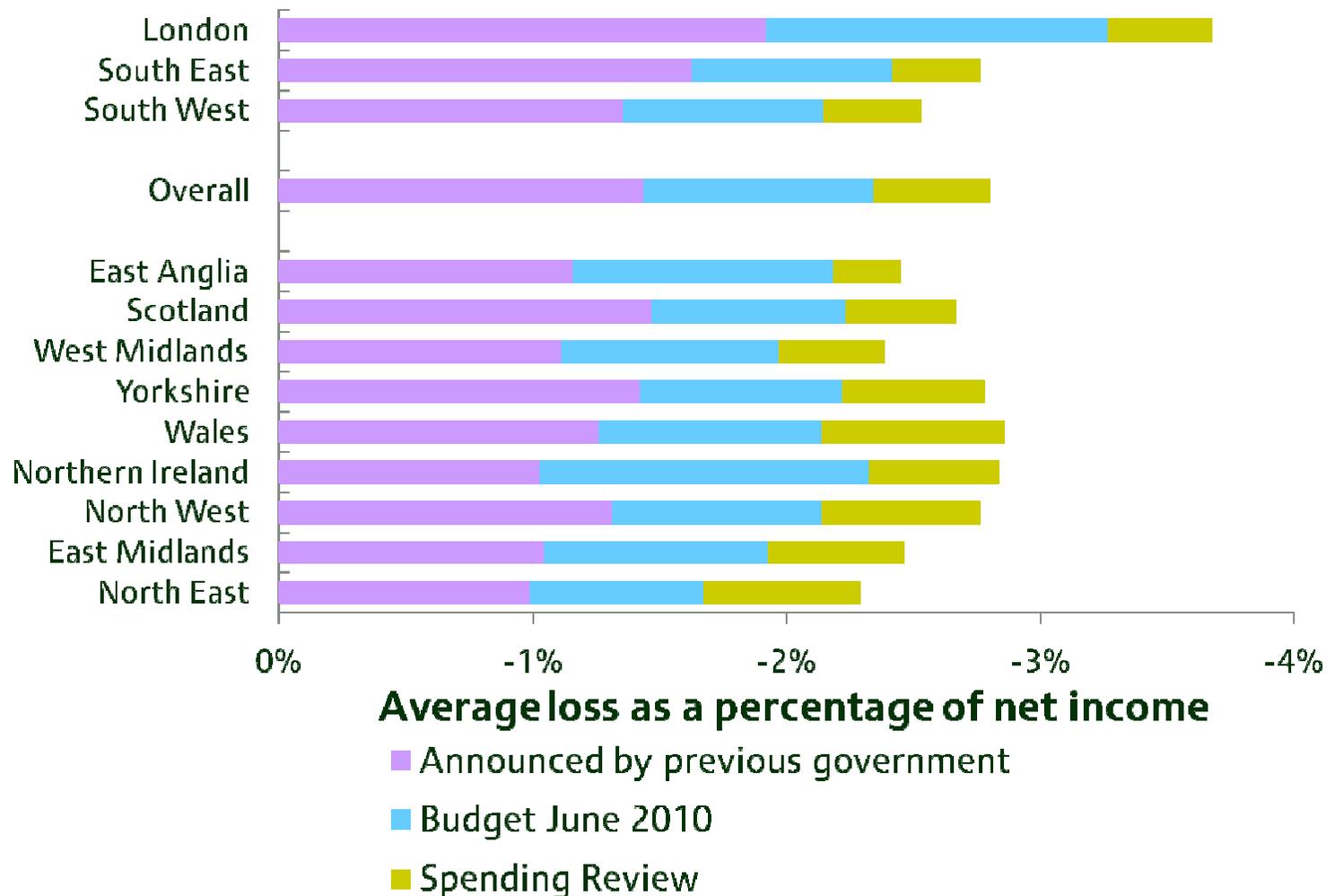
How do we calculate losses from tax and benefit changes?

- IFS tax and benefit microsimulation model, TAXBEN can calculate precise tax liabilities and benefit entitlements under ‘unreformed’ and ‘actual’ tax and benefit systems in most cases
- Cannot measure the impact of some reforms on particular households precisely, e.g.
 - Time-limiting contributory Employment and Support Allowance
 - Stricter disability test for Disability Living Allowance
 - Changes to the way in which in-year income changes affect tax credit awards
 - Localisation and reduction in spending on Council Tax Benefit
- This is because of limitations in the FRS data we use
- We think that we can roughly estimate the distributional impact of these reforms
 - Can identify likely losers and take benefits away from them

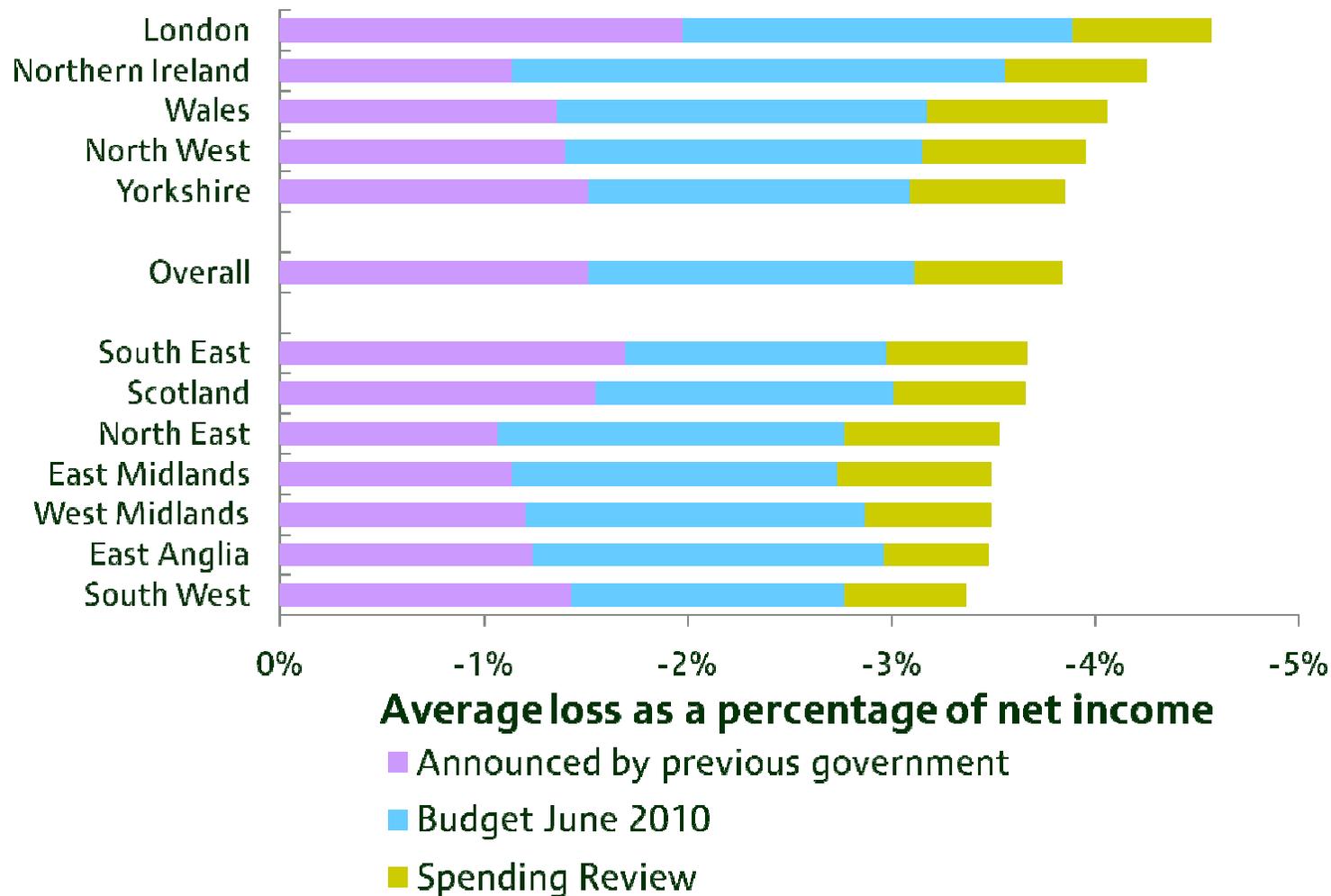
Average loss by region from reforms to be in place by 2012–13



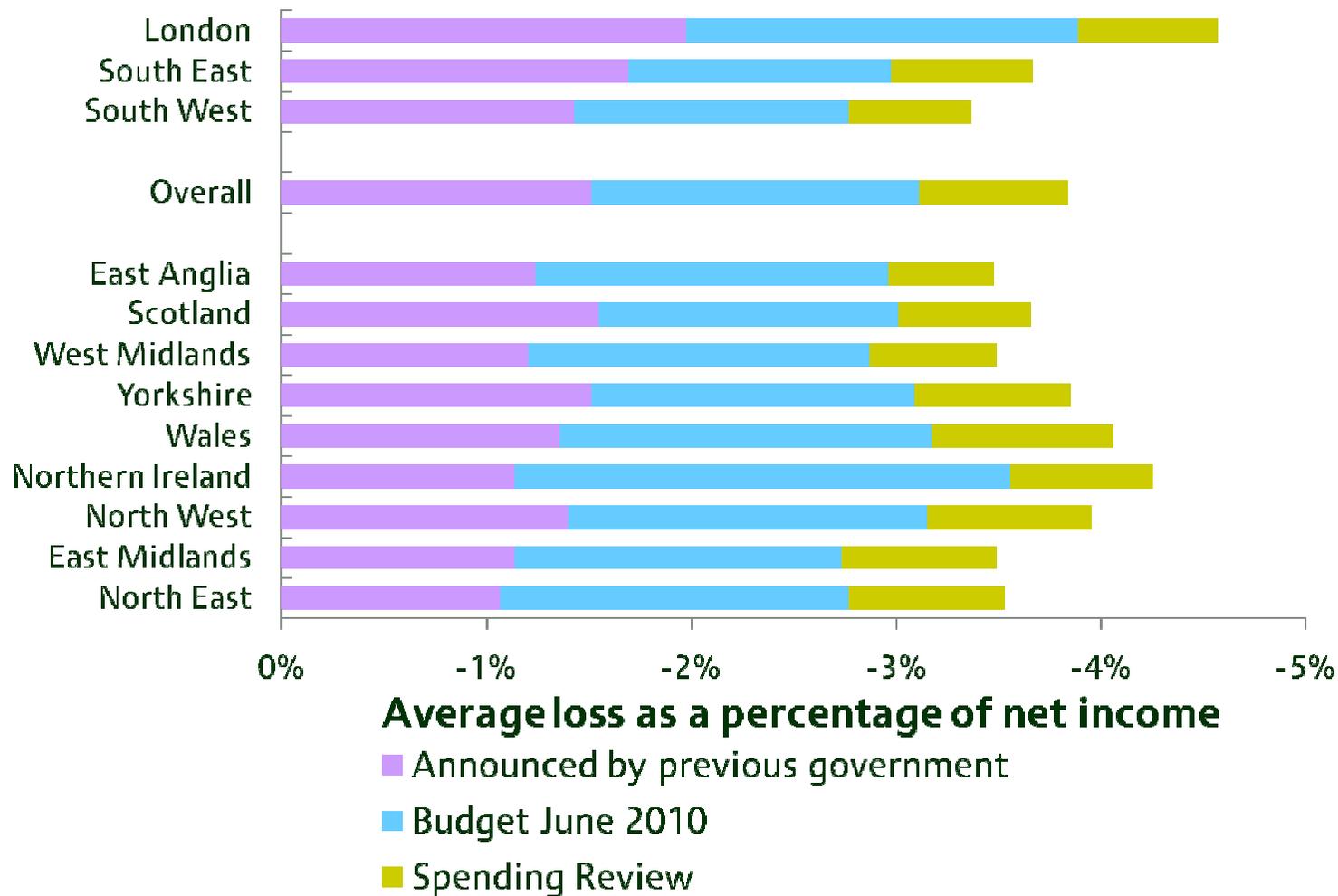
Average loss by region from reforms to be in place by 2012–13 (ranked richest to poorest)



Average loss by region from reforms to be in place by 2014–15



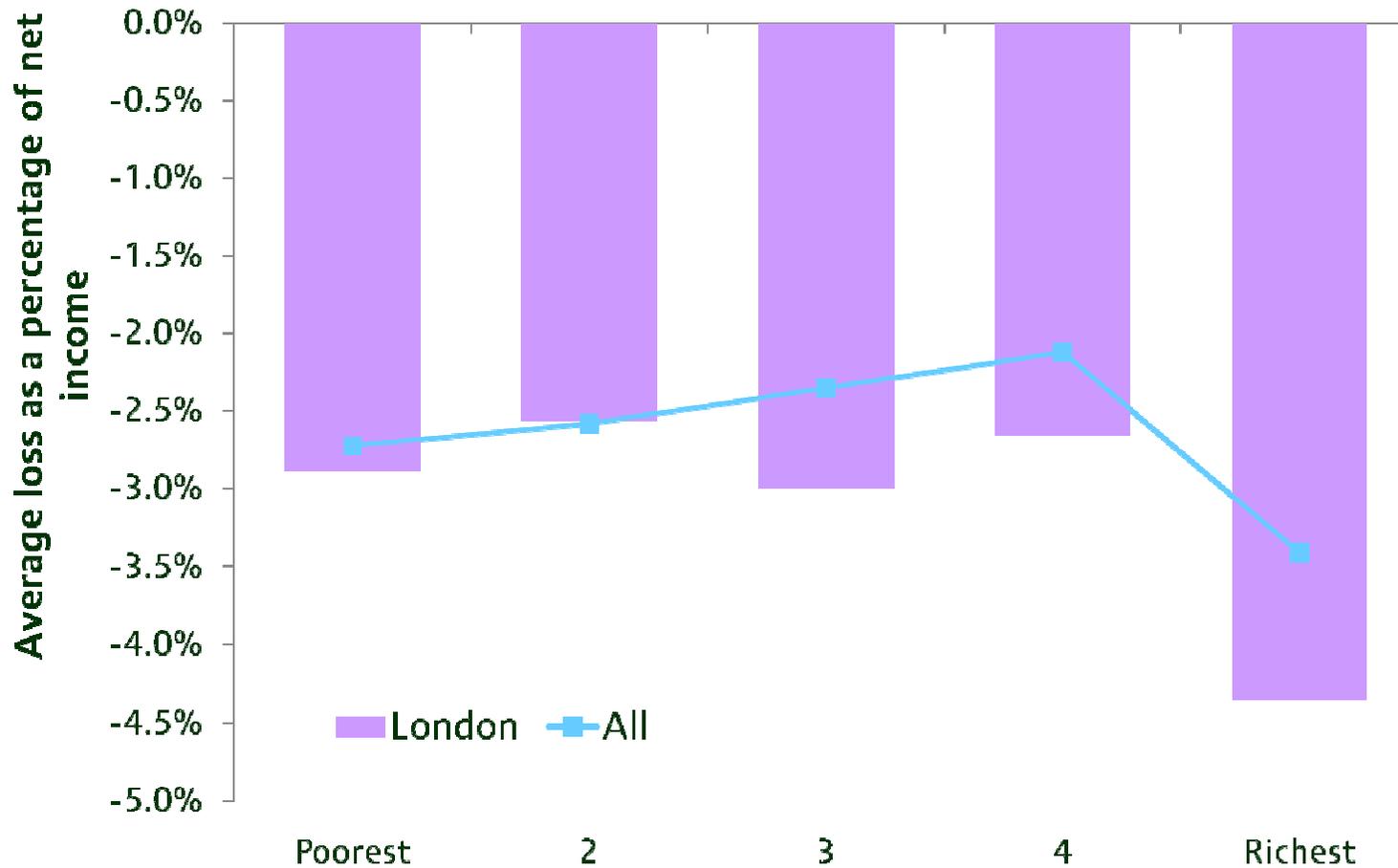
Average loss by region from reforms to be in place by 2014–15 (ranked richest to poorest)



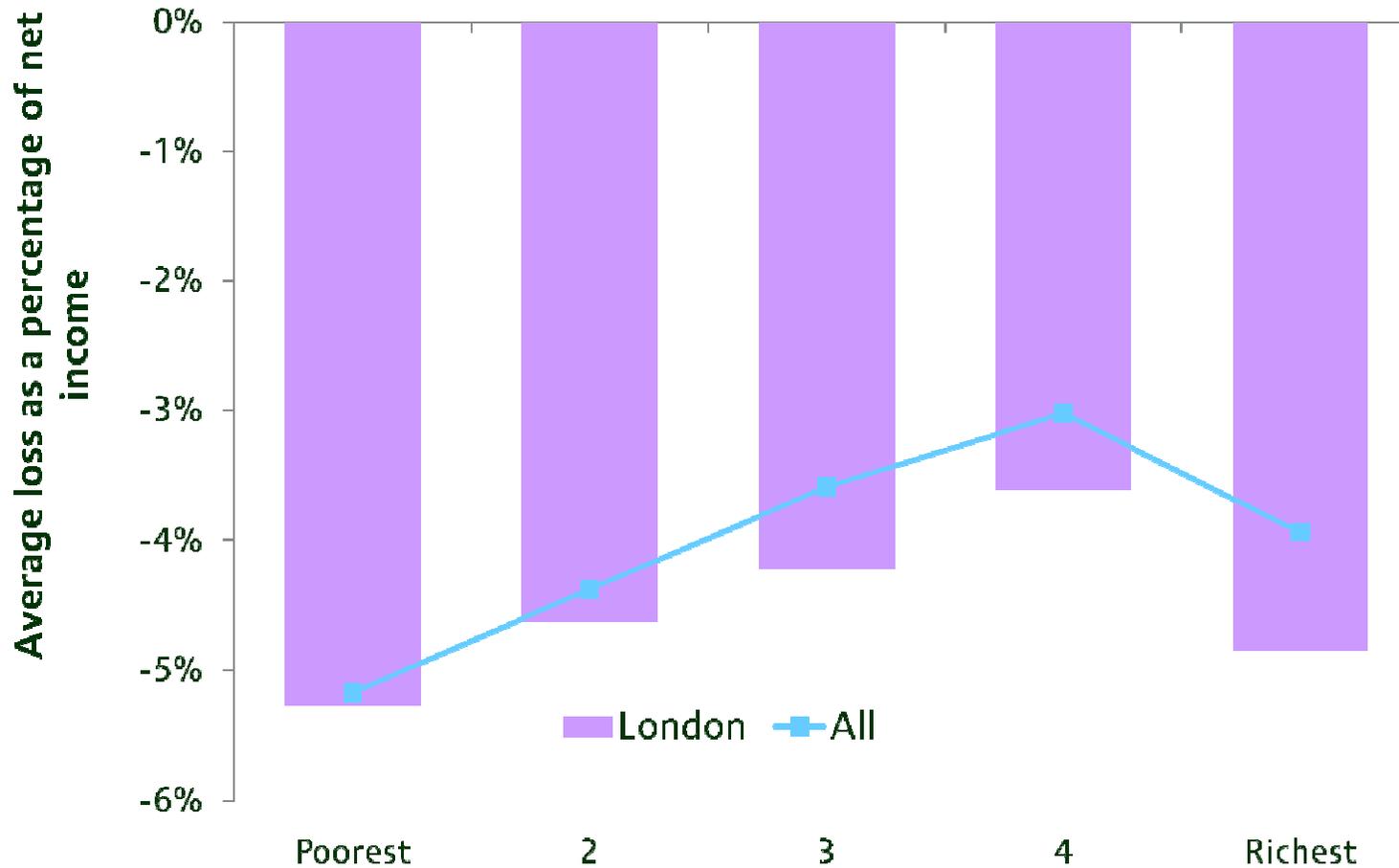
Summary

- Households in London lose more on average than those in any other region from reforms to be in effect by 2012–13
 - Lose most from reforms announced by previous government and those announced in June Budget
 - For different reasons in each case:
 - London has more of the UK's very richest households. They are particularly affected by the restriction of tax relief on pension contributions from April 2011 announced by Labour (but implemented in a different form by the coalition)
 - London is a high-rent area and so is particularly affected by cuts to Housing Benefit.
- This is still true if we look at all reforms to 2014–15, but other regions catch up
 - Benefit cuts from 2013 hit poorer regions harder than London
 - Northern Ireland has a particularly large number of DLA recipients
 - We assume that DLA recipients in each region are equally likely to lose entitlement
- But much of what appear to be differences between regions are in fact differences between income groups...

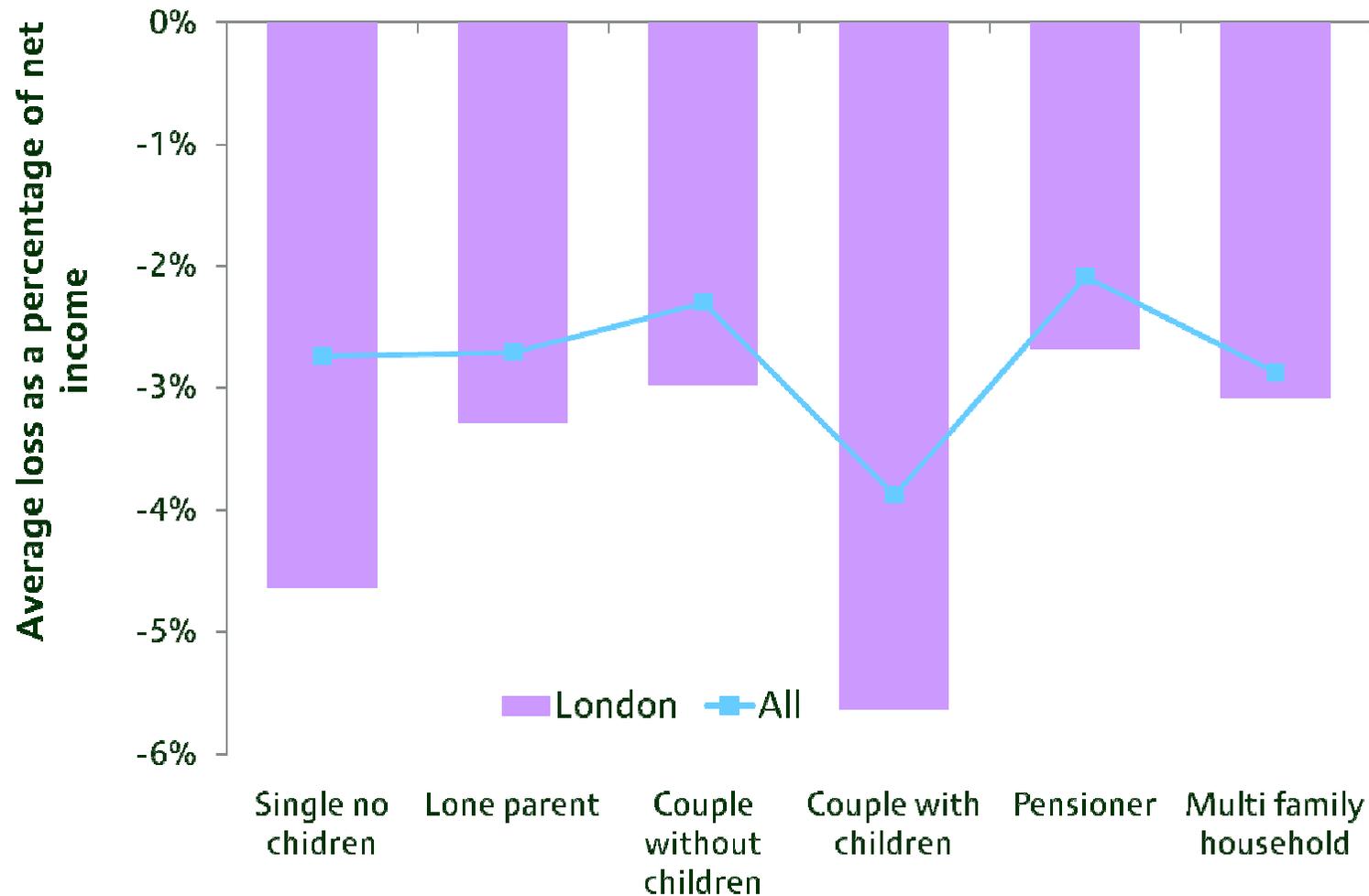
Average loss as a percentage of income by UK income quintile, reforms to 2012–13



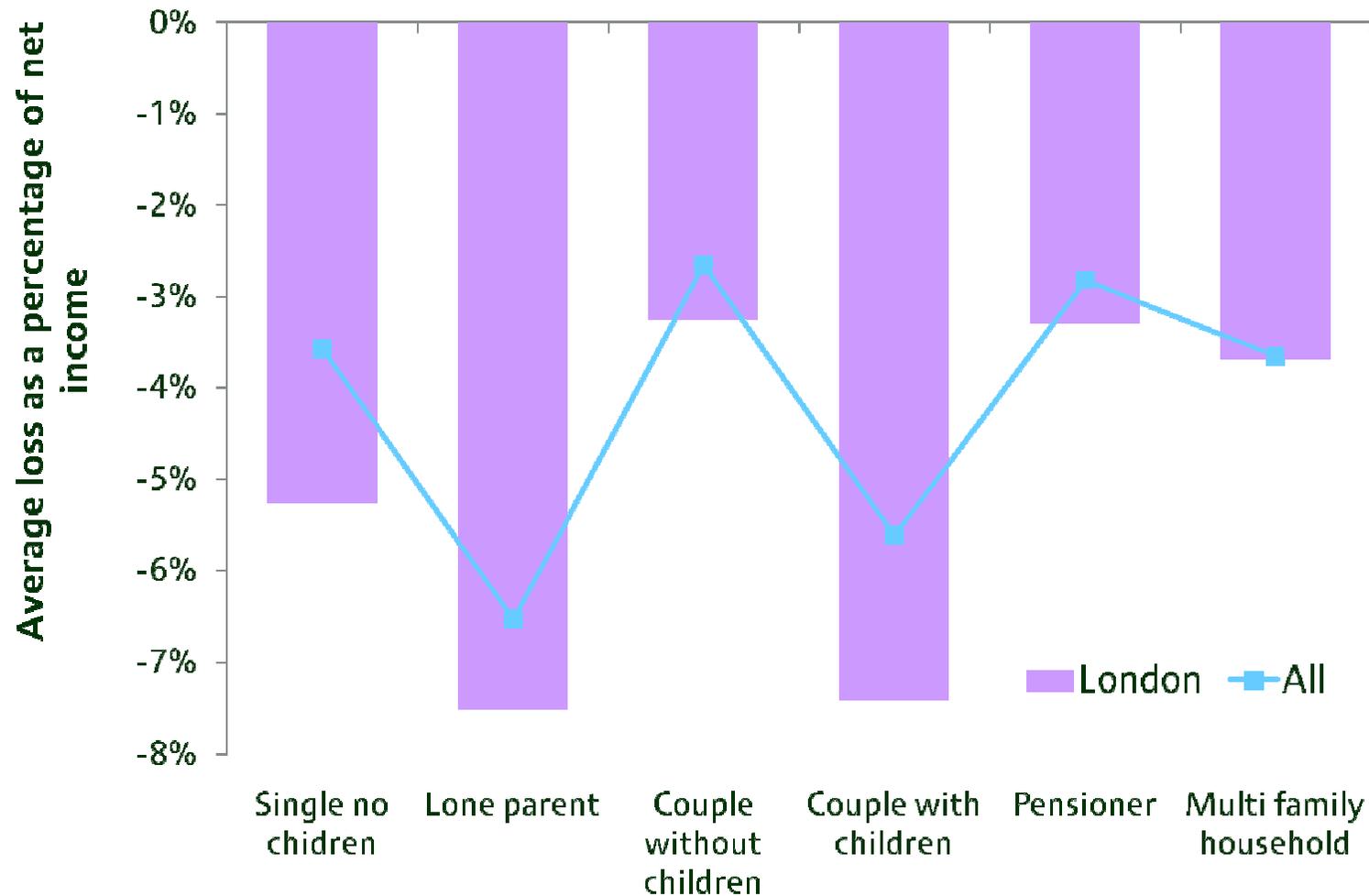
Average loss as a percentage of income by UK income quintile, reforms to 2014–15



Average loss as a percentage of income by household type, reforms to 2012–13



Average loss as a percentage of income by household type, reforms to 2014–15



Summary

- Much of the overall difference between London and the rest of the UK is caused by differences in the income distribution
 - More very rich households in London
- Single-person households and couples with children in London lose more as a proportion of income than their counterparts in the rest of the UK
 - These are the household types with the biggest concentration of the highest earners in London
- At the other end of the income scale, cuts to housing benefit likely to affect London more than other areas of the UK