



## 2008/09 income tax and tax credit changes: key statistics

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Author: Bryn Morgan

Economic Policy & Statistics Section

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This short note presents some of the key statistics about the changes to the income tax and tax credit system that were introduced from April 2008. For more information on the policy background to these changes see Library Standard Note SN/BT/4685 [Income tax: changes from April 2008](#).

This note has now been updated to include the £600 increase to the personal allowance announced on 13 May 2008.

### Contents

A.	Background	2
	1. What changes have been made?	2
B.	Fiscal impact	2
C.	Winners and losers	3
	1. How many winners and losers are there?	3
	2. How many losers are there in each constituency?	5
D.	Impact of income tax/National Insurance changes by income	5
	1. What are the overall effects of the Budget measures by income?	7
E.	Further information	7

## A. Background

### 1. What changes have been made?

The 2007 Budget report set out the package of changes to income tax, national insurance and tax credits.<sup>1</sup>

The reforms announced in this Budget represent the next stage in the Government's programme of reform to the tax and benefit system. The Government will:

- remove the starting rate and cut the basic rate of income tax from 22 pence to 20 pence creating a simpler structure of two rates: a 20 pence basic rate and a 40 pence higher rate from April 2008;
- increase the upper earnings limit for national insurance by £75 a week above indexation in April 2008, and then from April 2009 fully align it with the higher rate threshold – the point at which taxpayers start to pay the higher rate of income tax, further simplifying the system;
- raise the aligned higher rate threshold and upper earnings limit by £800 a year above indexation from April 2009;
- increase the higher personal allowances for those aged 65 or over by £1,180 above indexation from April 2008;
- raise the child element of the Child Tax Credit by £150 a year above earnings indexation in April 2008, making further progress in helping families and tackling child poverty, and raising the child element to £2,080 a year;
- increase the threshold for Working Tax Credit by £1,200 to £6,420 a year in April 2008, further increasing the incentives to work for families with children and low income working households; and
- raise the withdrawal rate on tax credits by 2 per cent to 39 per cent in April 2008, helping to retain their current focus.

Calculations in this note compare the actual 2008/09 system, with the 2007/08 rates and allowances uprated according to the usual indexation. If the starting rate had been retained it would have applied to the first £2,320 of taxable income.<sup>2</sup>

In his statement to the House on 13 May, the Chancellor announced that the personal allowance for 2008/09 would be increased by £600 to £6,035. In order to limit the benefit from this increase to basic rate taxpayers, the basic rate limit would be reduced by £1,200.<sup>3</sup>

## B. Fiscal impact

In his 2007 Budget speech, the then Chancellor said “the changes that I make today will be broadly neutral for the public finances.”<sup>4</sup> This is shown in the table below; overall changes to income tax, NICs and tax credits are projected to increase revenue by £860 million in 2008/09, but reduce it in later years. The increase in revenue from removing the starting rate is less than the loss from reducing the basic rate to 20 pence.

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<sup>1</sup> Budget 2007, HM Treasury, HC 342 2006-07 p109

<sup>2</sup> The main direct tax allowances and rates are set out in Library Research Paper 08/26 *Direct taxes and allowances: 2008-09*

<sup>3</sup> [HC Deb 13 May 2008 c1201](#)

<sup>4</sup> HC Deb 21 March 2007 c819

Table 1

**Effect on Exchequer yield of selected measures announced in Budget 2007 which took effect in April 2008**  
£ million

	2008/09	2009/10	2010/11
Remove starting rate on non-savings income	+7,440	+8,840	+8,870
Increase aged allowances by £1,180 and raise for 75 and overs to £10,000	-810	-940	-970
Increase child tax credit by £150 above indexation	-910	-1,000	-1,050
Raise the threshold of working tax credit by £1,200	-970	-980	-990
Increasing the tax credit withdrawal rate by 2 percentage points	+420	+490	+530
Income tax and NICs: phased alignment of the higher thresholds	+4,090	+1,560	+1,750
Income tax and NICs: raising the higher rate threshold and upper earnings limit	+0	-260	-490
Basic rate of income tax reduced to 20 pence	-8,400	-10,050	-10,180
Net impact	+860	-2,340	-2,530

Source: Budget 2008, Table A.11

In his statement to the House on 13 May 2008, the Chancellor said it would cost £2.7 billion in 2008/09 to increase the personal allowance by £600 and reduce the basic rate threshold by £1,200.<sup>5</sup>

## C. Winners and losers

### 1. How many winners and losers are there?

#### *Original changes*

The most commonly quoted figure is that were 5.3 million **households** who would lose from the overall package of changes.<sup>6</sup> 21 million households would be better off or no worse off. The impact can only be measured at a household level as the changes to tax credits take account of the household situation.

An alternative and more detailed analysis was prepared by the Institute for Fiscal Studies showing the numbers of households gaining or losing more than £1 per week. This shows 3.6 million households who would have lost by more than £1 per week.<sup>7</sup>

<sup>5</sup> [HC Deb 13 May 2008 c1201](#)

<sup>6</sup> [HC Deb 18 October 2007 c1266-70W](#)

<sup>7</sup> There are a few differences between the assumptions used by the treasury and IFS. First, the Treasury counts anyone with a change in income of more than 5 pence per week as a winner or loser, whereas the IFS uses a figure of £1. Any family with less than a £1 gain or loss is classed as "broadly unaffected". Also, the IFS look at families, while the Treasury figures count households - so for the IFS elderly relatives or grown up children living in the home would count as separate families, as would siblings or young professionals sharing a flat.

Table 1

**Winners and losers from April 2008 income tax, National Insurance and tax credit changes**

	Number of households by weekly change in net income (thousands)					% of households losing more than £1 per week
	Less than -£10	-£10 to -£1	-£1 to +£1	+£1 to +£10	More than +£10	
Single, no children	0	538	1,854	1,455	12	14%
Single, children	0	0	21	1,088	395	0%
Couple, no children	0	1,153	997	2,323	209	25%
Couple, children	0	444	625	2,754	670	10%
Pensioners	0	275	3,360	2,557	201	4%
MBU, no children (a)	23	983	967	1,173	141	31%
MBU, children	1	193	138	772	161	15%
Total	24	3,585	7,963	12,121	1,788	14%

Notes: (a) multiple benefit unit

Source: IFS Green Budget 2008, Table 14.7

*Increase to personal allowance*

In his statement on 13 May, the Chancellor said:

That will mean that 22 million people on low and middle incomes will gain an additional £120 this year. It will mean that 4.2 million households will receive as much, or more than, they originally lost. The remaining 1.1 million households will see their loss at least halved. In other words, 80 per cent. of households are fully compensated, with the remaining 20 per cent. compensated by at least half. In addition, 600,000 people on low incomes will be taken out of income tax altogether.

People aged between 60 and 64, whose average loss was £100, will also get the advantage of the increased personal allowance worth up to £120. They will also receive the additional £50 winter fuel payment for this year, which I announced in the Budget. The increased personal allowance will apply to all income for this tax year and so will be backdated to 6 April. As a result, from September, basic rate taxpayers will see a one-off increase in their monthly income of £60 and then an increase of £10 per month for the rest of the financial year.

Again, the IFS have done their own analysis of winners and losers. They estimate that there are 0.9 million households who are still worse off by more than £1 per week after the increase to the personal allowance. Of these 500,000 are single adults aged under 25 without children, 115,000 are single adults aged 25-55 without children and 140,000 are couples without children. There are a few pensioner families (20,000) and households with children (15,000) who also lose.<sup>8</sup>

<sup>8</sup> "The 10% tax rate: where next?", IFS Briefing Note BN77, 21 May 2008

## 2. How many losers are there in each constituency?

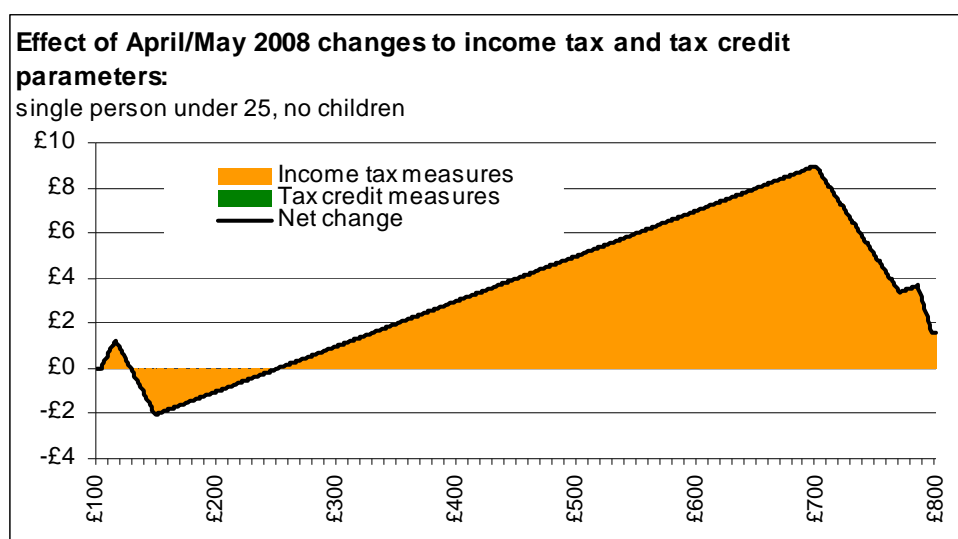
It is not possible to calculate this from published figures. A recent Parliamentary Answer gave some figures for Scotland and said “it is not possible to estimate the impact of the reform package below devolved administration or Government Office Region level”.<sup>9</sup>

### D. Impact of income tax/National Insurance changes by income

A single individual will pay 10 pence more in income tax for every £1 of earnings between the personal allowance (£6,035) and the notional starting rate limit (£7,755). This figure is the 2007/08 starting rate limit, adjusted using the usual indexation formula. Between this starting rate limit and the basic rate limit (£40,835, the point at which higher rate taxation applies), the individual will pay two pence less in income tax for each £1 of earnings.

This means that the maximum loss for an individual will be £112 at £7,755 per annum. Once income rises above £13,335, there is a gain.

The chart below shows the net impact for a single individual with no entitlement to tax credits:



Before the increase to the personal allowance was announced, the maximum loss for a single individual would have been £232 per annum comes at an income of £7,755. The benefit of the reduction in the basic rate would come in above that income, and it is at £19,355 that the increased tax paid on starting rate income is offset by the reduced tax paid at the basic rate.

The personal allowances of pensioners aged 65 and over increased by £1,180 above indexation. They will all pay less income tax. An individual aged 65 or over at the top of the

<sup>9</sup> [HC Deb 21 April 2008 c1679-80W](#)

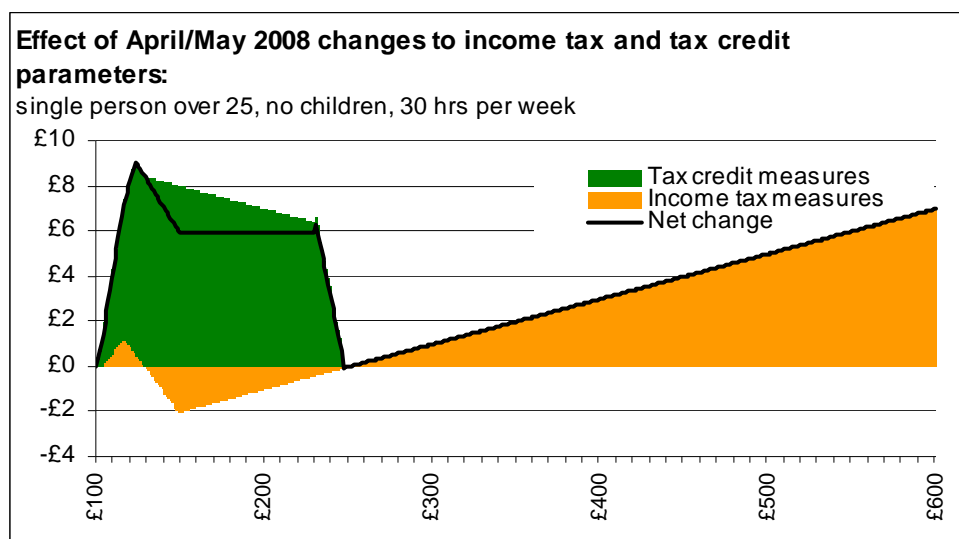
starting rate would have paid £232 per annum more in income tax if the personal allowance was only increased by indexation. However, as they have an additional £1,180 on which they no longer pay any income tax, their income tax bill is actually reduced by £4 per annum.

### Tax credit changes

As soon as there is an entitlement to tax credits, the position changes and some households that lose from the changes to income tax will become overall beneficiaries.

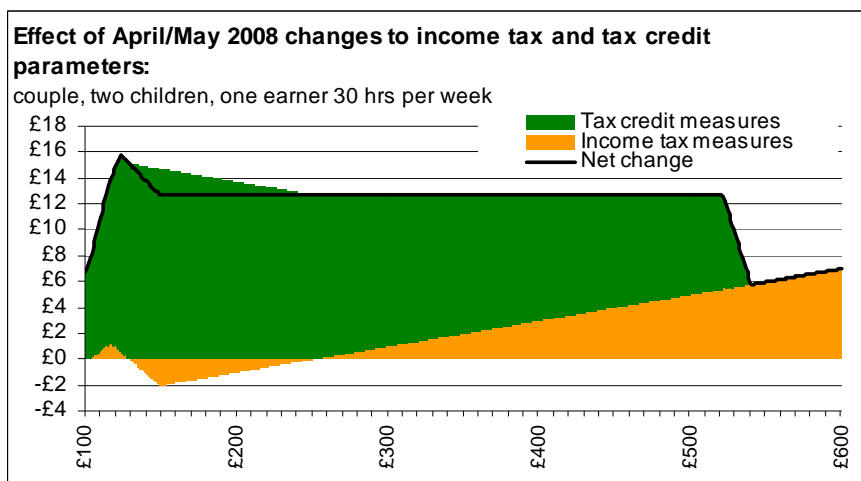
The main tax credit changes were an increase to the child element of child tax credit of £150 above indexation, an increase to the level at which working tax credit is reduced by an addition £1,120 and an increase in the withdrawal rate from 37% to 39%. Other things being equal, the first two measures would increase tax credit entitlement, while the third reduces it.

Chart 2 shows the situation for a single individual aged over 25 and working full-time.



The effect of changes to tax credits means that almost all individuals claiming working tax credit are net “winners” from the changes.

For a couple with a single, full-time earner, and two children, no household should lose once tax credit changes are included.



## 1. What are the overall effects of the Budget measures by income?

The Institute for Fiscal Studies show that, on average, all income deciles have a net increase in income. The second and third lowest income deciles have the highest average increase in net income (1.5%). However, around 60% of the losers are in those two deciles. The top decile has a 0.6% increase. The average loss of those losing is £1.59; the average gain of those gaining is £5.68.<sup>10</sup>

## E. Further information

For more analysis of the original changes, see:

- [“The impact of tax and benefit reforms to be implemented in April 2008”](#), *IFS Green Budget 2008*, Chapter 14, January 2008  
 This also includes an analysis of reforms since 1997 by income and household type. This shows that overall, low income pensioners and households with children have benefited, but that other low income households have not (figure 14.7).

The IFS also published a briefing note that analysed the impact of increasing the personal allowance and what the position would be if the increase was for one year only:

- [“The 10% tax rate: where next?”](#), IFS Briefing Note BN77, 21 May 2008

The Treasury Committee published its report on the changes on 28 June 2008:

- [Budget Measures and Low-Income households](#), Treasury Select Committee, HC 326 2007-08

<sup>10</sup> [“The 10% tax rate: where next?”](#), IFS Briefing Note BN77, 21 May 2008, Table A2, p33