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Income tax: increases in the personal allowance since 2010

By Antony Seely

Inside:

Contents

Summary

In May 2010, the new Coalition Government announced that in its first Budget it would introduce a substantial increase in the personal tax allowance, a first step to its longer-term objective to raise the allowance to £10,000.[1] All taxpayers are eligible for this tax-free allowance – which represents the amount of income someone may earn before paying any income tax. The allowance was set at £6,475 for 2010/11. In his Budget speech on 22 June 2010 the then Chancellor, George Osborne, confirmed that it would rise to £7,475 from April 2011, at a cost of £3.5 billion in 2011/12.

At this time Mr Osborne stated that the allowance would continue to rise "during the rest of this Parliament."[2] In turn, the allowance went up by £630 for 2012/13, by £1,135 for 2013/14, and by £560 to reach £10,000 from April 2014. It is estimated that by 2014/15 these successive increases in the personal allowance resulted in 2.7 million people not having to pay tax on their income, at an annual cost of around £10.7 billion.[3] By comparison the Coalition Government's decision in its first Budget to increase the standard rate of VAT from 17.5% to 20% was estimated to raise about £13.5 billion in the same year.[4]

Individuals of working age are liable to pay National Insurance contributions (NICs) on their earnings as well as income tax. In the past the point at which individuals start to pay NICs has been aligned with the point at which they start to pay income tax. However, this threshold has not been increased in line with the rise in the personal allowance, so that one section of those individuals 'lifted out' of income tax will still be paying NICs.[5]

In the Autumn Statement in December 2014 the Chancellor announced that the personal allowance would rise by £600 to £10,600 for 2015/16. In previous years most, if not all, of the potential benefit for higher rate taxpayers has been 'clawed back' by cutting the higher rate threshold – the level above which individuals start to pay the 40% rate on their income.[6] In his 2014 Budget Mr Osborne had proposed that this threshold – the sum of the personal allowance and the basic rate limit – would rise by 1% for 2014/15, and by 1% for 2015/16. Most higher rate taxpayers would receive a tax cut of an equivalent size to that received by basic rate taxpayers.[7] However, in the Autumn Statement the Chancellor announced that the threshold would rise by 1.2% for 2015/16 – in line with inflation – so that the full gains of the last increase in the personal allowance would be passed on to higher rate taxpayers. Overall it was estimated that 3.4m working age individuals would have been taken out of income tax over the Parliament. The tax saving over this period was estimated to be £825 for a typical basic rate taxpayer, and £676 for a typical higher rate taxpayer, in cash terms.[8]

Over this period the Coalition Government's approach to increasing the personal allowance was generally welcomed, although critics noted that many households

1 HMG, *The Coalition: our programme for government*, 20 May 2010 p30
2 *Budget 2010*, HC 61, June 2010 p40 (Table 2.1 – item 12); HC Deb 22 June 2010 c179
3 *Budget 2013*, HC 1033, March 2013 para 1.166-71; *Green Budget 2014*, Institute for Fiscal Studies, February 2014 p151.
4 *Budget 2010*, HC 61 June 2010 (Table 2.1 – item 1).
5 The Institute for Fiscal Studies estimated that 1.0 million individuals would pay NICs but not income tax in 2013/14 (*Green Budget 2013*, February 2013 p190)
6 In 2010/11 the higher rate threshold (HRT) was £43,875: the personal allowance of £6,475, combined with the basic rate limit of £37,400). In 2014/15 the HRT was £41,865. Details of the structure and parameters of income tax in past years are collated on Gov.uk.
7 HC Deb 19 March 2014 c792
8 *Autumn Statement*, Cm 8961, December 2014 para 1.216

benefitting from these tax cuts were adversely affected by other tax changes – such as the increase in the standard rate of VAT – as well as reforms to tax credits and social security benefits.[9] It was also pointed out that for those taken out of income tax, further increases in the allowance were of no benefit, and there was a case to increase the threshold at which individuals started to pay NICs,[10] or, as suggested by the then Labour leader, Ed Miliband, that a 10p starting rate of income tax should be introduced.[11]

The Coalition Government made a second important change to the structure of income tax during its period of office, cutting the additional rate of income tax paid on incomes over £150,000.[12] The Labour Government had introduced the additional rate, set at 50%, from April 2010, estimating this would raise £1.3 billion in 2010/11, rising to £3.05 billion in 2011/12.[13] In his 2011 Budget George Osborne argued that the 50p rate "would do lasting damage to our economy if it were to become permanent" and confirmed that HM Revenue & Customs would review "how much revenue it actually raises."[14]

In his Budget the next year Mr Osborne announced the additional rate would be cut to 45p from April 2013. HMRC had found evidence of considerable 'forestalling' – taxpayers shifting income into the previous tax year to avoid the 50p rate – "at a cost to the taxpayer of £1 billion", and, in his words, "no Chancellor can justify a tax rate that damages our economy and raises next to nothing."[15] HMRC's assessment of the impact of the 50p rate was set out in a detailed report, which estimated that the cost of cutting the rate to 45p would be only £100m by 2014/15, given the anticipated response by taxpayers to the new rate.[16]

In its manifesto for the 2015 General Election the Conservative Party proposed further increases in the personal allowance, as well as the higher rate threshold, so that by the end of the Parliament in 2020/21 they reach £12,500 and £50,000 respectively. The Liberal Democrats also proposed increasing the personal allowance by this amount, but made no commitment to increase the higher rate threshold. By contrast in their manifesto the Labour Party proposed a new 10% starting rate of income tax, and increasing the additional rate to 50%.[17]

The Chancellor George Osborne presented the Conservative Government's first Budget on 8 July 2015. Mr Osborne confirmed the Government's plans with regard to the personal allowance and the higher rate threshold, and announced that for 2016/17 the allowance would be set at £11,000, and the higher rate threshold would be £43,000 – the first time that the threshold had been increased by more than inflation alone since 2010.[18] For the

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9 For example, see the exchange of views when provision for the allowance in 2011/12 was debated at the Committee stage of the Finance Bill: Public Bill Committee, *Second sitting*, 10 May 2011 cc50-56.
10 For example, see "Chapter 7: Policies to help the low paid", *Green Budget 2014*, Institute for Fiscal Studies, February 2014
11 Labour Party press notice, *Speech by Ed Miliband : Rebuilding Britain with a One Nation economy*, 14 February 2013
12 This issue is discussed in detail in a second Library briefing paper: *Income tax: the additional 50p rate*, CBP 249, 26 September 2018.
13 HC Deb 22 April 2009 c244; *Budget 2010*, HC 451, March 2010 p140 (Table A11 : item l)S
14 HC Deb 23 March 2011 c957. See also, HC Deb 14 September 2011 c1191W
15 HC Deb 21 March 2012 cc805-6
16 HMRC, *The Exchequer effect of the 50 per cent additional rate of income tax*, March 2012 pp48-53. The report estimated that the 'static cost' of this tax cut, with no allowance for any behavioural response, would be £3.35 billion in 2014/15. See also, *Budget 2013*, HC 1033, March 2013 p66 (Table 2.2 – item t)
17 For details see, *Taxes and Benefits: The Parties' Plans*, Institute for Fiscal Studies, April 2015
18 HC Deb 8 July 2015 c336; *Summer Budget 2015*, HC246, July 2015 paras 1.130-4. The increase in both allowance and threshold was estimated to cost just over £1.1bn in 2016/17 (*op.cit.* Table 2.1 – items 1,2).

following year, the allowance and threshold were increased to £11,500, and £45,000 respectively – another real-terms increase.[19]

Following the 2017 General Election, the Chancellor Philip Hammond presented the Autumn Budget on 22 November. Mr Hammond reiterated the Government's commitment to increase the allowance and higher rate threshold so that they reached £12,500 and £50,000 by 2020 – though each would be increased in line with inflation only for 2018/19.[20] Mr Hammond presented the Government's second Autumn Budget on 29 October this year, and announced that both the personal allowance and higher rate threshold would be increased to meet the Government's manifesto commitment, but from April 2019.[21] This is estimated to cost £2.79 billion in 2019/20, falling to £1.94 billion the following year.[22]

19 *Spring Budget 2017*, HC 1025, March 2017 para 3.4. The increase in both allowance and threshold was estimated to cost just over £2bn in 2017/18 (*op.cit.* Table 2.2 – items x,y).

20 As a result for 2017/18, the personal allowance was £11,850, and the higher rate threshold was £46,350. HC Deb 22 November 2017 c1053; *Autumn Budget 2017*, HC587, November 2017 paras 3.4-5

21 HC Deb 29 October 2018 cc667-8

22 *Budget 2018*, HC 1629, October 2018 para 3.7, Table 2.1 – item 10; HMRC, *Income Tax: Personal Allowance and basic rate limit from 2019-20*, 29 October 2018; PQ186423, 5 November 2018

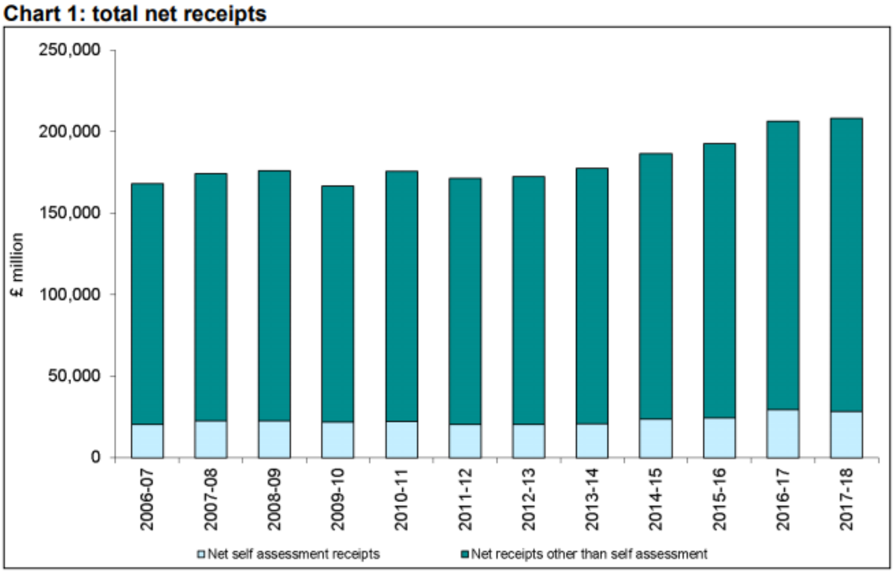
1. Income tax – an introduction

1.1 Tax receipts

Income tax raised £180.7 billion in 2017/18.[23] It is estimated that 30.8 million people paid the tax in this year.[24] The tax is the single largest contributor to the Exchequer, accounting for around a quarter of all government tax receipts. Taken together with VAT and National Insurance contributions, these three taxes account for almost two thirds of total tax revenue.[25]

HMRC regularly publish figures for income tax receipts, repayments and tax credits; total net income tax receipts over the last ten years are shown below:[26]

Chart 1: total net receipts



HMRC make a number of observations about this trend in receipts:

> Chart 1 shows total net income tax receipts from 2006-07 to 2017-18. Total net receipts have increased between 2016-17 and 2017-18 by 1.9% and are now at their highest ever level, recovering from a sharp dip in 2009-10. The overall increase since 2008-09 is 17.4%. The increase in 2017-18 is due to growth in PAYE receipts.
>
> Between 2010-11 and 2011-12 net income tax receipts fell by 1.7% (or £2.6 billion) largely due to lower receipts of Self Assessment income tax. The lag in the Self Assessment payment regime means that receipts in 2010-11 and 2011-12 relate largely to liabilities for 2009-10 and 2010-11 respectively. The introduction of the 50% additional rate of income tax in 2010-11 had a major effect on the behaviour of taxpayers with incomes above the additional rate threshold of £150,000 with large amounts of income forestalling, i.e. income brought forward into 2009-10 from later years in order to be taxed at 40% before the

23 Office for Budget Responsibility, *Economic and fiscal outlook*, Cm 9713, October 2018 p108, Table 4.6.
24 HMRC, Statistics: Number of individual income taxpayers (Table 2.10), May 2018
25 In 2017/18 NICs are forecast for raise £137bn, and VAT is forecast to raise £132bn. Total receipts are forecast to be £788bn (Cm 9713, October 2018 Table 4.6).
26 HMRC, *Income tax receipts statistics*, August 2018 p12

50% rate came into effect. Self Assessment income tax liabilities were therefore inflated in 2009-10 and depressed in 2010-11 as the effects of forestalling started to unwind. This then boosted receipts in 2010-11 and depressed them in 2011-12.

Self Assessment income tax receipts increased by 1.5% in 2013-14 and 13.4% in 2014-15, and are now above their 2008- 09 level by £6.0bn. Self Assessment tax receipts increase from £24.3 billion in 2015-16 to £29.3 billion in 2016-17 (an increase of 20.4%). This large increase is likely driven by changes to dividend taxation rules. In 2017-18 this has decreased by 3.4% to £28.3 billion.

In its July 2015 Budget, the Government announced reforms to the taxation of individual dividend income, raising the basic, higher and additional rates by 7.5 percentage points and introducing a tax-free allowance on the first £5,000 of taxable annual dividend income (cut to £2,000 as of April 2018 in the Spring Budget 2017).

The July Budget 2015 changes came into effect in April 2016, giving those affected a period in which to bring forward dividend income into 2015-16 so that it was taxed at the lower rate. Dividends are subject to income tax (with the same thresholds but different rates) mainly via SA, so 2015-16 liabilities were mostly paid in January and February 2017 (receipts covered by these statistics). This may explain this decrease in SA receipts in 2017-18.[27]

1.2 Tax schedule

Income from earnings, pensions, profits

All 'non-savings' income – income from earnings, pensions, taxable social security benefits, trading profits and income from property – are subject to income tax at the same rates.

For 2018/19 income tax on these categories of income is charged at three rates: the basic rate of 20%, the higher rate of 40% and the additional rate of 45%. All three rates are unchanged from 2017/18.

The 20% basic rate applies to taxable income up to a threshold of £34,500. Taxable income excludes personal allowances, which represent the amount of money someone may receive free of tax. (Personal allowances are discussed in section 2 of this paper.)

Taxable income in excess of the threshold is charged at the higher rate of 40%, up to £150,000. Income earned above this threshold is charged tax at 45%.

2017/18		**2018/19**	
Taxable income	**Tax rate**	**Taxable income**	**Tax rate**
£0 - £33,500	**20%**	**£0 - £34,500**	**20%**
£33,501 - £150,000	**40%**	**£34,501 - £150,000**	**40%**
Over £150,000	**45%**	**Over £150,000**	**45%**

27 *op.cit.* pp12-13

A 10% starting rate of tax used to apply on non-savings income, but was withdrawn in April 2008.

From April 2017 two new allowances apply to income from property and income from trading. Individuals with property income or trading income below the level of the allowance do not need to declare this income or pay tax on it. Both allowances are set at £1,000 for 2018/19. The Low Incomes Tax Reform Group has noted that strictly speaking these allowances are nil-rate bands of tax which will apply to these categories of income.[28]

Scottish taxpayers

From 2017/18 the Scottish Government has had the power to set all income tax rates and thresholds to apply to Scottish taxpayers' non-savings and non-dividend income. The Scottish Government does not have the power to set the level of the income tax personal allowance.

For 2018/19 the Scottish Government has set five rate of income tax: the starter rate of 19%; the basic rate of 20%; the intermediate rate of 21%; the higher rate of 41%; and the top rate of 45%. It has also set the four thresholds at which these rates take effect.

These rates and thresholds are set out below – the table assumes someone is in receipt of the UK personal allowance:[29]

Taxable income	**Tax rate**
Over £11,850 - £13,850	**19%**
Over £13,850 - £24,000	**20%**
Over £24,000 - £43,430	**21%**
Over £43,430 - £150,000	**41%**
Above £150,000*	**46%**

* Personal Allowance is reduced by £1 for every £2 earned over £100,000[30]

Savings and dividend income

For 2018/19 savings income is charged at 0% for income up to £5,000. Above this limit savings income is charged tax at the basic rate of 20%, up to the basic rate limit of £34,500. Savings income above this limit is charged at the 40% higher rate, up to the higher rate limit of £150,000. Savings income above this limit is charged at the 45% additional rate.

[28] LITRG press notice, *Property and trading income allowances could simplify some individuals' tax position*, 16 March 2016. See also, HMRC, *Income Tax: new tax allowance for property and trading income – tax information & impact note (TIIN)*, December 2016

[29] The Scottish Government publishes details of these rates and thresholds on its site. See also, Low Incomes Tax Reform Group press notice, *Scottish income tax rates and thresholds confirmed*, 23 February 2018.

[30] HMRC is responsible for collecting the tax; general guidance is on Gov.uk. See also, HMRC press notice, *Changes to tax reliefs following the Scottish Government's Budget*, 21 March 2018.

Since April 2016 savers have been entitled to claim a new Personal Savings Allowance (PSA). This applies a 0% rate for up to £1,000 of savings income for basic rate taxpayers. The allowance applies a 0% rate for up to £500 of savings income for higher rate taxpayers. Additional rate taxpayers are not eligible for the allowance. Historically savings income has been taxed at source by banks and building societies at 20%. Alongside the introduction of the PSA, automatic deduction of tax at source was withdrawn.[31]

For 2018/19 dividend income is charged at 0% for income up to £2,000 – the Dividend Allowance. Above this limit dividend income is charged tax at a basic rate of 7.5%, up to the basic rate limit. Dividend income above this limit is charged at a higher rate of 32.5%, up to the higher rate limit. Dividend income above this limit is charged at an additional rate of 38.1%.

In calculating tax liability, dividend and savings income are regarded as the 'top slice' of income, with dividends the highest.[32]

1.3 Tax allowances

All individuals are entitled to claim a personal allowance which they can set against income tax. An allowance is also given to individuals who are blind.

Personal allowance

Every taxpayer resident in the United Kingdom is entitled to a **personal allowance** that can be set against any type of income for tax purposes. For 2018/19 this allowance is £11,850.

In May 2010, the Coalition Government announced that over the 2010-15 Parliament it would substantially increase the personal allowance, set at £6,475 for 2010/11, up to £10,000. The allowance was increased each year, to reach £10,000 for 2014/15. In the Conservative Government's first Budget after the 2015 General Election, the then Chancellor George Osborne pledged to increase the allowance to £12,500 and the higher rate threshold to £50,000, by the end of the Parliament.[33] In the Government's first Budget after the 2017 General Election, the Chancellor Philip Hammond, confirmed that the Government would meet this commitment by 2020. At this time Mr Hammond announced the personal allowance would be increased by a further £350 from April 2018, in line with CPI inflation.[34]

Since April 2010 the personal allowance has been withdrawn from individuals whose incomes exceed £100,000. The allowance is reduced by £1 for every £2 above this income limit, until completely withdrawn. This income limit is unchanged for 2018/19.

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31 For details see, HMRC, *Tax on savings income*, ret'd November 2018

32 The Low Incomes Tax Reform Group publishes guidance on the taxation of savings and dividend income on their site.

33 HC Deb 8 July 2015 c336; *Summer Budget 2015*, HC246, July 2015 paras 1.130-4

34 HC Deb 22 November 2017 c1053; *Autumn Budget 2017*, HC587, November 2017 paras 3.4-5

Blind person's allowance

Any person registered as blind is entitled to the **blind person's allowance**. The allowance is set at £2,390 for 2018/19. If someone has insufficient income to make use of the allowance it can be transferred to their spouse or civil partner.

Transferable allowance for married couples & civil partners

Individuals whose income is insufficient to make full use of their personal allowance may transfer a fraction of the allowance to their spouse or civil partner, up to a set amount. Individuals cannot make use of the transferable tax allowance for married couples and civil partners – or, **marriage allowance**, as it is known – if their spouse or partner is liable to tax above the basic rate of tax. The allowance was introduced in April 2015. For 2018/19 the maximum that can be transferred is £1,190. In effect the recipient is entitled to a tax credit worth up to £238 to set against their tax bill.

Individuals who may wish to apply to have part of their allowance transferred in this way to their partner may register with HMRC either online or by phone. Eligible couples can backdate their claim for the allowance for up to four years; couples will have until 5 April 2020 to backdate their claim to the 2015/16 tax year when the allowance was first introduced.[35] In the Autumn 2017 Budget the Government announced that claims for the allowance would be allowed in cases where a partner has died before the claim was made, and that these claims would be able to be backdated by up to 4 years.[36]

Indexation

For many years income tax legislation has required the main personal allowances and income tax thresholds to be increased in line with the Retail Prices Index (RPI) unless Parliament determines otherwise.

This statutory requirement - the so-called "Rooker-Wise" amendment - was introduced under section 22 of the *Finance Act 1977*.[37] The amendment was successfully made through the cross-party co-operation of Jeff Rooker, Audrey Wise and Nigel Lawson. All three argued that without indexation, inflation acted as an unauthorised, unintended and unknown increase in taxation. By requiring that any real changes in allowances would be voted on, the amendment ensured that changes in the income tax structure would be 'out in the open'. Indeed, for most years since then, allowances went up in line with inflation - or by more than inflation.[38]

In the 2011 Budget the Coalition Government announced that from April 2012 the default indexation assumption for direct taxes would be

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35 HMRC, *Marriage allowance*, ret'd November 2018

36 *Autumn Budget 2017*, HC587, November 2017 para 3.6. For details see, *Income tax allowances for married couples*, Commons Briefing paper CBP870, 4 May 2018.

37 The statutory requirement to uprate allowances and thresholds, is consolidated in sections 57 & 21 of the *Income Tax Act 2007*, as amended

38 HL Deb 7 January 2010 c121WA

the Consumer Price Index (CPI), though RPI would be retained for some allowances and thresholds for the duration of the 2010 Parliament.[39] This approach was amended in the light of three measures: the phased withdrawal of the age-related allowances for taxpayers from April 2013; the increase in the personal allowance in 'real terms' – by more than inflation – in both 2014/15 and 2015/16; and, the increase in the higher rate threshold by 1% in the first of those years.

Any elements of the direct tax system that were indexed by reference to RPI are covered by CPI.[40] The threshold for the additional rate (£150,000), and the income limit for the tapered withdrawal of the personal allowance (£100,000), have not been included in these provisions, and are fixed in monetary value.

When uprating the main allowances and thresholds, the relevant inflation rate is the increase in inflation in the year to September, prior to the start of the following tax year.[41] When allowances and thresholds are increased in line with inflation, they are rounded up to the nearest £10 or £100. For personal allowances, this income limit is £10; for the basic rate limit, it is £100. CPI rose by 2.8% in the year to September 2017.[42]

Age-related allowances (withdrawn)

Prior to 2013/14, individuals were entitled to claim one of two age-related additions to the personal allowance, if they were aged between 65 and 74 years of age, or were 75 or over. The allowance was withdrawn if an individual's income exceeded a set limit. This was done by cutting the allowance by £1 for every £2 by which an individual's income exceeded a set income limit.

In the 2012 Budget the Coalition Government announced that from April 2013 both allowances would be phased out: each allowance would be frozen in cash terms, until they became aligned with the personal allowance. In addition, only existing recipients would be entitled to claim either allowance. At this time these allowances were frozen at £10,500 (for taxpayers born after 5 April 1938 but before 6 April 1948), and £10,660 (for taxpayers born before 6 April 1938).[43]

From 2016/17 both age-related allowances have been overtaken by the personal allowance and have been withdrawn. Taxpayers that were claiming these allowances are now eligible for the 'basic' personal allowance.

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39 *Budget 2011*, HC 836, March 2011 para 1.128. see also, Office of National Statistics, *Users and uses of consumer price inflation statistics*, October 2016
40 HM Treasury, *Budget 2018 : policy costings*, October 2018 pp49-53 (Annex A: Indexation in the public forecast baseline).
41 for details see, HM Treasury, *Tax benefit reference manual: 2009-2010 edition*, July 2009, paras 1.16-19. [HC DEP 2009-1987]
42 ONS, *UK Consumer Price Inflation: September 2017*, October 2017
43 For more details see, *Age-related personal allowance*, Commons Briefing Paper CBP6158, 11 May 2016.

Transitional allowances for older people

Four allowances were withdrawn from April 2000: the married couple's allowance (MCA) for couples aged under 65 at that time; the additional personal allowance; the maintenance allowance for separated or divorced couples under 65; and the widow's bereavement allowance.[44]

The MCA and tax relief on maintenance payments were retained for individuals where either they, or their current or former spouse, had reached the age of 65 by the start of the tax year 2000/01; i.e., they were born on or before 5 April 1935.

Married couple's allowance

Married couples, in which at least one partner reached 65 by 6 April 2000, are still entitled to claim a **married couple's allowance**.[45] For 2018/19, this allowance is set at £8,695, increased in line with inflation. Tax relief for the allowance is 'restricted' to 10%. In effect taxpayers receive a credit worth 10% of the MCA to set against their final tax bill: ie, £870.

The value of the MCA is gradually reduced for taxpayers earning above an income limit, in the same way as the age-related personal allowances were (see above). For 2018/19 this income limit is set at £28,900. The withdrawal of the MCA from older couples is subject to a minimum allowance set at £3,360 for 2018/19, restricted to 10%. No couple entitled to the allowance will receive less than this.

Where a couple marry during the tax year the allowance is reduced by one twelfth for each complete tax month pre-marriage. In the first instance the MCA is given to the husband, though if couples elect to do so, the minimum MCA can be transferred to the wife or split equally between spouses. In previous years, in line with the personal allowance, an age-related MCA was given to couples aged between 65 and 74, and a second, higher MCA to those 75 or over. Given that anyone who reached 65 by 6 April 2000 will be 84 or over this tax year, it is only the second of these allowances that remains applicable.

Civil partners may also claim the MCA provided – as with married couples – at least one partner was born before 6 April 1935.[46]

Tax relief for maintenance payments

Generally, maintenance payments are made outside the tax system: those who make payments cannot claim them against tax, and those who receive them are not taxed on them. Separated or divorced individuals who pay maintenance direct to their ex-spouse under a legally binding agreement may qualify for a limited form of tax relief – often referred to as a '**maintenance allowance**' – provided that one or

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44 The abolition of these allowances was announced in the March 1999 Budget; for further details see *Direct taxes: rates & allowances 2000/01*, Commons Briefing paper RP00/38, 29 March 2000 pp11-12.

45 When a person born on or before 5 April 1935 newly gets married, that person or their spouse is entitled to claim this allowance.

46 More guidance is given on Gov.uk. In March 2005 the then Labour Government announced that civil partners would be treated the same as married couples for tax purposes, when the *Civil Partnership Act 2004* came into force on 5 December 2005.

more of the parties reached 65 prior to 6 April 2000. This relief is set equal to the 'minimum' MCA that couples can receive if they are now 84 or over (which is £3,360 restricted to 10% for 2018/19). Individuals who make maintenance payments to a child, or to someone to whom they have not been married, do not qualify for this relief. Tax relief is withdrawn if the ex-spouse who receives maintenance remarries.[47]

1.4 Historic trends

In its survey of the UK tax system the Institute for Fiscal Studies provides an overview of the changes made to the structure of income tax over the last thirty years. The first and most striking change there has been is in the schedule of tax rates:

> In 1978–79, there was a starting rate of 25%, a basic rate of 33% and higher rates ranging from 40% to 83%. In addition, an investment income surcharge of 15% was applied to those with very high investment income, resulting in a maximum income tax rate of 98%.
>
> In its first Budget, in 1979, the Conservative government reduced the basic rate of income tax to 30% and the top rate on earnings to 60%. In 1980, the starting rate was abolished; in 1984, the investment income surcharge was abolished; and through the mid-1980s, the basic rate of tax was reduced. In 1988, the top rate of tax was cut to 40% and the basic rate to 25%, producing a very simple regime with three effective rates – zero up to the tax allowance, 25% over a range that covered almost 95% of taxpayers and 40% for a small group of those with high incomes.

Table 10. Income tax rates on earned income, 1978–79 to 2016–17

	Starting rate	*Basic rate*	*Higher rates*
1978–79	25	33	40–83
1979–80	25	30	40–60
1980–81 to 1985–86	—	30	40–60
1986–87	—	29	40–60
1987–88	—	27	40–60
1988–89 to 1991–92	—	25	40
1992–93 to 1995–96	20	25	40
1996–97	20	24	40
1997–98 to 1998–99	20	23	40
1999–2000	10	23	40
2000–01 to 2007–08	10	22	40
2008–09 to 2009–10	—	20	40
2010–11 to 2012–13	—	20	40–50
2013–14 to 2016–17	—	20	40–45

Note: Prior to 1984–85, an investment income surcharge of 15% was applied to unearned income over £2,250 (1978–79), £5,000 (1979–80), £5,500 (1980–82), £6,250 (1982–83) and £7,100 (1983–84). Different tax rates have applied to dividends since 1993–94 and to savings income since 1996–97.

47 For more guidance see, Low Incomes Tax Reform Group, *What tax allowances am I entitled to?*, July 2018

> The basic rate of tax on savings income has been 20% since 1996–97, while the 10% starting rate (which was largely abolished in 2008–09) continued to apply to some savings income until April 2015. The effective rate of tax on dividends (once offsetting dividend tax credits are taken into account) was constant at zero for basic-rate taxpayers, 25% for higher-rate taxpayers and 30.56% for additional-rate taxpayers between 1993–94 and 2015–16. As of 2016–17, a savings income tax allowance has been available for basic- and higher-rate taxpayers …
> Since 2016–17, dividend income above a £5,000 allowance is taxed at 7.5% up to the basic-rate limit, 32.5% between the basic-rate and additional-rate limits and 38.1% above that. When calculating which tax band different income sources fall into, dividend income is treated as the top slice of income, followed by savings income, followed by other income.[48]

The 1990s saw the return of a more complicated rate schedule, initially with the reintroduction of a starting rate of tax on a relatively small band of income. In his 1992 Budget, which took place just before the General Election that year, the then Chancellor Norman Lamont announced that a 20p rate would apply to the first £2,000 of taxable income. Mr Lamont described it as a "decisive first step" to establishing a 20% basic rate, though the basic rate threshold was £23,700 at this time.[49] In turn Gordon Brown, when Chancellor in 1999, announced a series of income tax reforms, including a cut in this starting rate to 10p.[50] Eight years later Mr Brown announced that the Government would set the basic rate at 20% from 2008/09, although to help fund this measure, he decided to abolish the 10p rate.

It was not until after the Budget the following year that Mr Brown's successor as Chancellor, Alistair Darling, responded to public concern about the number of losers from this change. Rather than alter tax rates, Mr Darling announced a substantial increase in the personal allowance, limiting the benefit that would accrue to higher rate taxpayers by reducing the basic rate threshold.[51] Mr Darling introduced two further reforms which have complicated the rate structure: the withdrawal of the personal allowance from those on incomes over £100,000, and the new 50% rate on incomes over £150,000. Both measures took effect from 2010/11.

Over this period, while the personal allowance has increased considerably, the point at which individuals start to pay the higher rate of tax has actually fallen:[52]

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48 Thomas Pope & Tom Waters, *A survey of the UK tax system*, IFS Briefing Note BN09, November 2016 pp40-1
49 HC Deb 10 March 1992 c760
50 In 1998/99 the 20p starting rate covered the first £4,300 of taxable income. The 10p starting rate introduced from 1999/00 covered the first £1,500 of income. The basic rate threshold was increased over the next eight years to £2,230 by 1997/98.
51 The controversy over the abolition of the 10p rate is examined in an older Library paper: *Income tax : the 10p starting rate*, SN4685, 5 March 2013.
52 IFS Briefing Note BN09, November 2016 pp41-2

Table 11. Personal allowance and basic-rate limit in real terms (April 2016 prices)

	Personal allowance (£ p.a.)	*Basic-rate limit (£ p.a.)*
1979–80	5,623	48,272
1984–85	5,927	45,534
1989–90	6,386	47,466
1994–95	6,262	43,078
1999–2000	6,878	44,424
2004–05	6,697	44,318
2009–10	8,024	46,348
2014–15	10,250	32,663
2015–16	10,768	32,290
2016–17	11,000	32,000

Note: 1990 marked the introduction of independent taxation. Prior to that date, the personal allowance was known as the single person's allowance … A complete series of allowances in nominal terms, is on this site. … RPI used to uprate to April 2016 prices using Office for National Statistics, Dataset: Consumer Price Inflation.

In turn this trend has been associated with a marked increase in the number of taxpayers paying income tax at the highest marginal rates:[53]

Table 12. Numbers liable for income tax (thousands)

	Number of individuals paying tax	*Number of starting-rate taxpayers*	*Number of basic-rate taxpayers*[a]	*Number of higher-rate taxpayers*[b]
1979–80	25,900	—[c]	25,226[c]	674
1984–85	23,800	—	22,870	930
1989–90	25,600	—	24,040	1,560
1994–95	25,300	5,180	18,200	2,000
1999–2000	27,200	2,280	22,354	2,510
2004–05	30,300	3,570	23,333	3,330
2009–10	30,600	163[d]	27,202	3,190
2014–15[e]	30,500	236[d]	25,516	4,759
2015–16[e]	30,200	—	25,249	4,957
2016–17[e]	30,100	—	25,309	4,743

Notes :

[a] Includes those whose only income above the starting-rate limit is from savings or dividends. [b] Includes additional-rate taxpayers from 2010–11. [c] Figure for 1979–80 covers both starting-rate and basic-rate taxpayers. [d] From 2008–09, the starting rate applies only to savings income that is below the starting-rate limit when counted as the top slice of taxable income (except dividends). [e] Projected. Source: HM Revenue & Customs, table 2.1, Inland Revenue Statistics 1994.

The number of higher- and additional-rate taxpayers has grown quickly over the last 30 years or so, from less than 3% of the taxpaying population in 1979–80 to around 15% in 2016–17.

Some of this growth reflects periods when the threshold above which higher-rate tax is due has not been raised in line with price

53 IFS Briefing Note BN09, November 2016 pp43-4

> inflation, some reflects the fact that incomes on average have grown more quickly than prices, and some the fact that the dispersion of incomes has grown, with especially rapid increases in the incomes of those already towards the top of the income distribution, pushing more of them into higher-rate income tax liability.
>
> In recent years, this trend has also been driven by large increases in the personal allowance, taking many low earners out of income tax altogether. The number of starting-rate taxpayers climbed in the years after 1992 as the width of the starting-rate band was increased, but it fell sharply in 1999– 2000 as the 10% rate applied over a much narrower range of income than the 20% rate that it replaced.
>
> The abolition of the starting rate for non-savings income in 2008-09 massively reduced the number of starting-rate taxpayers, before it was abolished for savings income too in 2015–16.

The authors underline that in 2016/17 it was estimated that 30.1m individuals were liable for tax, out of an adult population in the UK of around 53.2m. "This is a reminder that attempts to use income tax reductions to help the poorest in the country are likely to fail, since less than three-fifths of the adult population have high enough incomes to pay income tax at all."[54]

Although the numbers of taxpayers paying the additional and/or higher rates of tax have grown, they remain a minority – around 15% of all taxpayers.[55] However, this group pays a very large share of the total amount of income tax that is paid. It is estimated that in 2018/19, 60% of all income tax was paid by the top 10% of income tax payers and 28% was paid just by the top 1% of taxpayers.[56]

The percentage shares paid by the top 10% and 1% have risen a little over time; in 2012/13 they were 56% and 25% respectively. Commenting on these figures in their 2013 Green Budget, the IFS noted "since income tax payers make up less than three-fifths of the UK's adult population, these contributions are actually coming from the top 5.8% and 0.58% of individuals respectively."[57]

Of course, income tax is only one part of national taxes, and the tax is more progressive than the other broad-based taxes, VAT and NICs.[58]

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54 *op.cit.* pp43-4. The authors add, "We might be more interested in the proportion of adults who live in a family containing a taxpayer. Authors' calculations using the IFS tax and benefit model, TAXBEN, run on data from the Family Resources Survey, suggest that this figure stood at 73% for Britain in 2014–15 (the latest year for which data are available): most nontaxpaying adults do not have taxpayers in the family."

55 HMRC estimate that in 2018/19, there will be just under 4.3m higher tax ratepayers, and 393,000 additional rate taxpayers, in a total taxpayer population of 31m (HMRC, *Statistics: Number of individual income taxpayers* (Table 2.1), May 2018.

56 HMRC, *Statistics : Shares of total income tax liability* (Table 2.4), May 2018

57 *The IFS Green Budget 2013*, February 2013 pp 250-1. The 2013 Budget report illustrated this pattern of income tax receipts (see, *Budget 2013*, HC 1033, March 2013 p58, Chart 1.21).

58 For a wider discussion as to the options for raising tax see the IFS's last *Green Budget* published in October this year (see, Chapter 5: Options for raising taxes).

2. The Coalition Government's tax priorities

In its Agreement published in May 2010, the new Coalition Government set out a number of priorities for the personal tax system; principal among these was a commitment to increase the personal allowance each year, so that it would reach £10,000 by 2015:

> We will announce in the first Budget a substantial increase in the personal allowance from April 2011, with the benefits focused on those with lower and middle incomes … We will further increase the personal allowance to £10,000, making real terms steps each year towards meeting this as a longer-term policy objective. We will prioritise this over other tax cuts, including cuts to Inheritance Tax.[59]

The Coalition Agreement combined elements from both parties' manifestos for the General Election. In this case, the idea of substantially increasing the personal allowance had been raised by the Liberal Democrats. The Party proposed that the allowance should be set at £10,000 at a projected cost of £16.8 billion, to be funded by a series of tax increases, including a new limit to the value of tax relief on pension contributions, a 'mansions tax' on residential property, reforms to capital gains tax and air passenger duty, and a variety of measures to increase tax receipts from reducing avoidance.[60] In its commentary on the main parties' fiscal plans, the IFS noted that the Liberal Democrats anticipated keeping the basic rate threshold unchanged, giving most taxpayers a tax cut worth £705:

> Those with the lowest incomes – non-taxpayers – would not gain from this reform. And families with two taxpayers would gain more than families with one taxpayer, who tend to be worse off. Thus, overall, better-off families (although not the very richest) would tend to gain most in cash terms from this reform. But clearly £705 would be less valuable to those on higher incomes than to those on lower incomes: as a percentage of income, the largest gains are around the upper-middle of the income distribution rather than at the top. In isolation, this giveaway could not be described as progressive; but to judge the distributional impact of the Liberal Democrats' package as a whole we must also consider who would lose from the tax rises they would introduce to pay for this tax cut.[61]

In his first Budget the Chancellor, George Osborne, announced that the basic personal allowance would be increased by £1,000 from April 2011. In his speech Mr Osborne argued that increasing the allowance was important "to lift people out of the income tax system and allow them to keep more of their hard-earned money":

> A responsible society is one that rewards the efforts of those who choose to work. The income tax system-in particular, the abolition of the 10% rate of income tax-has meant that many people on

[59] HMG, *The Coalition: our programme for government*, 20 May 2010 p30
[60] *Liberal Democrat Manifesto: Change that works for you*, April 2010 p13-14, p100
[61] Stuart Adam et al., *Taxes and benefits: the parties' plans: IFS Election Briefing Note*, 27 April 2010 pp35-6

> lower incomes face higher average tax rates. I believe that it is important to lift people out of the income tax system and allow them to keep more of their hard-earned money. It is especially important to make progress in this Budget, in which we are asking so much of so many, and this demonstrates that the coalition Government put fairness first.
>
> In the current system, everyone under the age of 65 is eligible for a tax-free personal allowance of £6,475. That means that many thousands of people have their income taken away from them in tax, only to have to apply to get it back in benefits. That does not reward work. So today I can announce that we will increase the personal allowance by £1,000 in April. People will be able to earn £7,475 before they have to start paying income tax, 23 million people who are basic-rate taxpayers will each gain by up to £170 a year, and 880,000 of the lowest-income taxpayers will be taken out of tax altogether. Higher-rate taxpayers will not benefit from the change, and the higher-rate income tax threshold will have to remain frozen until 2013-14.
>
> Our long-term objective remains to increase the personal allowance to £10,000, as set out in the coalition agreement, and we will take real steps towards achieving that objective during the rest of this Parliament.[62]

Generally reactions to the Budget focused on the Chancellor's plans for reducing public expenditure in future years, and two tax increases for 2011: an increase in the standard rate of VAT from 4 January, and a new levy on the banking sector to be introduced in the same month.[63] Taken together, the two tax measures were estimated to raise £14.8 billion by 2012/13. However, the amount of money to be raised by the Budget was significantly less than this, owing to two tax cuts the Chancellor announced as well: an increase in the threshold for employers National Insurance contributions, and the £1,000 increase in the personal allowance.[64]

The 2010 Budget made no mention of the age-related allowances (ARAs) for those aged 65 and over. In December 2010 the Government announced tax rates, thresholds and allowances for the 2011/12 tax year; as part of this, it confirmed that the two ARAs would rise in line with inflation from April 2011.[65] It is standard practice to announce personal allowances for the coming year at this time, first, to allow updated tax codes to be issued to taxpayers prior to the new tax year, and second, for the government of the day to take into account the statutory requirement to uprate allowances in line with inflation.

In the 2011 Budget the Government announced a further increase in the basic allowance – which would go up by £630 to £8,105 in 2012/13. In his speech the Chancellor noted that in the previous year the higher rate threshold had been cut sufficiently to restrict the benefit of the higher allowance to basic rate taxpayers. By contrast for 2012/13 this threshold would be reduced by an equivalent sum, so as not to

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62 HC Deb 22 June 2010 c179
63 For example, "Chainsaw massacre is delayed", *Times*, 23 June 2010
64 It was estimated these measures would cost £3.15bn and £3.7bn in 2012/13, respectively: *Budget 2010*, HC 61, June 2010 (Table 2.1 – items 1, 8, 11, 12).
65 HC Deb 2 December 2010 c85WS

increase the numbers of higher rate taxpayers.[66] The Government also announced that from April 2012 the default indexation assumption for direct taxes would be the Consumer Price Index (CPI). RPI would be retained for some allowances and thresholds for the duration of the Parliament: specifically, the employer NICs threshold, the age-related allowance and other thresholds for older people.[67]

As before, other elements of Mr Osborne's speech dominated the press coverage of the 2011 Budget – in particular, the Chancellor's decision to cut the rate of fuel duty and suspend plans, inherited from the previous Government, to increase duties in real terms in future years.[68] Both decisions involved considerable sums of money.[69] The Budget report stated that, with the increase in the personal allowance announced in the previous Budget, 1.1 million people would be taken out of income tax. A regional breakdown of these numbers was given in answer to PQs though no estimates were produced at a constituency level.[70] As the Government underlined subsequently, "reliable estimates are not available at parliamentary constituency level due to greater uncertainties in making projections for small geographical areas."[71]

Provision for the first increase in the allowance was made in s3 of the *Finance Act 2011*. This was the subject of a short debate at the Committee stage of the Finance Bill in May that year. Speaking for the Opposition, David Hanson was positive about the change, but went on to argue that it could not be taken in isolation: "[the increase] is of great benefit to those who pay income tax. However, we also have to face a rise in VAT, a freeze in child benefit and cuts in working family tax."[72] In response the Treasury Minister David Gauke acknowledged that the increase would benefit 23 million people "at a time when we have to make difficult choices", but went on to argue "it is unfair that people who earn relatively small amounts of money should be caught up in the income tax system."[73]

Provision to increase the allowance by a further £630 for 2012/13 was made by s3 of the *Finance Act 2012*. Although the provision was not selected for debate on the floor of the House, it was debated at some length in Committee.[74] Speaking for the Opposition, Owen Smith did not oppose the increase itself, but argued that the Government should publish a review of its impact on families compared with other tax and benefit reforms: "the reality is that the increase in personal allowances is far outweighed by the increases in VAT, by the cuts to tax credits, by the changes to child benefit rules and by the increased prices paid

66 HC Deb 23 March 2011 c963
67 *Budget 2011*, HC 836, March 2011 paras 1.127-8
68 For example, "Priming the pump", *Times*, 24 March 2011
69 The cut in fuel duty was estimated to cost £1.6bn in 2012/13; the increase in the personal allowance for that year was set to cost £1.1bn: HC 836, March 2011 (Table 2.1 – items 27 & 22).
70 HC Deb 13 May 2011 cc1392-4W. see also, *The increase in the personal allowance : regional statistics*, Commons Briefing paper CBPSN6280, 29 March 2012
71 HC Deb 11 February 2013 cc446-7W. see also, PQ 907976, 10 March 2015
72 Public Bill Committee (Finance Bill), *Second sitting*, 10 May 2011 c51
73 *op.cit.* c55. In the event this provision was agreed without a vote.
74 PBC (Finance Bill), *Second, Third & Fourth sittings*, 24-26 April 2012 cc46-103

everywhere in the country, including for fuel."[75] Mr Smith argued that the Government had misrepresented the distributional impact of this policy, as "the reality is that the benefit is largely felt in the middle and at the upper end of the income spectrum."[76] In response the Treasury Minister David Gauke argued that the Budget report provided a detailed assessment of the impact of tax and benefit changes across the income spectrum:

> The reality is that the biggest contribution is coming from the highest earners, and the reality is that we have been able to find, even within the constraints, the money to increase the personal allowance in a way previously unseen, taking millions out of tax, reducing the burden on 25 million people and benefiting basic rate taxpayers. That is something of which the Government can be proud.[77]

In the event the Committee rejected the Opposition's amendment by 15 votes to 13.[78]

As noted, the allowance was increased by another £1,335 from April 2013, to £9,440 for 2013/14. The Chancellor had initially proposed the allowance should go up by £1,100 in his 2012 Budget,[79] but revised this by an additional £235 in his Autumn Statement on 5 December 2012.[80] It was estimated that this would lift another 250,000 individuals out of income tax.[81] A regional breakdown of the total numbers taken out of income tax by these increases to the personal allowance was also given in answer to PQs.[82]

Although the higher rate threshold was cut in April 2013 – from £34,070 to £32,010 – this did not withdraw all the extra benefit of the higher personal allowance from higher rate taxpayers.[83] Furthermore, at this time the Government announced that for the two year period 2014/16 the higher rate threshold would be increased, though by 1% only, rather than in line with inflation.[84]

In the 2012 Budget the Chancellor announced two other important changes to the structure of income tax, to take effect from April 2013. First, the two age-related allowances would be frozen at their 2012/13 levels, until they became aligned with the personal allowance. In addition, from this date only existing recipients of these extra allowances would be entitled to claim them. Second, the 50p additional rate of tax would be cut to 45%. As with previous Budgets, the increase

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75 PBC (Finance Bill), *Second sitting*, 24 April 2012 c47
76 *op.cit.* c49
77 PBC (Finance Bill), *Third sitting*, 26 April 2012 c91. The Minister is referring to an annual analysis of the distributional impact of tax and benefit reforms, initiated in the Coalition Government's first Budget. Annex B to the 2012 Budget looked at the cumulative impact of reforms on households since June 2010.
78 PBC, *Fourth sitting*, 26 April cc102-3
79 HC Deb 21 March 2012 c807
80 HC Deb 5 December 2012 c882
81 *Autumn Statement*, Cm 8480, December 2012 para 1.144.
82 HC Deb 28 January 2013 cc620-1W
83 This was illustrated in calculations published in the *Autumn Statement* (Cm 8480 December 2012 p47).
84 *Autumn Statement*, Cm 8480 December 2012 para 1.160. At the time it was estimated this would raise £320m in 2014/15 rising to £1.04bn by 2017/18: *Budget 2014*, HC 1104, March 2014 p59 (Table 2.2 – item bm).

in the personal allowance attracted little comment in the coverage of the 2012 Budget, in comparison to these other changes.[85]

In their 2013 *Green Budget* the IFS noted that cutting the higher rate threshold in April 2013 would increase the number of higher rate taxpayers:

> [From April 2013] the higher-rate threshold – the point at which the marginal income tax rate rises from 20% to 40% – is being reduced by £1,025 in cash terms. The upper earnings limit – the point at which the marginal rate of employee National Insurance contributions falls from 12% to 2% – is sensibly being kept aligned with the higher-rate threshold. The combined effect of these income tax and National Insurance changes on earners who pay the higher rate of income tax is a gain of just £8.50 in 2013–14, relative to the default of RPI indexation.[86]
>
> This continues the recent pattern of restricting the gains to higher-rate taxpayers (and hence the exchequer cost) from increases in the personal allowance.[87] The higher-rate threshold – that is, the point at which an individual starts to pay the higher marginal rate of income tax – will be £41,450 in 2013–14. Had it simply been uprated in line with the RPI since 2010–11, it would have been 20% higher, at £49,845, and there would have been an estimated 1.6 million fewer higher-rate income tax payers in 2013–14 as a result.[88],[89] Note that, because the higher-rate threshold and the upper earnings limit have been kept aligned … the effect has been to raise the combined income tax and employee National Insurance rate from 32% to 42% on income between £41,450 and £49,845.

The authors went on to note that increasing the personal allowance provides a tax cut for all basic rate taxpayers: by itself, this approach would not target relief to those on the lowest incomes, and, as noted above, it is expensive:

> By lowering the marginal income tax rate from 20% to 0% over a range of (low) income, increases in the personal allowance strengthen the financial incentive for low earners to work and for those with incomes no higher than the allowance to earn a little more (although it is important to note that for those also subject

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85 Two other Library papers discuss these changes: *Age-related personal allowance*, CBP6158, 11 May 2016; and, *Income tax : the additional 50p tax rate*, CBP249, 26 September 2018.

86 This does not apply to those with taxable incomes exceeding £100,000 per year, who lose overall from these changes. The personal allowance is gradually withdrawn as taxable income rises between £100,000 and £118,880, so individuals with incomes this high do not gain (or gain only partially) from increases to the personal allowance, but they lose from reductions to the higher-rate threshold.

87 In fact, without any adjustment to the basic-rate limit, higher-rate taxpayers would gain twice as much in cash terms as basic-rate taxpayers from personal allowance increases. This is because the higher-rate threshold is not a tax parameter that is explicitly uprated – rather, it is simply the sum of the personal allowance and the basic-rate limit, which are each uprated individually. Therefore, an increase in the personal allowance in isolation increases the higher-rate threshold by the same amount. Without a corresponding adjustment to the basic-rate limit, the effect on higher-rate taxpayers is to save them 40% tax over a range of income (rather than 20% as for basic-rate taxpayers).

88 Source: authors' calculations using the 2010–11 Family Resources Survey and TAXBEN, the IFS tax and benefit microsimulation model.

89 The government also plans to increase the higher-rate threshold by 1% in cash terms – a further real cut, provided inflation exceeds 1% as currently forecast – in both April 2014 and April 2015.

to the withdrawal of benefits and tax credits when entering work or increasing earnings, the strengthening of work incentives can be much more modest than the decline in headline income tax rates suggests). But they are also giveaways to every basic-rate taxpayer aged under 65 in the country, and this has two important consequences.

First, alongside the fact that the lowest-income families tend not to pay income tax anyway, it helps explain why, contrary to popular perception, the policy is not 'progressive'. The largest average gains – in cash terms and as a percentage of income – go to those in the middle and upper-middle of the income distribution. In particular, two-earner couples gain twice over. (This is, however, the most progressive way of cutting income tax.)

Second, increases in the personal allowance are expensive. Even net of the various adjustments to the higher-rate threshold that have been used to limit the gains to higher-rate taxpayers, the government's discretionary increases to the personal allowance in this parliament will cost the exchequer about £9.0 billion in 2013-4.[90]

[90] *The Institute for Fiscal Studies Green Budget*, February 2013 pp188-9

3. Setting a £10,000 allowance

With the allowance set at £9,440 for 2013/14, it was noted that the goal of a £10,000 allowance could be reached in two years' time, by April 2015, simply by uprating it in line with inflation.[91] Prior to the 2013 Budget, there was some discussion of how income tax should be reformed once this goal was met. The Conservative backbencher, Robert Halfon, launched a campaign for the introduction of a 10p starting rate of tax, as an alternative to any further increase in the allowance. Mr Halfon put his case in a debate in Westminster Hall in January:

> My hope is that once the threshold reaches £10,000, we will consider bringing back the 10p rate for the lower-paid. Some Liberal Democrats disagree; they have suggested that the best way to help families is to raise the personal allowance even further, to something like £12,500 a year. I absolutely agree the coalition should fulfil its £10,000 commitment, but it would be unwise to raise the personal allowance even further. Everyone should feel that they have a stake in the state, and they should have some stake in the tax system even if they pay only a small amount, because they need to realise that public services are not free and that there is no magic money tree.
>
> My fear is that the Liberal Democrats want to pay for their policy, which will cost £14 billion if applied to everyone, by dragging even more workers into the 40p band. That is what has happened historically. The problem is that we will soon have families with not very high wages paying a marginal rate of 40p, and that will include police officers, shop owners, managers and senior nurses in the national health service.[92]

On this occasion Shadow Treasury Minister, Catherine McKinnell, argued that it would be preferable for the Government to retain the 50% rate and abandon its proposals to cap the annual uprating of most working-age benefits to 1%.[93] Ms McKinnell characterised the Opposition's approach to protecting those on lower-incomes as follows:

> The Labour party's approach has been clear—to tackle issues of low pay and to ensure that work always pays. We therefore want support for those who need extra help to make work pay, to keep them off benefits and to ensure that they can afford necessities such as child care so that they can stay in work. We have made our policy clear and we are therefore proud of what we achieved through the tax credit system.[94]

In response Treasury Minister David Gauke said that the Government would not make any commitments as to future changes, once the allowance had reached £10,000, while he acknowledged "there are pros and cons both to personal allowance increases and to a new lower rate." The Minister went on to contrast the Government's approach to

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91 Institute for Fiscal Studies, *2013 Green Budget*, February 2013 p187
92 HC Deb 22 January 2013 c36-7WH
93 HC Deb 22 January 2013 c50WH. Provision to this effect is made in the *Welfare Benefits Uprating Act 2013* (Library Research paper 13/01, 4 January 2013). For details of the current state of play see, *2018 Benefits Uprating*, CBP8162, 12 January 2018.
94 HC Deb 22 January 2013 c46WH

setting the allowance with the previous Government's decision to abolish of the 10p rate in 2008:

> People under the age of 65 with non-savings income between £5,435 and £19,355 would have paid more [from the abolition of the 10p rate], because they lost more from the abolition of the 10% rate than they gained from the cut in the basic rate …The loss was greatest, at £232 a year, for someone earning £7,755 - the top of where the 10% band would have been. Those most affected by the abolition of the 10p rate appear to have been those below the age of 65 with an income under £18,500 who were in childless households …
>
> [One way to look at the current situation] is by comparing the approach that we have taken in increasing the personal allowance with the approach that the previous Government took in doubling the 10p rate of income tax. I talked about those who earn £7,755 a year and lost the most—£232 a year—as a consequence of the doubling of the 10p rate in 2008-09. In that year, an individual would have paid £344 in income tax.
>
> Under the present Government, in 2012-13, such an individual, with income adjusted for inflation to £8,299 a year, will pay about £39 in income tax—not £344 but £39 in tax, which is a saving of £305. In 2013-14, again with income adjusted for inflation, such an individual will pay no income tax at all. That is a contrast that I am very happy to highlight.[95]

In his speech, Mr Gauke noted that there would be a substantial fiscal cost in reintroducing the 10p rate, and a written answer at this time gave an estimate of how much it might cost:

> **Robert Halfon:** To ask the Chancellor of the Exchequer if he will estimate the cost to the Exchequer of reintroducing an income tax rate of 10p on all earnings between £9,205 and £12,000 from financial year 2013-14; and if he will make a statement.
>
> **Mr Gauke:** The autumn statement announced that the income tax personal allowance for 2013-14 will be increased to £9,440. This supersedes the Budget 2012 announcement that it would be increased to £9,205.
>
> The cost to the Exchequer of reintroducing an income tax rate of 10p on all earnings between £9,440 and £12,230 (i.e., in the same band as the starting rate for savings) is estimated to be around £7.3 billion in 2013-14.
>
> This estimate is based on the 2009-10 Survey of Personal Incomes, projected to 2013-14 using economic assumptions consistent with the Office for Budget Responsibility's December 2012 economic and fiscal outlook.[96]

In February 2013 the Labour leader Ed Miliband gave a speech on economic policy in which he stated that an incoming Labour Government would reintroduce a 10p starting rate, financed by a 'mansions tax' – an annual levy on houses worth over £2m. Mr Milband did not give any details of how much this levy might raise, or how wide a 10p band could be:

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95 HC Deb 22 January 2013 cc53-4WH
96 HC Deb 14 January 2013 cc566-7W

> It is different choices and new priorities that will turn our economy around. That means starting by protecting the incomes of working people with new priorities in taxation …
>
> Let me tell you about one crucial choice we would make, which is different from this government. We would tax houses worth over £2 million. And we would use the money to cut taxes for working people. We would put right a mistake made by Gordon Brown and the last Labour government. We would use the money raised by a mansion tax to reintroduce a lower 10 pence starting rate of tax, with the size of the band depending on the amount raised. This would benefit 25 million basic rate taxpayers …
>
> We've rightly said that we will only set out our tax and spending commitments at the next general election. That is the way a responsible opposition should conduct itself. However this is a clear signal about the priority we attach to a fairer tax system and the living standards of working people.[97]

The speech was not accompanied by a policy document, although the Shadow Chancellor, Ed Balls, was reported to have suggested that the tax would raise about £2 billion.[98] Mr Miliband's proposal gathered quite a lot of coverage, although some commentators raised doubts as to its effectiveness. The IFS published a short commentary in which it argued that the mansions tax reflected "a problem with the current tax system … but does not take the idea forward to its logical conclusion". On the 10p rate, the authors suggested that it had "no plausible economic justification":

> Reintroducing Labour's 10p rate in full would reduce tax revenues by around £7 billion a year and benefit basic rate taxpayers by up to £271 a year, though … it is unlikely that anything close to this amount could be raised through a mansion tax alone. To introduce a £1,000 10p tax band, which would benefit all 23.5 million basic-rate taxpayers, one would need to raise £2 billion, or around £30,000 on average from each of the 70,000 owners of 'mansions' …
>
> A 10p tax rate would reduce taxes for those on low incomes and strengthen their work incentives. A far simpler and more sensible way of achieving these aims would be to spend the same amount of money on increasing the personal allowance … This would have virtually the same impact on individuals' tax payments …, be slightly more progressive, take some people out of income tax altogether and avoid the complexity involved in introducing a new income tax rate. An even better alternative … would be to increase the point at which individuals start paying employee National Insurance Contributions. This would also bring the income tax and National Insurance systems more in line and would take some people out of direct tax altogether. And if one wanted to focus the gains from the policy on low-income working families … increasing Working Tax Credits would be another sensible alternative to look at …

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97 Labour Party press notice, *Speech by Ed Miliband : Rebuilding Britain with a One Nation economy*, 14 February 2013. See also, "Miliband attempts to shake off Brown legacy", *Financial Times*, 15 February 2013 & "Ed Miliband aims to right a wrong with restoration of 10p tax rate", *Guardian*, 14 February 2013

98 "Ed Miliband backs 'mansion tax' to fund 10p tax rate return", *BBC News*, 14 February 2013. For further details of the proposal for a 'mansions tax' see, *Land Value Taxation*, Commons Briefing paper CBP6558, 17 November 2014.

> The proposal for a new 10p starting rate of income tax … appears to repeat the same error perpetrated by Denis Healey in 1978 (undone by Geoffrey Howe in 1980), Norman Lamont in 1992 and Gordon Brown in 1999 (which he himself undid at considerable political cost in 2007). To have observed lower starting rates of tax being introduced and abolished by governments of both complexions over the last three decades and then to propose the same thing again suggests a remarkable failure to learn from history.[99]

Writing in the *Financial Times*, John Kay suggested that a reduced starting rate had only a superficial appeal, the result of "a confusion of algebra and a mistake about data." On the first point, Professor Kay argued that many individuals confused the marginal rate with the actual share of someone's income paid in tax – their average rate. He went on to suggest that those on very low incomes tended to be *secondary* earners contributing to household income – married women, retired parents, and young people. Poor households would be characterised more accurately as those with only a single earner, just slightly off the very bottom of the income distribution. These households would be much better targeted by measures through the benefits system, not changes to the schedule of tax rates: "tax systems are delicate, complex instruments and politicians tinker with them at their peril. But they never learn that lesson, which is why history, and this column, is so often repeated."[100]

Writing in the *Observer* Andrew Rawnsley argued that "as a piece of politics" the announcement was "pretty sharp". He suggested that a mansions tax would be the "next best alternative" to rebanding council tax, but questioned whether its proceeds should be used to reintroduce a 10p starting rate: "Lower starting rates of tax have been introduced by both Labour and Tory chancellors looking for an eye-catching headline that they hoped would deliver an electoral dividend. These new bands have then been undone later by another chancellor because he wanted the money to generate a different kind of eye-catching headline in the hope of winning votes."[101] An editorial in the *Guardian* was more critical:

> It is all very neurotic, but the impulse to use the income tax system to send silly signals is not an exclusive Labour preserve. And the signals are reliably silly because – with income tax bringing in only 26p in every pound of government revenue – what is given with one hand is invariably taken away with the other …
>
> In more recent times, it has been the Liberal Democrats who have taken the income tax fetish to new heights; their costly fixation with raising the allowance is supposed to justify every anti-poor horror committed by the coalition. Always described as "lifting the poorest out of tax", the case for the higher threshold seems unanswerable – until you consider that the very lowest earners get less of the gain, and that those without work get nothing at all …

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99 James Browne et al., *Better options exist to help low earners than 10p tax rate: IFS Observations*, 14 February 2013

100 "Labour's new tax policy is a mistake – one it has made before", *Financial Times*, 20 February 2013

101 "Ed Miliband's 10p tax pledge is smart politics but poor policy", *Observer*, 17 February 2013

> All these shortcomings of Nick Clegg's personal allowance policy also apply to Ed Miliband's 10p band, which is a somewhat more complicated means of achieving the same thing, or – to be blunt – of achieving not very much … It is high time for avowedly progressive politicians to come up with a smarter idea than cutting the most progressive big tax of the lot.[102]

The issue was the subject of an Opposition Day debate on the fairness of the tax system the following month. Opening the debate for the Opposition, Chris Leslie argued that any revenue from a mansions tax "should fund the reintroduction of a 10p starting rate", though Mr Leslie did not give many details on the design of such a tax:

> There are ways of introducing a mansion tax that could take account of the specific circumstances in which people are asset-rich and cash-poor, but there would probably be very few such cases … [In a radio interview the Deputy Prime Minister, Nick Clegg] said that individuals in such circumstances might be able to defer payments until the house was sold or to "leverage" the value of the property by remortgaging. I am not sure that that strategy provides the complete solution to the conundrum, but I do think that those in the Treasury should turn their minds to how to tackle these rare circumstances.[103]

Mr Leslie went on to explain why, in his view, the 10p rate should be reintroduced:

> I believe that a steadier incline moving from zero tax to 10p and from 10p to 20p could be the bedrock of a more progressive tax system, sending out an important signal that tax cuts for working people are a priority. The 10p starting rate would provide a tax incentive to enter work, especially for those on lower wages. It was a mistake to remove the 10p rate in 2007, even though it enabled the then 22p basic rate to be reduced to 20p, where it stands today. Reintroducing a 10p rate would be the right thing to do and, if the Liberal Democrats are correct that the mansion tax could raise £2 billion, the Chancellor could make that change next week in the Budget.[104]

In response Treasury Minister David Gauke set out a number of concerns about a new annual levy on mansions:

> A third of the properties in London worth more than £2 million have been in the same ownership for over 10 years, and that a mansion tax could hit asset-rich but potentially income-poor households … [This] would need to be addressed in the design and would obviously have an impact on the costing … [The tax] would be administratively burdensome for HMRC to operate, not to mention intrusive for the person having their home inspected. We would have concerns that in Labour's hands, the starting level for such a tax would not stay at £2 million for very long. What began as a mansion tax would soon become a homes tax.[105]

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102 "Editorial: Politicians and income tax: 10p or not 10p - that is the irrelevant question", *Guardian*, 17 February 2013

103 HC Deb 12 March 2013 c164, c167. At a later stage in the debate the Shadow Treasury Minister, Catherine McKinnell suggested the mansion tax could raise £2bn, "to fund a 10p tax band of up to £1,000, benefiting 25 million basic rate taxpayers to the tune of £100" (*op.cit.* c210).

104 *op.cit.* cc171-2

105 *op.cit.* c177

The Minister went on to discuss the Government's case for the two income tax changes set for 2013/14: the third increase in the personal allowance, and the cut in the additional rate of tax to 45%:

> In 2010, someone on £6,500 was paying income tax at 20%. From next month, someone has to earn £9,440 before paying any income tax at all … Our constituents on £9,000 a year will soon be paying no income tax at all, saving more than £500 since the coalition came to power. Labour turned a 10p rate of income tax into a 20p rate. This coalition has turned a 20p rate into a 0p rate…
>
> Let me say something that I hope is not controversial: the principal purpose of income tax is to raise revenue. So we commissioned HMRC to analyse just how effective the 50p rate was in raising revenue. That HMRC report, laid before the House, set out thorough and compelling evidence on the impact of the 50p rate. It showed that the rate was uncompetitive, distortive and inefficient. Not only did it not raise much revenue, but it could even have cost the Exchequer money when the indirect impacts on other taxes were taken into account.
>
> This Government were not prepared to maintain a rate of income tax that was both ineffective at raising money and that left us with the highest statutory rate of income tax in the G20, so we acted, in the interests of the country, and the top rate of tax will fall to 45p from April this year. This will see our top rate of tax drop below that of Australia, Germany, Japan and Canada, which will send a signal to businesses taking decisions on investment and location that the UK is a competitive environment.[106]

In his Budget statement on 20 March the Chancellor announced that the allowance would be set at £10,000 from April 2014:

> From 2014, there will be no income tax at all on the first £10,000 of your salary—£10,000 of tax-free earning. That is £700 less in tax for working families than when this Government came to office. Almost 3 million of the lowest paid will pay no income tax at all. It is a historic achievement for this Government and for hard-working families across the country.
>
> I am aware that the concept of a 10p tax rate has caused problems for Labour Members. First, they introduced it before deciding that introducing it was a mistake and that it ought to be abolished. Then they decided that abolishing it was a mistake and that they ought to introduce it again. To put them out of their misery, we are going to turn their 10p band into a 0p band, so they do not have to worry about it any more. Every person who is paying at the 10p rate that Labour doubled will now pay no income tax at all.[107]

The Budget report provided details of the tax saving that individuals would make, across the income spectrum.[108] People on the highest incomes would see little if any tax saving from the rise in the personal allowance. As noted, since 2010/11 the personal allowance has been

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[106] *op.cit.* cc178-9, c181. In the event the Opposition's motion was defeated by 304 votes to 241 (c215).

[107] HC Deb 20 March 2013 c944. The Chancellor's calculation wass "based on an individual with an income in 2007-08 of up to £7,455, equal to the personal allowance plus the starting rate threshold, and adjusted in line with earnings growth to £8,520 in 2014-15" (*Budget 2013*, HC 1033, March 2013 p52 fn51).

[108] Budget 2013, HC 1033, March 2013 pp52-3

withdrawn from individuals earning over £100,000, by £1 for every £2 someone's income exceeds the threshold. Of course, a second factor at play has been the reduction in the higher rate threshold – the point at which someone's income becomes liable to the 40% rate.

In the Autumn Statement in December 2012, the Government had proposed that for the two years 2014-16 the threshold would rise by 1% a year, rather than going up in line with inflation. This was confirmed in the 2013 Budget. As the personal allowance would be £10,000 from April 2014, the basic rate threshold would be cut to £31,865 – a change estimated to raise £1.04 billion by 2016/17. By comparison, the cost of setting the personal allowance at £10,000 was estimated to be £1.16 billion in 2014/15.[109] The Budget also confirmed that, with the allowance reaching £10,000, from 2015/16 the inflation index to be used for uprating the personal allowance would be CPI, rather than RPI.[110]

As with Budgets past, commentary on the 2013 Budget tended to focus on other issues.[111] In his post-Budget presentation, the director of the IFS, Paul Johnson, noted the rising cost of this policy, and the other two tax cuts that had been a continued feature of Mr Osborne's Chancellorship – reductions in the main rate of corporation tax, and freezing duty rates on road fuels:

> Three of [the tax cuts set out in the Budget] were very much continuations on a familiar theme – a further increase in the income tax personal allowance, yet another cancellation of increase in fuel duties, and a further cut to rate of corporation tax. Add together all the cost of all the changes to these taxes since 2010 – including the cost of abolishing the fuel duty escalator – and the Chancellor will be spending a pretty remarkable £24 billion a year on these changes by 2016-17 … It's a combined tax cut worth nearly double the amount raised by the rather painful increase in the main rate of VAT to 20% in 2011.
>
> The biggest of these investments – at nearly £11 billion in 2016/17 – is in the increase in the personal tax allowance. The Chancellor will also be bringing in £5 billion less fuel duty revenue than he might have done had he continued with the duty escalator. Between them these changes help explain why basic rate taxpayers, middle earners – those in the upper middle part of the overall income distribution – have been least squeezed by the tax and benefit changes implemented as part of the fiscal consolidation. Poorer households have been hit harder by benefit cuts. Higher rate taxpayers, and especially richer higher rate taxpayers, have seen their tax bills rise quite sharply. In terms of effects on household budgets this year yesterday's announcements were something of a non-event. But don't forget that there are some substantial benefit cuts happening in April and some tax cuts too.[112]

Provision to set the personal allowance for 2013/14 was made by s2 of the *Finance Act 2013*.

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109 *Budget 2014*, HC 1104, March 2014 p59 (Table 2.2 – item bm & item az)
110 *op.cit.* para 1.170
111 see, *Budget 2013: Reaction*, Lords Library Note LLN2013/007, 21 March 2013
112 Paul Johnson, IFS Budget briefing: introductory remarks, 21 March 2013 pp6-7

When considered in Committee, the debate focused on the freezing of age-related allowances, and the distributional impact of the Government's tax and benefit changes. Speaking for the Labour Party Catherine McKinnell said "the Opposition do not believe that the increase in personal allowance is a bad thing …Taking people on the lowest incomes out of tax altogether and reducing the level of income tax paid by those on low and middle incomes is a positive move", though she went on to note an estimated "3 million households will see no benefit from [both this and next this year's increase] … because their income is simply too low to be taxed at all."[113] In response Treasury Minister David Gauke said, "this is a policy that supports hard-working individuals on low incomes and has ensured that those on the national minimum wage have seen their income tax bills cut in half under this Government."[114]

113 Public Bill Committee (Finance Bill), *First Sitting*, 23 April 2013 cc23-4
114 PBC (Finance Bill), *Second sitting*, 23 April 2013 c76

4. Budget 2014 & Budget 2015

In his 2014 Budget Mr Osborne announced that the allowance, rather than going up in line with inflation, would rise to £10,500 from April 2015. In previous years most, if not all, of the potential benefit for higher rate taxpayers had been 'clawed back' by cutting the higher rate threshold. In his Budget Mr Osborne confirmed that this threshold – the sum of the personal allowance and the basic rate limit – would rise by 1% for 2014/15, and by 1% for 2015/16. As a consequence, most higher rate taxpayers would receive a tax cut of an equivalent size to basic rate taxpayers:

> Next year, there will be no income tax at all on the first £10,500 of your salary—£10,500 tax free and £800 less in tax every year for the typical taxpayer. Our increases in the personal allowance will have lifted over 3 million of the lowest paid out of income tax altogether ...
>
> I can also confirm today that the higher rate threshold will rise for the first time this Parliament, from £41,450 to £41,865 next month, and then by a further 1% to £42,285 next year. Because I am passing the full benefit of today's personal allowance increase on to higher rate taxpayers, people earning £42,000, £43,000, £50,000, £60,000—all the way up to £100,000—will be paying less income tax because of this Budget.[115]

Most commentary on the Budget focused on the Government's proposed reforms to the pensions regime, specifically changes to the requirements to purchase an annuity,[116] although there was some mention of the decision to raise the allowance, and the fact that the numbers of 40% taxpayers would rise.[117]

As part of the IFS' post-Budget analysis, IFS director Paul Johnson noted the impact of the Chancellor's decision to increase the higher rate threshold by 1%:

> By sticking with his policy of raising the higher rate threshold by just 1% in 2015-16 Mr Osborne ensured that higher rate tax payers will not gain any more than those paying the basic rate. Our calculations suggest that there will be around 5.3 million higher rate taxpayers in 2015-16, up from 4.7 million this year and 3.3 million in 2010-11.

Mr Johnson went on to say, "it remains unclear, though, why the Chancellor continues to ignore the fact that there is another direct tax on earnings, National Insurance Contributions, which kicks in at significantly lower earnings levels."[118]

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[115] HC Deb 19 March 2014 cc791-2. The Budget report gave details of these tax savings across the income spectrum (*Budget 2014*, HC 1104, March 2014 pp48-9).

[116] For more details see, *Pensions: income drawdown*, Commons Briefing paper CBP 712, 23 May 2014

[117] For example, "More dragged over higher rate tax threshold", *Times*, 20 March 2014 & "For those around the higher rate threshold, Osborne has been far from generous", *Guardian*, 20 March 2014. See also, *Budget 2014: Reaction*, Lords Library Note LLN2014/012, 20 March 2014

[118] Paul Johnson, *IFS Budget analysis 2014: introductory remarks*, 20 March 2014 p5. See also, David Phillips, *IFS Budget 2014 analysis: Personal tax and welfare measures*, 24 March 2014

In its Green Budget the previous month, the IFS presented some analysis of the distributional impact of setting the allowance at £12,500, arguing that any further increase in the allowance, whatever its size, would mostly go to "families in the top half of the income distribution, or with no one in work (mostly pensioners)", with many lower-income gainers having any gain reduced by automatic reductions in "their universal credit and/or council tax support."[119]

When statutory provision to set the allowance was debated in Committee, Shabana Mahmood reiterated the Opposition's support for increasing the allowance while reiterating concerns about the distributional impact of the Government's tax and spending changes as a whole: "although we welcome the increase in the personal allowance—we have seen big increases—it is important to remember that those costly measures in and of themselves are not doing enough to counteract the things being taken away, which leave people worse off."[120] Ms Mahmood also touched on the Opposition's policy for a 10p starting rate of income tax, arguing that it would improve work incentives: "the steadier incline is preferable; rather than going from 0% to 20%, the climb to 10% first and then from 10% to 20% does more for work incentives than a simple jump from zero to 20%."[121]

In response Treasury Minister David Gauke suggested that there was no compelling reason to have a new starting rate, rather than a higher personal allowance:

> Our increases to the personal allowance have replaced the 10% rate that [the Labour Government] doubled, with successive increases to the tax-free personal allowance—effectively creating a 0% band. This is considerably more than the width of the former 10p starting rate band and means that this Government's policy has been considerably more supportive than a reintroduction of the 10p band … I also have to say that in a lengthy and thorough speech from the hon. Member for Birmingham, Ladywood, I am not sure that I heard a convincing case why a 10p rate was better than a further increase in the personal allowance.[122]

Subsequently in his Autumn Statement in December 2014 Mr Osborne announced that the Government would set the allowance £100 higher, at £10,600, and increase the higher rate threshold, so that higher rate taxpayers would get the full benefit of this tax cut. In his statement Mr Osborne also alluded to the long-term goal, announced by the Prime Minister at the Conservative Party Conference three months before, of an allowance set at £12,500, and a higher rate threshold of £50,000:

> Next year, the tax-free personal allowance, which was set to rise to £10,500, will rise instead to £10,600 … It is the first step to the new goal that we have set of raising the personal allowance to £12,500 so that people working full time on the minimum wage pay no tax at all.

119 "Chapter 7: Policies to help the low paid", *IFS Green Budget*, February 2014 p141
120 Public Bill Committee (Finance Bill), First sitting, 29 April 2014 c20
121 *op.cit.* c23
122 PBC (Finance Bill), Second sitting, 29 April 2014 c53

> Today, I can also announce that, unlike previous increases in the personal allowance threshold, this increase will be passed on in full to higher-rate taxpayers paying 40% tax. So the higher-rate threshold goes from £41,865 this year to £42,385 next year. That is the first increase in the higher threshold in line with inflation for five years. This year's increase means that 138,000 fewer people will pay the higher rate than would otherwise be the case. It is a down-payment on our commitment to raise the higher-rate threshold to £50,000 by the end of the decade.[123]

This addition increase raised the Government's estimate of the numbers of working-age individuals taken out of tax – to 3.4m – and the tax savings to be made – to £825 for a typical basic rate taxpayer, and £676 to a typical higher rate taxpayer, in cash terms.[124]

The combined cost of setting the allowance at £10,600 was estimated to be around £1.9bn in 2015/16, rising to £2.6bn by 2018/19.[125] In October 2014 the OBR published its annual assessment of its own forecasting record – and, as part of this, noted that the cost of this policy was likely to be higher than initially thought:

> A number of lessons from previous FERs have been reinforced this year … [One of these] relates to the composition of labour income – the source of over 40 per cent of tax revenues. Employment-driven growth is less tax rich because a given amount of labour income attracts a larger number of tax-free personal allowances, reducing the effective tax rate. This suggests that recent increases in the income tax personal allowance will have been more costly than they otherwise would have been. And slow earnings growth reduces fiscal drag – the positive effect on receipts of earnings rising faster than tax thresholds and allowances.
>
> As the trend of employment-driven growth has continued in 2014-15, we will be working closely with HM Revenue & Customs to explore further the issue of effective tax rates in general – and the implied cost of personal allowance measures in particular – to inform our December EFO forecast of income taxes. Our forecast judgements about the composition of labour income are driven by our view on productivity growth, which remains a source of great uncertainty.[126]

In his Budget in March 2015 the Chancellor proposed further increases in the personal allowance, and the higher rate threshold, for the next Parliament – announcing that they would reach £11,000, and £43,300, respectively by 2017/18.[127] At this time it was estimated that the cost of these proposals would be £960m in 2016/17, rising to £1.68bn by 2019/20.[128] The Budget report also estimated that the number of working-age individuals taken out of income tax would rise to 3.7m by

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[123] HC Deb 3 December 2014 c315. For details of this announcement see, "David Cameron pledges tax cuts 'for 30m people'", *BBC News*, 1 October 2014.

[124] *Autumn Statement*, Cm 8961, December 2014 pp55-6

[125] *Budget 2014*, HC 1104, March 2014 (Table 2.1 – item 3) & *Autumn Statement*, Cm 8961, December 2014 (Table 2.1 – item 1). HMRC published impact notes of these changes at the time of the March Budget (*Income Tax personal allowance for 2015/16* March 2014), and the Autumn Statement (*Income tax personal allowance for 2015/16*, December 2014).

[126] *Forecast evaluation report*, October 2014 pp6-7. See also, "Raising personal tax allowance costs more than expected, says OBR", *Financial Times*, 16 October 2014

[127] HC Deb 18 March 2015 cc777-8

[128] *Budget 2015*, HC 1093, March 2015 (Table 2.1 – item 1).

2017/18.[129] Legislation to set the allowance for the next three years was included in the *Finance Act 2015*.[130] Scrutiny of this legislation was compressed into a single day's debate in the Commons, so that the Act would receive Royal Assent in time for Parliament's Dissolution. The provisions in the Bill setting the personal allowance for 2015/16 to 2017/18 were formally debated, thought the focus of the debate on this occasion was an Opposition amendment, calling for an assessment of the impact of restoring a 50% additional rate of tax.[131]

Most discussion of the Budget focused on other measures, and, more generally, the impact the Chancellor's statement might have on the forthcoming General Election. In a survey of the Government's record over the previous five years, the *Financial Times* noted that, with regard to taxation, "the Coalition stuck to its guns on its biggest reform proposals by pushing through big corporate tax cuts and a large rise in the income tax personal allowance." Assessing the Government's record, Vanessa Houlder noted one important trend – mentioned in the first section of this note: the skewed distribution of income tax receipts across the income distribution:

> The coalition can claim to have achieved most of its goals, although it has not proved that it picked the right priorities. It made the corporate tax system more competitive but did not increase incentives aimed at attracting manufacturing investment.
>
> The increase in the personal allowance left 44 per cent of adults paying no income tax but poorer households did not make the biggest gains. The public finances are vulnerable to a growing dependence on a small group of very wealthy individuals and a tendency for permanent tax cuts to be financed with temporary tax increases.[132]

At this time some commentators suggested that this pattern in income tax receipts raised much wider concerns over public perceptions of the tax system. Discussing election commitments by both the Conservative and Labour parties not to increase the rates of income tax, NICs or VAT – the so-called 'tax lock' – the *Financial Times*' economics editor, Chris Giles, argued "Britain's politicians have forgotten that one of the fundamental purposes of tax systems is to bind people into shared national endeavour":

> Highlighting how many people have been taken out of tax, as Mr Cameron likes to do, fosters the idea that undefined "others" can and should pay. It ferments taxation grievances in Scotland and London; and among the young, the old, the rich, those on middle incomes and the poor. Efforts to ensure others pay has left Britain too heavily reliant on small numbers for receipts …
>
> How much the rich should pay is a political question, but the economic reality is that the present degree of concentration is a risk to the public finances. What seems a secure revenue stream can vanish, like corporate tax revenues from the financial sector in

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129 *Budget 2015*, HC 1093, March 2015 p54
130 Section 3 of *FA2015* set the allowance at £10,600 for 2015/16. Section 5 of *FA2015* set the allowance for the next two years.
131 HC Deb 25 March 2015 cc1497-1513
132 "To austerity and beyond: the Coalition's record in power", *Financial Times*, 19 March 2015

> 2008/09. Expensive further increases in the personal income tax allowance undermine the integrity of income taxation and help the hardworking poor much less than a rise in tax credits. Hollow tax promises undermine the state's ability to function and leave Britain few desirable options if the world does not turn out as we all hope. Politicians: please stop.[133]

From another perspective the tax barrister and commentator Jolyon Maugham suggested that one consequence of these increases in the personal allowance had been to encourage the idea that "taxes are things other people can be relied on to pay":

> We need an intellectual compelling counter-argument to the view, slowly taking hold and fostered by ongoing increases in the personal allowance, that taxes are things other people can be relied upon to pay. There are those on the right who see taxes as a confiscation of personal wealth under compulsion of law by a spendthrift state. The left's equivalent would soak high earners until the pips squeak for the sin of financial success. They deserve each other, these ideologues. But for the rest of us, the only question we should be asking is, how much tax is too much?[134]

133 "The battle for Britain's most reckless pledge", *Financial Times*, 8 April 2015
134 "Why the Right is losing the argument on tax – and why it matters to all of us", *Waiting for Godot: musings on tax*, 13 April 2015

5. Recent developments

5.1 Increases in the personal allowance 2015-17

In its manifesto for the 2015 General Election the Conservative Party confirmed that in government it would continue to increase the personal tax allowance so that it reached £12,500 by 2020, and that it would pass legislation to permanently align the allowance with the National Minimum Wage:

> Over the last five years, we have cut people's taxes wherever possible. We have raised the tax-free Personal Allowance to £10,600 from £6,475: over 26 million people are now keeping more of their hard-earned money and 3 million of the lowest paid are paying no Income Tax at all …
>
> A Conservative Government will not increase the rates of VAT, Income Tax or National Insurance in the next Parliament. Instead, we will ease the burden of taxation by raising the tax-free Personal Allowance – the amount you can earn before you start paying tax – to £12,500.
>
> This will cut Income Tax for 30 million people and take everyone who earns less than £12,500 out of Income Tax altogether. That means by the end of the decade, one million more people on the lowest wages will be lifted out of Income Tax, and people who work for 30 hours a week on the increased National Minimum Wage will no longer pay any Income Tax at all.
>
> We will pass a new law so that the Personal Allowance automatically rises in line with the National Minimum Wage. The new Tax Free Minimum Wage law will be applied from the first Budget after the General Election. The change will update the 1977 'Rooker-Wise' amendment which forced governments to uprate tax thresholds in line with inflation, meaning the Personal Allowance will now increase more quickly.[135]

Following the Election, the new Conservative Government confirmed these plans in the Queen's speech.[136] At the time the NMW was £6.50, so that someone working 30 hours a week would earn £195. The Conservative Manifesto had said, "we accept the recommendations of the Low Pay Commission that the National Minimum Wage (NMW) should rise to £6.70 this autumn, on course for a Minimum Wage that will be over £8 by the end of the decade."[137] On this assumption, someone working 30 hours a week on the NMW would earning be £240 a week in 2020/21 – which is equivalent to an annual personal allowance of £12,500.

The Institute for Fiscal Studies' assessment of the parties' tax and spending plans, published during the 2015 Election, made some

135 Conservative Party, *2015 General Election Manifesto*, April 2015 pp25-7
136 Cabinet Office, *The Queen's Speech 2015 Briefing Notes*, May 2015 p21
137 Conservative Party, *2015 General Election Manifesto*, April 2015 pp19-21. The main rate of the NMW is currently £7.83, wef 1 April 2018 (*The National Minimum Wage: rates and enforcement*, Commons Briefing paper CBP6898, 11 April 2018).

comments on the commitment to link the personal allowance with the NMW …

> After 2020–21, the Conservatives have said they would increase the personal allowance in line with the National Minimum Wage rather than CPI inflation as at present (they would pass a 'Tax Free Minimum Wage law' to change the default for increasing the personal allowance), increasing the cost of the policy over time.
>
> Linking increases in the personal allowance to increases in the minimum wage might be justified by a desire to ensure that fiscal drag does not increase the number of income tax payers over time or that those earning the minimum wage do not pay income tax (though only if they do not work for more than 30 hours per week and do not have any taxable income from other sources). It is to be hoped that such a rule would not lead to government rejecting proposed increases to the minimum wage on the grounds that to do so would be expensive in terms of lost tax revenue.

… as well as the increasing gap between this threshold for income tax, and the equivalent threshold for NICs:

> More importantly, those working for 30 hours per week at the National Minimum Wage would still be paying National Insurance contributions (which effectively act as a second income tax on earned income). It is curious that the coalition has introduced significant real increases in the personal allowance but has not announced any increases in the primary threshold (the point at which employee NICs start to be payable), despite this being significantly lower than the personal allowance at £155 per week or £8,060 a year for full-year workers.
>
> Increasing the primary threshold would help more low earners – both those who work for the full year and earn between £8,060 and £10,600, and those who work for part of the year but whose incomes are less than £10,600 for the whole year. It would also do more to strengthen work incentives: since NICs only apply to earned income, the tax cut on earned income would be larger for a given exchequer cost. The ongoing emphasis on income tax and neglect of NICs highlights the absurdity of continuing to have two similar but separate taxes given that National Insurance is not a true social insurance scheme.[138]

As it transpired, over the next two years the Conservative Government increased both the personal allowance and higher rate threshold by more than Mr Osborne had initially proposed before the Election.

First, in the Conservative Government's first Budget on 8 July 2015 Mr Osborne announced that for 2016/17 the allowance would be set at £11,000, and the higher rate threshold would be £43,000 – the first time that the threshold had been increased by more than inflation alone since 2010.[139] The increase in both allowance and threshold was estimated to cost just over £1.1bn in 2016/17.[140]

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138 *Taxes and Benefits: The Parties' Plans - IFS Briefing Note BN172*, April 2015 pp13-15. For a longer discussion of the case for merging the two taxes see, *National Insurance contributions: an introduction*, CBP 4517, 17 July 2017.

139 HC Deb 8 July 2015 c336; *Summer Budget 2015*, HC246, July 2015 paras 1.130-4.

140 *op.cit.* Table 2.1 – items 1,2

Second, in his Budget on 16 March 2016, Mr Osborne announced that the allowance and threshold would rise to £11,500, and £45,000 respectively for 2017/18, another real-terms increase.[141] The increase in both allowance and threshold was estimated to cost just over £2bn in 2017/18.[142]

Following the EU referendum and David Cameron's resignation, Prime Minister Theresa May appointed Philip Hammond as Chancellor in July 2016. In his Autumn Statement in November Mr Hammond announced that from autumn 2017 the Government would present a single autumn Budget, to allow for greater Parliamentary scrutiny of Budget measures ahead of their implementation. Mr Hammond did not make any further proposals regarding the personal allowance in the last Spring Budget on 8 March 2017.

After the 2017 General Election, Mr Hammond presented the first Autumn Budget on 22 November. Mr Hammond reiterated the Government's commitment to increase the allowance and higher rate threshold so that they reached £12,500 and £50,000 by 2020 – though each would be increased in line with inflation for the coming year. As a result for 2018/19, the personal allowance was £11,850, and the higher rate threshold was £46,350.[143]

5.2 Budget 2018

The Chancellor Philip Hammond presented the Government's second Autumn Budget on 29 October this year. In his Budget speech Mr Hammond announced that both the personal allowance and higher rate threshold would be increased to meet the Government's manifesto commitment, but from April 2019:

> As well as making work pay, we want working people to keep more of the money that they earn. When we came into office, the personal allowance stood at £6,475 and the higher rate threshold was at £43,875. In April, I raised the personal allowance to £11,850 and the higher rate threshold to £46,350, as steps towards our manifesto commitments of £12,500 and £50,000 respectively by 2020 ...
>
> I did not come into politics to put taxes up, and the improvement that we have delivered in the public finances means that, based on the Office for Budget Responsibility's forecast published today, I do not need to do so. I can therefore confirm today that I will meet our manifesto commitments for April 2020 to raise the personal allowance to £12,500 and the higher rate threshold to £50,000, before indexing both in line with inflation from 2021 to 2022. But our careful management of the economy allows me to go further, so I will raise both the personal allowance and the higher rate threshold to these levels from April 2019, delivering our manifesto commitments one year early.
>
> A tax cut for 32 million people, £130 in the pocket of a typical basic rate taxpayer, meaning that, since 2015, we have taken 1.7 million people out of tax altogether and nearly 1 million people

141 HC Deb 16 March 2016 cc966-7.
142 *Spring Budget 2017*, HC 1025, March 2017 p28 (Table 2.2 – items x,y)
143 HC Deb 22 November 2017 c1053; *Autumn Budget 2017*, HC587, November 2017 paras 3.4-5

> out of higher rate tax. As a result of the announcements that I have made today, a single parent, receiving universal credit and working 25 hours a week on the national living wage will benefit by £890 next year—the hard work of the British people paying off in hard cash in their pockets.[144]

Further details were given in the Budget report:

> **3.7 Personal Allowance and higher rate threshold** – The Budget announces that the government will meet its commitment to raise the PA to £12,500 from April 2019, one year earlier than planned. The threshold will remain at the same level in 2020-21 and then increase by CPI. The £650 increase to the PA means that in 2019-20 a typical basic rate taxpayer will pay £130 less tax than in 2018-19 and £1,205 less tax than in 2010-11. This will increase the number of tax payers taken out of income tax since 2015-16 to 1.74 million.
>
> The government will also meet its commitment to increase the HRT to £50,000 from April 2019, one year earlier than planned. The threshold will remain at the same level in 2020-21. This means that there will be nearly one million fewer higher rate taxpayers than in 2015-16. Overall, 32 million individuals will see their tax bill reduced in 2019-20 compared to 2015-16.[145]

This measure is estimated to cost £2.79 billion in 2019/20, falling to £1.94 billion the following year,[146] and was the largest single tax change in the Budget in revenue terms. A breakdown of the two elements to this costing was provided in answer to a PQ after the Budget:[147]

Q Asked by **Stephanie Peacock** (Barnsley East) [N] Asked on: 31 October 2018

Treasury (C) 186423

Income Tax: Tax Allowances

To ask the Chancellor of the Exchequer, with reference to table 2.1 of Budget 2018, what estimate he has made of the cost of the public purse of (a) increasing the personal allowance to £12,500 and (b) increasing the higher rate threshold to £50,000, in each year of the forecast period.

A Answered by: Mel Stride Answered on: 05 November 2018

A breakdown for the Exchequer impact of the changes to the Income Tax Personal Allowance (PA) and Higher Rate Threshold (HRT) announced at the Budget 2018 on 29 October 2018 is provided in Table 1.

Table 1: Exchequer Impact of Budget 2018 announcement– "Personal Allowance and Higher Rate Threshold: increase to £12,500 and £50,000 for 2019-20 and 2020-21", and Exchequer Impacts of the Personal Allowance and Higher Rate Threshold Elements.

Budget 2018 announcement (£ million)	2018-19	2019-20	2020-21	2021-22	2022-23	2023-24
Personal Allowance and Higher Rate Threshold: increase to £12,500 and £50,000 for 2019-20 and 2020-21	0	-2,790	-1,935	-1,445	-1,605	-1,780
of which						
(i) Personal Allowance: increase to £12,500 for 2019-20 and 2020-21*	0	-1,980	-885	-600	-650	-725
(ii) Higher Rate Threshold: increase to £50,000 for 2019-20 and 2020-21 (given (i))**	0	-810	-1,050	-845	-955	-1,055

* This line assumes no change to the Basic Rate Limit (BRL).

** This line reflects the impact of increasing the HRT to £50,000, assuming the PA has been increased to £12,500.

The Exchequer impact above includes the impact from the Upper Earnings Limit and Upper Profits Limit for National Insurance being aligned with the Income Tax Higher Rate Threshold. Further information on the Exchequer impact from the "Personal Allowance and Higher Rate Threshold: increase to £12,500 and £50,000 in 2019-20 and 2020-21" measure can be found in "Budget 2018: policy costings".

Totals may not sum due to rounding.

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144 HC Deb 29 October 2018 cc667-8
145 HMRC analysis based on Survey of Personal Incomes (SPI) 2015-16 data, and Budget 2018 OBR forecast
146 *Budget 2018*, HC 1629, October 2018 p36, Table 2.1 – item 10
147 PQ186423, 5 November 2018

In its *Economic and Fiscal Outlook* the OBR noted, "The direct effect of Government decisions in this Budget reduces receipts by £4.0 in 2019/20, but boosts them by £0.7 billion in 2022/23 [and] the largest near-term giveaways are raising the income tax personal allowance and the traditional freeze in fuel duties."[148] By comparison the Chancellor's decision to freeze the rates of excise duty on road fuels is estimated to cost around £900m a year.[149]

HMRC's impact note on this measure gives details of how the allowance and higher rate threshold will be set …

> Legislation will be introduced in *Finance Bill 2018-19* to set the Personal Allowance for 2019 to 2020 at £12,500, and the basic rate limit for 2019 to 2020 at £37,500.
>
> These thresholds will remain set at £12,500 and £37,500 for 2020 to 2021 and will be increased in line with CPI thereafter.
>
> The table below sets out the thresholds to include the changes from this measure. Thresholds from 2021 to 2022 onwards have been forecast in line with the Office for Budget Responsibility's Budget 2018 forecasts of CPI inflation and will be subject to change.

	2018 to 2019	2019 to 2020	2020 to 2021	2021 to 2022	2022 to 2023	2023 to 2024
Personal Allowance (PA)	£11,850	£12,500	£12,500	£12,760	£13,030	£13,310
Basic Rate Limit (BRL)	£34,500	£37,500	£37,500	£38,300	£39,200	£40,100

> The National Insurance contributions Upper Profits and Upper Earnings Limits are aligned to the higher rate threshold and will therefore also increase in 2019 to 2020.

… provides more analysis on the impact this is anticipated to have on taxpayers for the next two years …

> **Impact on individuals, households and families**
>
> The impact analysis that follows relates specifically to the impact of the legislative provisions outlined above. Gains and losses are presented compared to the Income Tax and National Insurance contributions individuals would have faced if these thresholds were indexed with inflation from 2019 to 2020 onwards.
>
> **2019 to 2020 impacts**
>
> In 2019 to 2020, this measure will benefit 30.6 million individuals of whom 26.2 million will be basic rate taxpayers and 4 million are higher rate taxpayers. A basic rate taxpayer will have an average real gain of £66. A higher rate taxpayer will have an average real gain of £387. An additional rate taxpayer will have an average real gain of £236.
>
> The above inflation increase will take 499,000 individuals out of Income Tax, and 479,000 individuals out of higher rate Income Tax in 2019 to 2020 compared to previously announced policy.

148 *Economic & Fiscal Outlook*, Cm 9713, October 2018 para 4.37
149 *Budget 2018*, HC 1629, October 2018 p36, Table 2.1 – item 11

625,000 individuals will have an average real loss of £107 in 2019 to 2020. These losses are mostly the result of increases in the Upper Profits and Upper Earnings Limits for National Insurance.

Cumulative changes to the Personal Allowance and higher rate threshold between 2015 to 2016 and 2019 to 2020 mean a typical basic rate taxpayer will have an overall cash gain of £380 and a real terms gain of £236. A typical higher rate taxpayer will have an overall cash gain of £1,142 and a real terms gain of £694.

Cumulative changes to the Personal Allowance and higher rate threshold since 2010 to 2011 mean a typical basic rate taxpayer will have an overall cash gain of £1,205 in 2019 to 2020. A typical higher rate taxpayer will have an overall cash gain £1,818 in 2019 to 2020.

2020 to 2021 impacts

In 2020 to 2021, this measure will benefit 30.7 million individuals, of whom 26.1 million will be basic rate taxpayers and 4.1 million higher rate taxpayers. A basic rate taxpayer will have an average gain of £20. A higher rate taxpayer will have an average real gain of £228. An additional rate taxpayer will have an average real gain of £169.

148,000 fewer individuals are expected to pay Income Tax, and 314,000 fewer are expected to pay higher rate Income Tax, in 2020 to 2021 compared to previously announced policy.

901,000 individuals will have an average real loss of £64 in 2020 to 2021. These losses are mostly the result of increases in the Upper Profits and Upper Earnings Limits for National Insurance.

Cumulative changes to the Personal Allowance and higher rate threshold between 2015 to 2016 and 2020 to 2021 mean a typical basic rate taxpayer will have an overall cash gain of £380 and a real terms gain of £190. A typical higher rate taxpayer will have an overall cash gain of £1,142 and a real terms gain of £555.

Cumulative changes to the Personal Allowance and higher rate threshold since 2010 to 2011 mean a typical basic rate taxpayer will have an overall cash gain of £1,205 in 2020 to 2021. A typical higher rate taxpayer will have an overall cash gain £1,818 in 2020 to 2021.

All taxpayers with income of £125,000 or above in both years have their Personal Allowance tapered to zero. Therefore they derive no benefit from the Personal Allowance increase.

Actual gains for individual taxpayers will vary according to individual circumstances.

This measure is not expected to impact on family formation, stability or breakdown.

… and addresses the equalities impact of this change:

Equalities impacts

Income Tax changes apply regardless of personal circumstances or protected characteristics such as gender, race or disability. Equalities impacts will reflect the composition of the Income Tax paying population.

From this measure, 2019 to 2020 estimated impacts by gender are:

- 30.6 million individuals will benefit - of these, 17.8 million (58%) are male and 12.8 million (42%) are female
- 499,000 individuals will be taken out of tax - of these, 219,000 (44%) are male and 280,000 (56%) are female
- 479,000 individuals will be taken out of the higher rate of tax - of these, 333,000 (70%) are male and 145,000 (30%) are female
- 625,000 individuals lose, of which 393,000 (63%) are male and 233,000 (37%) are female

From this measure, 2019 to 2020 estimated impacts by age are:

- 30.6 million individuals will benefit - of these, 24.5 million (80%) are below State Pension age and 6.0 million (20%) are above State Pension age
- 499,000 individuals will be taken out of tax - of these, 331,000 (66%) are below State Pension age and 168,000 (34%) are above State Pension age
- 479,000 individuals will be taken out of the higher rate of tax - of these, 420,000 (88%) are below State Pension age and 58,900 (12%) are above State Pension age
- 625,000 individuals lose, of which the majority are below State Pension age

From this measure, 2020 to 2021 estimated impacts by gender are:

- 30.7 million individuals will benefit - of these, 17.9 million (58%) are male and 12.8 million (42%) are female
- 148,000 individuals will be taken out of tax - of these, 65,100 (44%) are male and 82,600 (56%) are female
- 314,000 individuals will be taken out of the higher rate of tax - of these, 221,000 (70%) are male and 93,800 (30%) are female
- 901,000 individuals lose, of which 562,000 (62%) are male and 339,000 (38%) are female

From this measure, 2020 to 2021 estimated impacts by age are:

- 30.7 million individuals will benefit - of these, 24.6 million (80%) are below State Pension age and 6.1 million (20%) are above State Pension age
- 148,000 individuals will be taken out of tax - of these, 105,000 (71%) are below State Pension age and 43,200 (29%) are above State Pension age
- 314,000 individuals will be taken out of the higher rate of tax - of these, 277,000 (88%) are below State Pension age and 37,900 (12%) are above State Pension age
- 901,000 individuals lose, of which the majority are below State Pension age.[150]

There was some press coverage of the Chancellor's announcement, generally focusing on the fact the decision to raise both the personal

150 HMRC, *Income Tax: Personal Allowance and basic rate limit from 2019-20*, 29 October 2018

allowance and the higher rate threshold provided a larger tax cut to those on higher incomes.

The *Times* noted that for those on incomes between £50,000 and £100,000 – the point at which the personal allowance is tapered away – the income tax saving could be up to £860, compared with a £130 saving for basic rate taxpayers.[151] The *Guardian* underlined that those on the lowest incomes would not benefit, quoting Tom Evennett at accountants EY, as observing "a move to align the NI and tax threshold would have a much bigger impact on the really low paid."[152] In their response to the Budget the Low Incomes Tax Reform Group also made this observation:

> Commenting on the increase in the personal allowance from £11,850 to £12,500 from 6 April 2019, Victoria Todd, Head of LITRG team, said … "Those earning under the current personal allowance of £11,850 will see no gain from this change. Those earning above £11,850 may benefit but it depends on whether they receive tax credits or other means-tested benefits such as Universal Credit. This is because Universal Credit, like other means tested benefits, is based on net income (after tax and National Insurance have been deducted).
>
> As the amount of tax they pay reduces, their Universal Credit award also reduces. They will not see the full tax gain of £130 from the increase in the personal allowance; instead, they will only gain overall by £48.10, as their Universal Credit award will be reduced by £81.90. However, those earning above £11,850 who receive tax credits will benefit from the full £130 because tax credits are based on gross income.
>
> "LITRG has previously commented that a better method of assisting those on the very lowest incomes would be to restore the previously cut work allowances in Universal Credit. We therefore welcome the fact that the work allowance is to be increased by £1,000 per annum from April 2019. Unfortunately, this increase is limited to households with children and people with disabilities, and will not assist all Universal Credit claimants.
>
> "In addition, the Government could consider increasing the National Insurance primary threshold. This has now lagged behind the personal allowance for a long time. This would allow more people to earn National Insurance credits without actually having to pay National Insurance contributions."[153]

By contrast the *Financial Times*, quoted Les Cameron at Prudential noting the continued impact of marginal tax rates from tapering the allowance: "those with incomes over £100,000 will see an effective tax rate of 60 percent on £25,000 of their incomes."[154]

In his opening comments on the IFS' response to the Budget, IFS director Paul Johnson noted that the impact of the higher personal

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[151] "High earners are big winners as tax cuts brought forward", *Times*, 30 October 2018

[152] "Low earners gain little or nothing from £3bn income tax giveaway", *Guardian*, 30 October 2018

[153] LITRG press notice, [Personal allowance increase does little for those on lowest incomes](), 29 October 2018

[154] "Income tax cut brought forward", Financial Times, 30 October 2018

allowance could be seen in the fact that 40% of adults now pay no income tax:

> At a cost of about £1.4 billion in 2020-21 the income tax personal allowance will rise to £12,500 and the higher rate threshold to £50,000. That will mean the personal allowance will be 55% higher in real terms than it was back in 2010-11. Taking account of offsetting cuts in the basic rate limit (the amount of taxable income you need before the higher rate kicks in) this has come at a cost of over £15 billion a year (£25 billion if you ignore those offsetting cuts).
>
> It means there will be nearly 6 million fewer income tax payers than there would have been had the allowance only been raised in line with prices since then. That's one of the reasons why more than 40% of adults pay no income tax in any given year.

Mr Johnson went on to discuss the impact of the higher rate threshold, contrasting it with the impact of the Chancellor's announcement in the Budget of additional spending on Universal Credit:

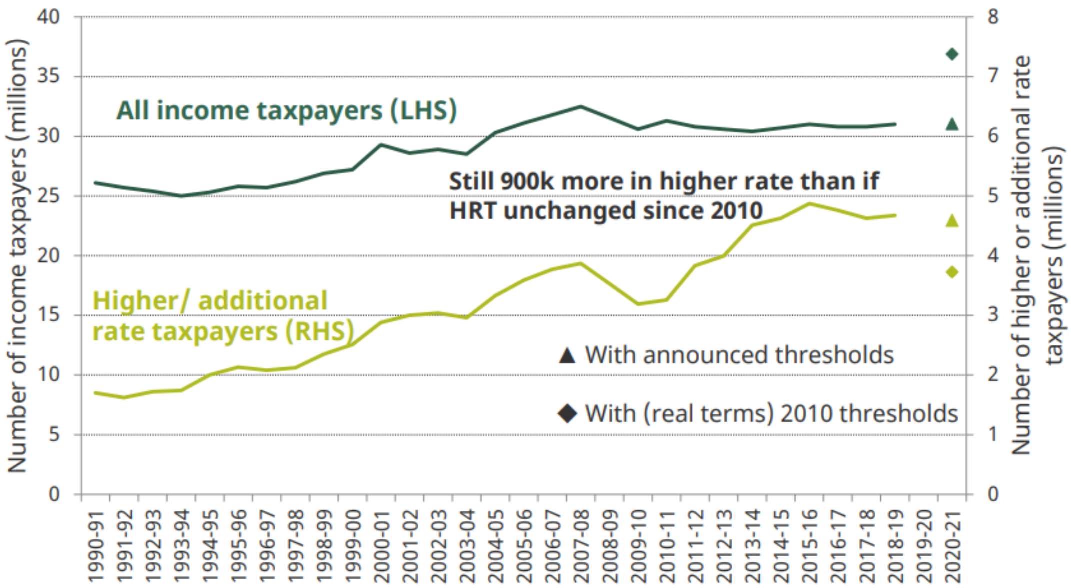
> The increase in the higher rate threshold is, on the other hand, something of a policy reversal rather than the continuation of a trend. Even after this increase it will be around 9% lower in real terms than it was in 2010-11 with the result that there will be around 900,000 more higher rate taxpayers than there would have been had it risen in line with inflation.
>
> Of course these changes benefit the better off – though you only need £12,500 in income to benefit from the personal allowance increase. On average they will benefit over 30 million people by an average of around £44 a year, with the typical higher rate taxpayer gaining £156 and the typical basic rate taxpayer gaining £21. Contrast that with the changes to Universal Credit. They help far fewer people – about 2.4 million families – but help them a lot more, by over £600 a year.[155]

In his presentation of the personal tax and benefit measures in the Budget, Tom Waters at the IFS made the point that, on current estimates, increasing the allowance and higher rate threshold in line with inflation *only* would mean they would reach £12,390 and £48,590 by 2020/21.

Mr Waters also presented figures to illustrate the impact of the Government's policy to setting these thresholds on the numbers of taxpayers as a whole, and the numbers of higher rate taxpayers, as opposed to raising them just in line with inflation:[156]

155 "Paul Johnson's Opening Remarks", *Autumn Budget 2018: IFS analysis*, 30 October 2018 p5. For details of the increased spending on UC, see *Budget 2018*, HC 1629, October 2018 para 5.30-8.

156 "Personal tax and benefit measures", *Autumn Budget 2018: IFS analysis*, 30 October 2018



Source: HMRC, Table 2.1
Note: Data points for 2008-09 are linear interpolations

In evidence to the Treasury Committee as part of their inquiry into the Budget, the Institute of Chartered Accountants argued the changes were "welcome" but lacked "coherence with other tax and benefit decisions" …

> **Personal allowance/higher rate threshold**
>
> The Conservative manifesto commitment to raise the personal allowance to £12,500 and the higher rate threshold to £50,000 by 2020 has been brought forward a year and will now happen with effect from 6 April 2019 rather than 2020 as planned. Although welcome, this lacks coherence with other tax and benefit decisions, for example, Universal Credit (UC) claimants will not receive the full benefit. As tax paid goes down by raising the personal allowance from £11,850 to £12,500, a basic rate taxpayer would expect to be £130 better off. Because like other means tested benefits, UC is based on net income, those in receipt of £130 more net income will lose UC at the taper rate of 63%, and will only gain £48 of the £130 received by others.

… and also raised concerns as to the fact that the rise in the higher rate threshold created a wider disparity between the tax schedule in Scotland, and that applying in the rest of the UK

> **Impact of rate change measures on tax devolution**
>
> Several of the changes in this Budget will not apply in Scotland and Wales. In 2018/19, the higher rate threshold for income tax in Scotland, was already £3,350 higher than the rest of the UK. Following this Budget, the difference will increase. As more differences are legislated, tax simplification becomes more problematic. Employers near the Scottish border will already have people working for them who have different residence status such that people doing the same job will be taking home different net pay. We suggest that now might be the time to reflect on whether and to what extent the public will be able to understand this and whether in the interest of clarity, a simple list of the

> different taxes and benefits available in the different jurisdictions could be maintained on GOV.UK?[157]

In his evidence to the Committee Paul Johnson highlighted the impact of this policy to increasing the personal allowance over the long-run:

> An increase in the personal allowance was just adding to the same thing that has happened Budget after Budget for the last eight years, so essentially the same people were winning, but the increase in the higher rate threshold was actually slightly undoing very big reductions in the higher rate threshold over the last eight years. In the end, if we put all of that together, higher rate taxpayers have lost quite a lot and basic rate taxpayers have gained quite a lot. Looking at these things in a longer-term context, as well as just what was in this particular Budget, really matters for understanding what the impacts are.[158]

The Chancellor gave evidence to the Committee on 5 November and on this occasion the issue was raised with him by Alison McGovern:

> **Alison McGovern :** … What was the rationale for going for [these tax cuts] a year early?
>
> **Mr Philip Hammond:** Because I am taking a balanced approach, as I have said before, wanting to keep taxes low … We were able to make a very large commitment to public services with the NHS funding commitment. We were able to put a significant amount of money into Universal Credit £1.7 billion a year when rollout is complete.
>
> **Alison McGovern:** … Almost all of the money that you have put into these tax cuts will accrue to those in the top half of the income distribution and those who gain the most will be in the top 10% of earners in our country. Chancellor, do you feel satisfied that your priority is the top 10% of earners in our country?
>
> **Mr Philip Hammond:** No, it is not. It manifestly is not … If you look at page 36 of the Red book … If you look at 2023-24, at line 10 you will see that the personal allowance and higher rate tax threshold in 2023-24 costs £1.78 billion and the changes to Universal Credit work allowance cost £1.695 billion. It is around £1.7 billion in both cases at the end of the forecast period …
>
> **Alison McGovern:** Can I just bring you back to my question, Chancellor? Are you happy that this year, of £2.8 billion of our country's resources—it absolutely dwarfs the amount that you have found for Universal Credit—a significant amount accrues to the top 10% of earners?
>
> **Mr Philip Hammond:** No, it does not. It does not absolutely dwarf it and it is a bogus analysis to look at a single fiscal event. You have to look at what we are building here and we are not always able to do everything in one go. I am sure you will recall that Paul Johnson, when he appeared in front of the Committee for the IFS, said that Universal Credit after these changes will be about as generous as the system it is replacing.[159]

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[157] Treasury Committee, *Budget 2018 : Written Evidence – ICAEW*, 5 November 2018 p6. By contrast the Chartered Institute of Taxation did not raise the issue in their evidence.
[158] *Oral evidence: Budget 2018*, HC 1606, 1 November 2018 Q106
[159] *Oral Evidence: Budget 2018*, HC 1606, 5 November 2018 Qs298-301

BRIEFING PAPER
Number 6569, 15 November 2018