

Impact of April 2015 tax and welfare measures on households

1.1 The analysis in this note sets out the estimated impact on weekly household incomes of moving from the tax and welfare system as it was in 2014/15 to the one that came into effect in April 2015. Weekly household incomes in April 2015 are compared to what they would have been had 2014/15 tax and benefit thresholds been indexed in line with inflation. The analysis captures the impact of new measures (such as the introduction of the income tax marriage allowance), as well as measures that came into effect in earlier years but which continue to have an impact on household incomes in 2015/16 (such as the 1% cap on working-age discretionary benefits). All estimates are derived using HM Treasury’s tax and benefit microsimulation model (IGOTM), which was also used to produce the distributional analysis of tax and welfare reforms published alongside Budget 2015.¹

1.2 Table 1.A shows the number and proportion of households gaining, and average gains, as a result of modelled 2015/16 tax and welfare measures, while Chart 1.A presents these gains as a proportion of net income across the household income distribution. Average gains are in 2015/16 prices, and gaining households are defined as those who see an increase in net income of at least 5p per week. The analysis only captures those measures that can be modelled robustly at a household level – a full description of the measures modelled and the underlying methodology is set out from paragraph 1.3.

Table 1.A: Number and proportion of households gaining, and average gains, as a result of modelled 2015/16 tax and welfare measures

	Number of households gaining	% of households gaining	Mean gain (£pw)
All households	22.5m	87%	£3.44
Pensioner households*	6.9m	92%	£3.47
Working households**	14.6m	94%	£4.03

* Pensioner couples, single pensioners, and mixed-age couples

** Households with at least one working-age adult in employment

Chart 1.A: Impact of modelled tax and welfare changes on households in April 2015, compared to a 2014/15 system indexed with inflation, as a percentage of net income, by income decile



¹ "Impact on Households: distributional analysis to accompany Budget 2015" (HM Treasury, March 2015)

https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/413877/distributional_analysis_budget_2015.pdf

Methodology

1.3 As outlined above, all estimates are derived from HM Treasury's tax and benefit microsimulation model (IGOTM). This model is based on data collected from the Living Costs and Foods Survey (LCF)², which has been projected forward to 2015/16 earnings and prices.

1.4 To derive the impact of April 2015 measures on households, the rules of the tax and benefit system in April 2015 are first applied to the dataset to produce estimates of household net incomes. These are then compared against a counterfactual where no new measures come into effect, and where the majority of tax and benefit thresholds are indexed in line with inflation (full details below). To ensure these estimates isolate the impact of modelled government measures alone, household earnings, inflation and other non-policy related drivers of income are held constant in the comparison.

Which measures have been included in the analysis?

We have modelled the impact of the following tax and benefit measures:

Direct tax

- Personal Allowance increased to £10,600 with full gains to higher rate taxpayers
- Savings tax: 10% rate abolished and 0% band extended to £5,000
- The Personal Allowance for those born between 6 April 1938 and 5 April 1948 set at the same level as the working-age Personal Allowance (£10,600). The Personal Allowance for those born before 6 April 1938 frozen at £10,660
- Income tax marriage allowance of £1,060 introduced
- Funding for local authorities in England to freeze council tax in 2015/16

Welfare

- Working age discretionary benefits and tax credits increased by 1%
- Child Benefit increased by 1%
- Basic State Pension increased by 2.5% (the higher of the 'triple lock' of earnings, inflation and 2.5%)
- The standard minimum income guarantee in Pension Credit increased in line with the cash rise in the basic State Pension. The Savings Credit threshold increased by 5.1%

Indirect tax

- Fuel duty: no increase
- Alcohol duty: 1p off a pint of beer, 2% reduction in cider and spirits duty, and wine duty frozen
- Tobacco duty: increased by 2% above RPI

² <http://www.ons.gov.uk/ons/about-ons/get-involved/taking-part-in-a-survey/information-for-households/a-to-z-of-household-and-individual-surveys/living-costs-and-food-survey/index.html>

What counterfactual is assumed?

To produce estimates of the impact of the above measures on household incomes in April 2015, the following counterfactual has been assumed:

Direct tax

- Income tax Personal Allowance and Basic Rate Limit increased in line with CPI
- Savings tax: no change in the starting rate, and the 10% band increased in line with CPI
- Income tax marriage allowance not introduced
- All age-related Personal Allowances increased in line with CPI
- Council tax rates in England rise by 2.9% (the average pre-freeze increase for a Band D property between 2008/09 and 2010/11)

Welfare

- All working-age discretionary benefits, tax credits, the Basic State Pension and Pension Credit elements updated in line with CPI

Indirect tax

- All alcohol, tobacco and fuel duty rates increased in line with RPI

For direct taxes and benefits, the September 2014 CPI rate of 1.2% is assumed. For indirect taxes the forecast Q3 2015 RPI rate of 0.9% is assumed. Both of these rates are consistent with DWP and HMRC uprating rules.

What has not been included in the analysis?

Due to modelling limitations³, the analysis does not capture the impact of the following 2015/16 tax and welfare measures:

- NS&I bonds for people aged 65 and over
- Air Passenger Duty: exempting under-12s, and abolishing bands C and D
- Pensions flexibility: reduction in the withdrawal rate from 55% to the marginal tax rate
- Inheritance Tax: threshold freeze for 3 years from 2015/16

Due to difficulties involved in modelling local Council Tax Support (introduced April 2013), the previous system of Council Tax Benefit is assumed to have remained in place throughout the analysis.

³ See Table 3.A of "Impact on Households: distributional analysis to accompany Budget 2015" (HM Treasury, March 2015) for fuller description of the modelling and its limitations:

https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/413877/distributional_analysis_budget_2015.pdf