The fiscal outlook and tax and benefit changes affecting low-earners

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Presentation to Low Pay Commission
2nd October 2019
Note: OBR’s March forecast is the variant that includes the impact of a student loan accounting change, which has since been reflected in the ONS’ historical outturn data. However, it did not include some other minor accounting changes that have since been made, so the 2019-20 data point is not strictly comparable with the others, though differences will be minor.

Source: Office for Budget Responsibility and Office for National Statistics
Spending Round 2019: £13.4 billion giveaway in 2020–21

Day-to-day spending on public services (~3% since 2010–11)

Excluding Department of Health and Social Care (~16% since 2010–11)

Note: £11.7bn of the £13.4bn was for day-to-day spending; the remaining £1.7bn was for capital budgets.
Source: ‘Chancellor ends austerity for public services – but risks breaching current fiscal rules’, IFS Press Release, 4 September 2019
March 2019 forecast: cyclically-adjusted borrowing in 2020–21

Note: The ONR figures are from a variant that included a change to student loans accounting which has subsequently been incorporated in official statistics.

Source: Office for Budget Responsibility and Spending Round 2019.
Impact of tax and benefit reforms
May 2015 – April 2022 (including universal credit)

Change as a percent of net income

Income Decile Group

-20%
-15%
-10%
-5%
0%
5%

Poorest
2
3
4
5
6
7
8
9
Richest
All

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

Note: Assumes full take-up of means-tested benefits and tax credits and all changes fully in place

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Benefit changes: where we are

- 4-year freeze on most working-age benefits finally lifted in April 2020...
  - Inflation has cut real value of these benefits by around 6%

- ...but some cuts/changes continue to work way through the system
  - Child tax credits
  - Employment and Support Allowance
  - Introduction of universal credit
Changes being phased in since April 2016
Child tax credit

• Extra tax credits for third and subsequent children abolished for new claimants and new births
  • Long run: around 900k families to lose average of £3700 p.a (about 550k of them are in work)
  • By 2020: only about half of long run impact

• Per-family element removed for new claimants
  • £545 p.a less for all new claims
  • About 4m families affected in long run

• CTC is means-tested so both cuts tend to strengthen work incentives for low-earning parents
Changes being phased in since April 2016
Employment and Support Allowance

• New claimants in Work Related Activity Group (those assessed as less ill) get same rate as JSA claimants – cut of £30 per week

• Will affect roughly 500k people (20% of ESA claimants)
Rollout of Universal Credit

• Schedule has been pushed back many times and it’s still not set to be fully in place until end-2023 (OBR bake in extra 6 month delay)

• The “managed migration” of existing claims is still to come
  • Though the longer it’s left, the less there is (due to natural ‘churn’)

• But:
  • There are already 2.4 million claimants
  • For new claims it is in place nationwide
UC rollout

~ 1/3 of total foreseen caseloads to be covered by 2019-2020

March 2013 forecast
Successive forecasts
October 2018 forecast
March 2019 OBR
November 2017 forecast
Universal Credit: the big picture

• In the long run:
  
  • It’s clearly a reduction in *entitlements* compared to legacy system
  
  • Mainly due to cuts to ‘work allowances’
  
  • Take-up is a key uncertainty. Good reasons to expect it to increase under UC; though can make arguments the other way too.
  
  • Impacts on work incentives mixed; but does get rid of weakest incentives
Income tax and National Insurance thresholds

- Government reached its previous target of a £12,500 IT personal allowance a year “early” and will freeze it in April 2020
- But PM said during leadership campaign he wants to raise NICs threshold from current level of £8,632
- Didn’t say when, by how much, or which thresholds exactly
- Raising employee and self-employed thresholds by £1,000 p.a. in 2020-21 would cost £3bn; £4bn if employer threshold also raised
  - Overdue in a sense, after the fixation on income tax, e.g. if on NLW you have to average 29 hours per week through year to pay IT, 20 to pay employee NICs
  - But in comparison with other options it is not a well targeted way of helping low-earning individuals (and still less low-earning households)
Raising NICs thresholds: comment

• In some sense this is overdue, after fixation on income tax
  • IT threshold now almost 50% higher than NICs threshold
  • If on NLW you have to average 29 hours per week through year to pay IT, 20 to pay employee NICs

• If you want to help low paid – as PM stressed – and you restrict yourself to using direct taxes, this is the best thing you can do

• But if the primary goal is really to help low earners, there are much more fine-tuned tools for that job (e.g. work allowances in universal credit)
  • Most of the gains from higher NICs threshold go to higher earners