

RESOLUTION FOUNDATION – DETAILED POST BUDGET 2012 ANALYSIS

1. Impact of upcoming main changes to tax, tax credits and benefits (excluding 50-45p top rate tax cut)

Chart 1 – Impact by income group of main upcoming changes to taxes, tax credits and benefits

Cumulative impact in 2013-14 on household income groups of selected tax, tax credit and benefit measures due to be implemented over the next two years



Source: RF analysis using the IPPR tax benefit model

The results show:

- Changes still to come are set to fall heaviest on the higher income group in cash terms, costing households an average of £243 a year
- However, when taken as a proportion of income, the measures will hit members of the benefit reliant group hardest, reducing average household incomes by 1.3 per cent
- Low to middle income households face a 0.6 per cent reduction in their incomes, representing a larger proportional fall than in the higher income group (-0.5 per cent)

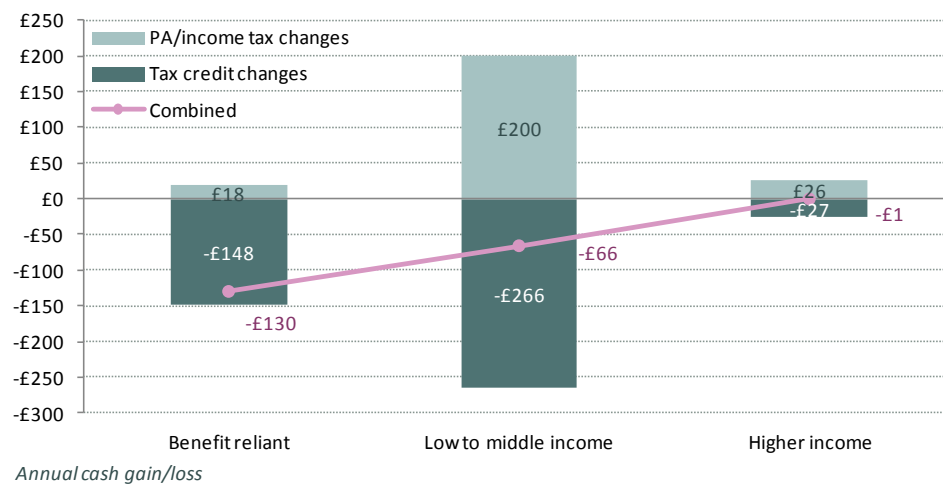
It is important to note that we have been unable to include the cut to the 50p top tax rate. Inclusion of the cut in the additional rate of tax to 45p would be likely to improve the outlook slightly for the higher income group, while inclusion of indirect tax changes would be likely to make the picture look still more regressive. Inclusion of the tax credit elements we have been unable to model (namely the in-year income disregard and the use of real-time data) would similarly fall more heavily outside of the higher income group, with low to middle income households potentially being worst hit.

2. Comparing the impact of changes to the personal tax allowance and tax credits

Next we focus specifically on changes relating to the personal allowance and tax credits, in order to compare and contrast their effects on our three household income groups.

Chart 2 – Impact by income group of changes just to the personal income tax allowance and tax credits - annual cash gain

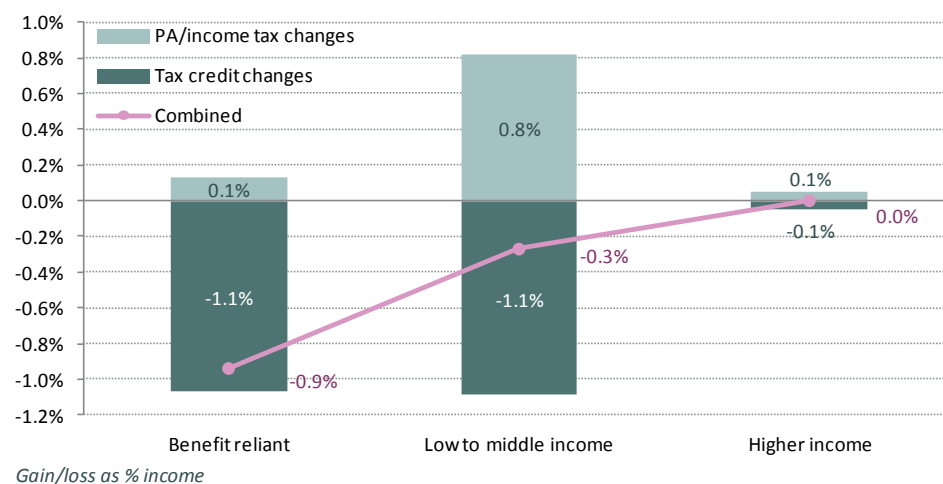
Comparison of cumulative impact in 2013-14 on household income groups of income tax and tax credit measures due to be implemented over the next two years



Source: RF analysis using the IPPR tax benefit model

Chart 2.1 – Impact by income group of changes just to the personal income tax allowance and tax credits - annual gain/loss as % of income

Comparison of cumulative impact in 2013-14 on household income groups of income tax and tax credit measures due to be implemented over the next two years



Source: RF analysis using the IPPR tax benefit model

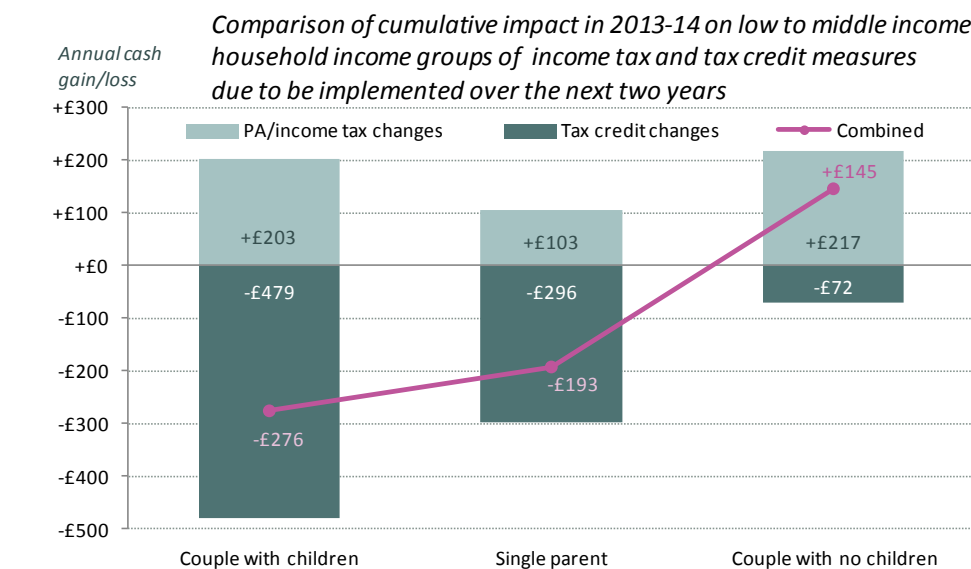
The results show:

- While the various personal allowance and income tax changes have the biggest positive impact on low to middle income households, these gains are set to be more than offset by the negative impact of forthcoming tax credit cuts
- Taken in combination, the measures will be largely neutral for higher income households but will reduce the incomes of low to middle income households by 0.3 per cent

Again, it is important to note that inclusion of the cut in the additional rate of tax to 45p would be likely to improve the outlook slightly for the higher income group, while inclusion of the tax credit elements we have been unable to model (namely the in-year income disregard and the use of real-time data) would similarly fall more heavily outside of the higher income group, with low to middle income households potentially being worst hit.

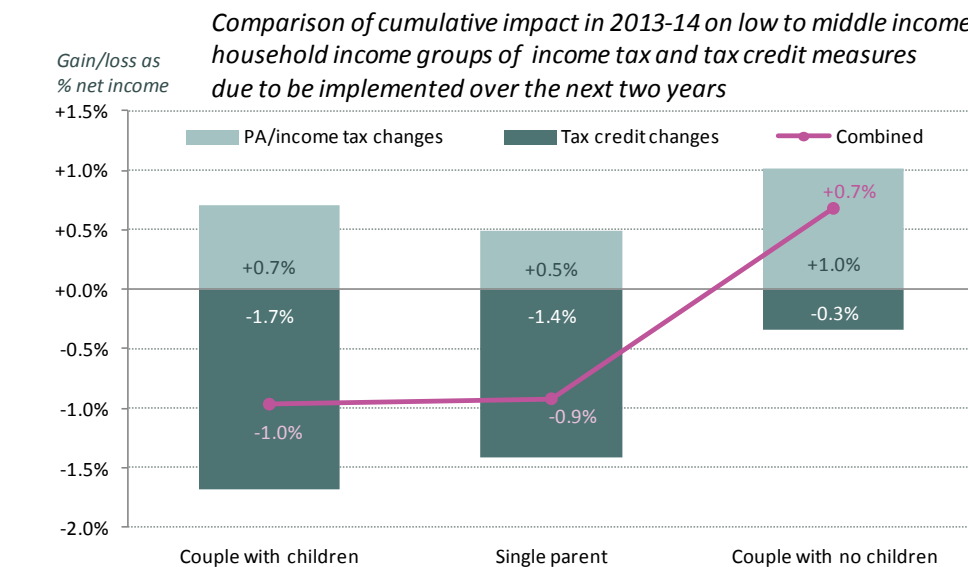
Clearly, within these overall averages, the impact varies by family type. The charts below compare the gains and losses made under these measures by low to middle income households with children with those without.

Chart 2.2 – Impact for low to middle income family types of changes just to the personal tax allowance and tax credits - annual cash loss



Source: RF analysis using the IPPR tax benefit model

Chart 2.3 – Impact for low to middle income family types of changes just to the personal tax allowance and tax credits - annual gain/loss as % of income



Source: RF analysis using the IPPR tax benefit model

The results show:

- Couples with children are set to lose £479 a year on average as a result of the tax credit cuts, more than double the £203 gain they can expect from changes to the income tax and NICs system. Overall, the changes will reduce net incomes in such families by 1 per cent.
- Similarly, these two sets of measures will reduce net incomes among single parents in the low to middle income group by 0.9 per cent on average.
- By contrast, couples with no children in the group will achieve a net gain of £145 a year, or 0.7 per cent.

3. Family case studies

As noted in the analysis above, the financial landscape is set to look quite different for different family types in the coming years. Below, we set out case studies for five stylised families, showing how their incomes are set to change over time. We consider the impact of both the wage squeeze (that is, the fact that average wages have been growing less quickly than inflation in recent years) and the tax/benefit squeeze (as modelled above).

Ben & Mandie

Two children, aged under-1 and 4; dual-earners working 42 hours a week in total

2011-12 prices (£)	2010-11	2011-12	2012-13	2013-14	Change from 2010-11	
					in 2012-13	in 2013-14
Gross earnings	41,181	39,175	38,725	38,920	-2,456	-2,261
Post-tax earnings	32,479	31,364	31,250	31,737	-1,229	-742
Working Tax Credit	4,618	2,150	1,804	1,379	-2,814	-3,239
Child Tax Credit	6,008	5,655	5,752	5,756	-256	-252
Child Benefit	1,850	1,752	1,701	1,663	-149	-187
Total household income	44,956	40,922	40,508	40,535	-4,448	-4,421
<i>of which: resulting from change in gross earnings (the wage squeeze)</i>					-2,456	-2,261
<i>resulting from changes in taxes, benefits and tax credits (the tax/benefit squeeze)</i>					-1,992	-2,160
<i>resulting from changes announced in Budget 2012</i>					+	+325
<i>Proportionate change in total income</i>					-9.9%	-9.8%

Notes: All increases in rates and thresholds and earnings based on information in Budget 2011, Autumn Statement 2011 and Budget 2012. Budget 2011 measures specified here include shift to CPI indexation of direct taxation and above inflation increase in income tax personal allowance in 2012-13. Autumn Statement measures relate to removal of the above-indexation increase in the child element of the CTC and the freezing the couple and single parent elements of the WTC. Fuel duty changes are absorbed in the underlying inflation forecasts. Budget 2012 measures include the above-inflation increase in the personal allowance in 2013-14.

Source: RF calculations based on stylised family

- Compared with a baseline of 2010-11, the wage squeeze (the extent to which RPI inflation outstrips growth in average earnings) reduces Ben & Mandie's gross household earnings by £2,456 in 2012-13. A slight relaxation of this squeeze in 2013-14 reduces the overall loss to £2,261.
- Various changes in income tax and NICs rates help to offset these losses to some extent. However, the family is further hit by cuts to tax credits (in particular the cuts WTC childcare support element) and the freeze in Child Benefit. Overall, this tax and benefit squeeze costs the family £1,992 in 2012-13 and £2,160 in 2013-14 compared with 2010-11. Budget 2012 improved the picture for 2012-13 by £325.
- Overall, the family's income is set to fall by £4,448 in 2012-13 compared with 2010-11 (or 9.9 per cent). Although 2013-14 looks slightly better, the family is still £4,421 (or 9.8 per cent) worse off.

Simon & Gwen

Young couple, one child; dual earners, one working full-time, one part-time

2011-12 prices (£)	2010-11	2011-12	2012-13	2013-14	Change from 2010-11	
					in 2012-13	in 2013-14
Gross earnings	27,454	26,117	25,817	25,947	-1,637	-1,507
Post-tax earnings	23,007	22,484	22,472	22,915	-535	-92
Child Tax Credit	575	545	0	0	-575	-575
Child Benefit	1,115	1,056	1,025	1,002	-90	-113
Total household income	24,697	24,085	23,497	23,917	-1,200	-780
<i>of which: resulting from change in gross earnings (the wage squeeze)</i>					-1,637	-1,507
<i>resulting from changes in taxes, benefits and tax credits (the tax/benefit squeeze)</i>					+437	+727
<i>resulting from changes announced in Budget 2012</i>					+	+325
<i>Proportionate change in total income</i>					-4.9%	-3.2%

Notes: All increases in rates and thresholds and earnings based on information in Budget 2011, Autumn Statement 2011 and Budget 2012. Budget 2011 measures specified here include shift to CPI indexation of direct taxation and above inflation increase in income tax personal allowance in 2012-13. Autumn Statement measures relate to removal of the above-indexation increase in the child element of the CTC and the freezing the couple and single parent elements of the WTC. Fuel duty changes are absorbed in the underlying inflation forecasts. Budget 2012 measures include the above-inflation increase in the personal allowance in 2013-14.

Source: RF calculations based on stylised family

- Compared with a baseline of 2010-11, the wage squeeze (the extent to which RPI inflation outstrips growth in average earnings) reduces Simon & Gwen's gross household earnings by £1,637 in 2012-13. A slight relaxation of this squeeze in 2013-14 reduces the overall loss to £1,507.
- Various changes in income tax and NICs rates help to offset these losses to some extent, outweighing both the Child Benefit freeze and the cuts to CTC they face because of a restriction in eligibility. Overall, their interaction with the tax and benefit system boosts their income by £437 in 2012-13 and £727 in 2013-14 compared with the baseline. Budget 2012 improved the picture for 2012-13 by £325.
- Overall, the family's income is set to fall by £1,200 in 2012-13 compared with 2010-11 (or 4.9 per cent). Although 2013-14 looks slightly better, the family is still £780 (or 3.2 per cent) worse off.

Aaron & Sophie

Three children, aged 3, 5 and 7; single-earner working 35 hours a week

2011-12 prices (£)	2010-11	2011-12	2012-13	2013-14	Change from 2010-11	
					in 2012-13	in 2013-14
Gross earnings	47,517	45,202	44,683	44,908	-2,834	-2,609
Post-tax earnings	34,698	32,826	32,497	32,616	-2,201	-2,082
Child Tax Credit	575	0	0	0	-575	-575
Child Benefit	2,586	2,449	2,378	2,324	-208	-262
Total household income	37,860	35,275	34,875	34,940	-2,985	-2,919
of which: resulting from change in gross earnings (the wage squeeze)					-2,834	-2,609
resulting from changes in taxes, benefits and tax credits (the tax/benefit squeeze)					-151	-311
resulting from changes announced in Budget 2012					+	+42
Proportionate change in total income					-7.9%	-7.7%

Notes: All increases in rates and thresholds and earnings based on information in Budget 2011, Autumn Statement 2011 and Budget 2012. Budget 2011 measures specified here include shift to CPI indexation of direct taxation and above inflation increase in income tax personal allowance in 2012-13. Autumn Statement measures relate to removal of the above-indexation increase in the child element of the CTC and the freezing the couple and single parent elements of the WTC. Fuel duty changes are absorbed in the underlying inflation forecasts. Budget 2012 measures include the above-inflation increase in the personal allowance in 2013-14.

Source: RF calculations based on stylised family

- Compared with a baseline of 2010-11, the wage squeeze (the extent to which RPI inflation outstrips growth in average earnings) reduces Aaron & Sophie's gross household earnings by £2,834 in 2012-13. A slight relaxation of this squeeze in 2013-14 reduces the overall loss to £2,609.
- Various changes in income tax and NICs rates help to offset these losses to some extent. However, the family is further hit by cuts to tax credits and the freeze in Child Benefit. Overall, this tax and benefit squeeze costs the family £151 in 2012-13 and £311 in 2013-14 compared with 2010-11. Budget 2012 improved the picture for 2012-13 by £42.
- Overall, the family's income is set to fall by £2,985 in 2012-13 compared with 2010-11 (or 7.9 per cent). Although 2013-14 looks slightly better, the family is still £2,919 (or 7.7 per cent) worse off.

Nikki

Two children, aged 3 & 17 (still in education); single-parent working 32.5 hours a week

2011-12 prices (£)	2010-11	2011-12	2012-13	2013-14	Change from 2010-11	
					in 2012-13	in 2013-14
Gross earnings	29,566	28,126	27,803	27,943	-1,763	-1,623
Post-tax earnings	22,432	21,488	21,364	21,637	-1,068	-796
Working Tax Credit	3,658	2,131	1,865	1,562	-1,792	-2,096
Child Tax Credit	5,433	5,655	5,752	5,756	+320	+323
Child Benefit	1,850	1,752	1,701	1,663	-149	-187
EMAs	412	70	0	0	-412	-412
Total household income	33,785	31,096	30,683	30,617	-3,102	-3,167
<i>of which: resulting from change in gross earnings (the wage squeeze)</i>					-1,763	-1,623
<i>resulting from changes in taxes, benefits and tax credits (the tax/benefit squeeze)</i>					-1,338	-1,544
<i>resulting from changes announced in Budget 2012</i>					+	+162
<i>Proportionate change in total income</i>					-9.2%	-9.4%

Notes: All increases in rates and thresholds and earnings based on information in Budget 2011, Autumn Statement 2011 and Budget 2012. Budget 2011 measures specified here include shift to CPI indexation of direct taxation and above inflation increase in income tax personal allowance in 2012-13. Autumn Statement measures relate to removal of the above-indexation increase in the child element of the CTC and the freezing the couple and single parent elements of the WTC. Fuel duty changes are absorbed in the underlying inflation forecasts. Budget 2012 measures include the above-inflation increase in the personal allowance in 2013-14.

Source: RF calculations based on stylised family

- Compared with a baseline of 2010-11, the wage squeeze (the extent to which RPI inflation outstrips growth in average earnings) reduces Nikki's gross household earnings by £1,763 in 2012-13. A slight relaxation of this squeeze in 2013-14 reduces the overall loss to £1,623.
- Various changes in income tax and NICs rates help to offset these losses to some extent. She also gains slightly from above-inflation increases in CTC, but is hit hard by cuts in WTC, the freezing of Child Benefit and the removal of Education and Maintenance Allowances. Overall, this tax and benefit squeeze costs her £1,338 in 2012-13 and £1,544 in 2013-14 compared with 2010-11. Budget 2012 improved the picture for 2012-13 by £162.
- Overall, the family's income is set to fall by £3,102 in 2012-13 compared with 2010-11 (or 9.2 per cent). 2013-14 looks worse still, with Nikki being £3,167 (or 9.4 per cent) worse off.

Josh & Katie

Couple, no children; dual earners, one working full-time, one part-time

2011-12 prices (£)	2010-11	2011-12	2012-13	2013-14	Change from 2010-11	
					in 2012-13	in 2013-14
Gross earnings	20,591	19,588	19,363	19,460	-1,228	-1,130
Post-tax earnings	17,876	17,289	17,214	17,465	-662	-411
Total household income	17,876	17,289	17,214	17,465	-662	-411
<i>of which: resulting from change in gross earnings (the wage squeeze)</i>					-1,228	-1,130
<i>resulting from changes in taxes, benefits and tax credits (the tax/benefit squeeze)</i>					+566	+720
<i>resulting from changes announced in Budget 2012</i>					+	+162
<i>Proportionate change in total income</i>					-3.7%	-2.3%

Notes: All increases in rates and thresholds and earnings based on information in Budget 2011, Autumn Statement 2011 and Budget 2012.
Budget 2011 measures specified here include shift to CPI indexation of direct taxation and above inflation increase in income tax personal allowance in 2012-13. Autumn Statement measures relate to removal of the above-indexation increase in the child element of the CTC and the freezing the couple and single parent elements of the WTC. Fuel duty changes are absorbed in the underlying inflation forecasts. Budget 2012 measures include the above-inflation increase in the personal allowance in 2013-14.

Source: RF calculations based on stylised family

- Compared with a baseline of 2010-11, the wage squeeze (the extent to which RPI inflation outstrips growth in average earnings) reduces Josh & Katie's gross household earnings by £1,228 in 2012-13. A slight relaxation of this squeeze in 2013-14 reduces the overall loss to £1,130.
- Various changes in income tax and NICs rates help to offset these losses to some extent and, with no children and no eligibility for tax credits, the couple are unaffected by the cuts modelled here. Their income is therefore boosted by £566 in 2012-13 and £720 in 2013-14 compared with the baseline. Of the gain in 2013-14, £162 flows from changes announced in Budget 2012.

ANNEX - details on analysis

1 Chart 1 - the overall impact of changes due in 2012-13 and 2013-14

In considering the cumulative distributional impact in 2013-14 of measures yet to kick in we model a specific set of variables by establishing a 2013-14 counterfactual in which various changes do not take place, namely:

- Reversal of the Baby Addition element of the CTC in 2012-13 (Budget 10)
- Removal of the upper threshold for tapering of the family element of CTC in favour of tapering immediately after the child element from 2012-13 (Budget 10)
- Freeze in the basic rate limit in 2013-14 (Budget 10)
- Freeze in Child Benefit rates in 2012-13 and 2013-14 (Budget 10)
- Increase in the working hours requirement for couples with children to 24 hours (SR10)
- Removal of Child Benefit from families with a higher rate taxpayer from January 2013 (SR10) and introduction of a tapered reduction from £50k to £60k (Budget 12)
- Freeze in basic and 30-hour elements of WTC in 2012-13 and 2013-14 (SR10)
- Switch in default index assumption for direct taxes from RPI to CPI from 2012-13 (Budget 11)
- Increase of £630 in personal allowance in 2012-13, with offsetting adjustment to basic rate limit and no change in higher rate threshold (Budget 11)
- One-off increases in Pension Credit in 2012-13 (Autumn Statement 11)
- Freeze in couple and lone parent elements of WTC in 2012-13 (Autumn Statement 11)
- Freeze in age-related personal allowances from 2013-14 (Budget 12)
- Increase of £1,100 in personal allowance in 2013-14, with offsetting reduction in basic rate limit and higher rate threshold (Budget 12)

Instead, all rates and thresholds are subject to uprating in line with the indexation defaults set out in the Budget 12 policy costings document and used by the government for setting its own baseline.

Several key measures are not modelled, affecting the completeness of the findings, including:

- Above-inflation increases in excise duties
- Reduction in additional rate of income tax to 45p in 2013-14 (Budget 12)
- Introduction of in-year income disregard for tax credits from 2012-13
- Introduction of real-time data in assessing tax credit awards from 2013-14
- Removal of the 50-plus element of WTC from 2012-13
- Changes in CTB and HB awards and administration
- Benefit payments cap
- Cap on unlimited tax reliefs
- SDLT on residential properties over £2 million

Nor does it model any changes made prior to April 2012, including the introduction of the additional rate of income tax, the increase in the main rate of VAT and the faster tapering of tax credits.

2 **Chart 2 - comparing the impact of personal allowance and tax credit changes in 2012-13 and 2013-14**

In this analysis we again considering the cumulative distributional impact in 2013-14 of measures yet to kick by establishing a 2013-14 counterfactual in which various changes do not take place, namely:

- Reversal of the Baby Addition element of the CTC in 2012-13 (Budget 10)
- Removal of the upper threshold for tapering of the family element of CTC in favour of tapering immediately after the child element from 2012-13 (Budget 10)
- Freeze in the basic rate limit in 2013-14 (Budget 10)
- Increase in the working hours requirement for couples with children to 24 hours (SR10)
- Freeze in basic and 30-hour elements of WTC in 2012-13 and 2013-14 (SR10)
- Switch in default index assumption for direct taxes from RPI to CPI from 2012-13 (Budget 11)
- Increase of £630 in personal allowance in 2012-13, with offsetting adjustment to basic rate limit and no change in higher rate threshold (Budget 11)
- Freeze in couple and lone parent elements of WTC in 2012-13 (Autumn Statement 11)
- Freeze in age-related personal allowances from 2013-14 (Budget 12)
- Increase of £1,100 in personal allowance in 2013-14, with offsetting reduction in basic rate limit and higher rate threshold (Budget 12)

Instead, all rates and thresholds are subject to uprating in line with the indexation defaults set out in the Budget 12 policy costings document and used by the government for setting its own baseline. Several key measures are not modelled, affecting the completeness of the findings, including:

- Reduction in additional rate of income tax to 45p in 2013-14 (Budget 12)
- Introduction of in-year income disregard for tax credits from 2012-13
- Introduction of real-time data in assessing tax credit awards from 2013-14
- Removal of the 50-plus element of WTC from 2012-13