

## Money for everyone?

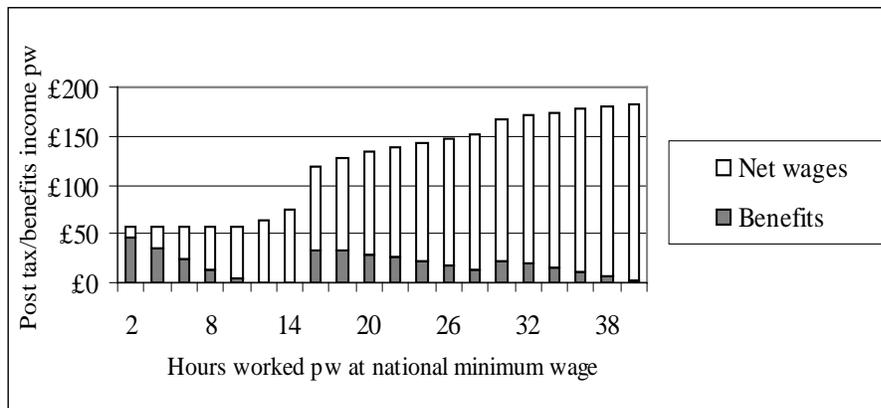
### An appendix to chapter 14

#### An example of a revenue neutral Citizen's Income funded by reducing tax allowances and means-tested and other benefits

If a Citizen's Income were to be funded by reducing tax allowances and means-tested and National Insurance benefits, then the costings might look like this:

##### *The current system*

Putting housing-related benefits to one side, in 2006 the net income of a single earner aged 25 or over after income tax, national insurance contributions, income support/jobseeker's allowance and 'Working Tax Credits' was as follows:



The chart clearly reveals the benefit trap. As earned income rises, earnings are taxed and benefits are withdrawn. Someone working between 11 and 16 hours per week retains their additional earnings in full, but when they work more than 16 hours per week and become entitled to 'Tax Credits', their net income rises much more slowly. If someone earning the national minimum wage (£5.35 in 2006) starts working 40 rather than 16 hours, his or her *gross* income increases by £128 per week, but his or her *net* income increases by only £65 per week – having suffered £34 in income tax and national insurance contributions and lost £29 in working 'Tax Credits'. The increase in net income is only 51% of gross income, so there is a 'marginal deduction rate' or 'withdrawal rate' of 49%. For many family types, withdrawal rates are 85% of earned income up to nearly £400 per week; and for some family types and some earnings ranges the withdrawal rate is higher than 95%.

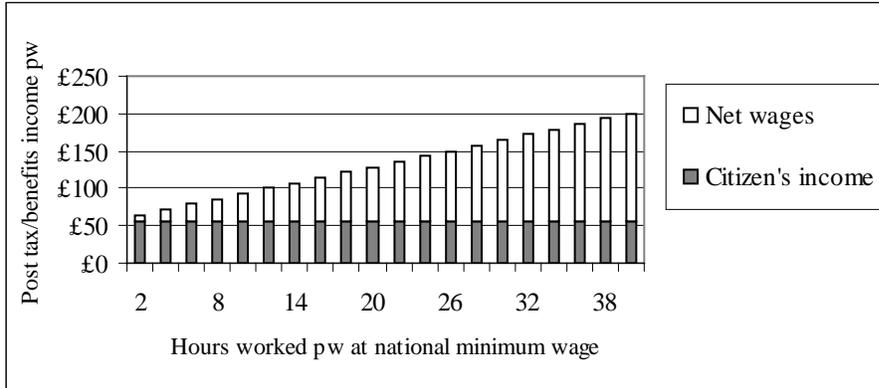
##### *A Citizen's Income proposal:*

The relatively uncontroversial Citizen's Income scheme proposed here assumes the following rates of Citizen's Income:

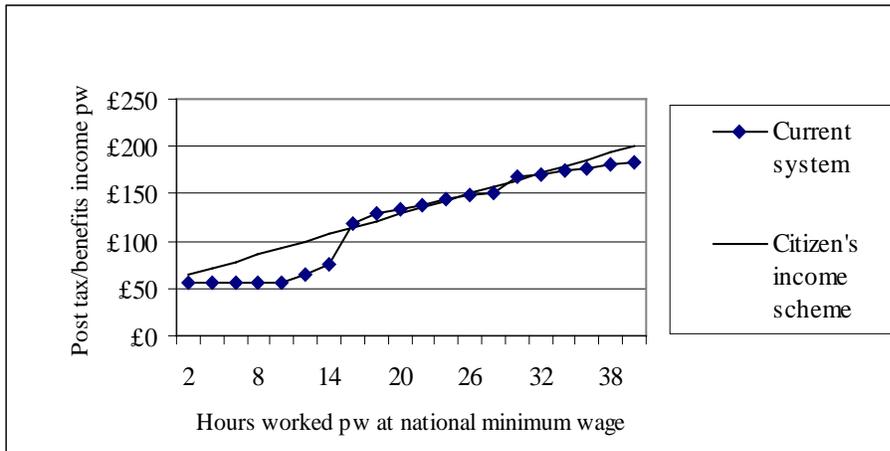
Age	Weekly CI	2006-07 rates:
0 to 18	£34	Income Support for 16-17 year olds
19 to 24	£45	Income Support for 18-24 year olds
25 to 64	£57	Income Support for 25-59 year olds

65 and over      £114

Pensions Credit rate



Overlapping the two previous charts shows that the system will increase work incentives at most levels of income:



The Citizen's Income scheme outlined here is intended to be revenue and cost neutral. For simplicity, we shall assume a flat rate of tax on earned income of 33% (22% income tax plus 11% employee's national insurance contributions), with a higher rate as at present on higher earnings. Rates of 22% are assumed for pensioners and of 20% for unearned income. The estimated total cost of benefits and tax reliefs and allowances that would be replaced is as follows:

Social security spending	£100 bn	(Calculation 1, below)
Tax reliefs and allowances	£94 bn	(Calculation 2, below)
DWP <sup>1</sup> running costs	£6 bn	(DWP <sup>1</sup> expenditure budget)
HMRC <sup>2</sup> (tax credit administration)	<u>£1 bn</u>	
Total	<u>£201 bn</u>	

The total cost of the proposed scheme is as follows:

Age	Population survey 2006	Citizen's Income Cost per week	
0 to 18	13,912,600	£34	£25 bn
19 to 24	4,770,800	£45	£11 bn
25 to 64	32,141,500	£57	£95 bn
65 and over	<u>9,708,100</u>	£114	<u>£58 bn</u>
	60,533,000		£189 bn
Running costs (1%)			<u>£2 bn</u>
Total cost p.a.			<u>£191 bn</u>

We assume that tax relief for pension contributions will be restricted to 22%, the same as the rate of income tax deducted from pensions in payment. Running costs are estimated at one per cent, which is the approximate cost of administering child benefit (non-contributory, non-means tested, non-taxable).

In the short term some of the £10bn saved will be needed to compensate those for whom transitional measures are required, as explained later.

That the UK can afford a Citizen's Income scheme is also illustrated by the fact that per capita GDP was £391 per week in 2005 (UK National Accounts 2006, Table 1.5, Item IHXT).

1 DWP: Department for Work and Pensions

2 HMRC: Her Majesty's Revenue and Customs

### Calculation 1

DWP Table 3, estimated outturn, 2006-07	£m	Note
Basic state pension	44,840	
Pension Credit	6,200	(1)
Jobseeker's allowance	2,460	
Incapacity benefit	4,700	(2)
Statutory maternity and sick pay	800	
Income support (less child allowances)	6,000	
Carer's allowance and other minor benefits	<u>2,000</u>	
sub-total, Great Britain only	67,000	
<i>add 3% for Northern Ireland</i>	2,000	
HMRC annual report 2005-06		
Child benefit and child trust fund	11,700	(3)
'Tax Credits'	17,300	(4)
Student grants/low interest loans	<u>2,000</u>	(5)
Total	<u>100,000</u>	

Notes

- (1) Any disability-related elements will be retained.
- (2) The total cost according to Table 3 is £6,529m. If those eligible for incapacity benefit at the long term rate of £78 per week are paid £21 in addition to the Citizen's Income rate of £57, the cost is reduced by  
 $(£57 \div £78) \times £6,529m = £4,771m$ .
- (3) Child trust fund estimated at 700,000 births x £250.
- (4) Figure excludes £4,600m included in Appendix 2
- (5) Figure per [www.donttaxmytalent.co.uk](http://www.donttaxmytalent.co.uk)

## Calculation 2

	£m	
HMRC Table 1.5		
Cost of tax reliefs and allowances (2006-07)		Note
Personal allowance (income tax)	30,100	(1)
Age-related personal allowances	2,400	
'Tax Credits' (treated as negative income tax)	4,600	(2)
Income tax relief for approved pension schemes	16,300	(3)
National insurance rebates for pension schemes	17,000	(4)
PEP, ISA, VCT and EIS reliefs	2,300	(5)
HMRC Table 1.6 (2007-08)		(6)
Additional tax if all earned income were taxed at 33%		
Increase starting rate from 10% to 22%	6,600	(7)
Remove lower earnings/profits limit (national insurance)	12,600	(8)
Align Class 4 and Class 1 national insurance rates	900	(9)
Align upper earnings/profits limit with higher rate tax threshold (national insurance)	<u>1,500</u>	(10)
	<u>94,300</u>	

### Notes

- (1) Table 1.5 gives a figure of £40,000m, but this assumes that the basic state pension would be taxable, which would raise £9,900m (£44,837m x 22%). The potential saving shown here is lower as the Citizen's Income paid to pensioners will be non-taxable.
- (2) These are in addition to the 'Tax Credits' treated as benefit payments.
- (3) Table 1.5 shows £16,300m as the net cost, i.e. the cost of tax relief (at up to 40%) minus tax paid on pensions in payment (largely at 22%). If tax relief for pensions contributions is restricted to 22%, the net long-run cost will be minimal.
- (4) Under a Citizen's Income scheme, national insurance will be merged into the overall tax rate and all benefits will be non-contributory, so there will be no additional national insurance rebates or reliefs.

- (5) These are regressive subsidies. A higher rate taxpayer benefits twice as much as a basic rate taxpayer and benefit claimants lose benefits if they have significant savings.
- (6) The figures for 2006-07 are no longer published.
- (7)  $12 \times \text{£}550\text{m}$
- (8)  $\text{£}97 \div \text{£}2 \times (\text{£}240\text{m} + \text{£}20\text{m}) = \text{£}12,610$
- (9)  $3 \times \text{£}315\text{m} = \text{£}945\text{m}$
- (10) Higher rate threshold  $\text{£}38,335$  minus upper earnings/profits limit  $\text{£}33,600 = \text{£}4,735$ .  $\text{£}4,735 \div \text{£}520 \times (\text{£}150\text{m} + \text{£}15\text{m}) = \text{£}1,502$

### *Transitional arrangements*

There will be clear winners under the Citizen's Income system proposed here, in particular:

- earners with low or fluctuating incomes
- students
- families with children on low to average earnings
- pensioners with small savings and pensioner couples

It is also clear that if the Citizen's Income scheme were adopted outright then transitional measures will be required for

- lone parents with no earned income who receive no maintenance from the absent parent
- women aged between 60 and 65 eligible for the state pension
- single earner households earning between  $\text{£}8,000$  and  $\text{£}16,000$  per annum, for whom the Citizen's Income envisaged would not compensate for the withdrawal of both child tax credit and working tax credit
- civil servants at Her Majesty's Revenue and Customs and the Department for Work and Pensions who have to be retrained or made redundant.

The Citizen's Income scheme outlined here ignores the fact that some residents have not been in the UK long enough to qualify, and it also ignores pensioners living abroad who receive a state retirement pension. It is assumed that the two issues will cancel each other out so that a negligible overall cost or saving will be the result.