TUC research note

July Budget 2015 reforms – impacts on households

INTRODUCTION

In the previous parliament, the coalition government published a document alongside every Budget that showed the distributional impact on households by income deciles and quintiles. This analysis provided clarification of how the effects of spending decisions – in particular tax and benefit policies with direct impacts on household incomes – would be felt by families with differing income levels.

In the first Budget since the 2015 election, while an accompanying document was published by HM Treasury that included information on household impacts, this was not provided in the same form as previously, and there was no analysis of the impacts of policies across the income distribution by deciles and quintiles.

The TUC therefore commissioned research using the IPPR tax-benefit model to provide this analysis with the aim of improving transparency and public understanding of the future impacts of the Chancellor's decisions on families.

FINDINGS

The following tables provide details of income changes from the direct effects of decisions made in the July 2015 Budget.

All the tables represent the combined impacts of changes to Universal Credit work allowances, benefit freeze, minimum wage, personal income tax allowance and higher rate income tax threshold.

The data in the tables is calculated on the basis of incomes before housing costs and includes households of all types and ages.

The analysis is presented in 2015/16 prices.

TABLE 1 – Household income changes from 2015/16 to 2020/21 by decile for all households

Household income decile	Change in annual income (2015/16 £)	percentage change in weekly income
1st (poorest)	-170	-1.44
2nd	-200	-1.26
3rd	-200	-1.05
4th	-100	-0.49
5th	40	0.17
6th	200	0.73
7th	300	0.92
8th	390	1
9th	510	1.09
10th (richest)	780	0.92

TABLE 2 - Household income changes (£) from 2015/16 to 2020/21 by quintile for households that are (i) not working and (ii) working

Household income quintile	Change in annual income (2015/16 £)	
	not working	*working*
1st (poorest)	-30	-460
2nd	-10	-300
3rd	50	160
4th	130	420
5th (richest)	490	670
All households	*50*	*210*

TABLE 3 - Household income changes (%) from 2015/16 to 2020/21 by quintile for households that are (i) not working and (ii) working

Household income quintile	Percentage change in weekly income	
	not working	*working*
1st (poorest)	-0.29	-2.42
2nd	-0.05	-1.22
3rd	0.28	0.55
4th	0.53	1.07
5th (richest)	1.08	0.97
All households	*0.27*	*0.51*

Distribution within deciles and quintiles

It is important to note that within each income decile there will be some people with gains and others with losses.

So even for a decile or quintile with an average loss – such as the £460 annual loss to the income of the first quintile – there will be people within that decile who have a net gain.

However, households with net gains in the lower deciles and quintiles will generally only have small gains when compared to the gains of the higher deciles and quintiles. And other households in the lower deciles or quintiles will have losses even larger than the average loss.

METHODOLOGY

Benefit reforms included in the analysis

This note sets out the way we have used the IPPR tax-benefit model to simulate a number of the reforms to taxes and benefits announced at the July 2015 Summer Budget. We model out to 2020 and provide the distributional impact, both overall (by decile) and disaggregating working and non-working households (by quintile). We provide the annual average change in disposable household income, before housing costs, and the associated percentage change.

The model only includes changes to Universal Credit, and not to tax credits, as it is expected that most households will have been transferred from tax credits to Universal Credit by 2020. However we have also looked at the impact of tax credits cuts on working households. This is shown below in table 4. More detailed analysis of tax credit cut impacts will be published in a future TUC research note.

TABLE 4 - Household income changes (£) from 2015/16 to 2020/21 by quintile for households that are (i) not working and (ii) working as a result of tax credit cuts

Household income quintile	**Change in annual income (2015/16 £)**	
	not working	*working*
1st (poorest)	-40	-740
2nd	-30	-880
3rd	-10	-380
4th	-10	-80
5th (richest)	-10	-10
All households	*-30*	*-340*

Benefit freezes

The model includes the announced freezes in working-age benefit by holding them at their 2016 value until 2019/20, before up-rating them in line with CPI inflation for one year to reach 2020/21 values. We model freezes in the following benefits against a baseline where they are uprated in line with CPI:

- Jobseekers' Allowance
- Child Benefit

While the freeze extends to child and working tax credits, housing benefit and income support, we assume Universal Credit has been fully implemented and therefore these benefits have been fully grandfathered out. The budget made no announcements regarding freezing any of the elements of Universal Credit.

Universal Credit work allowances

Again, under this scenario, we have assumed all households have migrated to Universal Credit. The Summer budget announced the following changes to the work allowances within Universal Credit by 2020;

- Work allowances for those without housing costs will be reduced to £5,000 for those with children and those with a limited capability for work, and removed entirely for those without children
- Work allowances for those with housing costs will be reduced to £2,400 for those with children, removed entirely for those without children, and unaltered for those with a limited capability to work

These are measured against a baseline where the work allowances, past their announced freeze, rise in line with CPI.

We also model the combined impact of the reduction in Universal Credit work allowances and the benefit freeze. These three scenarios are provided in the tab marked ‘welfare’ in the accompanying excel workbook. We provide the decile impact of the benefit freeze and cuts to Universal Credit work allowances, and a detailed set of distributional impacts of the combined changes.

Tax

While not announced at the budget, it is the government’s stated policy to increase the personal tax allowance to £12,500 over this parliament, and the Higher Rate Threshold (the point at which individual’s begin paying higher rate tax) to £50,000. We model the detailed distributional impact of these changes, relative to a baseline where both rise in line with CPI, in the tab marked ‘Tax’.

The National Living Wage

In order to model the impact of the introduction of the National Living Wage, we adjust individual’s earnings in the base data underlying the IPPR tax-benefit model (the Family Resources Survey) so that those aged over 24 with hourly earnings between the minimum wage and the new National Living Wage see an uplift in their earnings.

The Family Resources Survey collects data on weekly incomes and weekly hours. Because of data collection issues involved in a household survey of its kind, some individuals report earnings and hours that imply they are earning less than the National Minimum Wage. This issue has to be dealt with by excluding some of those individuals from the analysis. We include those whose implied hourly wages are within 5 per cent of the National Minimum Wage threshold. Therefore, our modelling should be treated with some caution.

We model the detailed distributional impact of the National Living Wage reaching £9.35 an hour by 2020, relative to a baseline where the National Minimum Wage increases by average earnings. The results of this modelling are contained in the ‘Living Wage’ tab of the attached spreadsheet.

Combined impact of national living wage, benefit changes and tax cuts

The above reforms (benefit freezes, work allowance cuts, tax cuts and the National Living Wage) have been aggregated into a combined scenario.

Reforms not modelled include:

- From next year, in London the benefit cap will fall to £23,000, outside London it will fall to £20,000. The IPPR tax-benefit model does not currently provide the facility to model a regional benefit cap.
- The budget announced that, for new claims, the family element in Universal Credit would be removed for new claims, and the child element would be limited to two children. The IPPR tax-benefit model does not provide the facility to model flows into and between benefits, so these changes are also excluded from the analysis.
- Ending the automatic entitlement to housing benefit for under-21s in Universal Credit; the July 2015 budget announced the end of an ‘automatic’ entitlement to housing support

under Universal Credit for under-21s. In practice, the majority of young people claiming Universal Credit will not be impacted by this claim, as young people with children, those estranged from their parents, and those in work for six months prior to claiming, will not see their access to housing benefit restricted, and make up the majority of claimants. It is not possible within the FRS to distinguish between these groups (other than those with children)

- Reducing the rate of ESA for the work-related activity group to the same rate as Jobseekers allowance; currently within the Family Resources Survey there is a mixture of individuals who have transitioned to the new Employment Support Allowance, and a group of individuals who are still claiming Incapacity Benefit. We are currently working to implement ESA in our model, which will be possible with the next year (2013/14) of Family Resource Survey data.

These benefits primarily support those in the lowest income deciles. Their exclusion means that the analysis is likely to understate the scale of the losses among lower income groups.