Reducing income inequality in the UK: testing the idea of a Basic Income

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University of Essex

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Motivation

- Income inequality in the UK is high

- Tax-benefit reforms in the UK led to increased reliance on means-testing
  - high marginal tax rates at the bottom
  - unmet need due to benefit non-take-up

- Basic Income (BI) put forward as an idea to deal with these issues
  - unconditional and universally paid benefit which decouples income from work, or any other condition, and replaces family with individual benefit entitlements
  - in the UK: trial options being explored (e.g. Sheffield, Scotland) and idea promoted by the Green and Labour parties

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What we do

- We use the tax-benefit model UKMOD to test the impact of different Basic Income schemes
  - account for interactions between Basic Income and the rest of the tax-benefit system
  - design budget-neutral schemes

- A Basic Income alongside the current tax and benefit system can be an effective way to reduce poverty and inequality

- Even in the most generous scenario we have to retain the means-tested safety net to avoid a large number of low-income losers

Policy	1 no PA
income tax schedule: tax rates and tax thresholds	abolish personal tax allowance (£12,500 per year) and married couples allowance
National Insurance contributions	abolish primary threshold (£166 per week)
Child Benefit (£ per week)	abolish withdrawal for higher-income families
means-tested benefits	BI enters income-test of CTC, WTC, HB, CTR, PC, income-based JSA and ESA, UC
Basic Income (£ per year)	£2,990

Policy	1 no PA	2 tax rates+3pp
income tax schedule: tax rates and tax thresholds	abolish personal tax allowance (£12,500 per year) and married couples allowance	tax rates ↑ by 3 % points (23%, 43%, 48%)
National Insurance contributions	abolish primary threshold (£166 per week)	
Child Benefit (£ per week)	abolish withdrawal for higher-income families	
means-tested benefits	BI enters income-test of CTC, WTC, HB, CTR, PC, income-based JSA and ESA, UC	
Basic Income (£ per year)	£2,990	£3,750

Policy	1 no PA	2 tax rates+3pp	3 CB+
income tax schedule: tax rates and tax thresholds	abolish personal tax allowance (£12,500 per year) and married couples allowance		
		tax rates ↑ by 3 % points (23%, 43%, 48%)	
National Insurance contributions	abolish primary threshold (£166 per week)		
Child Benefit (£ per week)	abolish withdrawal for higher-income families		
			raise benefit to: ~0.3 of the 2019 relative poverty line (£63 [£3,260 per year])
means-tested benefits	BI enters income-test of CTC, WTC, HB, CTR, PC, income-based JSA and ESA, UC		
			reduce child/family rates of CTC/HB/UC
Basic Income (£ per year)	£2,990	£3,750	£3,260

Policy	1 no PA	2 tax rates+3pp	3 CB+	4 tax rates++	
income tax schedule: tax rates and tax thresholds	abolish personal tax allowance (£12,500 per year) and married couples allowance				
		tax rates ↑ by 3 % points (23%, 43%, 48%)		tax rates ↑: 30%, 40% and 50% (UK)	
National Insurance contributions	abolish primary threshold (£166 per week)				
Child Benefit (£ per week)	abolish withdrawal for higher-income families				
			raise benefit to: ~0.3 of the 2019 relative poverty line (£63 [£3,260 per year])		
means-tested benefits	BI enters income-test of CTC, WTC, HB, CTR, PC, income-based JSA and ESA, UC				
				reduce child/family rates of CTC/HB/UC	
Basic Income *(£ per year)*	£2,990	£3,750	£3,260	£4,410	

Policy	1 no PA	2 tax rates+3pp	3 CB+	4 tax rates++	5 tax rates & thresholds +++	
income tax schedule: tax rates and tax thresholds	abolish personal tax allowance (£12,500 per year) and married couples allowance					
		tax rates ↑ by 3 % points (23%, 43%, 48%)		tax rates ↑: 30%, 40% and 50% (UK)	tax rates ↑: 30%, 40%, 50%, 60%, 65%	
					tax thresholds: £25,000; £45,000; £90,000; £190,000; £190,000+	
National Insurance contributions	abolish primary threshold (£166 per week)					
					raise Upper Earnings Limit for Class 1 and 4 (to £55,000 per year)	
Child Benefit (£ per week)	abolish withdrawal for higher-income families					
			raise benefit to: ~0.3 of the 2019 relative poverty line (£63 [£3,260 per year])			
means-tested benefits	BI enters income-test of CTC, WTC, HB, CTR, PC, income-based JSA and ESA, UC					
			reduce child/family rates of CTC/HB/UC			
Basic Income (£ per year)	£2,990	£3,750	£3,260	£4,410	£5,170	

Policy	1 no PA	2 tax rates+3pp	3 CB+	4 tax rates++	5 tax rates & thresholds +++	6 CB 1st child+
income tax schedule: tax rates and tax thresholds	abolish personal tax allowance (£12,500 per year) and married couples allowance					
		tax rates ↑ by 3 % points (23%, 43%, 48%)		tax rates ↑: 30%, 40% and 50% (UK)	tax rates ↑: 30%, 40%, 50%, 60%, 65%	
					tax thresholds: £25,000; £45,000; £90,000; £190,000; £190,000+	
National Insurance contributions	abolish primary threshold (£166 per week)					
					raise Upper Earnings Limit for Class 1 and 4 (to £55,000 per year)	
Child Benefit (£ per week)	abolish withdrawal for higher-income families					
			raise benefit to: ~0.3 of the 2019 relative poverty line (£63 [£3,260 per year])			0.5 of the poverty line for the 1st child (£110 [£5,721 per year]) and 0.3 for any other child
means-tested benefits	BI enters income-test of CTC, WTC, HB, CTR, PC, income-based JSA and ESA, UC					
			reduce child/family rates of CTC/HB/UC			
Basic Income (£ per year)	£2,990	£3,750	£3,260	£4,410	£5,170	£4,810

Impact on the fiscal budget

	2019/20 (billion £ per year)	1 no PA	2 tax rates+3pp	3 CB+	4 tax rates++	5 tax rates & thresholds +++	6 CB 1st child+
		change (relative to 2019/20 current system) in £ billion per year					
spending on:							
Means-tested benefits	59	-18	-22	-29	-35	-39	-38
Child Benefit	11	+1	+1	+33	+36	+36	+54
Basic Income	0	+153	+191	+166	+225	+264	+245
revenues from:							
direct taxes	199	+106	+140	+140	+196	+231	+231
NI contributions	90	+30	+30	+30	+30	+30	+30

Poverty and inequality
in 2019/20 and across BI scenarios

Poverty rate

Bars:
- 2019/20 current system: 17
- 1 no PA: 15
- 2 tax rates+3pp: 14
- 3 CB+: 14
- 4 tax rates++: 12
- 5 tax rates & thresholds +++: 9
- 6 CB 1st child+: 8

Gini

Bars:
- 2019/20 current system: 31
- 1 no PA: 29
- 2 tax rates+3pp: 28
- 3 CB+: 28
- 4 tax rates++: 27
- 5 tax rates & thresholds +++: 25
- 6 CB 1st child+: 24
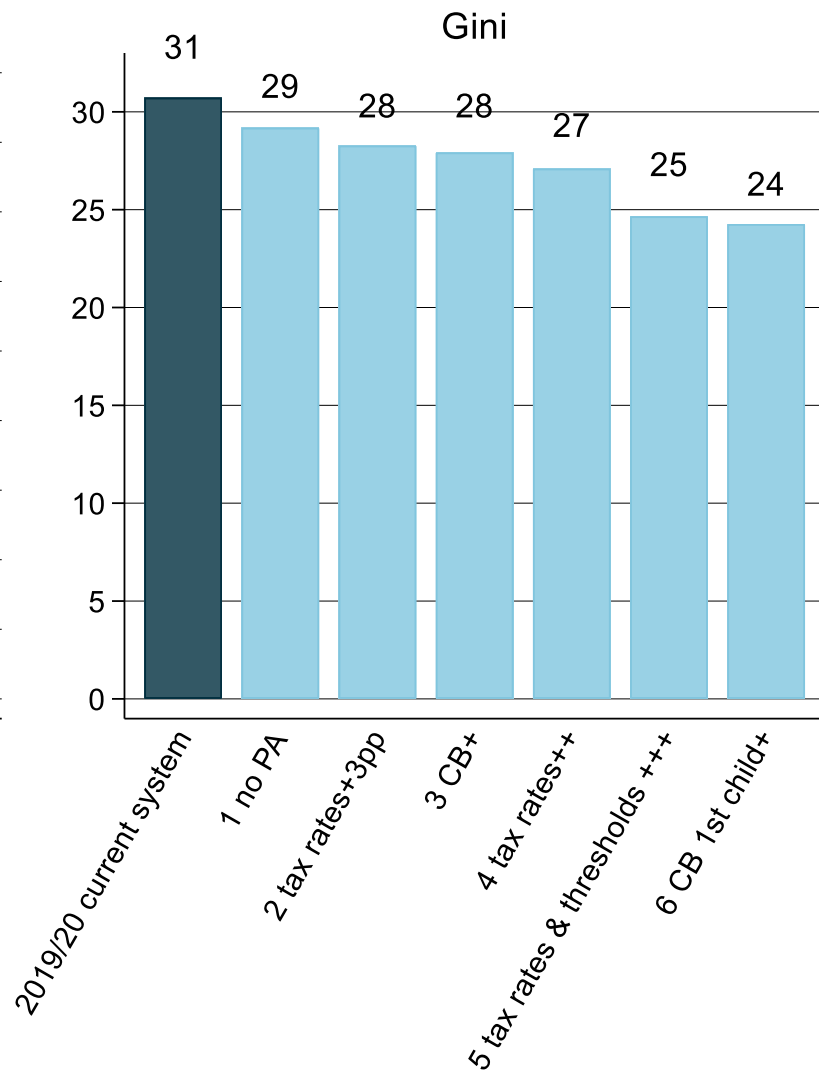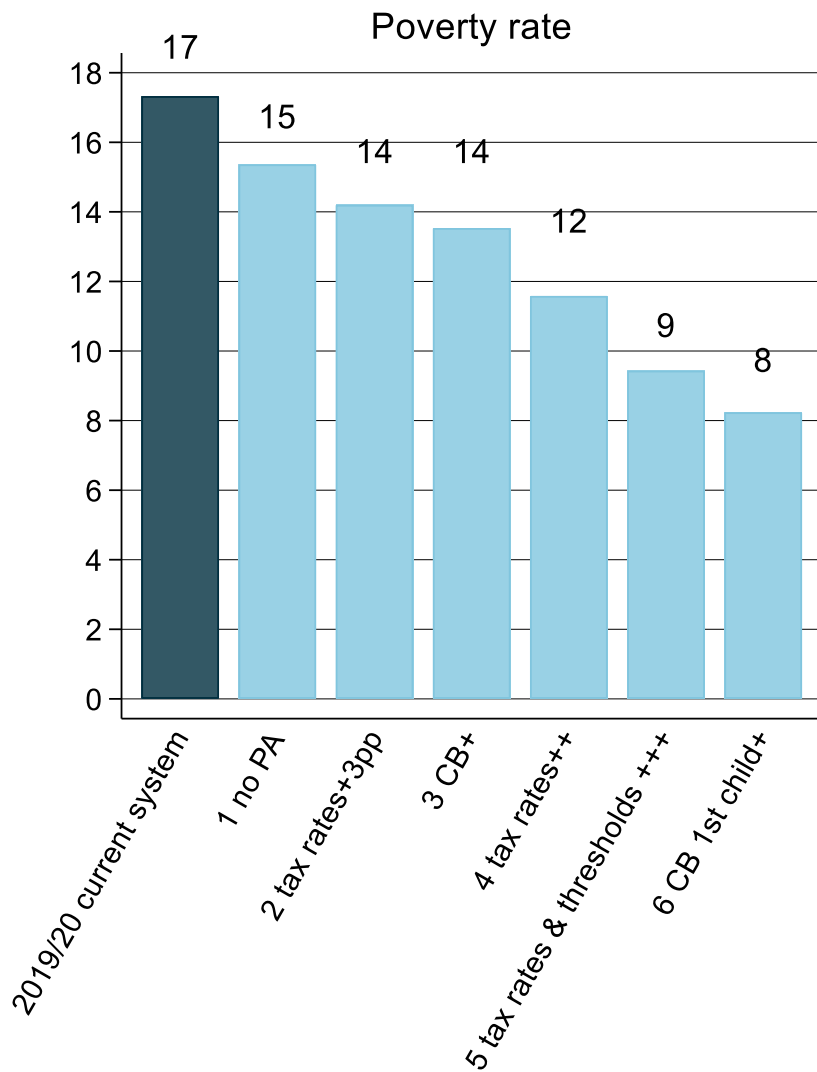
Notes: poverty line is 60% of 2019 median equivalised hh net income.

Change (%) in net income by _decile_
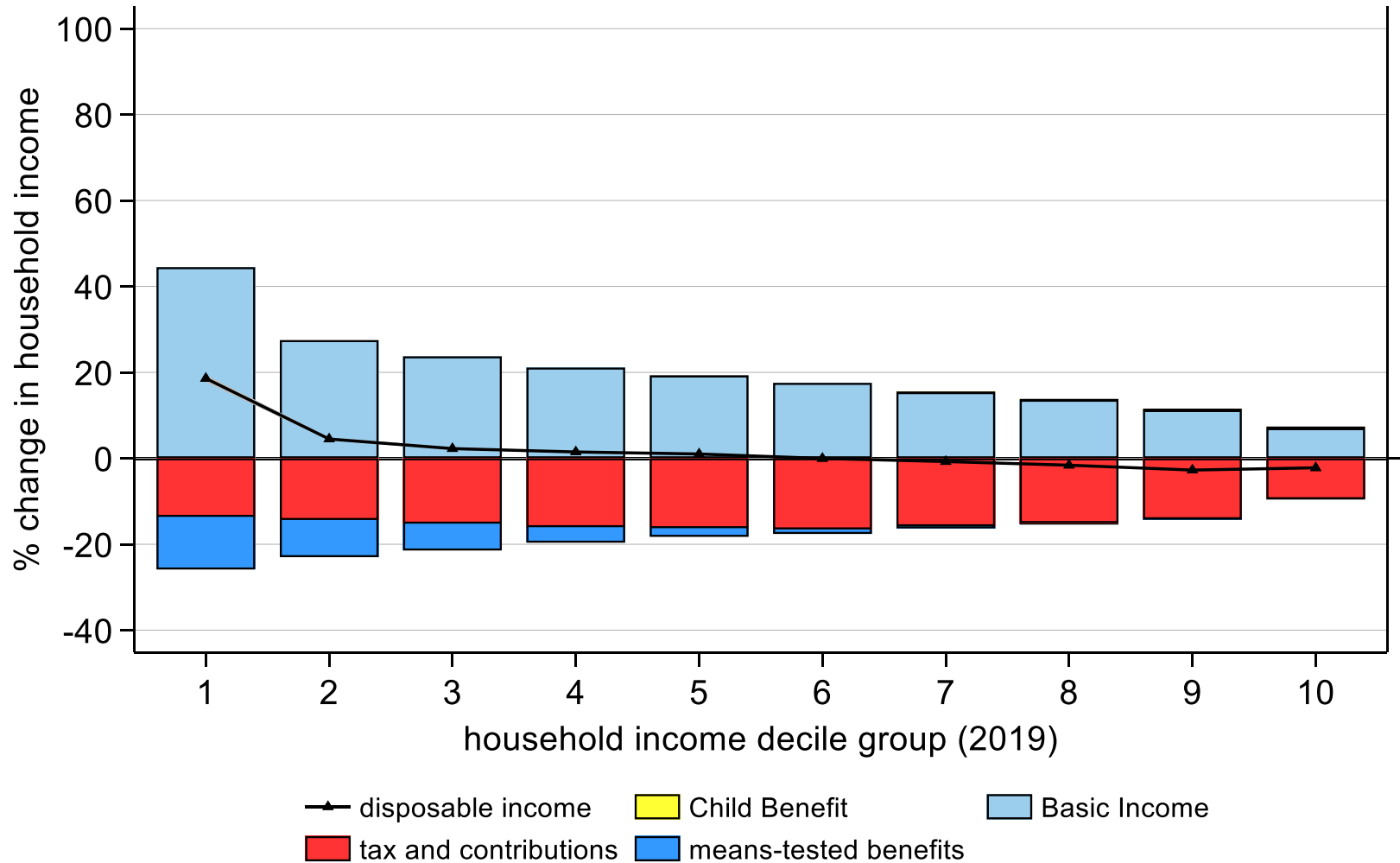
Change (%) in net income by _decile_

6 CB 1st child+

household income decile group (2019)

% change in household income

- disposable income
- tax and contributions
- Child Benefit
- means-tested benefits
- Basic Income

Change (%) in net income by _age_

1 no PA

6 CB 1st child+

% change in household income

age group
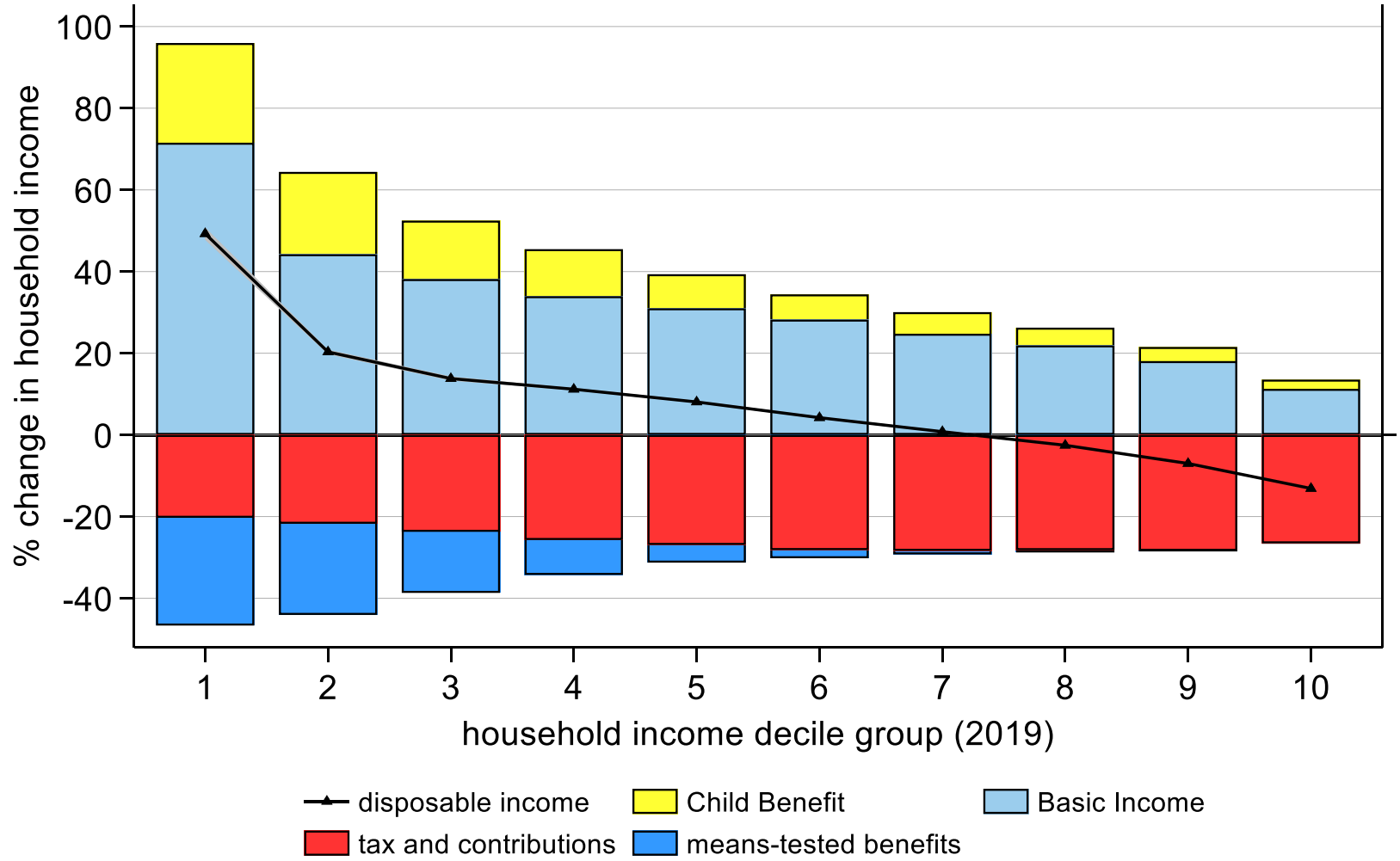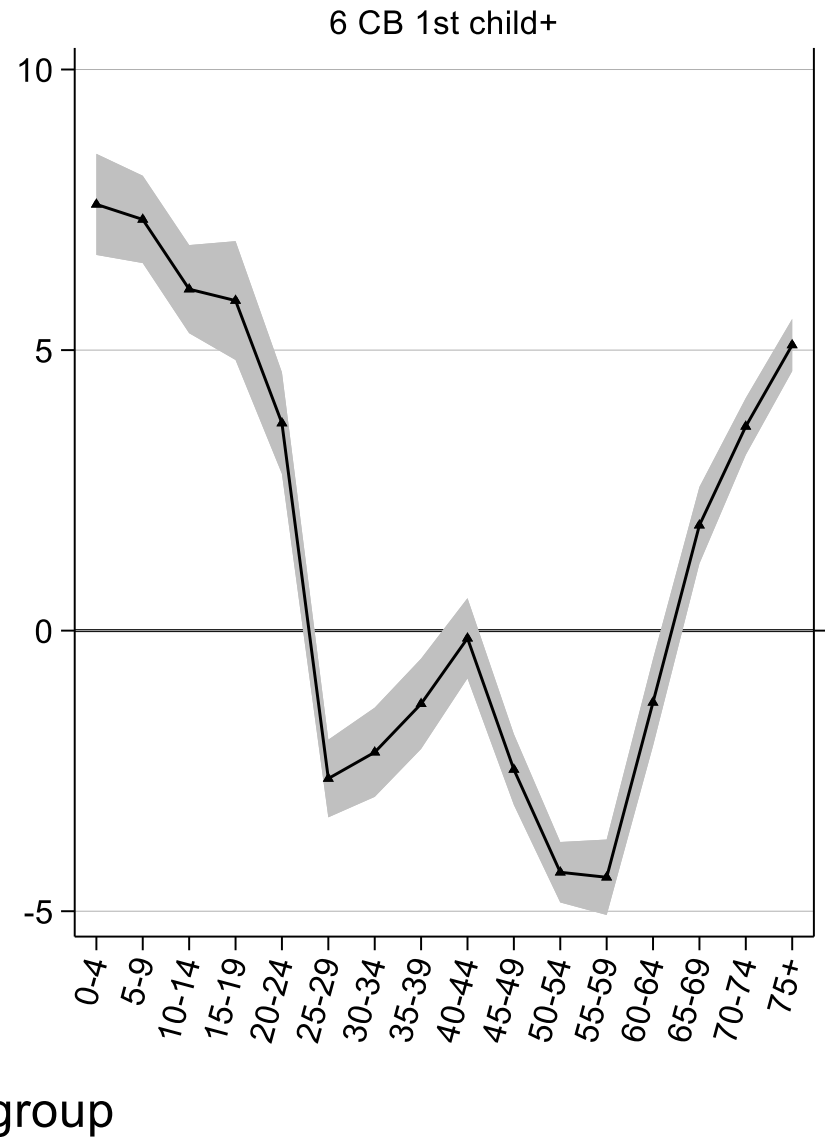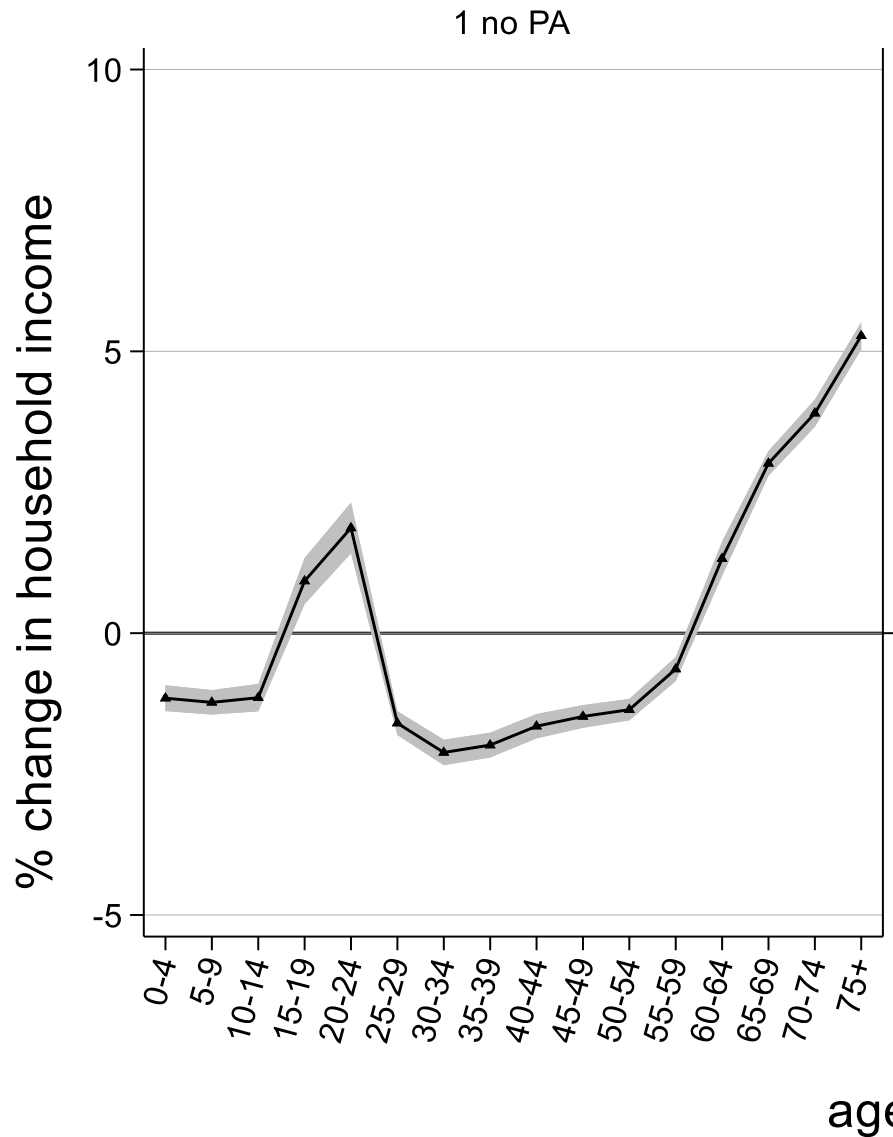
disposable income

Summary

- A BI alongside the current tax and benefit system can be an effective way to reduce poverty and inequality

- Cashing out the PA and NIC allowance is a start but to make a bigger difference a larger BI is needed, financed by progressive tax increases

- To avoid low income losers or very high tax rates, need to retain means-tested safety net
  - BI reduces reliance on means-testing (e.g. spending reduction ranged from 30% to 66%) but it can't entirely remove the need for it

- A universal child benefit is a powerful tool for redistribution
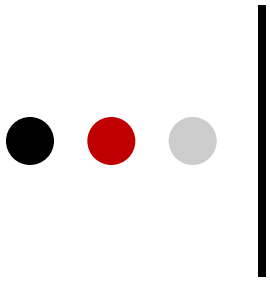
Thank you!

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What we do (cont.)

- We use the tax-benefit model UKMOD with household micro-data from the Family Resources Survey (FRS) for 2017/18. UKMOD calculates:
    1. <u>who</u> in the data is entitled to a benefit / liable to pay taxes/NI
    2. <u>how much</u> is the benefit entitlement and tax/NI liability
    3. households' <u>net income</u> = reported earned income + simulated benefits – simulated taxes/NI

- Legacy benefits and Universal Credit simulated in the 2019/20 system
    - Eligible families/households randomly allocated to LB or UC
    - 41% of claimants on UC (OBR estimate)
    - Incomplete take-up of LB and UC

- All interactions between direct taxes and cash benefits taken into account
    - BI included in existing income-tests
        - reduces reliance on means-testing (LB+UC)
        - can lift some families out of it entirely
        - 100% benefit for those not currently taking up their means-tested entitlements

- We evaluate the morning-after effect of the reform scenarios on
    - Benefit spending and revenues
    - Income poverty and inequality
    - Mean income across the distribution
    - Gainers and losers across the income distribution

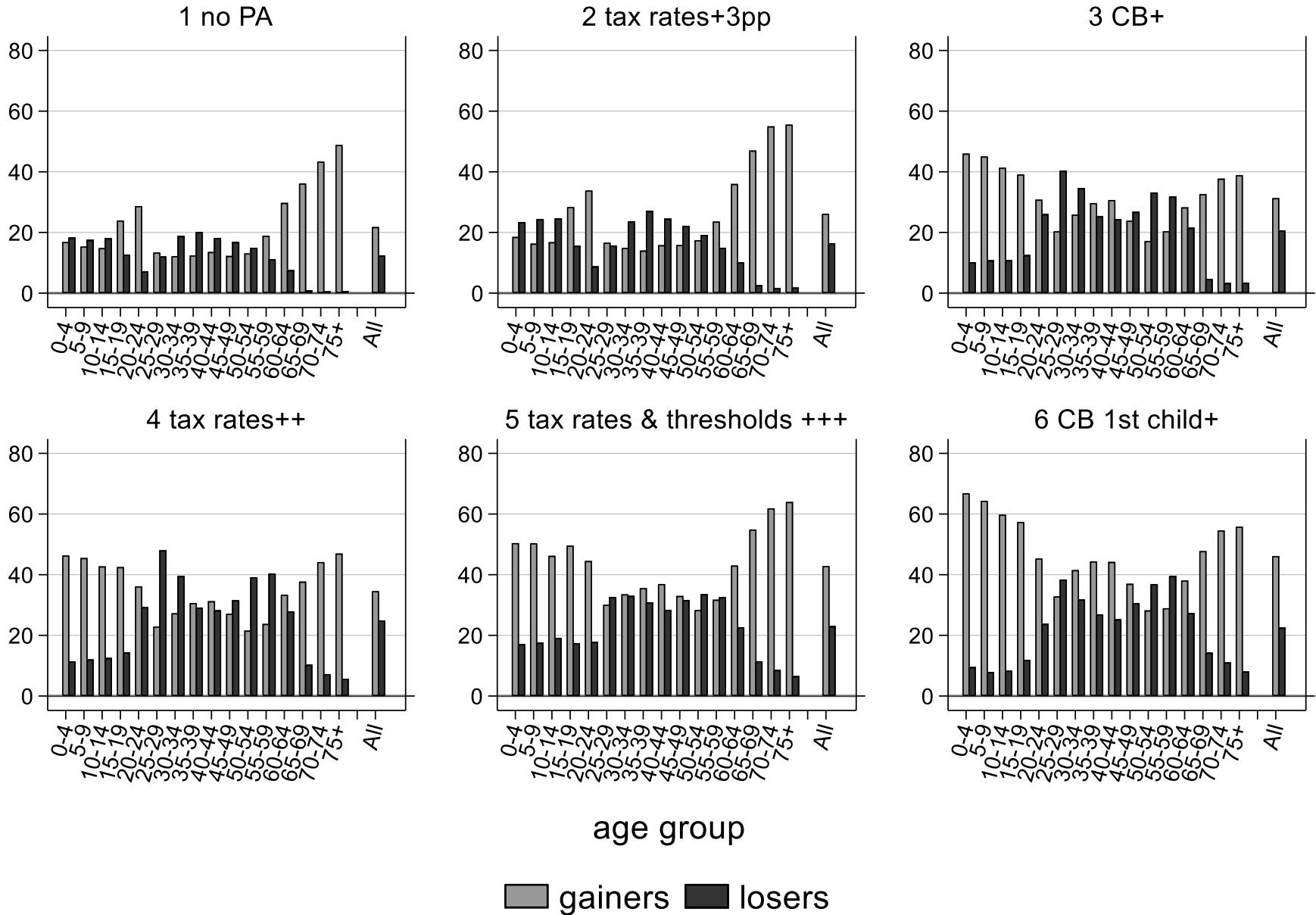# Share of gainers/losers (in %) by decile
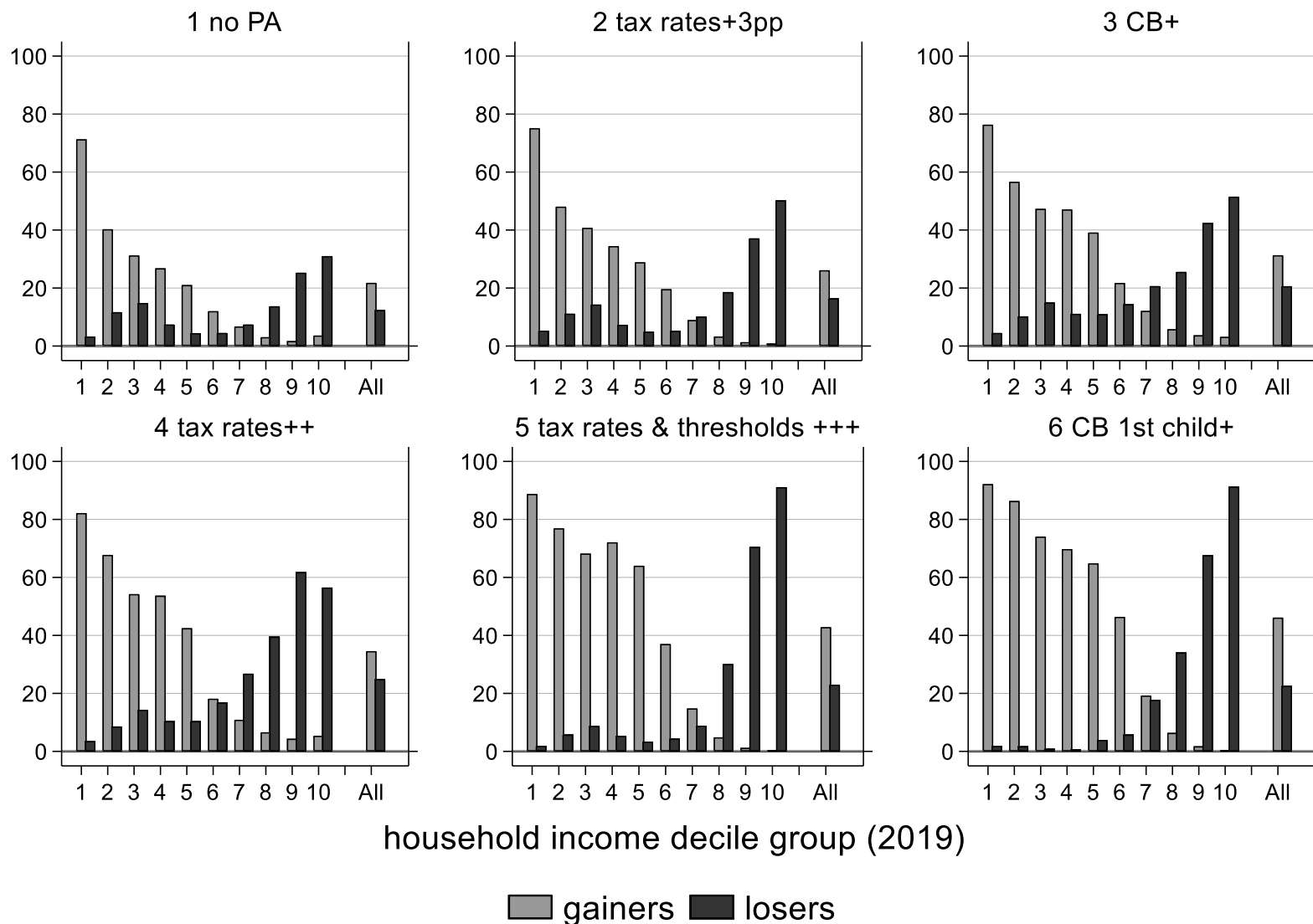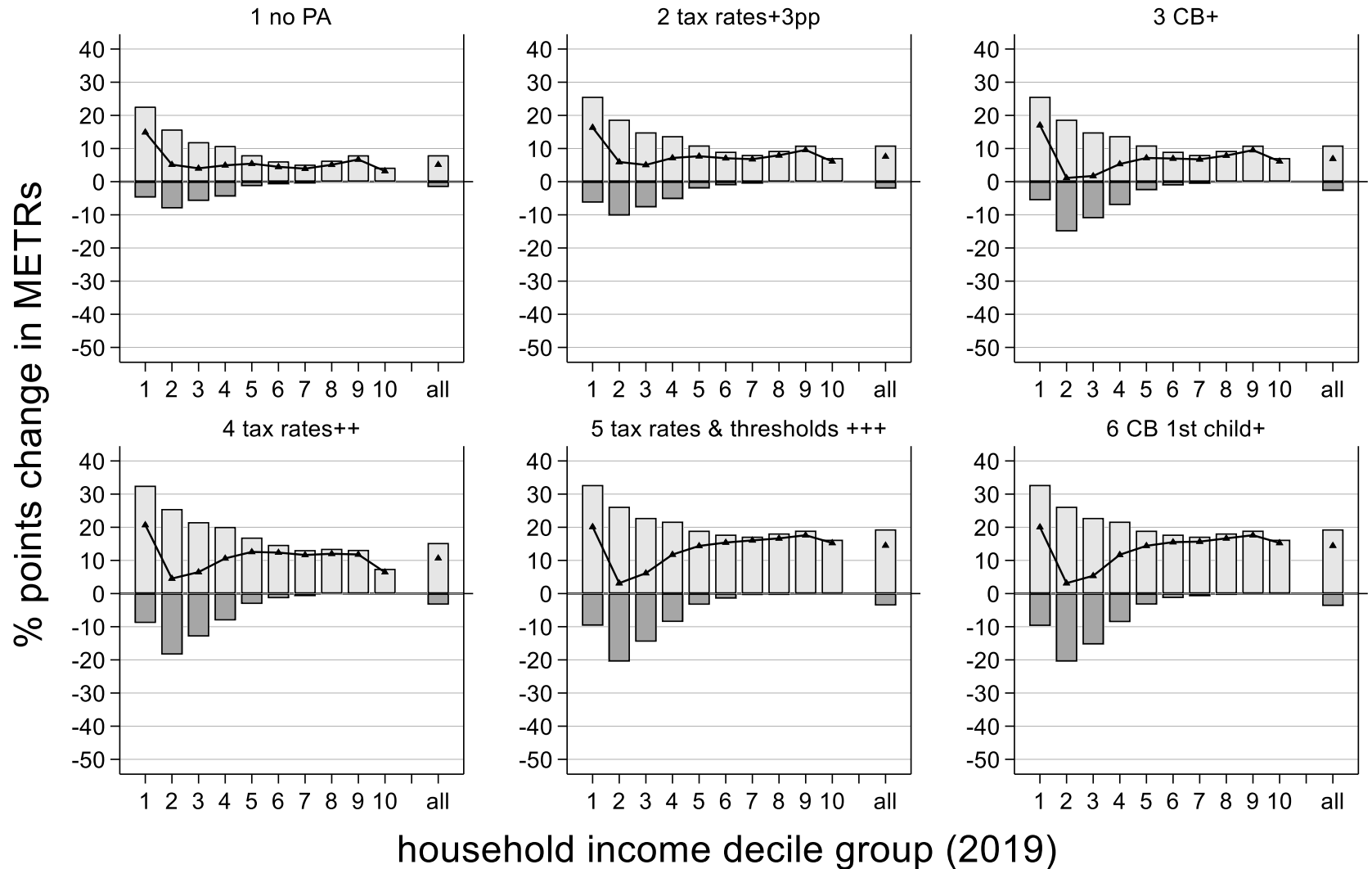

household income decile group (2019)

gainers · losers

Note: individuals with a change in equivalised household net income of 5% or more.
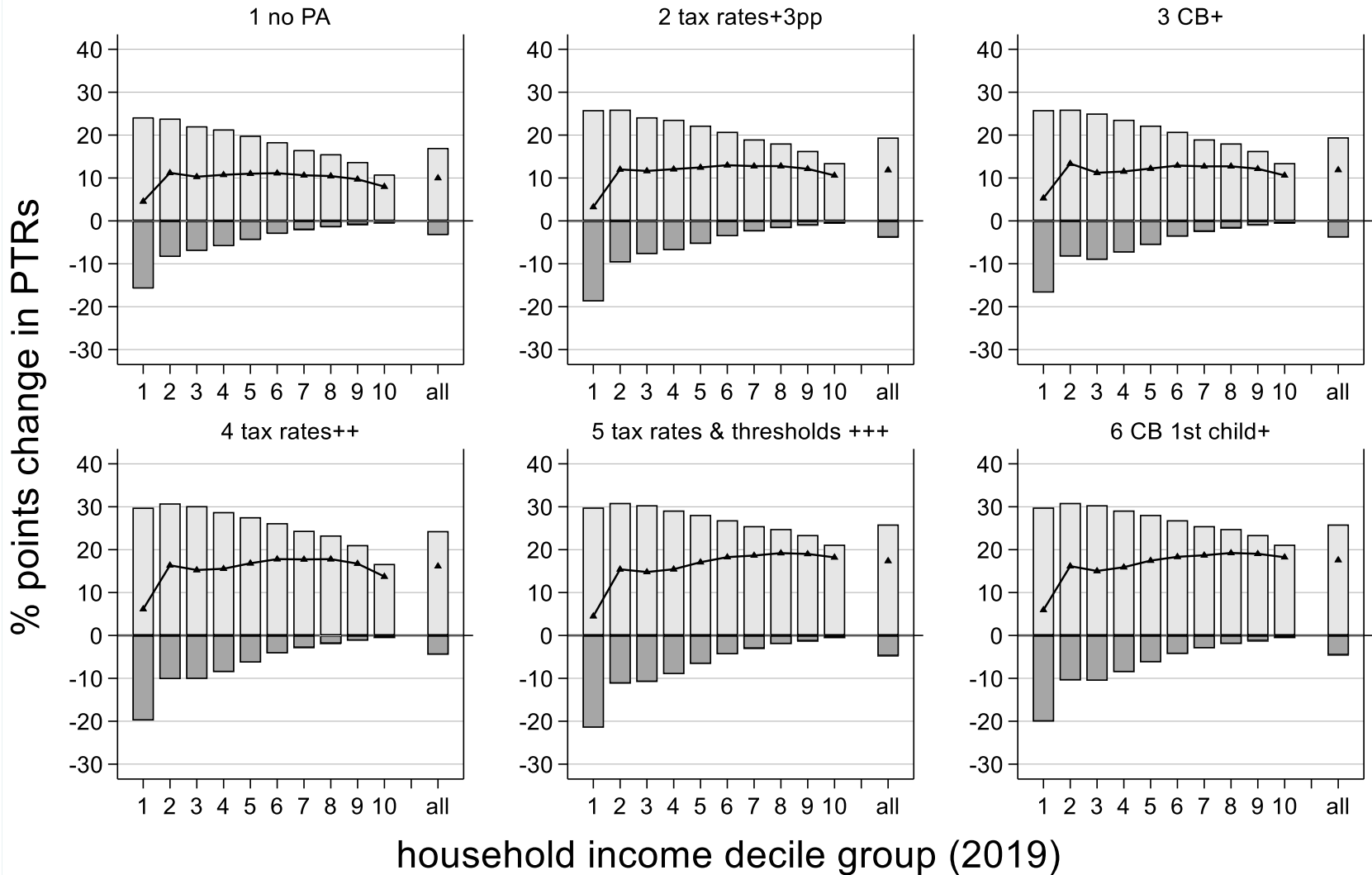
Share of gainers/losers (in %) by age

Change in the mean Marginal Effective Tax Rates by policy and decile

household income decile group (2019)

← total   ■ means-tested benefits   □ tax and contributions

Change in the mean Participation Tax Rates by policy and decile

household income decile group (2019)

total — means-tested benefits — tax and contributions