NEW ECONOMICS FOUNDATION

NOTHING PERSONAL

REPLACING THE PERSONAL TAX ALLOWANCE WITH A WEEKLY NATIONAL ALLOWANCE

HOW WE CAN CHANGE THE TAX SYSTEM TO BE MORE PROGRESSIVE WHILE INCREASING THE BREADTH, DEPTH AND GENEROSITY OF THE UK'S INCOME SAFETY NET

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EXECUTIVE SUMMARY

On 1 April 2019, the government will complete one of the most expensive and regressive public spending projects of the 21st century so far: a decade-long expansion of the personal allowance of income tax. The personal allowance will rise to £12,500, protecting personal incomes from the basic rate of tax – and in some cases the higher rate of tax as well. Her Majesty's Revenues and Customs (HMRC) estimate the scheme to be worth an eye watering £107 billion in forgone tax receipts for the 2018/19 tax year alone: equivalent to 14% of total government income and worth more than the departments for defence, local government and transport combined. This cost is set to rise further in 2019/20 with the increase in the threshold. New NEF modelling also shows that the allowance is worth significantly more for higher income households. In 2019/20, the allowance will be worth £6,500 in reduced tax liabilities for the 10% highest income families, but worth just £600 for the poorest 10%'.

New giveaways to the UK's highest income households in the tax system have coincided with social security reforms that have hit the poorest families hardest. Significant reductions to disposable income for the UK's poorest families have been driven by large-scale cuts such as the working age benefit freeze and the two child limit to payments under working tax credits, housing benefit and universal credit. The flagship transition to universal credit itself is also failing. Its implementation has been incompetent, flawed and harmful. And its design is internally incoherent given its own stated objectives of increasing simplicity, reducing costs and improving work incentives. Yet despite consensus growing over the scale of failings in universal credit and the lack of resources in the social security system as a whole, too little work has been done on how to structurally improve the UK's safety net in a fundamental way.

A weakened and threadbare social security system also represents heightened risk to the economy as a whole. Monetary policy – altering the cost of credit in the economy – is becoming increasingly ineffective as a recession fighting tool. At the same time, the future response from discretionary fiscal policy – actively changing tax and spending – is uncertain given continued ill-judged government commitments to austerity. Social security would normally be a first line of defence during economic downturn, maintaining a minimum level of spending in the economy even if unemployment starts to rise. But, given the lack of prospect for monetary or fiscal interventions, at the next recession there is a danger it may be among the last lines of defence as well. With the risk of a no deal Brexit growing, the need to ensure social security has the strength, breadth and generosity to help the economy navigate the next recession safely is now an urgent priority.

The main contribution of this policy paper is the proposal that government should create a 'Weekly National Allowance' by repurposing resources currently foregone every year through the personal allowance of income tax. We posit that this reform is both implementable on a relatively short-time frame, but nonetheless capable of meaningfully improving the progressivity of the UK's tax and benefit system as a whole. It also has the potential to significantly expand the country's recession fighting toolkit. However, the policy is not intended as a silver bullet to meet all, or even most, of the UK's short and long-term challenges with respect to tax and social security. We therefore present this proposal as one brick in the road to a radically reformed system as a whole.

The specifications of our proposal are as follows:

- Replace the personal allowance of income tax with a weekly payment equal to the value of tax that would otherwise be paid on the full £12,500 of personal allowance. For 2019/20, this payment would be worth £48.08 per week in England, Wales and Northern Ireland, or £2,500 per year. In Scotland, the 19% income tax band introduced in 2018/19 means that the cash payment would be set at £45.68, worth £2,375.15 per year. Eligibility for the

payment would be extended to everyone over the age of 18 with a UK national insurance number. New payments could be administered by HMRC and would be tax free, but they would also score in the means testing of other benefits. The basic rate of income tax (or starter rate in Scotland) would then be applied to the first £1 of most forms of income.

- Restore child benefit to its real terms 2010/11 value (in other words reverse the effect of freezes to child benefit since 2010) and combine this with the new cash payment above to complete the 'Weekly National Allowance'.

New research and modelling presented in this paper has demonstrated that the Weekly National Allowance has the following characteristics:

- **Highly redistributive:** the net distributional effect of the Weekly National Allowance is to take around £8bn currently spent on tax allowances for the 35% highest income families and reallocate this to the remaining 65% of families. The policy would also lift 200,000 families out of poverty, driven largely by a fall in adult poverty of 400,000 people. Inequality would also fall significantly, whether measured in terms of comparing the gap between the richest and poorest households (90:10 or 75:25 ratios), or by a measure of inequality that takes the shape of the entire income distribution into account (for example the gini coefficient).

- **Fiscally neutral**: the total cost of the Weekly National Allowance is more than met by the combined savings from abolishing the personal allowance and from reduced overall costs in means-tested benefits.

- **Improved macroeconomic stabilisation**: The Weekly National Allowance would significantly improve the UK's recession fighting toolkit. Converting the personal allowance into an equivalent, weekly payment alone would represent a 66% increase on existing Jobs Seeker's Allowance or the unemployment element of universal credit that is set to replace it. Evidence shows that people on lower incomes are more likely to spend additional earnings than those on higher incomes. This means a higher proportion of the weekly payment would be spent during a recession than in normal times, leading to an automatic boost to the economy when it is most needed. The Weekly National Allowance would also give government a powerful discretionary tool to boost spending further during a recession by temporarily increasing the value of the weekly payments when required.

We suggest that such a reform could be implemented relatively quickly and easily, within a single parliament if required. Much of the necessary administrative infrastructure is already in place through the existing tax credit and tax remuneration systems administered by HMRC and there is already precedent for largely non-conditional benefit payments from government in the form of child benefit and the state pension. In effect, the Weekly National Allowance will go to everyone earning below £125,000 as a new, non-conditional weekly payment direct into a personal bank account or in the form of a cheque, and as an increase in child benefit. This brief policy paper marks the first in a broader programme of work being conducted at NEF over the coming months and years, which will examine personal tax allowances, social security and public service provision as three closely interrelated schemes. As part of this work we plan to make a number of cross-cutting recommendations for government to evolve and strengthen the UK's social insurance and security systems to meet the challenges of the 21st century. This paper and it's recommendations are therefore not intended as the final word and we hope it instigates further debate

1. THE PERSONAL ALLOWANCE: WELFARE FOR THE RICH AT A TIME OF CUTS FOR THE POOR

1.1 TAX GIVEAWAY TO HIGHER INCOME HOUSEHOLDS

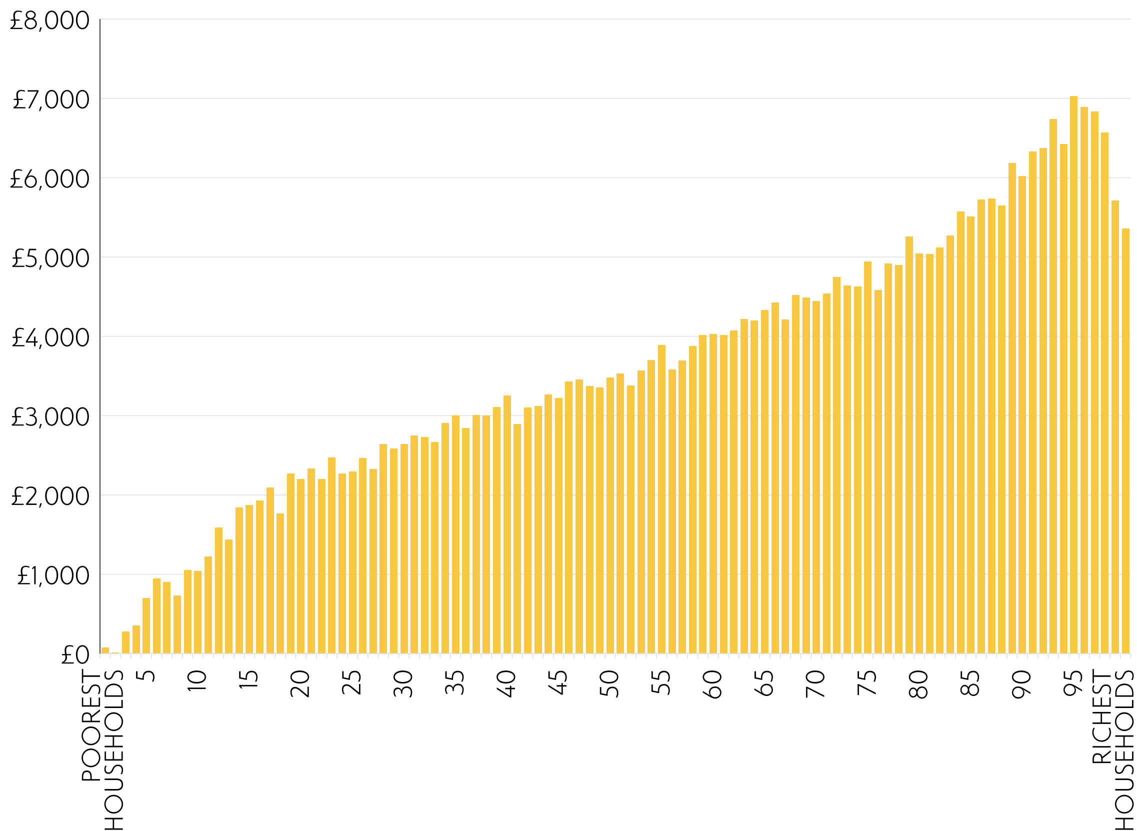
The recent increases in the personal allowance of income tax represent one of the most expensive and regressive public spending projects of the 21st century so far. Her Majesty's Revenues and Customs (HMRC) estimate the scheme to be worth an eye watering £107 billion in forgone tax receipts for the 2018/19 tax year alone[i]: equivalent to 14% of total government income[1] and worth more than the departments for defence, local government and transport combined[2]. The distributional effects of the policy are deeply regressive. In 2019/20, the allowance will be worth £6,500 in reduced tax liabilities for the 10% highest income families, but worth just £600 for the poorest 10% (see figure 1:1 below). This is despite HMRC and the National Audit Office (NAO) classifying the personal allowance as a tax expenditure to"improve the progressivity of tax"[3].

Why is the personal allowance so regressive? The personal allowance is designed to protect an individual's initial income from personal taxation (although earnings from work

FIGURE 1.1

The personal allowance distributes more than £100 billion in foregone tax receipts every year, with the largest gains flowing to the highest income households

Distributional effects of the personal allowance of income tax: Change in disposable family income before housing costs across percentiles for equivalised household income, 2019/20



Source: Authors' analysis using the IPPR tax and benefit model based on data from the ONS and OBR (various) and the 2016/17 Family Resources Survey

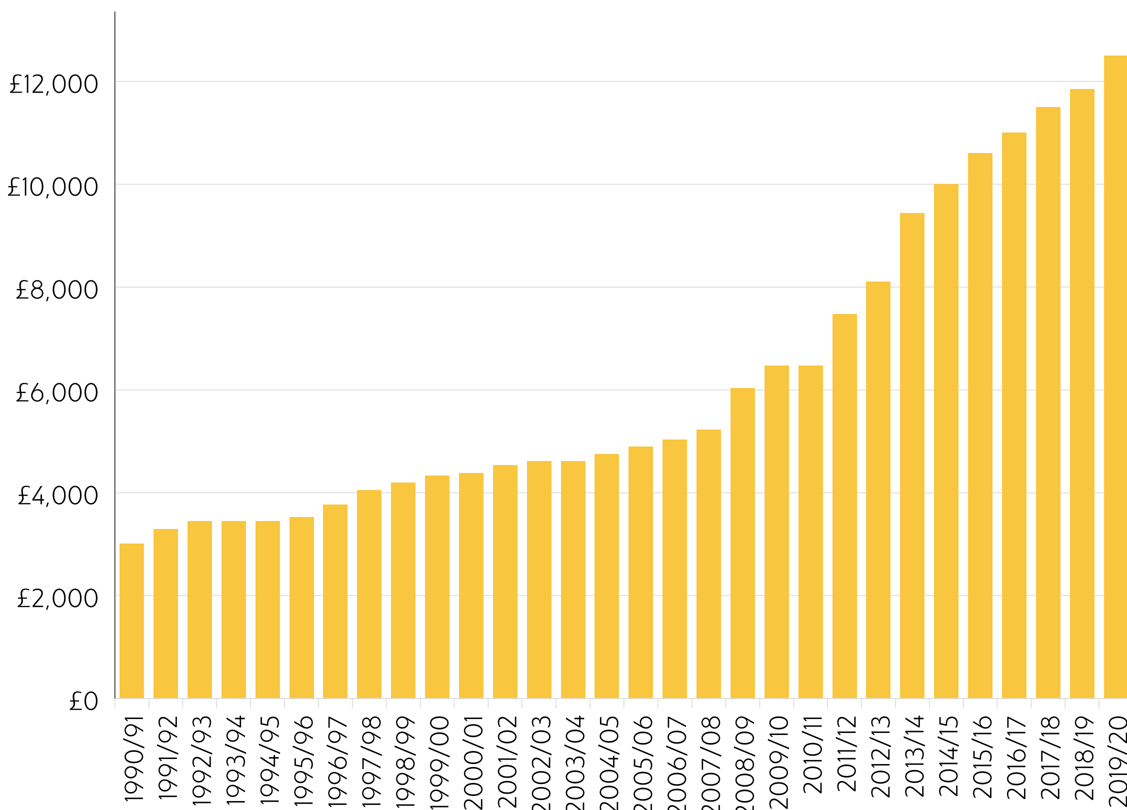
i It should be noted that a small proportion of these costs are recouped in the form of lower means tested benefit payments that would otherwise by higher if the personal allowance of income tax wasn't in place.

below this level can still accrue liabilities under national insurance contributions) and is scheduled to apply to the first £12,500 in income for the 2019/20 financial year. But those families with little or no taxable income, who make up the majority of the UK's poorest households, by definition miss out on the benefits of a higher tax allowance altogether. Meanwhile, families with two or more people receiving a taxable income – which tend to be higher up the income distribution on average – can receive twice the benefit or more. On top of this, the personal allowance is also worth double for individuals with pre-tax incomes above the 'higher rate threshold' – the level beyond which additional income gets taxed at a rate of 40%, and set at £50,000 for 2019/20.[ii] This is because the higher rate threshold is defined as a specified amount above the personal allowance, so the threshold rises pound-for-pound automatically for any increase in the allowance. However, gains for the richest 5% of households are limited by the fact that the personal allowance is gradually withdrawn for personal incomes above £100,000 (see figure 1.1 above).

In recent years the magnitude of these distributional effects has grown. On 1 April 2019, the government will complete almost a decade of accelerated increases in the personal allowance. It's easy to underestimate the scale of change seen over this period. Having taken more than two decades for the threshold to rise by around £3,500 between 1990/91 and 2010/11, it has since risen by more than £6,000 in just nine years, up to a value of £12,500 for the 2019/20 financial year (see figure 1.2).

The distributional effects of these recent increases in the personal allowance largely reflect the regressive outcomes of the policy as a whole. The cash increase in disposable incomes for the richest 20% of households have been 6.5 times higher compared with the

FIGURE 1.2
The personal allowance of income tax has increased rapidly since 2010
Personal allowance of income tax, 1990/91 to 2019/20



Source: HMRC (2018) 'Income Tax personal allowances and reliefs' https://www.gov.uk/government/statistics/income-tax-personal-allowances-and-reliefs

ii In Scotland the higher rate is 41%

poorest 20%. In percentage terms, gains have been highest for the upper to middle portion of the income distribution (see Figure 1.3 below). During the years of coalition government reform, the regressive impacts of increasing the personal allowance were offset to a limited extent by actively holding down or lowering the higher rate threshold. However, since 2015, a higher personal allowance has been accompanied by a raft of other tax measures that have also disproportionately benefitted higher income households. These have included increasing the higher rate threshold to £50,000 in terms of gross income by 2019/20 and increasing the amount of savings income that is tax-free through the 0% savings starter rate and tax free individual savings accounts (ISAs), among other measures.

The personal allowance represents a vast sum of poorly allocated resources: exacerbating rather than reducing UK income inequality; and making attempts to reduce poverty harder to achieve. By the time the government's flagship social security reform is fully rolled out – replacing six major existing social security payments with a single benefit payment[iii] – the personal allowance will cost almost twice as much in foregone tax receipts as the majority of working age benefits combined. This programme of expansive welfare for better off families at a time of significant tightening on transfers to the poorest is an indictment on the priorities of the past three UK governments that have overseen its expansion. A key question for politicians and policy makers going into the 2020s should be: can the funds being spent on the personal allowance be put to better use?

1.2 WELFARE CUTS AND WEAKENED ECONOMIC STABILISERS

Disproportionate giveaways to the UK's highest income households have coincided with social security reforms that have hit the poorest families hardest. The effects of the so-called 'bedroom tax' (reductions in housing benefit for households deemed to have a 'spare bedroom'), the benefit cap and the move from disability living allowance (DLA) to personal independence payments (PIP) have all disproportionately impacted on the UK's lowest income families. In addition to this, two further reforms in particular have significantly reduced living standards. First, since 2016/17, most working age benefits – outside of disability-related payments and carer's allowance – have been subjected to a four-year freeze. This means that payments are no longer uprated with inflation, and have therefore seen their value fall in real terms since 2016. Second, payments for children living in families receiving housing benefit, tax credits and universal credit have been largely limited to the first two children only, leaving families with three or more children significantly worse off. The combined effects of these two reforms alone are expected to reduce disposable incomes for the poorest third of families by well over £300 per year on average by 2020/21, and in some cases by more than £1000.[4]

The separate process of moving most social security claimants to the new system of universal credit has also been fraught with failures. The 2018 progress report from the independent National Audit Office (NAO) was damning.[5] The programme is already five years behind schedule – equal to the entire amount of time that the whole rollout was originally intended to take[6]. Having initially been due for completion in October 2017, only 10% of claimants have been enrolled so far and the Department for Work and Pensions (DWP) now don't expect universal credit to be fully operational before 2023.[7] Despite prioritising the most straightforward claimants at this stage of the rollout[iv], running costs per claimant are already 5% over budget, and overall costs are four times higher than their original target for 2023[8].

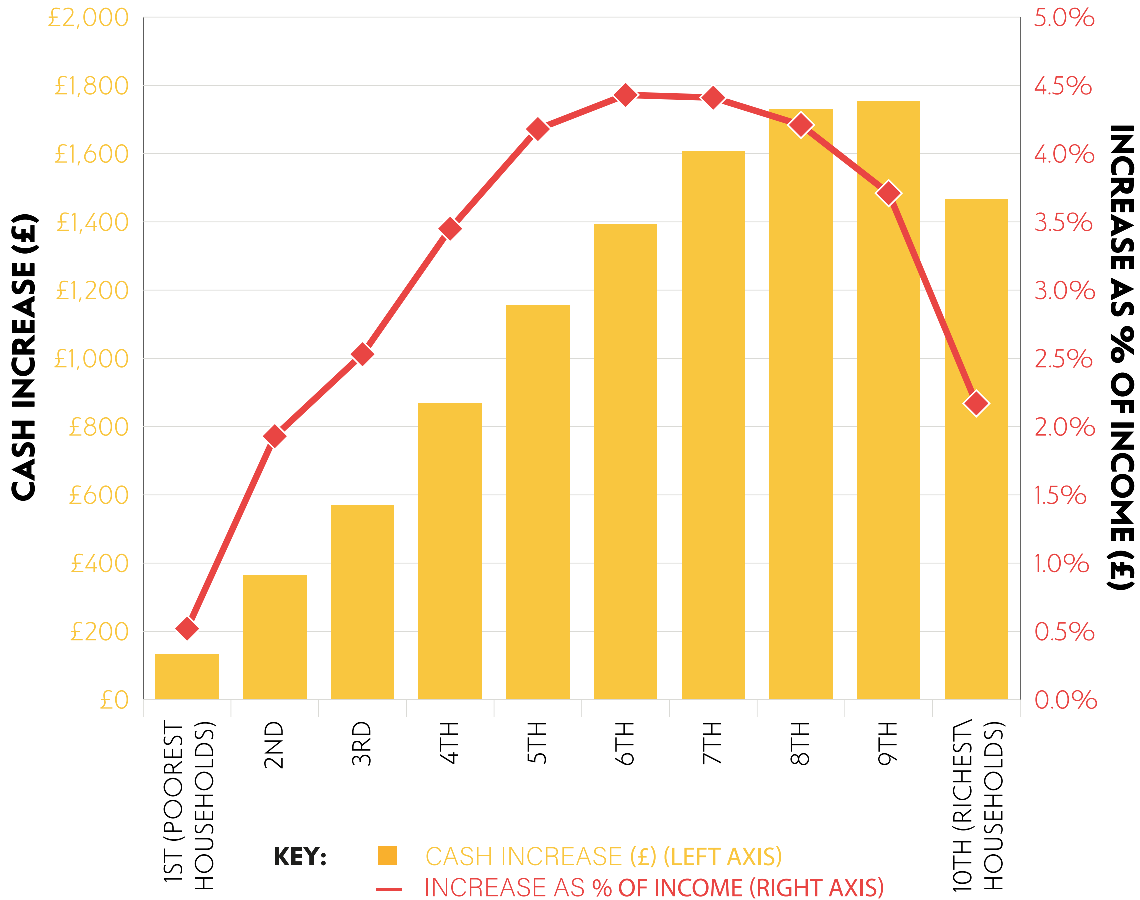
The lived experience for a significant minority of early universal credit claimants has also been unacceptable. A quarter of new claimants in 2017 received their first payment at least four weeks late on average, with one in five of those affected by late claims failing to receive any money at all for almost five months. Even

iii The six payments scheduled to be replaced represent a mixture of in- and out-of-work benefits: job seekers allowance (JSA, out-of-work), employment and support allowance (ESA, out-of-work), income support (out-of-work), housing benefit (in- and out-of-work), working tax credit (in-work) and child tax credit (in-work).
iv Single and couple adult households with no children

FIGURE 1.3

Changes to the personal allowance since 2010 have seen richer households benefit far more than poorer households

Distributional effects of changes to the personal allowance of income tax between 2010/11 and 2019/20: Change in disposable family income before housing costs across deciles for equivalised household income in 2019/20



Source: Authors' analysis using the IPPR tax and benefit model based on data from the ONS and OBR (various) and the 2016/17 Family Resources Survey

NB: The policy effects include increases to the personal allowance in isolation from any discretionary changes to the higher rate threshold. They also include the effects of the new transferable allowance introduced in 2015/16.

those who have received their payments on time have nonetheless had to grapple with an online system undermined by a series of IT failures, as well as the difficulties of moving from regular weekly payments to monthly lump sums. And because universal credit claimants receive their housing element in cash, rather than being paid direct to their landlords – as is the case under existing housing benefit – rent arrears have grown considerably, while private landlords have become increasingly reticent in accepting tenants who are in receipt of the scheme[9]. The effect has been to increase debt and poverty, with foodbank use rising almost three times faster in areas where universal credit has been rolled out, compared to the average elsewhere.[10]

The internal objectives within universal credit, to both reduce costs to government while also improving work incentives, have also proved in immediate contradiction to one another. Attempts in 2015 by the then chancellor, George Osborne, to reduce the public 'deficit'[v] led to cuts in universal credit in excess of £3bn per year by 2021.[11] The most

v The difference between annual government expenditure and income

important changes were a reduction in the so-called 'work allowances' – the amount of money a claimant could earn in work before their benefits started to be withdrawn – and an increase in what is known as the taper rate – the rate at which benefits would be withdrawn from earned income above the work allowance – from 55% to 65%. Since then, the present chancellor Phillip Hammond, has reversed some of these affects, restoring much of the real-terms value of the original work allowance, but only reducing the taper rate a little to 63%. The overall effects of these money-saving cuts was to reduce the financial incentives to increase paid hours of work while on universal credit. For example, under the current taper rate, an increase in pay of £1 per hour for a main earner on minimum wage and from a couple with two children could see net take-home pay increase by as little as 25p, implying an effective marginal tax rate of 75%.[12vi]

A weakened and threadbare safety net also represents heightened risk to the economy as a whole. The first line of defence during recession is the social security system – what economists call the 'automatic stabilisers'. Welfare payments help to soften recessions and accelerate recoveries by maintaining a minimum level of income and spending for families facing unemployment or real wage cuts. Monetary policy – altering the cost of credit for firms and households – would then normally do much of the heavy lifting in terms of catalysing further economy wide recovery. But at present, any cuts to interest rates would quickly come up against what economists call the 'effective lower bound' – a point beyond which further reductions have little or no positive effect on spending in the economy.[13] In such a situation, fiscal policy – active changes to government tax and spending – might normally be expected to take over the job of stimulating economy-wide spending. But given past and present commitments from governments to austerity, the direction of fiscal policy remains uncertain at best.

There is a risk that in the event of a future recession, social security may move from being among the first lines of defence to being among the last. It is within this context that the strength, breadth and generosity of the UK's safety net will be of utmost importance to navigating the next recession safely. And with the risk of a no deal Brexit mounting, the need to ensure social security is up to the task is now urgent.

1.3 EXISTING REFORM AGENDA FOR UK SOCIAL SECURITY

Universal credit may be a failing project, but its opponents are also failing to take the initiative. The majority of resources in the third sector are focused on damage limitation, with charities on the front line largely focused on mitigating immediate and acute harms for the people they work with on a day-to-day basis. While fully understandable, this means fewer organisations are looking to influence the implementation of universal credit in a way that goes beyond minimising harm and incompetence. What little new policy research has been done in this space has largely been limited to trying to get universal credit to work on its own terms. Proposals from the Centre for Social Justice (CSJ),[14] Resolution Foundation,[15] Joseph Rowntree Foundation (JRF)[16] and Child Poverty Action Group (CPAG)[17] (to name a few) have been well thought through and would likely lead to improved outcomes. But for the most part they are limited to reversing existing cuts within universal credit, rather than an ambitious reimagining of the social security system as a whole. While necessary and important, this work therefore cannot be sufficient given the scale of change required to meet the needs of the 21st century.

Unfortunately, what little 'big picture' thinking has been done on social security, has largely been dominated by campaigning and research around just a single idea: universal basic income (UBI). Papers published in recent months by Compass,[18] Institute for Policy Research (IPR),[19] the Institute for Public Policy Research (IPPR),[20] the Fabian Society[21] and the Royal Society for Arts and Manufactures and Commerce (RSA)[22] represent recent examples. Whether this is

vi The highest effective marginal tax rates under the old system of tax credits and JSA were slightly higher than the maximum currently thought possible under UC. But having initially been a point of significant differentiation and improvement on the old system, following the 2015 reforms the differences are now only marginal.

the right or wrong idea for the future (and many of the recent papers have disagreed with respect to this question) what's striking is that comparatively less work has been done on other system-wide alternatives – although work by Compass and the Fabian Society represents notable exceptions. This is a problem for the quality of informed debate in the UK.

More urgently, and in the absence of at least tens of billions being successfully raised from new higher marginal tax rates to fund a UBI that could effectively replace existing welfare, few political actors are talking about how to radically improve the UK's safety net on a budget. The Labour Party, for example, have committed to "stop the roll out of universal credit" but have provided little detail on what should be done next.[23] Similarly, the Scottish National Party (SNP) have committed to radically reducing child poverty in Scotland but have set out precious little detail on how to achieve this despite newly devolved powers set to come into force within the next few years.[24]

In the next chapter we present a new policy proposal as a practical but radical first step to a more effective and progressive tax and social security system. This brief policy paper marks the first in a broader programme of work being conducted at NEF over the coming months and years, which will examine personal tax allowances, social security and public service provision as three closely interrelated schemes. As part of this work we plan to make a number of cross-cutting recommendations for government to evolve and strengthen the UK's social insurance and security systems to meet the challenges of the 21st century.

2. SWAPPING THE PERSONAL ALLOWANCE FOR A 'WEEKLY NATIONAL ALLOWANCE'

2.1 POLICY SPECIFICATIONS

The main contribution of this policy paper is the proposal that government should create a 'Weekly National Allowance'. This reform would repurpose money currently foregone every year through the personal allowance of income tax into a new weekly payment to almost every adult in the country, as well as a restoration of child benefit.[vii] We posit that our reform is both implementable on a relatively short-time frame, but nonetheless capable of meaningfully improving the progressivity of the UK's tax and benefit system as a whole. It also has the potential to significantly increase the country's recession fighting toolkit. However, the policy is not intended as a silver bullet to meet all, or even most, of the UK's short and long-term challenges with respect to tax and social security. We therefore present this proposal as one brick in the road to a radically reformed system as a whole.

The specifications of our proposal are as follows:

- Replace the personal allowance of income tax with a weekly payment equal to the value of tax that would otherwise be paid on the full £12,500 of personal allowance. This payment would be worth £48.08 per week in England, Wales and Northern Ireland, or £2,500 per year, and could be uprated each year by at least the value of inflation just as the current personal allowance is. In Scotland, the 19% income tax band introduced in 2018/19 means that the personal allowance is worth £45.68 per week, or £2,375.15 annually. The weekly payment would administered by HMRC and eligibility for the payment would be extended to everyone over the age of 18 with a UK national insurance number and paid directly into personal bank accounts or in the form of a cheque.[viii] The new payment would be tax free, but it would score in the means testing of other benefits such as universal credit and pension credit. For the purposes of means testing, we score the new weekly payment as earned income on the same basis as untaxed earnings below the personal allowance threshold would have been treated.[25]
- Restore child benefit to its real-terms 2010/11 value (in other words reverse the effect of freezes to child benefit since 2010) and combine this with the new cash payment above to complete the 'Weekly National Allowance'. This equates to an increase in child benefit of £4.20 for the first child and £2.70 for any subsequent children, compared with the level of child benefit otherwise planned in 2019/20. As with all child benefit, these higher payments will not be included in the means testing of other benefits.

2.2 KEY OUTCOMES AND EFFECTS

New research and modelling presented in this paper has demonstrated that the Weekly National Allowance has the following characteristics:

- **Highly redistributive:** the net distributional effect of the Weekly National Allowance is to shift around £8bn currently spent on tax allowances for the 35% highest income families and reallocate this to the remaining 65% of families via the Weekly National Allowance. Individuals and families with low to middle incomes would receive more through new weekly payments than they would lose in higher tax payments. The highest earning households and individuals would pay a little bit more in tax than they receive through the new weekly payments. The policy would also lift 200,000 families out of poverty, driven largely by a fall in adult poverty of 400,000 people. Inequality

vii Our scheme has similarities with recent proposals from both Compass and the Fabian's Society who each recommend ways of putting foregone tax receipts under the personal allowance to alternative and better use.

viii Those earning more than £100,000 already see the personal allowance tapered away at a rate of 50p for every additional £1 of income. Their new cash payment would there also be tapered down at the same rate to mirror the existing value of their personal allowance. This means that those earning more than £125,000 would not receive the new weekly payment at all, since their personal allowance has already effectively been removed in the existing income tax system.

would also fall significantly, whether measured in terms of comparing the gap between the richest and poorest households (90:10 or 75:25 ratios), or by a measure of inequality across the entire income distribution (for example we use the gini coefficient, see Appendix B).

- **Fiscally neutral:** the Weekly National Allowance repurposes the £111.2bn (projected figure for 2019/20 based on NEF modelling using HMRC, OBR and ONS data, see table 2.1 below) already spent annually on the personal allowance of income tax and recycles this money into a new weekly payment made to every adult over the age of 18 at a total cost of £126.8bn, and an increase in child benefit costing £2.1 billion. The cost of means-tested benefits would fall by £20.6 billion since the new weekly payment will boost post tax income for the lowest income families. This means that we estimate the policy as a whole would generate a small surplus. Some of this money should be held back as a contingency against forecasting errors and any remaining surplus should be used either to increase child benefit further or else be invested into universal credit, such as by increasing work allowances or reducing the taper rate.
- **Improved macroeconomic stabilisation:** The Weekly National Allowance would significantly improve the UK's recession fighting toolkit. Converting the personal allowance into an equivalent weekly payment alone would represent a 66% increase on existing job seeker's allowance or the unemployment element of universal credit that is set to replace it – although most people claiming either of these awards will be in receipt of other benefit payments as well. Although this payment would be made to everyone irrespective of the health of the economy, the stabilisation effect would come from the fact that people are more likely to spend more of their income when they have less of it – what economists call the marginal propensity to consume.[26] Because the Weekly National Allowance would be retained by everyone whether in or out of work, a higher proportion of it would be spent during a recession than in normal times, leading to an automatic boost to the economy when it was most needed. The weekly payment would also represent a new and highly effective tool for discretionary fiscal policy as well. Because government would now have the apparatus established to pay new money to almost every adult in the economy, it could choose to boost temporary spending further during a recession by increasing the value of the Weekly National Allowance for a fixed amount of time.
- **Employment effects:** The Weekly National Allowance may lead to higher effective marginal tax rates for those already on universal credit since the basic rate of income tax (or starter rate in Scotland) will now apply on the first pound of earnings after moving into work. This may therefore reduce financial incentives to take a job, particularly if it is low paid, temporary or insecure work. On the other hand, the non-conditional weekly payment will give greater financial security for those prepared to search longer for a job with higher pay and better progression opportunities, while the extra cash for those looking for work will also make supporting services, such as childcare, more affordable. Further work and pilot testing would need to be done to understand how these different effects are likely to play out.

2.3 DISCUSSION OF MODELLING RESULTS

To model the effects of funding and delivering a 'Weekly National Allowance', NEF economists have conducted new analysis using the IPPR tax and benefit microsimulation model (see Text Box 1 above). Our modelling produces scenarios simulated for the 2019/20 financial year, but with universal credit assumed to be fully rolled out. In this sense, the modelling should be seen to represent a snapshot of the possible long-run effects during the 2020s.

Overall, the policy is cost neutral across the financial year. The weekly payment repurposes an estimated £111.2bn already spent annually on the personal allowance of income tax in 2019/20 and recycles this money into a new

weekly payment made to every adult over the age of 18 (at a total cost of £126.8bn) and an increase in child benefit (costing £2.1 billion). Because the new weekly payment is included in the means testing of other benefits, our modelling estimates annual net savings of £20.6bn, largely from universal credit and pension credit (see Table 2.1 for a full breakdown of fiscal results). Overall our modelling implies a surplus of around £2.9 billion pounds before behavioural effects are taken into account. However, in practice the surplus is likely to be even larger since calculations based on either the family resources survey (FRS) or HMRC admin data are known to underestimate the true value of the personal allowance.[27ix] Part of this surplus may need to be planned for as a contingency for any forecasting errors or unexpected behavioural effects leading to reduced revenues. After adjusting for contingencies we suggest that any final surplus generated from the Weekly National Allowance is used to either further increase child benefit or else is invested back into universal credit in the form of higher work allowances or a lower taper rate.

The Weekly National Allowance would be highly redistributive. Overall, the net distributional effect is to shift around £8bn currently spent on tax allowances for the 35% highest income families and reallocate this among the remaining 65% of families (see Figure 4.1 below). After taking into account both the new income received (minus the deductions in means-tested benefits) and higher income tax liabilities, families among the poorest 10% of households on average are estimated to see an increase in disposable income of £1,160 per year or around £20 per week, equal to a 15.8% increase. Among the richest 10% of households, families on average would see their disposable income fall by around £40 week or £1,870 per year, which equates to less than 2% of average disposable incomes in this decile. The fall in disposable income for the highest income families is caused by the higher rate threshold falling by the value of the personal allowance.[x]

MODELLING THE WEEKLY NATIONAL ALLOWANCE

In 2019, NEF became a research partner on the IPPR tax and benefit model.[28] The model uses micro data from the 2016/17 Family Resources Survey (FRS) – a dedicated survey for tax and benefit microsimulation modelling commissioned by DWP – and combines this with outturn and forecast estimates for key economic aggregates (such as interest rates and average earnings) from the Office for National statistics and Office for Budget Responsibility, respectively.[29] The model works by simulating new scenarios for the UK labour market, earned and unearned income and tax and social security. The model estimates the impacts of policy change, including a breakdown of fiscal effects (changes to government expenditure and receipts), distributional impacts across family incomes and the implications for various measures of inequality and poverty. The model is capable of accurately estimating interactions and co-dependencies within different elements of tax and means-tested benefits, but it does not attempt to estimate behavioural effects.

ix The Family Resources Survey is known to marginally underreport household incomes compared with HMRC administrative data. We therefore apply a grossing factor to our results from the IPPR tax and benefit model to make our estimate for the personal allowance consistent with HMRC forecasts. However, even this approach will produce an underestimate for the total value of the personal allowance because HMRC forecasts do not include people in receipt of total income that is below the personal allowance threshold. The estimated cost for the new weekly payment is also likely to represent an upper bound since our model makes the payment to every adult over the age of 18. However, in reality some of these adults may not be eligible for a national insurance number.

x The higher rate threshold is defined as a given amount above the personal allowance. In 2019/20, this value is £37,500. If the personal allowance of £12,500 were to be replaced with an equivalent cash payment from this year, then the higher marginal rate of tax would be applied to gross income above £37,500, rather than £50,000.

TABLE 2.1 THE WEEKLY NATIONAL ALLOWANCE WOULD BE COST NEUTRAL

Breakdown of government costs, receipts and savings associated with the Weekly National Allowance, 2019/20

Expenditure	£/billion
Weekly National Allowance	128.9
of which	
New cash payment*	126.8
Restored child benefit	2.1
Receipts and savings	
Personal allowance of income tax**	111.2
Means-tested benefits***	20.6
Total cost	128.9
Total receipts and savings	131.8
Total cost	-2.9

Source: Authors' analysis using the IPPR tax and benefit model based on data from the ONS and OBR (various) and the 2016/17 Family Resources Survey.

** This estimate should be seen as the upper bound cost and the true cost may be lower in practice. Our modelling assumed that everyone resident in the UK received the weekly payment, but in reality those adults who are unable to acquire a national insurance number would not be eligible.*

*** We apply a grossing factor to our estimate for the value of the personal allowance to improve consistency with HMRC forecasts. However, HMRC estimates do not take into account incomes below the personal allowance threshold, and therefore represent an underestimate of the true value of abolishing the personal allowance of income tax[30]*

**** The bulk of net savings from means-tested benefits are associated with reduced costs in universal credit and pension credit*

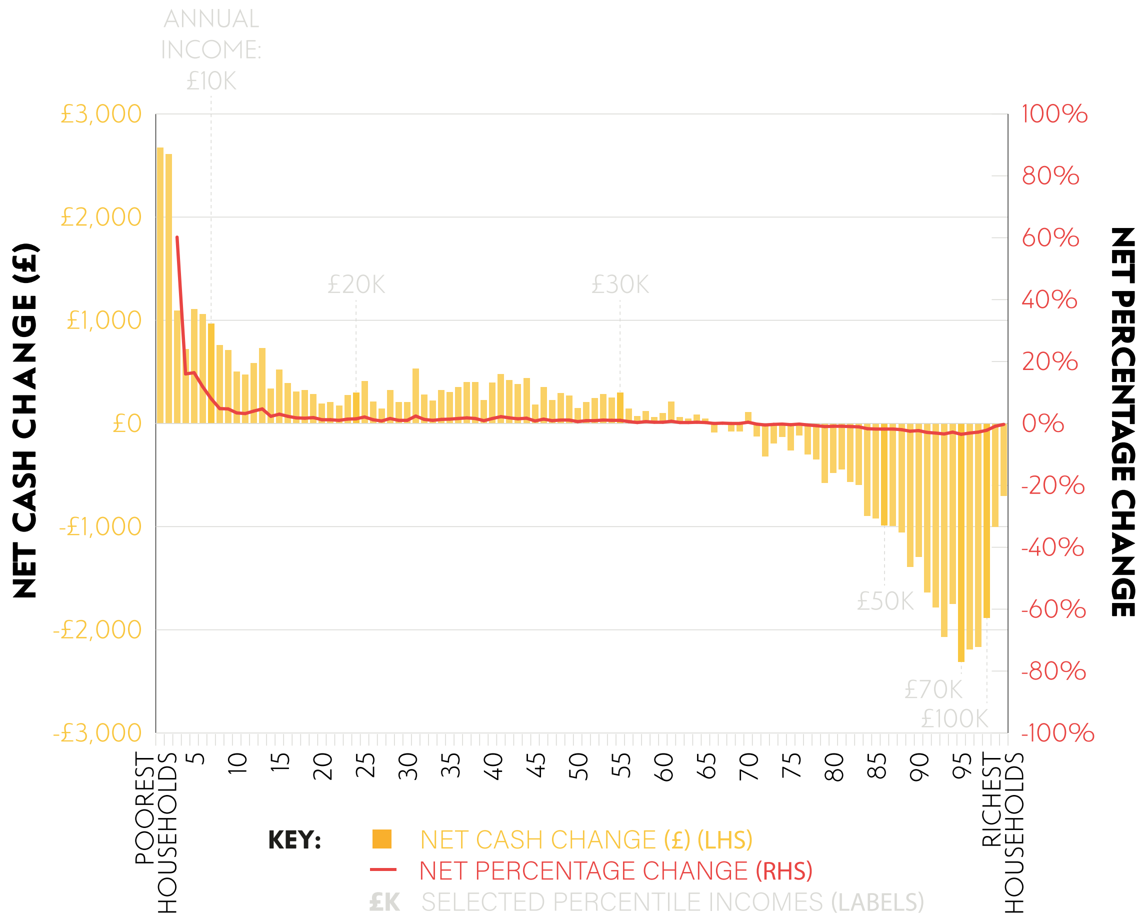
As Figure 2.2 shows, the trough in the distributional impact (from the Weekly National Allowance) around the first quartile (25th percentile) is largely driven by an increase in tax liability on earned income as a result of removing the personal allowance. The net benefits of the Weekly National Allowance then rise gradually up to around the 40th percentile due to the means testing of universal credit and pension credit against the new weekly payment. Nonetheless, all families in this part of the distribution are better off overall. The average impact on percentiles turns largely negative after the 65th percentile due to the higher tax burden above the higher rate threshold as a result of abolishing the personal allowance (see Figure 2.2 below).

Further distributional modelling and sensitivity testing of the policy shows that the average increase in disposable income for the poorest households is comprehensive across all major family types. On average, every major family type among the poorest quartile (25%) sees their income rise – whether a single or couple adult family, with or without children (including families with four or more children), in or out of work, or above or below the pension age (see appendix A for full distributional results). The policy would also lift 200,000 families out of poverty, driven largely by a fall in adult poverty of 400,000 people and inequality would also fall significantly, whether measured in terms of comparing the gap between the richest and poorest households (90:10 or 75:25 ratios), or by a measure of inequality that takes the shape of the entire income distribution into account (gini coefficient, see Appendix B). [xi]

Figure 2.3 presents distributional analysis by individual rather than household, and with

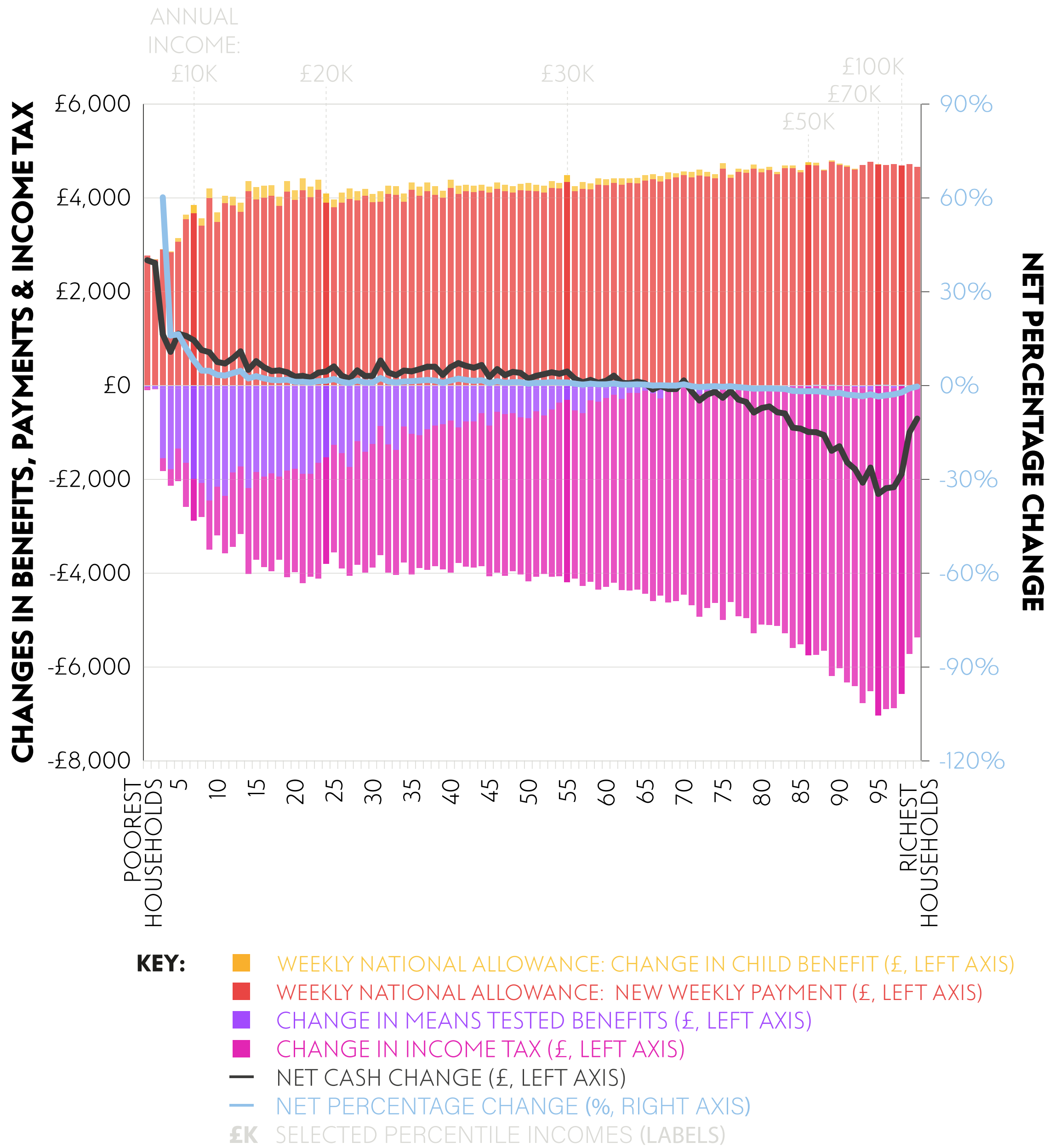
xi Reductions in household poverty are largely driven by increases in disposable income for adult couples without children. Child poverty remains broadly flat. However, further stress testing shows that if some or all of any further surplus generated by the Weekly National Allowance were reinvested into universal credit or further increases in child benefit, then child

FIGURE 2.1
The Weekly National Allowance redistributes around 8bn annually from the 35% highest income households to the remaining 65%, with gains and losses concentrated at the respective extremes of the household income distribution
Distributional effects of the Weekly National Allowance: change in disposable family income before housing costs across percentiles for equivalised household income, 2019/20



Source: Authors' analysis using the IPPR tax and benefit model based on data from the ONS and OBR (various) and the 2016/17 Family Resources Survey
NB: We do not report values for the series for 'net percentage change' below the 3rd percentile because incomes below this level are extremely small or negative

FIGURE 2.2
Under the bonnet, the new cash payment and the uplift and child benefit more than offsets the increase tax for 65% of households
Disaggregated distributional effects of the NEF Weekly National Allowance: Change in disposable family income before housing costs across percentiles for equivalised household income, 2020/21



Source: Authors' analysis using the IPPR tax and benefit model based on data from the ONS and OBR (various) and the 2016/17 Family Resources Survey
NB: We do not report values for the series for 'net percentage change' below the 3rd percentile because incomes below this level are extremely small or negative

respect to the changes in the tax system only. The repurposed personal allowance in the form of a new weekly payment is included in the analysis as a positive income tax, but any changes in family benefits – largely child benefit, universal credit and pension credit – are excluded. Overall, 42% of all adults see an increase in their post-tax income, paid for by a small increase in tax contributions from the 13% highest-income individuals.[xii] While around 45% of all adults would see no net change in their post-tax income.[xiii]

For the highest earning individuals, tax liabilities would rise by a small percentage. Those earning between £37,500 and £50,000 would see their net tax contribution rise gradually. For an individual with an annual income worth £38,000, their net annual tax liability would rise by around £100, or just 0.3% of gross income. However, families with children could have some or all of these losses entirely offset by an increase in child benefit.

Nearly everyone with incomes above £50,000 would see their net tax rise by £2,500, before any increases in child benefit are taken into account.[xiv] However higher earning individuals with partners earning less than 12,500 will also see any hits to household income offset by the gains from their partner under the new system. Those earning over

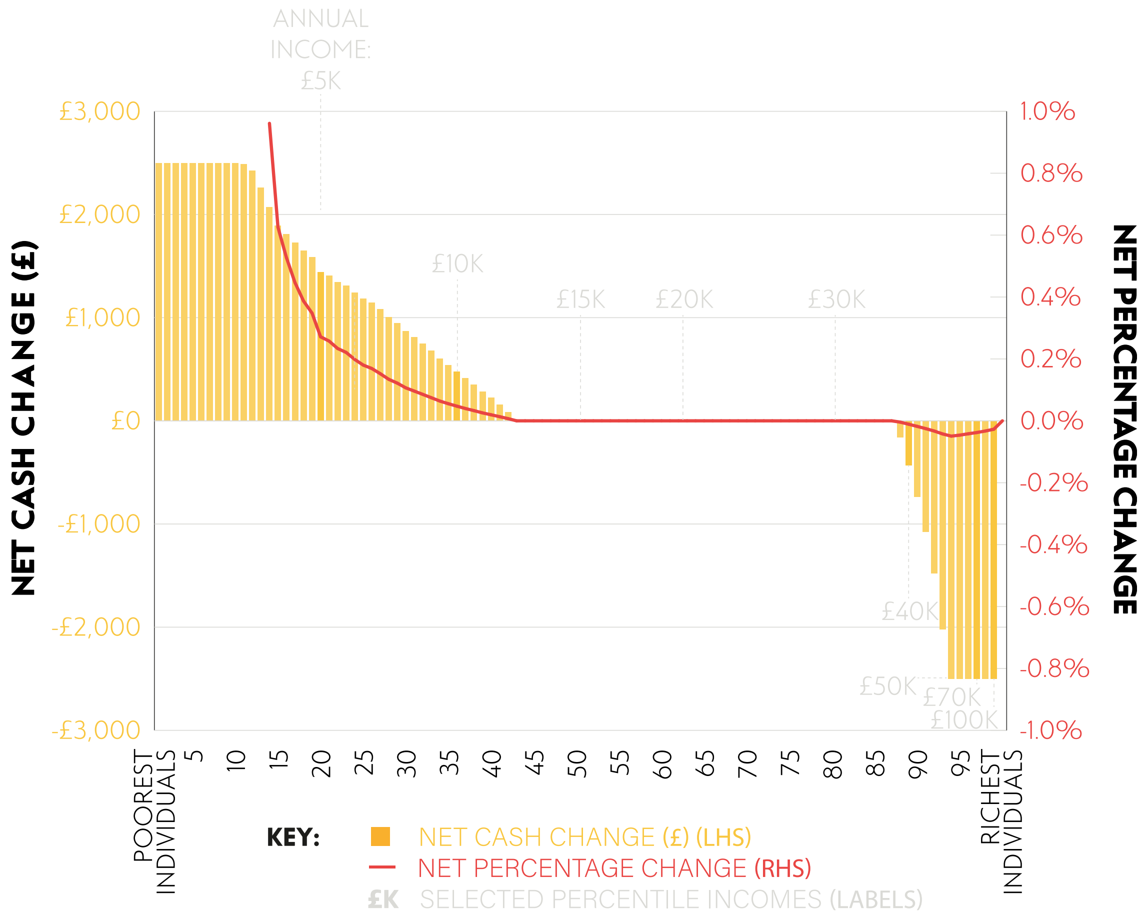
50,000 are also the individuals who have gained the most from the Conservative government's recent increases to the higher rate threshold since 2015. The increases to the higher rate threshold have reduced tax liabilities by £1,500 annually for those earning over £50,000. For this group, our proposal would therefore represent an increase in tax of less than £1,000 (2% or less), compared with what their contribution would have been before the higher rate threshold was increased above inflation.

poverty would also start to fall significantly.
xii The higher rate threshold is set at £37,500 above the personal allowance, so if the personal allowance is removed the higher rate threshold also falls
xiii As Figure 4.2 shows, many of these individuals would however benefit overall once changes to benefits – particularly child benefit – are taken into account
xiv Those earning above £125,000 would see no net change since their personal allowance has already effectively been removed

FIGURE 2.3

Post-tax incomes would either rise or stay the same for 88% of adults, with the 13% highest income adults paying for a redistribution to the poorest 42%

Distributional effects of the Weekly National Allowance within the tax system only (including the new weekly payment but before taking into account family benefits): Change in post-tax income by percentiles for gross income, 2019/20



Source: Author's analysis using the IPPR tax and benefit model based on data from the ONS and OBR (various) and the 2016/17 Family Resources Survey

NB: we do not report values for the series 'net percentage change' below the 14th percentile because incomes below this level are either nil or negligible

ILLUSTRATIVE EXAMPLES

Single unemployed adult in receipt of universal credit and no other earned income
Gross income would increase from a new weekly payment worth £2,500 per year. Universal credit payments would be withdrawn at a rate of 63p for every £1 of the new payment above any work allowance. Depending on whether the adult has a disability, and therefore has a work allowance, ***this household would see their net disposable income rise by between £925 and £2500 per year.***

Couple, two children, one adult with earned annual income of £5,000, in receipt of universal credit
Gross income would increase from a new weekly payment worth £5,000 per year, £2,500 per adult. Universal credit payments would be withdrawn at a rate of 63p for every £1 of the new payment above the work allowance. Child benefit would also increase by £358.8 per year. Depending on whether the universal credit award includes a housing element, ***this household would see their disposable income rise by between £1838.8 and £2408.32 per year.***

Single adult with earned annual income worth £20,000, no universal credit
Liabilities under income tax would rise by £2,500 per year due to the removal of the personal allowance. Gross income would also increase from a new weekly payment worth £2,500 per year. ***Overall, there would be no change in disposable income for this household.***

Couple, one child, primary earner with annual income worth £30,000, second earner with annual income worth £8,000, no universal credit
Liabilities under income tax for the primary earner would rise by £2,500 per year due to the removal of the personal allowance. Gross income would increase from a new weekly payment worth £2,500 per year, per adult. Child benefit would also increase by £218.4 per year. ***Overall, this household would see their disposable income rise by £1,118.4 per year, with £900 of this being paid directly to the second earner.***

Single adult with annual income worth £90,000, no universal credit
Liabilities under income tax would rise by £5000 per year due to the removal of the personal allowance, and the subsequent lowering of the higher rate threshold in terms of gross income. Gross income would also increase from a new weekly payment worth £2,500 per year. ***Overall, this household would see their disposable income fall by £2,500 per year.***

2.4 IMPLEMENTATION AND FURTHER LEARNING

We suggest that the Weekly National Allowance could be implemented relatively easily within a single parliament, and within a smaller number of years if required. Much of the necessary administrative infrastructure already exists through the existing tax credit and tax remuneration systems administered by HMRC, and eligibility could be based on existing national insurance numbers. There is also already a strong precedent for paying broadly non-conditional payments to a large number of people in the form of child benefit and the national state pension. If required, the implementation of a Weekly National Allowance could also easily be staggered over number of years: the personal allowance could be gradually reduced each year until it gets to zero, and with corresponding increases in child benefit and the weekly cash payment.

Further research and learning will be required before a full or staggered roll-out of the Weekly National Allowance is possible. In particular, NEF plans to develop the proposal further by learning from our new peer-led research methods. A particular area of research focus should be around any expected change in employment outcomes.

The Weekly National Allowance would lead to higher effective marginal tax rates for those already on universal credit since the basic rate of income tax will now apply on the first pound of earning above the work allowances. This may therefore reduce incentives to take on temporary insecure work in favour of higher-quality employment, improving longer-term job attachment and wider productivity in the economy as a whole but as a consequence of reducing poor-quality work, growth in the employment rate may also slow. The non-conditional payment would be expected to give more patient support for those seeking employment to wait for a job with more security and better progression opportunities, while the extra cash will also make employment supporting services, such as childcare, more affordable. Further work and pilot testing would need to be done to understand how these different effects are likely to play out. Such research should also look at how reforming conditionality in universal credit might make the most of the benefits of the Weekly National Allowance by valuing longer-term employment prospects and job progression, rather than just incentivising those in receipt of unemployment benefits to accept the first job opportunity they are offered, irrespective of quality.

APPENDIX A

Distributional effects of the Weekly National Allowance: change in disposable family income before housing costs across different characteristics and within quintiles for equivalised household income, 2020/21

TABLE A1
On average, the poorest 20% of households benefit from the reform irrespective of family type
Change in annual disposable income by quintile and family type

	single no children	single with children	couple no children	couple with children	single pensioner	couple pensioner
1st (poorest)	910	350	1370	580	260	1390
2nd	-100	-40	840	170	200	1070
3rd	-50	-230	660	90	200	760
4th	-50	-730	120	-540	120	440
5th (richest)	-1130	-1190	-1270	-1740	-620	-790

Source: Author's analysis using the IPPR tax and benefit model based on data from the ONS and OBR (various) and the 2016/17 Family Resources Survey

TABLE A2
On average, the poorest 20% of households benefit from the reform irrespective of the number of children in a family
Change in annual disposable income by quintile and number of children

	none	1	2	3	4 or more
1st (poorest)	980	180	310	660	1420
2nd	480	170	130	130	-120
3rd	410	200	30	-270	-530
4th	180	-190	-710	-1140	-1930
5th (richest)	-1100	-1820	-1730	-1350	-360

Source: Author's analysis using the IPPR tax and benefit model based on data from the ONS and OBR (various) and the 2016/17 Family Resources Survey[iv]

TABLE A3
Outside of the 40% highest income families, all workless households are better off on average
Change in annual disposable income by quintile and number of children

	not working	working
1st (poorest)	840	740
2nd	390	250
3rd	360	200
4th	280	-210
5th (richest)	-590	-1400

Source: Author's analysis using the IPPR tax and benefit model based on data from the ONS and OBR (various) and the 2016/17 Family Resources Survey

APPENDIX B

Distributional effects of the Weekly National Allowance: change in poverty and inequality across a number of metrics and definitions, 2020/21

TABLE B1
Adult poverty falls significantly but child poverty remains largely unchanged
Change in poverty (various definitions) following full implementation of the Weekly National Allowance, 2020/21

	Poverty threshold recalculated	Poverty threshold held constant
Number of households:		
Below 60% median BHC	-200000	-300000
Below 60% median AHC	-200000	-300000
Below 50% median BHC	-100000	-200000
Number of adults:		
Below 60% median BHC	-400000	-600000
Below 60% median AHC	-400000	-600000
Below 50% median BHC	-300000	-400000
Number of children:		
Below 60% median BHC	-	-
Below 60% median AHC	-	-
Below 50% median BHC	-	-100000

Source: Author's analysis using the IPPR tax and benefit model based on data from the ONS and OBR (various) and the 2016/17 Family Resources Survey

TABLE B2
Inequality falls across three different metrics
Change in inequality (various definitions) following full implementation of the Weekly National Allowance, 2020/21

Inequality measures	
Gini coefficient	-0.00946
90:10 ratio	-0.21292
75:25 ratio	-0.0385

Source: Author's analysis using the IPPR tax and benefit model based on data from the ONS and OBR (various) and the 2016/17 Family Resources Survey (Department for Work and Pensions [DWP] (2017b) 'Family Resources Survey: Financial year 2016/17'. https://www.gov.uk/government/statistics/family-resources-survey-financial-year-2016/17)

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