HM TREASURY DWP Department for Work and Pensions HM Revenue & Customs

Budget 2012 policy costings

March 2012

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1 Introduction

1.1 This document sets out the assumptions and methodologies underlying costings for tax and Annually Managed Expenditure (AME) policy decisions announced since Autumn Statement 2011, where those policies have a greater than negligible impact on the public finances. This continues the practice established at June Budget 2010 and the principles outlined in '*Tax policy making: a new approach*', published alongside June Budget 2010. This publication is part of the Government's wider commitment to increased transparency.

1.2 The costing for the change from a 50 per cent to a 45 per cent additional rate of income tax can be found in HMRC's additional rate evaluation document, published alongside Budget 2012. This sets out considerable detail on the additional rate, including estimates of forestalling, other behavioural responses and the steady state yield.

1.3 Chapter 2 presents detailed information on the key data and assumptions underpinning the costing of policies in Budget 2012. Each note sets out a description of the measure, the base, the methodology for the costing (including relevant adjustments for behavioural responses) and highlights any areas of additional uncertainty, beyond those inherent in the OBR's forecast. All costings are presented on a National Accounts basis. In the summer, the government and OBR intend to jointly publish a briefing paper explaining in more detail our approach to policy costings and the process for scrutiny and certification.

1.4 Costings for AME measures are only shown to 2014-15, the end of the current spending review period. In future years the costs are contained in the overall spending envelope for Total Managed Expenditure (TME), so do not have a direct effect on borrowing.

1.5 Annex A sets out the indexation assumptions included in the public finances forecast baseline, including all pre-announcements. Annex B, by the OBR, sets out the approach the OBR has taken to scrutiny and certification of the costings, and highlights areas of particular uncertainty.

2 Policy costings

The following policy decisions are included in this chapter:

- Personal allowance increase
- Child Benefit threshold and taper
- Main rate of corporation tax reduction
- Bank Levy increase
- Oil and gas decommissioning certainty
- North Sea oil and gas: securing new fields
- Changes to Controlled Foreign Companies regime
- Research and Development Tax Credits: above the line
- Animation and video games tax reliefs
- Enterprise Management Incentive
- Cap on unlimited tax relief
- Residential property: Stamp Duty Land Tax enveloping
- Stamp Duty Land Tax: additional band for properties above £2m
- Capital allowances: business cars
- Freeze Vehicle Excise Duty for Heavy Goods Vehicles in 2012-13
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- Loan relationship avoidance: debt buyback

- Office for Tax Simplification: abolition of reliefs
- Capital allowances: anti-avoidance
- Income tax, inheritance tax and capital gains tax: reliefs & avoidance
- Enhanced capital allowances: enterprise zones in Scotland, Yorkshire and Humber, London and Wales
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- General insurance: claims equalisation reserves
- Bank Levy amendments
- Scope of the supplementary charge on North Sea oil and gas profits
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- Capital allowances: Feed-in Tariffs and Renewable Heat Incentive
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- Local Housing Allowance: baseline for uprating
- Mobility component of personal independence payments for those in residential care
- Changes to the housing benefit social sector size criteria
- Changes to welfare and tax credits
- Public Works Loan Board certainty rate
- Paying down housing debt
- Tax increment financing

Personal allowance increase

Measure description

This measure increases the personal allowance (PA) by £1,100, from £8,105 in 2012-13 to £9,205 in 2013-14.

The basic rate limit (BRL) will be decreased by £2,125, from £34,370 in 2012-13 to £32,245 in 2013-14.

The higher rate threshold (HRT), which equals the sum of the PA and the BRL, will fall by £1,025, from £42,475 in 2012-13 to £41,450 in 2013-14. The national insurance contributions (NICs) upper earnings and profits limits (UEL/UPL) will remain aligned with the HRT, and so fall by equivalent annual amounts.

Given the OBR forecast for RPI inflation, this implies an £850 increase in the PA, a £2,125 reduction in the BRL, and a £1,275 reduction in the HRT in 2013-14, relative to their expected levels taking account of indexation and pre-announced policy measures.

The tax base

The tax base is estimated using two data sources:

- for income tax; data on taxable incomes is taken from the Survey of Personal Incomes (SPI), comprising a sample around 600,000 tax records, weighted to be representative of all taxpayers. The latest available data is for the tax year 2009-10; and,
- for national insurance; data on incomes subject to NICs are estimated using the Annual Survey of Hours and Earnings (ASHE), calibrated to NICs receipts outturns.

The income tax base, including taxpayer numbers and incomes, is grown over the forecast period in line with the relevant OBR forecast determinants. The NICs base is also grown in line with relevant OBR forecast determinants.

Static costing

The static Exchequer impact is calculated by applying the pre- and post-measure tax regimes to the tax base described above. This results in the following static costing:

Static Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	0	-3,280	-3,420	-3,480	-3,550

Post-behavioural costing

A behavioural adjustment is made to account for individuals adjusting their taxable incomes in response to changes to marginal tax rates. This can arise through changes in work effort, increased tax planning, avoidance or mitigation.

Behavioural effects are estimated using Taxable Income Elasticities (TIEs), which show how individuals' taxable incomes change in response to changes in marginal tax rates. These elasticities are derived from a range of evidence including academic studies; although precise results vary, there is a consensus that TIEs are greater for those on high incomes.

The TIE used in this costing is 0.03, to capture the response of those affected by the reduction in the HRT. An adjustment for those in the personal allowance taper region has been considered, but is judged to have a negligible impact on this costing.

The costing also allows for impact of the measure on the tax incentive to incorporate.

Post-behavioural Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	0	-3,320	-3,450	-3,510	-3,580

Areas of uncertainty

The main uncertainties in this costing relate to the projection of SPI survey data from 2009-10, which in particular affects the number of baseline taxpayers who will benefit from the measure.

Child Benefit threshold and taper

Measure description

A new income tax charge will apply to those taxpayers affected by this measure to reduce or remove the financial benefit of receiving Child Benefit. For taxpayers with income between £50,000 and £60,000, the amount of the charge will be a proportion of the Child Benefit received. For taxpayers with income above £60,000, the amount of the charge will equal the amount of Child Benefit received. The amount of Child Benefit payable will be unaffected by the new tax charge.

The cost base

The cost base for this measure is estimated using the Inter-Governmental Tax and Benefit Model (IGOTM). This is a model of individual households and their incomes, taxes and benefits, based on 2009-10 data from the Family Resources Survey. It is used for this costing because it combines estimates of the tax status of individuals with information on whether Child Benefit is being received by the household.

Static costing

The static Exchequer impact is calculated by applying the pre- and post-reform Child Benefit systems to the base described above.

Static Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	-145	-480	-390	-	-

Post-behavioural costing

The behavioural adjustment made in this costing is smaller than that for the previously announced policy. The new policy will affect fewer individuals and the introduction of a taper reduces distortions and the incentive to reduce taxable incomes. Individuals in the taper range will still face higher marginal deduction rates, for which an adjustment has been made. There is some evidence that these responses could be stronger among the self-employed.

These effects are captured through taxable income elasticities (TIEs) which generally show how taxable incomes respond to changes in marginal tax rates. These elasticities are derived from a range of academic studies; although precise results vary, there is a clear trend that TIEs are much higher for those on high incomes; the TIEs used in costings range from 0.03 to 0.45. A TIE of 0.05 has been applied to individuals' affected by the taper. A further adjustment is made for non-compliance.

Post-behavioural Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	-185	-690	-630	-	-

Areas of uncertainty

Areas of uncertainty within the costing include sampling error as a result of using survey data and the size of behavioural responses.

Main rate of corporation tax reduction

Measure description

This measure reduces the main rate of corporation tax (CT) by one per cent from April 2012. This is in addition to the rate reductions announced in June Budget 2010 and Budget 2011. As a result of all these measures, the main rate of CT will be reduced to 24 per cent in 2012-13, 23 per cent in 2013-14 and 22 per cent from 2014-15 onwards.

The tax base

Estimates of the tax base for the main rate of corporation tax are taken directly from the onshore CT revenue forecast of quarterly instalment payments by non-life assurance companies. This forecast is based on CT data for 2009-10, calibrated to an estimate of 2011-12 accruals based on the latest tax receipts. This is then projected in line with relevant determinants from the OBR's economic forecast.

The resulting estimate of net taxable profits charged at the main rate (and the main rate reduced by marginal relief) in 2012-13 is around £90 billion.

Static costing

The static Exchequer impact is calculated by applying the pre- and post-measure tax regimes to the tax base described above. This results in the following static costing:

Static Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	-490	-900	-1,010	-1,065	-1,110

Post-behavioural costing

The costing includes a behavioural response to account for changes in the incentives for multinational companies to shift profits in and out of the UK. A reduction in the CT rate makes the UK more attractive, relative to other locations, as a destination to locate profits.

The proportion of profits in the tax base that are mobile has been estimated at around 40 per cent, based on data from corporation tax returns. Within this data, the sectors where profits are known to be most mobile are examined and the profit flows for these sectors that are most likely to be shifted are identified. An elasticity of -2 has been applied to these mobile profits; a further one percentage point decrease in the corporation tax rate each year results in a two per cent increase in the size of the mobile profit base. The elasticity used is a central assumption, informed by multiple academic studies.

Post-behavioural Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	-405	-730	-820	-880	-920

Areas of uncertainty

The main uncertainties in this costing surround the CT revenue forecast on which it is based, and the behavioural effects included.

Bank Levy increase

Measure description

The Bank Levy was introduced with effect from 1 January 2011. This measure increases the effective full rate of the Bank Levy from 1 January 2013 onwards from 0.088 per cent to 0.105 per cent. The full rates are shown in the table below.

Bank Levy rate (%)

	2012-13	2013-14	2014-15	2015-16	2016-17
Bank Levy rate	0.088%	0.105%	0.105%	0.105%	0.105%

The tax base

The tax base is estimated from the latest receipts data collected by HMRC from those banks liable to pay the Bank Levy. Receipts data for the year to date are used to estimate Bank Levy liabilities for 2011-12, as well as the underlying total balance sheet size and chargeable equity and liabilities. An estimate of banks' balance sheets, chargeable equity and liabilities is arrived at across the forecast period (the estimated tax base) from these 2011-12 estimates using assumptions about future underlying balance sheet growth as well as behavioural impacts (as assumed for the introduction of the Bank Levy and updated according to more recent research). HMRC estimate that this tax base is expected to grow modestly over the duration of the forecast period.

Static costing

The static costing is calculated by applying the change in rate to the tax base described above. Most banks are likely to start paying the extra tax arising from the additional rate as part of their July 2013 quarterly instalment payment.

Static Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	0	+410	+450	+450	+450

Post-behavioural costing

The costing assumes that behavioural changes as a consequence of the increase in the rate for 2011 and beyond are proportionate to those assumed for the introduction of the Levy. The overall behavioural assumption is in line with that set out in the June Budget 2010.

Post-behavioural Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	0	+410	+445	+445	+445

Areas of uncertainty

The main uncertainties in this costing surround the Bank Levy tax revenue forecast on which it is based, and the behavioural effects included.

Oil and gas decommissioning certainty

Measure description

This measure will enable the Government to sign contracts with companies operating in the UK and UK Continental Shelf (UKCS), to provide assurance on the tax relief they will receive when decommissioning assets. The Government will consult further on the precise form and details of such contracts in the coming months.

The tax base

The tax base for the measure is the increase in investment and production arising from increased incremental activity and improved market efficiency in the UKCS, leading to asset trades, stimulated by certainty over the tax treatment of decommissioning costs. The size of this change in investment and production is estimated using HMRC modelling and the relevant determinants from the OBR's economic forecast. These estimates are consistent with consultation work to date.

Costing

The Exchequer impact is calculated by applying the oil and gas tax regime to the tax base described above.

Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	-115	+245	+385	+340	+290

Areas of uncertainty

The main uncertainties in this costing are the size of the increase in investment and production undertaken by oil and gas companies in response to the measure, including commercial constraints, and future oil and gas prices.

North Sea oil and gas: securing new fields

Measure description

This measure increases the total amount of small field allowance from £75 million to £150 million and increases the size of the field qualifying for the maximum allowance to 6.25 million tonnes (roughly equivalent to 45 million barrels of oil equivalent (boe)), tapering to £0 at 7 million tonnes (roughly equivalent to 50 million boe). It also introduces a £3 billion field allowance for West of Shetland fields that meet certain depth and reserve –size criteria.

The tax base

The tax base comprises the profits that would be eligible for the supplementary charge if no field allowances were available, including profits arising from additional investment. The analysis has been done using data from companies on their current and planned activity, broken down by individual fields. Estimates of oil and gas production, capital expenditure, operating expenditure, and decommissioning costs provided by companies have been used to calculate the expected profits from fields qualifying for the allowance. Oil and gas prices have been taken from the OBR's economic forecast.

Static costing

The static costing is calculated by applying the relevant rates of supplementary charge and ring fence expenditure supplement to the tax base described above.

Static Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	0	-5	-10	-20	-65

Post-behavioural costing

An adjustment has been made to account for the measure increasing the probability that relevant oil and gas fields will be developed, as these fields will be more profitable after the reform. This initially increases the Exchequer cost of the measure, due to extra field allowance and capital allowances; in subsequent years, the additional production and profits arising from this extra investment may increase the Exchequer yield.

Post-behavioural Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	-55	-100	+55	+20	+20

Areas of uncertainty

The main uncertainties in this costing result from incomplete information about the oil fields affected by the measure, the behavioural responses of companies, and future oil and gas prices.

Changes to Controlled Foreign Companies regime

Measure description

This measure introduces a modernised Controlled Foreign Company (CFC) regime that better reflects the way that businesses operate in a global economy whilst maintaining adequate protection of the UK tax base and reducing compliance burdens where possible. The measure was announced at Budget 2011 and the costings document from that year provides details of the major elements of the new regime. This note describes changes to the detailed policy design since Budget 2011, which are:

- the introduction of a Gateway which will make it straightforward for groups to establish whether or not their foreign subsidiaries are outside the scope of the new CFC regime;
- the introduction of a full exemption in two circumstances for profits to which the finance company rules apply;
- a targeted restriction that excludes profits from partial or full exemption where overseas external debt is replaced with UK debt;
- a broader approach than provided by the current rules to the amount of reinsurance that UK companies can locate overseas and exemption of UK captive insurance companies operating in the EU; and,
- the new regime will now have effect for CFCs with accounting periods beginning on or after 1 January 2013.

The tax base

A significant amount of analytical work has been undertaken since Budget 2011 including an HMRC survey of CFCs owned by UK headed groups. This survey provides underlying data for a number of aspects of the costing including the size of the tax base from CFC charges and the likely impact on the UK CT base from the changes to various aspects of the current rules.

Costing

The total cost of CFC reform is -£910 million in 2018-2019. The costs for each of the elements of CFC reform are, in 2018-19:

- The overall Exchequer impact of the finance company rules builds to -£325 million;
- The Exchequer impact of the rules for insurance builds to -£365 million;
- The Exchequer impact of the rules for captive insurers builds to -£110 million; and,
- Modernisation of the CFC rules for IP will have an overall Exchequer impact of -£110 million.

The Exchequer impact is the difference between the costing for CFC reform at Budget 2012 compared to that costed at Budget 2011. The costing reflects both changes to the detailed policy design as well as to modelling and data. As there is no precise way to separate these impacts they are presented together.

Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	+210	+365	+320	+150	+35

Areas of uncertainty

The costings are dependent on the likely behavioural response of UK groups.

Research and Development Tax Credits: above the line

Measure description

From 1 April 2013, the Government will introduce an "Above the Line" (ATL) credit for research and development, with a minimum rate of 9.1 per cent before tax. Loss making companies will be able to claim a payable credit. The Government will be consulting on the detailed design of the credit shortly after Budget. Final rates including for the payable credit will be decided following consultation.

The tax base

Details from claims for research and development expenditure are captured on CT600 returns, including detail on the type of claim. The relevant tax rates are applied to qualifying expenditure in order to calculate the cost of the relief. Future research and development expenditure is grown in line with the relevant OBR determinants.

Static costing

The static Exchequer impact is calculated by applying the pre- and post-measure tax regimes to the tax base described above. The static cost also includes loss-making companies who are newly eligible for the payable credit.

Static Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	0	-5	-200	-	-

Post-behavioural costing

It is expected that additional research and development investment will be undertaken as a result of this measure. This increases the tax relief claimed by up to £10 million per annum.

Post-behavioural Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	0	+5	-205	-	-

Areas of uncertainty

In addition to the uncertainties around the OBR's economic forecast, there is some uncertainty relating to the tax base as not all claims are captured by CT600 returns.

The final design of the scheme is subject to a consultation to be undertaken after Budget 2012.

Animation and video games tax reliefs

Measure description

These measures provide tax relief for expenditure on animated television production and video games development, following a similar approach to Film Tax Relief. Following consultation on the design, eligible companies will, from April 2013, be able to reduce their corporation tax liabilities at rates similar in generosity to Film Tax Relief.

The tax base

The tax base is the amount of qualifying expenditure on animated television productions and video games development, estimated using a range of external sources.

Costing

The static costing is calculated by applying the appropriate rates of tax relief to the tax bases described above.

Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	0	-15	-35	-	-

Areas of uncertainty

The main uncertainties in this costing are around the size of the tax base and any resulting behavioural impact.

Enterprise Management Incentive

Measure description

The Enterprise Management Incentives (EMI) scheme allows companies with assets less than £30 million and fewer than 250 full-time equivalent employees to grant tax advantaged share options to their employees. Any gains when the option is exercised do not attract Income Tax or National Insurance. This measure increases the maximum amount of options that an employee can hold from £120,000 to £250,000.

The tax base

The tax base for this measure comprises the gains arising from any additional tax advantaged share options issued as a result of the measure. In 2009-10 gains of £250 million were realised on shares in the EMI scheme. The measure is expected to increase the amount of options granted each year by around 15 per cent, based upon the awards in 2009-10 which were at or close to the £120,000 limit and behaviour following previous increases in the limit. These gains are projected forward in line with the OBR's forecast of equity prices.

Costing

The Exchequer cost is calculated by applying the relevant Income Tax and National Insurance rates to the tax base described above, with rates applied on the basis of the existing income distribution of EMI option recipients. An adjustment is made to account for the time between the options being granted and exercised, based on historical data.

Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	neg.	-5	-10	-20	-25

Areas of uncertainty

The main uncertainty in this costing is around the extent to which awards will increase in response to the measure.

Cap on unlimited tax relief

Measure description

This measure introduces a cap on the total amount of income tax relief an individual can claim from certain reliefs. If income tax relief claimed is in excess of £50,000 a year, the amount of relief an individual can claim is limited to 25 per cent of their total income. The measure will be effective from April 2013. The reliefs affected include but are not limited to:

- Loss reliefs against total income;
- Qualifying loan interest; and,
- Gift Aid and Charitable gifts of land and shares

The tax base

The tax base is estimated using data on reliefs from self assessment (SA) tax returns for 2008-09. These are projected forward in line with the OBR's forecast for earnings growth.

Static costing

The static yield is generated from individuals claiming income tax reliefs in excess of the cap. It is estimated by multiplying the restricted reliefs by the income tax rate.

Static Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	0	0	+870	+680	+720

Post-behavioural costing

The costing makes allowance for a range of behavioural responses to the measure:

- Loss relief: some, but not all, losses will be relieved in alternative ways, for example through using carry-forward loss reliefs.
- Qualifying loan interest: there will be some relief shifting as interest payable is restructured.
- Gift Aid and Charitable gifts of land and shares: There will be some scope to maintain existing relief by smoothing the level of donations across years. A small proportion of these reliefs result from avoidance activity; an adjustment is made to allow for some of this avoidance activity being diverted to other routes.

Post-behavioural Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact[1]	0	neg.	+490	+240	+300

Some forestalling behaviour has been anticipated. Given the interactions between this measure and the costing of the reduction of the additional rate of income tax to 45 per cent, these effects have been captured in that costing.

[1] The effect on tax liabilities underlying the exchequer receipts is £0 in 2012/13, £350m in 2013/14, £270m in 2014/15, £290m in 2015/16 and £310m in 2016/17. There is a lag between the tax liability arising and the tax revenue being collected via self assessment.

Areas of uncertainty

There are some uncertainties around the use of reliefs going forward and also around the extent of the behavioural impact.

Residential property: Stamp Duty Land Tax enveloping

Measure description

This measure introduces a higher rate of Stamp Duty Land Tax (SDLT) on residential property purchased by certain corporate bodies for a consideration greater than £2 million. This measure will reduce SDLT 'enveloping' avoidance, whereby high value residential property is purchased by a corporate body and sold on in a share structure not subject to SDLT.

The additional charge will come into effect on 21 March 2012. In addition, residential properties held within such corporate bodies will be subject to an annual charge as per the table below. This will be introduced from April 2013.

Property Value	£2m to £5m	£5m to £10m	£10m to £20m	Greater than £20m
Annual Charge	£15,000	£35,000	£70,000	£140,000

The tax base

The tax base for the higher charge is the value of residential transactions with a consideration over £2 million where the purchaser is a specific type of corporate body. The tax base for the annual charge is the stock of residential property valued at over £2 million owned by such corporate bodies. The tax base is estimated from SDLT administrative data for 2005 to 2011, held by HMRC.

The tax base is grown in line with the relevant element of OBR's SDLT forecast for revenues from residential properties over £2 million.

Static costing

The static costing is calculated by applying the pre- and post-measure tax regimes to the tax base described above. For the higher rate of SDLT, this is a 10 percentage point increase in the tax rate relative to the pre-measure rate.

Static Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	+160	+295	+325	+355	+395

Post-behavioural costing

The costing takes into account a range behavioural effects, including those who choose:

- not to envelope;
- to envelope and pay the new charges;
- to envelope and use a new avoidance route; or,
- to remove a property from an envelope.

A further adjustment has been made to allow for the impact on price and transaction levels for the affected properties. The costing assumes that the majority of new enveloping ceases and the stock of properties currently within envelopes falls significantly within two to three years.

Post-behavioural Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	neg.	+65	+65	+65	+75

Areas of uncertainty

The main uncertainties in this costing relate to estimates of the stock of properties, the volume of transactions captured by the measure and the behavioural responses.

Stamp Duty Land Tax: additional band for properties above £2m

Measure description

This measure adds a new Stamp Duty Land Tax (SDLT) band for high value residential properties. Transactions over £2 million will be subject to a 7 per cent charge.

The tax base

The tax base is the number of residential property transactions over £2 million and is obtained from a 10 per cent sample of transactions in HMRC administrative data. The latest sample relates to transactions from 2008-09 and is projected forward using OBR determinants for residential property prices and sales volumes.

Static costing

The static costing is calculated by applying the pre- and post-measure tax regimes to the tax base described above.

Static Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	+235	+290	+355	+415	+475

Post-behavioural costing

An adjustment is made to allow for introduction of the new band to reduce the number of transactions and lower residential prices in the price range affected. The elasticities used to estimate the reduction in transactions in each new band implicitly capture avoidance, fewer trades and increased bunching beneath the thresholds. Other measures announced to tackle corporate enveloping are assumed to significantly reduce the size of this avoidance.

Post-behavioural Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	+150	+180	+225	+260	+300

Areas of uncertainty

The main uncertainties in this costing relate to estimates of the bunching around the new thresholds, the reduction in transactions and sampling error arising from the low number of transactions in the data used. There is also uncertainty over the level of avoidance activity; the statement of intent to act swiftly to close down any new avoidance schemes could further increase the yield from the measure.

Capital allowances: business cars

Measure description

From April 2013, this measure reduces the CO_2 emissions threshold (from 160g/km to 130g/km) above which businesses can only claim:

- the special rate (8 per cent) capital allowances rather than main rate (18 per cent); and
- 85 per cent of the costs of leasing a car.

It also allows businesses to claim 100 per cent capital allowances for expenditure on cars with CO_2 emissions of 95g/km or less in 2013-14 and 2014-15. This will only apply to expenditure on cars which are not leased.

The tax base

The tax base is the level of expenditure by businesses on cars. This is derived from data on the sales of different cars from the Driver and Vehicle Licensing authority (DVLA), which includes information on CO_2 emissions. The latest data relates to 2010. Future years are projected forward using projections for reductions in CO_2 emissions, the Society of Motor Manufacturers and Traders' estimate for growth in sales of new cars, and the OBR's forecast for inflation.

In 16-17, the estimated level of expenditure by businesses qualifying for capital allowances on new cars is around £20 billion. The level of expenditure on leasing cars with CO_2 emissions figures over 130g/km and up to 160g/km is around £1.7 billion.

Static costing

The Exchequer cost is calculated by applying the pre- and post-measure tax regimes to the tax base described above.

Static Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	0	+30	+160	+230	+275

Post-behavioural costing

A behavioural adjustment has been made to reflect firms increasing purchases of vehicles with lower CO_2 emissions.

Post-behavioural Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	0	+25	+115	+185	+250

Areas of uncertainty

The main uncertainties in this costing arise from forecasts of future car CO_2 emissions figures, the number of cars bought or leased by businesses and the assumptions made when assessing changes to behaviour.

Freeze vehicle excise duty for heavy goods vehicles in 2012-13

Measure description

This measure freezes vehicle excise duty (VED) rates on heavy goods vehicles (HGVs) and other selected vehicles, such as buses, in 2012-13.

The tax base

The tax base comprises estimates of all HGVs, buses and other selected vehicles which are declared eligible for road use in the year 2012-13. This is derived from data on the stock of vehicles from the Department for Transport (DfT) and the Driver and Vehicle Licensing Agency (DVLA). In line with the VED revenue forecast model and DfT assumptions, estimated net annual increases in the number of vehicles are used to forecast future stock levels.

Costing

The costing is calculated by applying the pre- and post-measure tax regimes to the tax base described above.

Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	-10	-10	-10	-10	-10

Company car tax

Measure description

This measure makes two changes to company car tax:

- 'Appropriate percentage': in 2014-15, the appropriate percentage of the list price subject to tax will increase by one percentage point for cars emitting more than 75g of carbon dioxide per kilometre, to a maximum of 35 per cent. In both 2015-16 and 2016-17, the appropriate percentages will increase by two percentage points, to a maximum of 37 per cent. From April 2016, the Government will remove the 3 percentage point diesel supplement so that diesel cars will be subject to the same level of tax as petrol cars.
- Fuel benefit multiplier: the taxable benefit value of fuel provided by employers for private use in a company car is calculated by applying the 'appropriate percentage' to the 'fuel benefit multiplier' (£18,800 in 2011-12). This multiplier will be raised by RPI + 2 per cent in 2012-13 and 2013-14.

The tax base

The tax base is estimated using data from form P11D, on which taxable benefits in kind are reported. The value of the benefit base is projected forwards using a range of assumptions including reductions in carbon dioxide emission levels, on which the 'appropriate percentages' applicable to vehicles depend.

Take-up adjustments were also applied to the tax base. Car benefit take-up is assumed to remain constant as a proportion of the OBR's forecast for employees, while fuel benefit take-up will decline as a proportion of employees, reflecting recent trends.

Costing

The costing is calculated by applying the pre- and post-measure regimes to the tax bases described above, taking into account the distribution of tax rates over different emissions levels of company cars. Exchequer yield is reduced to take into account additional employees leaving fuel benefit charge in response to the measure.

Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
CCT appropriate percentages	0	0	+120	+375	+350
Fuel benefit multiplier	+5	+10	+10	+5	+5

Areas of uncertainty

The main uncertainties in the costing arise from future changes in the provision of company cars by employers and the behavioural response of individuals in relation to fuel benefit changes.

Remote gambling taxation

Measure description

This measure reforms the taxation of remote gambling by moving to a place of consumption based regime. Remote gambling is currently taxed on the basis of operator location. Under a place of consumption based system, all operators will be liable to tax on the gross remote gambling profits generated from UK-based customers. Conversely, UK-based operators will no longer be liable to gambling taxes on revenues from non-UK customers. The measure is planned to be introduced in December 2014.

Until the place of consumption based taxation regime is implemented, double taxation relief will ensure that UK-based operators do not incur double taxation on remote gambling supplied to customers in countries already operating a place of consumption based tax.

The tax base

The remote gambling sector is a new and rapidly growing sector, expected to grow faster than overall GDP over the forecast period. The size and growth of the tax base is estimated using data from published accounts, market reports and responses to an informal consultation. Profits from overseas customers will not be liable to tax, so they are removed from the tax base. Profits generated from UK customers by operators based overseas are added to the tax base. For 2012-13 the tax base is estimated to be £2 billion, rising to £3 billion by 2016-17.

The amount of double taxation has been estimated based on informal consultation and HMRC evidence. The tax base only takes into account UK based operators' revenue from remote gambling by consumers in those countries that either already have a place of consumption based taxation regime in place or have announced an intention to introduce one.

Static costing

The static costing is estimated by multiplying the tax base by the 15 per cent tax rate currently applied to remote gambling. The estimated remote gambling tax yield collected under the current system is then subtracted. The amount of double taxation relief claimed will depend on the profits made by UK based operators in countries with place of consumption based taxation regimes in place.

Static Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Remote Gambling	0	0	+90	+300	+340
Double Taxation Relief	-15	-20	-15	0	0

Post-behavioural costing

No significant impact on consumer behaviour is expected at the 15 per cent rate and compliance levels are expected to be high as the measure will be accompanied by further supporting legislation. However there is some uncertainty around compliance and behavioural response from both consumer and supplier and we assume that 80 per cent of the theoretical yield is collected.

No behavioural adjustment has been made to the double-taxation relief costing.

Post-behavioural Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Remote Gambling	0	0	+70	+240	+270
Double Taxation Relief	-15	-20	-15	0	0

Areas of uncertainty

The main uncertainties concern the level of compliance and behavioural response from consumer and supplier as well as the implementation details to be consulted upon.

Machine games duty

Measure description

This measure changes the system of taxation on gaming machines from a banded licence fee, amusement machine licence duty (AMLD) plus VAT to a gross profits tax. The scope of the new machine games duty (MGD) will extend beyond that of AMLD, to cover the playing of "dutiable machine games". These are games played on machines where customers hope to win a cash prize worth more than they stake. MGD will be a two-rate system, with the lower rate of 5 per cent applied to machines with a maximum stake of 10 pence and a maximum cash prize of £8 and the standard rate of 20 per cent applied to all other dutiable machines. The introduction of MGD is not intended to raise additional revenue. The measure will be implemented on 1 February 2013.

The tax base

Dutiable machines can be found across a range of business types, including casinos, betting offices, bingo halls, high street arcades, seaside arcades, clubs and pubs. The tax base is derived from the total number of machines and their net revenues, estimated using data from HMRC, the Gambling Commission, published financial accounts and consultation responses.

Machine profits are forecast to grow in line with the OBR's RPI forecast. Machine numbers are projected consistent with the current forecast of AMLD receipts. Machine profits taxable at the standard MGD rate are estimated to be approximately £2.7 billion in 2012-13, growing to approximately £2.8 billion by 2016-17. Profits taxable at the lower rate are estimated to be approximately £150 million per annum.

Static costing

The static costing is calculated by estimating the revenue lost from the abolition of AMLD and from making machine net takings VAT exempt; around £500 million per annum. The revenue raised from the new tax is then estimated.

The calculation of VAT liability on machine takings is based on information received during the consultation on net VAT rates, taking into account input VAT that reduces the final VAT liability. VAT recovery ratio varies by sector and business model. We estimate that, on average, between 25 per cent and 60 per cent of VAT on machines is recovered. The rates of MGD have been set with consideration of these different revenue impacts. MGD is expected to raise around £500 million per year, offsetting the amount of revenue lost from AMLD and VAT on machine games. Therefore the net Exchequer impact is negligible.

Static Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	neg.	neg.	neg.	neg.	neg.

Post-behavioural costing

A price elasticity of demand of -0.5 is used to estimate the size of behavioural response. However, the overall effect on prices faced by consumers is not expected to be significant. The overall behavioural impact on the costing is negligible.

Post-behavioural Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	neg.	neg.	neg.	neg.	neg.

Areas of uncertainty

A relatively large degree of uncertainty is present in this costing as it is based on the overall impact of three distinct components: the revenue lost from the licence fee, the revenue lost from VAT and the revenue raised from MGD. Given this uncertainty, a wide variety of data sources has been used in order to improve the accuracy of estimates.

Tobacco duty

Measure description

This measure increases the duty on tobacco products by five per cent above the retail price index (RPI). The ad valorem rate for cigarettes remains unchanged.

The tax base

The tax base comprises total receipts from all tobacco cleared for sale in the UK (clearances); this is estimated at £9.5 billion in 2011-12, of which cigarettes account for £8.5 billion. Total annual clearances are estimated from the tobacco duty receipts forecast. The forecast takes into account previously announced duty changes, and trends such as reductions in smoking and switching to lower priced products.

Static costing

The static costing is calculated by applying pre- and post-measure duty rates to the clearances described above.

Static Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	+260	+265	+270	+275	+280

Post-behavioural costing

Since duties make up a large proportion of tobacco prices, changes to duty rates can lead to significant changes in prices. Consumers are expected to respond to duty increases by reducing their consumption of duty-paid tobacco, including switching to non-duty paid products, and by switching to lower priced products. Both of these have a negative impact on Exchequer yield. For cigarettes, the behavioural response is captured by a long-run price elasticity of -1.05 and a short-run elasticity of -0.57 (applied to the first three months). For hand rolling tobacco, an elasticity of -1.17 is used throughout.

Post-behavioural Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	+70	+50	+50	+45	+45

Areas of uncertainty

The elasticity used to estimate this is based on extensive research, but is inevitably subject to some uncertainty. Since behavioural effects have a significant impact on the costing, Exchequer impacts are sensitive to any differences in the elasticity used.

Changes to carbon price floor

Measure description

The following measures take effect from April 2013:

- Change the carbon price floor (CPF) rate for solid fuel so that it is related to heat content/calorific value rather than weight and reflects the average calorific value of coal used to generate electricity within the UK.
- Exclude from CPF rates inferior coal slurry with a low calorific value.
- Introduce a generating capacity threshold for generators that have a combined generation capacity of two megawatts (MW) or lower.

The tax bases

For the coal measures, the tax base is the total amount of coal used for electricity generation in the UK, estimated from projections provided by the Department for Energy and Climate Change. In 2013-14 total consumption of coal for electricity generation is estimated to be about 186,000 gigawatt hours.

Coal with a gross calorific value of more than 15 gigajoules (GJ) per tonne will be subject to the CPS rate

For the de minimis measure, the tax base is the estimated consumption of all fossil fuels used in UK electricity generation, with a combined generation capacity of 2MW or lower. The tax base is estimated on the basis of data held by AEA technology, who administer the UK's CHP Quality Assurance (CHPQA) programme.

Costing

The Exchequer impact is calculated by applying the pre- and post-measure CPF regimes to the tax bases described above.

Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Coal calculation	0	-5	-5	-5	-5
Coal slurry	0	-5	-5	-5	-5
Capacity threshold (de minimis)	0	0	-5	-5	-10

Treatment of combined heat and power stations under the carbon price floor

Measure description

This measure exempts fossil fuels from carbon price floor (CPF) rates where these are used to generate heat in combined heat and power (CHP) stations. Only fossil fuels used in CHPs to generate electricity will be liable to CPF rates from 1 April 2013.

The tax base

The tax base is the consumption of fossil fuels used by CHP plants in the Good Quality CHP scheme to produce heat. Data on total electricity produced by CHP is provided by AEA Technology, who act as administrators of the UK's CHP Quality Assurance (CHPQA) programme. AEA's forecast of electricity and heat output is consistent with the Department of Energy and Climate Change's unpublished Updated Energy Projections (UEP).

The tax base incorporates the behavioural impact on total CHP fossil fuel consumption of the provision of an exemption to the CPS rates for 50 per cent of total fossil fuel consumption by CHP stations.

Costing

The cost is estimated by multiplying the tax base for heat by the relevant CPF fossil fuel rate.

Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	0	-35	-75	-100	-125

Areas of uncertainty

The main uncertainty in this costing is the size of the tax base.

Climate change levy: removal of the exemption for combined heat and power electricity

Measure description

This measure confirms the removal of the climate change levy (CCL) exemption for electricity that has been generated by combined heat and lower (CHP) and sold to an electricity utility. This exemption is administered through levy exemption certificates (LECs).The measure takes effect from 1 April 2013.

The tax base

The tax base is the proportion of electricity produced by CHP stations which receive LECs. Data on total electricity produced by CHP has been provided by AEA technology, who administer the UK's CHP Quality Assurance programme. AEA's forecast of electricity production is consistent with the Department of Energy and Climate Change's unpublished Updated Energy Projections. The tax base incorporates the behavioural impact of the removal of the exemption on electricity produced by the CHP sector.

Using data from Ofgem, a further revision is made to the tax base. The tax base is narrowed to the proportion of LECs exported to utility companies (export ratio) and supplied to the final consumers (redemption ratio).

Costing

The exemption is valued at the CCL rate of electricity: £5.24 per megawatt hour in 2013-14. The static costing applies the CCL rate for electricity to the tax base.

Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	0	+110	+125	+145	+165

Areas of uncertainty

The main areas of uncertainty in this costing are the size of the tax base and the export and LEC redemption ratios.

Further environment measures

Measure description

Budget 2012 announces the following three environment measures:

- Enhanced capital allowances (ECA): An update to the list of technologies and products covered by the energy-saving and water efficient ECA scheme;
- Aggregates levy: a delay to the expected inflation-based rate increase in 2012-13 until April 2013, when the rate will increase to £2.10 per tonne; and,
- Landfill Communities Fund (LCF): the value of the LCF will be maintained at its current level of £78.1m for 2012-13, rather than growing in line with inflation.

The tax base

For ECAs, the tax base is the change in qualifying sales resulting from the updated list of technologies and products. This was estimated using data provided by DECC and DEFRA.

For the Aggregates Levy, the tax base is the volume of primary aggregates commercially exploited in the UK and is estimated from historical tax returns, data from primary and recycled aggregates and ONS construction output.

For LCF, the tax base is estimated using outturn tonnages from historical tax returns and DEFRA's projection of future waste volumes. In 2013-14, the standard rate tonnage is estimated at around 20.8 million tonnes and lower rate tonnage at around 9.7 million tonnes.

Costing

In each case the costing is arrived at by applying the appropriate rates to the relevant tax base, under a pre- and post-measure tax regime. For ECAs an additional adjustment is made to account for take-up.

Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Capital Allowances for energy and water efficient technologies	+5	+20	+15	+10	+5
Aggregates Levy	-15	-10	-10	-10	-10
Landfill Communities Fund	0	+5	+5	+10	+10

Changes to age related allowances

Measure description

This measure restricts the availability of the income tax age related allowances to existing recipients. The allowance available to those aged 65-74 will in future be limited to those born between 6 April 1938 and 5 April 1948, and the higher allowance available to those aged 75 and over will be limited to those born before 6 April 1938.

From 2013-14, this measure also freezes the age related allowances at their 2012-13 levels (£10,500 for those born between 6 April 1938 and 5 April 1948, and £10,660 for those born before 6 April 1938) until the personal allowance catches up.

The tax base

The tax base is estimated using data on taxable incomes from the Survey of Personal Incomes (SPI), comprising a sample around 600,000 tax records, weighted to be representative of all taxpayers. The latest available data is for the tax year 2009-10. To estimate the size of the tax base over the costings period, the number of relevant taxpayers and their incomes are projected according to ONS population projections for the relevant age groups, and relevant OBR determinants.

Costing

The static costing is calculated by applying the pre- and post-measure tax regimes to the tax base described above.

Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	0	+360	+670	+1,010	+1,250

Areas of uncertainty

The main uncertainties in this costing relate to projected numbers of baseline taxpayers aged 65 and over who will be affected by the measure. Taxpayer numbers depend partly on levels of savings and investment income which must be imputed in the SPI survey.

Value added tax: boundaries simplification

Measure description

This measure addresses a number of anomalies in the definitions and application of the zero-rate of value added tax (VAT) and VAT exemptions. Specific products affected include self storage, hairdressers' chairs, alterations to listed buildings, static caravans, sports drinks and a broader measure of hot take-away food. All of these products will be clearly brought within the standard rate of VAT, from October 2012.

The tax base

The tax base is consumer expenditure on the affected products. The value for each tax base is estimated using data from a range of sources.

- For self storage, data is taken from commercial reports. The tax base affected in the first full year of the measure is estimated to be about £200 million;
- For hairdressers' chairs, data is taken from HM Revenue and Customs and trade association reports. The tax base affected is estimated to be about £70 million;
- For alterations to listed buildings, data is taken from the Department for Communities and Local Government and local authority planning applications. The tax base affected is estimated to be about £600 million, of which about one fifth is estimated to become subject to the 5 per cent reduced rate of VAT for residential conversions;
- For caravans, data is taken from commercial and trade association reports. The tax base affected is estimated to be about £300 million;
- For sport drinks, data is taken from commercial reports, and the tax base affected is estimated to be about £70 million; and,
- For hot take-away food, data is taken from the Department for the Environment, Food and Rural Affairs, the Office for National Statistics and commercial reports. The tax base affected is estimated to about £700 million.

Each tax base has been grown in line with appropriate OBR economic determinants, and the total tax base affected in the first full year of the measure, in 2013-14, is estimated at approximately £1.9 billion.

Static costing

The static costing for this measure is calculated by in most cases applying the 20 per cent standard rate of VAT to the tax bases described above, and is adjusted where applicable to take account of any additional input tax businesses will be able to reclaim. The 5 per cent reduced rate of VAT is applied to about one fifth of the tax base for alterations to listed buildings.

Static Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	+160	+355	+385	+410	+440

Post-behavioural costing

A behavioural response is included to take into account the fall in demand for goods in response to the increase in price. Elasticities of demand were applied to the products affected of -0.5 for self storage, -1.0 for hairdressers' chairs, -0.4 for alterations to listed buildings, -1.5 for static caravans and -0.8 for sports drinks and hot take-away food.

The costing is also adjusted to allow for some non-compliance in these markets once the goods become subject to the standard rate of VAT; a reduction of 10 per cent is applied, consistent with the expected level of the total VAT tax gap in the VAT receipts forecast.

Post-behavioural Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	+125	+270	+290	+315	+350

Areas of uncertainty

The main uncertainties in this costing relate to the exact size of the tax base and the behavioural response of consumers to the price increase.

Loan relationship avoidance: debt buyback

Measure description

The corporation tax legislation on debt and similar kinds of financial instruments is referred to as the rules on loan relationships. Broadly, these aim to tax and relieve for corporation tax (CT) purposes the profits and losses recognised by a company under UK Generally Accepted Accountancy Practice.

A number of companies have been exploiting the current CT rules to avoid being taxed on profits from transactions where debt instruments are repurchased from the market for commercial reasons. These buy backs have generated considerable profits for the entities concerned and the principal of the existing rules is that these profits should be taxed. The scheme concerned arose in 2011.

Closure of this loophole will prevent companies from avoiding Corporation Tax on the profit made from such transactions and took effect retrospectively from 1 December 2011 recovering the CT lost to the Exchequer in the 2011 calendar year. The measure will also act to protect substantial amounts of CT revenue across the wider financial and corporate sector.

The tax base

The tax base for this measure are the profits made by companies by buying back their own issued debt, who have the potential to avoid Corporation Tax.

Costing

In 2011 around £300 million of Corporation Tax was avoided using this scheme. The scheme relies upon the market price of redeemable debt securities being lower than their face value. Based on the OBR's economic forecast, this costing predicts opportunities to use this scheme would diminish over time as the market price of these securities increased. The costing is adjusted to account for the yield from the retrospective element of the policy in 2012-13.

Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	+395	+210	+55	0	0

Areas of uncertainty

The detailed yield profile is higher than initial estimates released by HMRC. This reflects a more detailed analysis of the likely behaviour of the scheme users going forward over the costing period. Broadly the total yield detailed is of similar magnitude.

Office of Tax Simplification: abolition of reliefs

Measure description

The abolition of the following reliefs has been announced since the Autumn Statement:

- Repeal of life assurance premium relief: from the 6 April 2015 relief will no longer be available on regular premiums paid into qualifying life assurance policies issued on or before 14 March 1984.
- Repeal of disadvantaged areas relief (DAR): this measure repeals the relief from Stamp Duty Land Tax (SDLT) for purchases of residential property in areas designated as 'disadvantaged,' where the purchase price is between £125,000 and £150,000. This will take effect from April 2013.

The tax base

For life assurance premium relief, the tax base comprises the repayments to life insurance providers in respect of tax relief on life policies taken out before March 1984; £13.7 million in 2010-11. Repayments have been declining steadily as many of these policies have matured.

For the repeal of DAR, the tax base is all residential property transactions where the relief is claimed, estimated from SDLT administrative data. Data from 2007-08 and 2008-09 is projected forward in line with the OBR's forecast for growth in the value of total UK residential transactions.

Static Costing

For life assurance premium relief, the static cost is the reduction in repayments, assumed at 11 per cent per annum over the forecast period. Under this assumption repayments will have fallen to £5 million by 2015-16.

For the repeal of DAR, the static costing is the projected tax base multiplied by the SDLT rate that applies in the absence of the relief.

Static Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Repeal of Life Assurance Premium Relief	0	0	0	+5	+5
Repeal of Disadvantaged Areas Relief	0	+30	+40	+40	+40

Post-behavioural costing

There are no behavioural impacts incorporated into the costing of the withdrawal of life-assurance premium relief.

The repeal of DAR has a behavioural impact that is captured by elasticities for the price and volume of transactions; both of these are -2. This implies that a 1 per cent increase in the rate of SDLT leads to a two per cent decrease in the average price of residential properties and a two per cent decrease in the volume of transactions. Taken together, the overall behavioural impact is to reduce the static costing by approximately four per cent each year.

Post-behavioural Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Repeal of life assurance premium relief	0	0	0	+5	+5
Repeal of disadvantaged area relief	0	+30	+40	+40	+40

Areas of uncertainty

The future rate of decline in life assurance premium repayments remains uncertain.

The main uncertainties for the DAR costing arise from the elasticity used and the assumption that the rate of change in residential property volumes and prices in disadvantaged areas are consistent with rates for the UK as a whole.

Capital allowances: anti-avoidance

Measure description

The following capital allowance anti-voidance measures have been announced since Autumn Statement 2011:

- Capital allowance anti-avoidance rule: where there is a 'transaction to obtain a tax advantage', this measure removes the first-year capital allowance or annual investment allowance for expenditure on plant and machinery and restricts the amount of allowance the 'buyer' of plant and machinery can claim; and,

- Plant and machinery leasing anti-avoidance: this measure makes changes to the long-funding lease legislation within the Corporation Tax regime, preventing lessees artificially reducing the disposal value of plant and machinery and therefore reducing taxable profits. The measure will require businesses engaging in transactions of this type to bring all relevant expenditure and receipts into account when calculating the disposal value.

The tax base

For the capital allowance anti-avoidance rule, the tax base is expenditure in respect of which businesses have sought to claim allowances for tax avoidance purposes. Current Exchequer losses from these types of avoidance are estimated using HMRC data on known cases up to 2009-10. This value has been projected forward to 2016-17 in line with investment growth in the OBR's economic forecasts.

For plant and machinery leasing, the tax base is the total amount of balancing charges which businesses have sought to avoid by artificially reducing the disposal value of plant or machinery. The total value of balancing charges avoided in this way to date is estimated at around £300-350 million, based on cases known to HMRC.

Costing

For the anti-avoidance rule, the costing is the removal of allowances for the base estimated above. An adjustment has been made to allow for the increased probability of these schemes being successfully challenged under the new legislation.

For plant and machinery leasing, the costing is calculated by applying the relevant corporation tax rates to the tax base described above.

In both cases, the Exchequer impact is adjusted to allow for alternative avoidance schemes, leading to attrition of the expected revenue.

Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Capital allowance: Changes to anti-avoidance rules	neg.	+5	+5	+10	+10
Plant and machinery leasing: anti-avoidance	+25	+40	+40	+35	+35

Income tax, inheritance tax and capital gains tax: reliefs & avoidance

Measure description

Budget 2012 announces the following measures on Income Tax (IT), Capital Gains Tax (CGT) and Inheritance Tax (IHT) reliefs and anti-avoidance:

- IHT corporate settlor-interested trusts: this measure amends the settlements legislation to confirm that income which arises under a settlement and originates from a settlor who is not an individual is not treated as that of the settlor. This closes an avoidance scheme involving corporate settlors and settlor-interested trusts by ensuring that the relevant provisions do not apply where the settlor is not an individual;
- IHT spouse relief: Transfers between spouses and civil partners are usually exempt from inheritance tax; where the transferor is domiciled in the UK and their spouse or civil partner is not, the relief is capped at £55,000. This measure offers non-domiciled spouses and civil partners the option of electing to be UK domiciled for inheritance tax purposes. For those who do not elect, the cap will increase to the nil rate band, currently £325,000; and,
- CGT change in anti-avoidance provisions: under the current CGT regime, gains from the disposal of assets held by UK residents through a closely-controlled foreign company attract CGT, where the UK resident holds more than a 10 per cent interest. This measure provides an exemption from the tax charge on CGT for certain types of property held in this way.

The tax base

The tax base for corporate settlor-interested trusts has been estimated using information provided to HMRC through the Disclosure of Tax Avoidance Schemes (DOTAS); it is estimated to be £45 million of dividend income.

For IHT Spouse Relief and the CGT anti-avoidance provisions change, the respective tax bases are estimated using HMRC administrative data. For IHT Spouse Relief, the average annual inheritance tax revenue from relevant assets is £3.5 million per year. For the CGT measure, a small amount of foreign close-company held property, (mainly furnished holiday letting) which will become eligible for the exemption from the tax charge, may currently be liable to CGT.

Costing

In each case the costing is arrived at by applying the appropriate rates and reliefs to the relevant tax base, adjusting for behavioural effects and any change in compliance. The CGT costing assumes an increased level of take-up.

Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Corporate settlor-interested trusts	0	+15	+10	+10	+10
IHT spouse relief	0	neg.	-5	-5	-5
CGT change in anti-avoidance provisions	0	neg.	neg.	neg.	-5

Enhanced capital allowances: enterprise zones in Scotland, Yorkshire and Humber, London and Wales

Measure description

This measure enables eligible companies to claim 100 per cent first-year capital allowances rather than the 18 per cent main rate capital allowances or the 8 per cent special rate capital allowance. This applies to qualifying expenditure on plant or machinery for use within the Scottish, Yorkshire and Humber, London and Welsh enterprise zones. This is subject to a cap of €125m from 2012-13 to 2016-17.

The tax base

Local Enterprise Partnerships have provided estimated levels of qualifying expenditure. For both Scotland and Yorkshire and Humber zones, the estimated qualifying expenditure ranges between £10 million to £100 million per annum over the forecast period.

Costing

An adjustment is made to the tax base to remove any behavioural effects from the estimate of the tax base. The capital allowance rates and main rate for corporation tax are applied to the estimated levels of qualifying expenditure.

Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	neg.	-5	-20	-15	neg.

Areas of uncertainty

It is assumed that the projected levels of expenditure that will qualify for the 100 per cent first-year capital allowance will take place. There is however some uncertainty around the qualifying expenditure as it is not yet certain which projects will go ahead within the designated areas. The Government is currently discussing Enterprise Zones with devolved administrations. Costs may increase if Enhanced Capital Allowances are offered to additional assisted areas.

Corporation tax regime for life insurance

Measure description

This measure introduces a new regime for the taxation of life insurance companies, in preparation for the introduction of the Solvency II capital adequacy regime in January 2013. It is an extension of the changes announced at Budget 2011, which will move life protection business out of the Basic Life Assurance and General Annuity Business (BLAGAB) category. This measure introduces several additional components. These include basing taxable profits on statutory accounts rather than regulatory returns, and combining Gross Roll-up Business (GRB) and Permanent Health Insurance (PHI) into a single category (to also include life protection business), which will be subject to tax on a trading profits basis. The "I minus E" system, unique to life insurance company taxation, will apply to BLAGAB only.

The tax base

Life insurance companies contribute around £1.5 billion per annum in corporation tax. The move to the new regime will impact the tax base in a number of ways. In some areas there will be substantial additional income that will now become chargeable to tax; in others areas, groups will be able to take advantage of more generous deductions.

Costing

Using data from HMRC, the Financial Services Authority, and industry, the costing is determined by the combined effect of a number of different impacts on taxable profits. Those that may reduce taxable profits include:

- Enabling more generous deductions for BLAGAB expenses;
- Combining GRB and PHI to free up in-year losses and enable the more flexible use of historic pension business losses; and,
- Reclassifying a proportion of life assurance trade losses from BLAGAB to the combined GRB/PHI category, potentially accelerating their usage.

The costing also allows for a range of positive impacts on taxable profits:

- The costs of acquiring new business, currently relieved when incurred, would now be written off over a number of years;
- Certain profits are recognised in accounts but not in regulatory returns and will now become taxable; and,
- The change in regime will bring into tax transitional amounts due to differences in the valuation of assets and liabilities and the timing of receipts and expenses.

The costings are presented below on a receipts basis. They have been projected forwards using OBR determinants for GDP and equity prices.

Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	0	+55	+30	-65	+30

Areas of uncertainty

This is a complex costing for which a range of interacting effects have been estimated; this is inevitably subject to uncertainty. Volatility in the bond and equity markets will impact on the costing, and in particular the transitional amounts.

Stop-loss insurance

Measure description

Stop-loss insurance is a type of re-insurance contract. Prior to this measure, premiums under member-level stop-loss contracts taken out by corporate members of Lloyd's of London could be deducted in advance of the year for which the related profits are recognised for tax purposes. This measure, which is effective from 6 December 2011, aligns the timing of the tax deduction for the premiums payable with the recognition of the profits to which they relate. It applies to all corporate members of Lloyd's and corporate partners in a partnership that is a member of Lloyd's.

The tax base

The tax base is made up of the reinsurance expenses of the corporate members that have been identified as taking deductions in advance of the year in which the related profits are recognised. Using the most recent Lloyds syndicate data available to HMRC, for 2008-09, HMRC were able to identify a number of affected corporate members. HMRC estimate the total member-level reinsurance expenses for these corporate members to be £2.7 billion and have forecasted future values based in line with the relevant OBR determinants.

Costing

The static costing is derived from the additional taxable profits generated by the measure. The Exchequer impact relates to the period over which the timing advantage unwinds, with an adjustment for when tax receipts are received and for OBR economic determinants.

This measure is not expected to have any behavioural impact.

Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	+170	+250	+260	+110	+25

Areas of uncertainty

The size of the tax base is subject to uncertainties regarding the future outlook for the insurance sector and wider economy.

General insurance: claims equalisation reserves

Measure description

There is currently a regulatory requirement for general insurance companies to maintain claims equalisation reserves (CERs) in respect of certain lines of business, with amounts transferred into CERs being tax deductible. However, under Solvency II that requirement will be withdrawn. This measure will repeal the current legislation for the tax treatment of CERs and introduce a rule to tax built-up CERs in equal amounts over a six year period, with an option to elect for an accelerated release. This measure will have effect from the date the Solvency II Directive capital requirements comes into force, which is expected to be 1 January 2014. Regulations will be made to cover equivalent reserves maintained for tax purposes by corporate and partnership members of Lloyd's.

The tax base

The size of the tax base is estimated using data from regulatory returns supplied to the Financial Services Authority covering the period to the end of 2008. This data is projected forward in line with relevant OBR determinants, to give an estimate of £3 billion of reserves held in aggregate at the end of 2013 by general insurance companies and Lloyd’s members.

Costing

The tax base is multiplied by the corporation tax rate to calculate the static costing. Companies will be able to use losses to offset some of the extra taxable income but past and forecasted losses are not sufficient to offset the full amount. An adjustment has been made to account for this offset of losses.

Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	0	neg.	+85	+90	+80

Areas of uncertainty

The main uncertainty is around the size of the reserves in 2014 as this estimate will depend on future claims and premiums as well as the wider economic outlook.

Bank Levy amendments

Measure description

This measure ensures that the Bank Levy applies appropriately to the liabilities of all joint ventures by aggregating them with the chargeable equity of a foreign banking group or relevant non-banking group. The changes to the rules will apply to chargeable periods ending on or after 1 January 2012.

The tax base

The tax base is estimated by identifying non-resident joint ventures that are held by foreign banking groups, where the venture's chargeable equity and liabilities are below £20 billion and so currently excluded from the Bank Levy.

Costing

The Exchequer impact is calculated by multiplying the tax base described above by the relevant Bank Levy rates, depending on whether liabilities are long- or short-term. The costing is projected forward in line with the relevant OBR determinants.

Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	+10	+10	+10	+10	+10

Scope of the supplementary charge on North Sea oil and gas profits

Measure description

This measure ensures that companies involved in UK oil and gas exploration and production are subject to both ring fence corporation tax (RFCT) and supplementary charge (SC) on taxable profits and chargeable gains. The measure achieves this by confirming that the scope of SC matches that of RFCT, and by ensuring that a ring fence chargeable gain cannot be transferred from a company carrying on a ring fence trade to a company not carrying on a ring fence trade.

The tax base

The tax base for this measure is chargeable gains within the ring fence oil and gas tax regime that would be transferred to another company within the same group outside of the ring fence oil and gas regime. This has been estimated from known past Exchequer losses where this has happened.

Costing

The costing is calculated by applying the pre- and post-reform tax regimes to the tax base described above. The Exchequer impact is then adjusted to control for the likelihood of alternative routes causing attrition to the expected revenue gains.

Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	+10	+10	+10	+10	+10

Areas of uncertainty

The main uncertainties in this costing relate to the size of the current tax losses and the way in which companies will respond to the measure.

Capital allowances: fixtures

Measure description

This measure changes the capital allowance rules for expenditure on qualifying fixtures, so that the original cost of a fixture should be claimed only once, with effect from April 2012.

The tax base

Information from capital allowances tax advisors is used to estimate the amount of capital allowances being claimed more than once for fixtures. The total tax base is estimated to be around £50 million per year.

Costing

Reductions in the level of expenditure for which capital allowances are claimed are estimated for different types of business and expenditure. The costing is calculated by applying the appropriate capital allowance rates to the pre- and post-measure tax base before. An adjustment is made for the proportion of capital allowances claims that will be tax-effective.

Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	neg.	+15	+20	+30	+35

Areas of uncertainty

The main uncertainty is around the level of expenditure for which capital allowances are being claimed more than once.

Capital allowances: Feed-in Tariffs and Renewable Heat Incentive

Measure description

The Renewable Heat Incentive (RHI) scheme enables incentive payments to be claimed for expenditure on environmentally-friendly technologies that can be used to generate heat. Some of this expenditure is also eligible for 100 per cent first year capital allowances. This measure will remove this entitlement if RHI payments are being claimed. This change will take effect from April 2012 for all technologies excluding combined heat and power systems, for which it will take effect from April 2014.

Feed in tariffs can be received for some renewable electricity generating technologies including solar panels. In some instances, the installers of solar panels are able to claim main rate capital allowances (18 per cent from 2012-13); this measure will restrict claims to the special capital allowances rate (8 per cent from 2012-13), from 2012-13.

The tax base

The tax base for this measure is the expenditure by businesses on eligible technologies affected by the measure. This has been estimated using research by DECC. Total expenditure is estimated to be up to £5 billion over the next five years.

Static costing

The static costing is calculated by first applying the change in capital allowances rates and applying the relevant tax rates. An adjustment is made for the proportion of capital allowance claims that will be tax-effective.

Static Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	+20	+40	+55	+70	+85

Post-behavioural costing

This measure will reduce expenditure on eligible technologies due to less generous capital allowance rates. It is also expected that some Combined Heat and Power (CHP) businesses may bring forward expenditure. This results in a small overall increase in yield between the static and post-behavioural costing.

Post-behavioural Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	+20	+45	+60	+80	+100

Areas of uncertainty

The main uncertainty in this costing relates to the levels of business expenditure on eligible technologies affected by this measure. Many of these are relatively new technologies and the use of them could change significantly over future years.

Auto-enrolment revised implementation schedule

Measure description

This measure redesigns the implementation schedule so employers with fewer than 50 workers will not be brought into the workplace pension reforms until the next Parliament. Overall, the staging timetable now extends to February 2018 and as a result the phasing of contributions now takes place over six years.

The tax base

The tax base comprises the tax relief that would have otherwise been paid on any additional pension contributions.

The contribution costs are estimated by modelling the number of individuals for whom additional contributions are due. Estimates of individuals' average qualifying earnings are estimated using the Annual Survey of Hours and Earnings (ASHE), multiplied by the contribution rates. Contribution rates are assumed to be the minimum prescribed by the reforms.

These aggregate costs are apportioned over the staging period. To estimate the tax relief on individuals' contributions, estimated contributions are multiplied by the appropriate rate of tax relief.

Costing

The costing is calculated by comparing the tax relief due under the implementation schedule described in the existing legislation with the tax relief due under the revised implementation schedule.

Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	0	0	+5	+35	+340

Areas of uncertainty

There is uncertainty around the number of individuals from whom additional contributions will be due under the workplace pension reforms. These estimates are based on an extensive programme of research and have been developed and agreed by a programme group of analysts from the Department for Work and Pensions, the National Employment Savings Trust and The Pensions Regulator.

Local Housing Allowance: baseline for uprating

Measure description

The fixing of Local Housing Allowance (LHA) rates will be brought forward from October 2012 to April 2012. Rates will be uprated in line with the Consumer Prices Index from April 2013, as planned.

The cost base

The cost base is derived from DWP administrative data and forecasts of the Local Housing Allowance caseload, which is expected to rise to around 1.4m over the medium term.

Costing

Costs are relative to a scenario in which LHA rates would not have been fixed until October 2012. It is assumed that on average Local Housing Allowance rates would otherwise have grown by two per cent between April and October 2012, in line with the LHA forecast.

DWP administrative data on the rents, locations and bedroom entitlement of HB claimants is used to estimate the impact on the average weekly Housing Benefit entitlement.

This average impact is applied to the forecast for the total number of LHA claims.

Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	+100	+170	+175	-	-

Areas of uncertainty

The main area of uncertainty in the costing is the growth in market rents during 2012-13.

Mobility components of personal independence payment for claimants in residential care

Measure description

This measure reverses the proposed policy which would cease payment of the personal independence payment (PIP) mobility component to publicly funded care home residents after 28 days. The removal of the current Motability extension for those leaseholders who remain inpatients of hospitals or similar institutions after 28 days will still go ahead.

The cost base

The cost base covers those Disability Living Allowance (DLA) recipients identified on DWP administrative data as a current claimant living in a care home – around 78,000 individuals. Quarterly updates on the DLA caseload have shown that caseload for this group is static.

Costing

Since the policy is now being reversed the scored savings become costs to the exchequer.

The original AME savings were estimated by calculating the annual total mobility component expenditure for the care home group, giving a steady state figure for predicted savings. The caseload of 78,000 receives an average mobility award of £33.40 and the measure was planned for introduction in April 2013.

The average mobility award has been grown in line with the OBR CPI forecast.

Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	0	-150	-155	-	-

Changes to the Housing Benefit Social Sector Size Criteria

Measure description

From April 2013, entitlement to Housing Benefit will be restricted for working age claimants living in the social rented sector whose accommodation is considered larger than their household requires. This measure introduces a proportionate reduction in awards and defines working age as those below the qualifying age for Pension Credit.

The cost base

Working age individuals are those below the qualifying age for Pension Credit, which will increase over time. The cost base has been estimated using the DWP's Policy Simulation Model, based on the 2009-10 Family Resources Survey.

Costing

Estimated savings have been expressed relative to the previous policy of fixed cash reductions for under-occupation and a fixed age threshold for the application of the size criteria. Under the reform, claimant's eligible rent is reduced by 14 per cent if the household under occupies the accommodation by one bedroom; or by 25 per cent if they under occupy by two or more bedrooms.

Savings have been calculated by applying the relevant percentage reduction in award to the eligible rent for affected claimants under-occupying their accommodation by one, two or more bedrooms.

Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	0	+30	+60	-	-

Areas of uncertainty

The main uncertainties in this costing are around any behavioural responses by claimants and landlords and the growth of social sector rents.

Changes to welfare and tax credits

Measure description

The following measures have been announced since Autumn Statement 2011 or at Budget 2012:

- Discretionary housing payments (DHPs): from 2012-13, additional funding will be made available to local authorities to enable them to help benefit claimants affected by the social sector size criterion and the benefit cap.
- Benefit cap: from 2013-14, claimants of the Support Component of the Employment and Support allowance (ESA) will be exempt from the cap; benefit claimants who were in work for twelve months prior to the start of their claim will be exempt from the cap for 9 months.
- Working Tax Credits (WTC): from 2012-13, a couple where at least one partner is entitled to Carer's Allowance may qualify for WTC, including the childcare element, where at least one partner works at least 16 hours per week.

The cost base

Discretionary housing payments are classified as AME, although they are cash limited. The cost base is therefore the announced increase in funds available.

For benefit cap and tax credit changes, eligible claimants are identified from the relevant administrative data, held by DWP and HMRC respectively.

Costing

The costings for benefit cap and tax credit measures are estimated by calculating the difference in the pre- and post-measure awards for the base identified above.

Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Discretionary housing payments	0	-30	-30	-	-
Benefit cap: ESA exemption	0	-75	-45	-	-
Benefit cap: unemployed grace period	0	-20	-20	-	-
WTC extend exemption carers' relief	-5	-5	-5	-	-

Areas of uncertainty

There is uncertainty in the grace period costing around whether the current proportion of claimants in work for twelve months prior to claiming will be representative of future trends.

Public Works Loan Board Certainty Rate

Measure description

This measure introduces a Public Works Loan Board (PWLB) certainty rate in 2012-13, at 20bps below the PWLB standard rate. This rate will be available to local authorities (LAs) who provide annually updated and publically available data on long-term borrowing and associated capital expenditure.

The cost base

Gross lending by the PWLB to LAs in England in 2011-12 is forecast to be £2.3 billion, based on lending data to 24 February 2012. It is assumed that local authorities in Scotland and Wales will exhibit a similar behavioural response to the introduction of a certainty rate.

Static costing

Since the increase in PWLB rates to 100bps above gilts, at Spending Review 2010, LA borrowing has been subdued. LAs may access borrowing from private sources, leading to an outflow of interest from the public sector. In the absence of the measure, LAs are expected to increase borrowing from the private sector, rather than PWLB.

Some LAs have already sought to borrow from the markets rather than PWLB. Around 40 per cent of LA borrowing could be financed this way, rather than from the PWLB; this could amount to £920 million by the end of the forecast period. The exchequer impact therefore represents the value of interest payments that will not come to the public sector as a result of this measure.

Post-behavioural costing

The certainty rate will only be available to principal local authorities subject to the CIPFA Prudential Code. It is assumed that not all eligible LAs will be willing to provide the capital spending and borrowing information necessary to secure the lower rate.

An adjustment to the expected yield has been made to account for LAs spending some of the savings from lower interest payments, arising from the difference in interest payments between the PWLB standard rate and the new certainty rate.

Post-behavioural Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	+5	+15	+25	-	-

Areas of uncertainty

The costing uses best estimates for LA borrowing, although there is uncertainty around the quantity and timing, as LAs are free to borrow in advance of need.

Paying down housing debt

Measure description

The Government is increasing the discounts available under Right to Buy (RTB). From 2 April the current range of regional caps on discounts will be replaced by a higher single cap of £75,000. The receipts from additional sales will be used to enable local authorities to pay down the outstanding debt associated with that property and on building new homes for affordable rent.

The cost base

The debt attributed to a unit of Housing Revenue Account housing has been derived from the HRA reform self-financing calculations.

Costing

The Department for Communities and Local Government have estimated the impact of increasing RTB discounts on take up using a module of the Department's Affordability Model, developed at the University of Reading.

Local authorities keep the proportion of the receipt needed to cover the debt associated with any property sold so that they can pay down the debt associated with that property and ensure that the local authority's HRA business remains viable.

Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	+55	+115	+175	-	-

Areas of uncertainty

There is uncertainty in this costing around take-up assumptions. Increased discounts should raise RTB sales, however take-up will be influenced by a number of factors including wider economic circumstances. There is also uncertainty about the behaviour of local authorities, given they will not be obliged to pay down debt.

Tax Increment Financing

Measure description

Tax increment financing (TIF) is a finance mechanism that allows local authorities to use anticipated future tax receipts to support upfront investment in their local area, using their prudential borrowing powers. From April 2013 all local authorities will be able to take forward TIF projects within the confines of the local government finance system (TIF 1). Government has also agreed to allow a limited number of projects to go ahead outside of the confines of the local government finance system, which will enable the local authority to retain growth in (and therefore borrow against) their tax base for longer (TIF 2). Schemes under TIF 2 will otherwise not have gone ahead and are therefore not already accounted for in the LASFE forecast. This additional capital spending needs to be offset by equivalent spending reductions elsewhere if it is to be cost neutral. Budget 2012 confirms that £150m will be made available for TIF2 projects in the period 2013-14 – 2018-19.

The cost base

The cost base is the amount announced as available to support the scheme.

Costing

In order to make TIF 2 revenue neutral DCLG Ministers have agreed that the local government resource settlement will be reduced by £20 million per annum. This will create headroom of £20 million of for capital spending. Ministers have also decided to provide an additional £40 million (£20 million in each of 2013-14 and 2014-15) that local authorities will be able to apply for. It is assumed that there will be 100 per cent take up and that this will lead to additional capital spending.

Exchequer impact (£m)

	2012-13	2013-14	2014-15	2015-16	2016-17
Exchequer impact	0	-20	-20	-	-

Areas of uncertainty

It is not certain whether or not the £20 million per annum reduction in total local authority resource will cause some local authorities to reduce their levels of capital expenditure.

A Indexation in the public finance forecast baseline

A.1 The following table shows the indexation assumptions that have been included in the public finance forecast baseline, including all pre-announcements, for Budget 2012 policy costings. Unless otherwise stated, changes are assumed to take place in April each year and tax rates are assumed to be fixed.

Forecast area	Element	Default indexation assumed in baseline	Pre-announced policy changes from 2012-13 onwards
Income tax	Personal allowances[1]	RPI[3], increase rounded up to the nearest £10; CPI once personal allowance for those aged under 65 reaches £10,000.	Personal allowance for those aged under 65 increased by £630 in cash terms in 2012-13
	Basic rate limit	RPI[3], increase rounded up to the nearest £100 until 2015-16, CPI[4] thereafter.	Basic rate limit reduced by £630 in cash terms in 2012-13., Basic rate limit will be held constant in 2013-14
	Starting rate limit	RPI[3], increase rounded up to the nearest £10 until 2015-16, CPI[4] thereafter	
	Threshold for additional (50 per cent) rate	Fixed at £150,000	
	Threshold for tapered withdrawal of personal allowances[iii]	Fixed at £100,000	
	Pensions tax relief annual allowance Pensions tax relief lifetime allowance Individual Savings Accounts limits for cash and equities	Fixed at £50,000 Fixed at £1.5m CPI rounded to the nearest £120	
	Threshold for Child Benefit income tax charge	Fixed at £50,000	
NICs	Lower earnings limit Primary Threshold / Lower Profits Limit Secondary Threshold	CPI,[4] rounded down to the nearest £1per week CPI,[4] rounded to the nearest £1pw / £5pa RPI[3], increase rounded to the nearest £1pw until 2015-16, CPI[4] thereafter	

Forecast area	Element	Default indexation assumed in baseline	Pre-announced policy changes from 2012-13 onwards
	Upper Earnings Limit / Upper Profits Limit	Aligned with income tax higher rate threshold	
	Small Earnings Exception	CPI,[4] rounded up to the nearest £10pa	
	Contribution rates	Fixed, apart from Class 2 and 3 weekly rates which rise by CPI, rounded to the nearest 5p.	Contracted out rebate rates reduced to 1.4 per cent for employees and 3.4 per cent for employers from 2012-13
Capital gains tax	Main annual exempt amount	CPI,[4] rounded up to the nearest £100	Frozen in 2012-13
	Annual exempt amount for trustees	CPI,[4] rounded up to the nearest £50	Frozen in 2012-13
	Lifetime allowance for entrepreneurs' relief	Fixed at £10m	
Inheritance tax	Nil rate band allowance threshold	CPI,[4] rounded up to the nearest £1,000	Nil rate band threshold will be frozen until 2014-15 inclusive
Disability Benefits (Disability Living Allowance, Attendance Allowance, Carer's Allowance). Income-related benefits (Jobseeker's Allowance, Income Support, Incapacity Benefit, Employment Support Allowance), Maternity Benefits and Statutory Sick Pay.	All main rates	CPI [4]	
Basic State Pension	All categories	Higher of earnings, CPI or 2.5%	
Additional State Pension	All elements	CPI [4]	
Pension Credit	Guarantee Credit	Earnings	Guarantee Credit uprated by 3.9% in 12/13.
	Savings Credit	Maximum Savings Credit award frozen in cash terms for 4 years from April 2011. It is then frozen in real terms.	Savings Credit threshold increased by 8.4% in 12/13.
Child Tax Credit	Family element	Fixed at £545 per year	
	Child element	CPI,[4] rounded up to the nearest £5	

Forecast area	Element	Default indexation assumed in baseline	Pre-announced policy changes from 2012-13 onwards
	Disabled and enhanced disabled child elements	CPI,[4] rounded up to the nearest £5	
Working Tax Credit	All award elements Maximum eligible childcare costs (for 1 and 2+ children)	CPI,[4] rounded up to the nearest £5 Fixed at £175 and £300 per week	Basic and 30 hour elements frozen for three years from 2011-12 Couple and lone parent elements frozen in 2012-13
Child Benefit	Eldest (or only) child and subsequent children amounts	CPI,[4] rounded to the nearest 5 pence	Frozen for three years from 2011-12
Corporation tax	Marginal relief lower limit Marginal relief upper limit Small profits rate	Fixed at £300,000 profit Fixed at £1.5m profit Fixed at latest announced rate	
Stamp Duties	Stamp duty land tax thresholds	Fixed at £125,000, £250,000, £500,000 and £1m	
Climate Change Levy	Levy amount	RPI [5]	
Aggregates Levy	Levy amount	RPI [5]	Aggregates levy will increase to £2.10 per tonne in 2012-13
Landfill Tax	Tax rates	RPI [6]	Landfill tax rates will increase by £8 per tonne until 2014-15
Vehicle Excise Duty	Duty rates	RPI,[6] rounded to the nearest £1 or £5	
Amusement Machine Duty	Duty rates	RPI [6] rounded to the nearest £5	
Air Passenger Duty	Duty rates	RPI,[6] rounded to the nearest £1	Defer RPI increase in 2011-12 to 2012-13 and implement the 2012-13 RPI increase on top of this.
Tobacco Duties	Duty rates on all tobacco products	RPI [6]	Increase by 2 percentage points above RPI every year until 2014-15 inclusive
Alcohol Duties	Duty rates on all alcohols	RPI [6]	Increase by 2 percentage points above RPI every year until 2014-15 inclusive
Fuel Duties	Duty rates on petrol and diesel [2] Duty rate on liquefied petroleum gas (LPG)	RPI [6] In line with changes in petrol and diesel duty rates	Defer the 2012-13 RPI increase to August 2012 Increase rate by 1p per litre above changes in petrol and diesel duty rates, every year until 2014-15 inclusive

Forecast area	Element	Default indexation assumed in baseline	Pre-announced policy changes from 2012-13 onwards
VAT	VAT registration threshold	RPI,[7] rounded to the nearest £1,000	
Gaming Duty	Gross gaming yield bands	RPI,[7] rounded to the nearest £500	
Business Rates	Business rates multiplier	RPI,[3] rounded to the nearest 3 significant figures	

Notes

[1] and other allowances e.g. married couples allowance, blind persons allowance
[2] and consequential rates for other fuels e.g. rebated oils
[3] RPI is measured in the year to September prior to the respective change
[4] CPI is measured in the year to September prior to the respective change
[5] RPI is measured in the year to the third quarter prior to the respective change
[6] RPI is measured in the year to the third quarter following the respective change
[7] RPI is measured in the year to December prior to the respective change

Office for
Budget
Responsibility

Certification of policy costings

B Office for Budget Responsibility: certification of policy costings

Office for Budget Responsibility: certification of policy costings

B.1 The Office for Budget Responsibility (OBR), led by the Budget Responsibility Committee (BRC), has certified that all of the costings of Budget 2012 policies described in this document represent a reasonable and central view given the information currently available.

B.2 The OBR has not scrutinised the costings of policies within Departmental Expenditure Limits (DELs) where the total cost or yield is wholly determined by a Government policy decision. This includes, for example, the funding of the Aerodynamics centre and the Science capital investment fund for universities.

Methodology

B.3 All costings have been produced on the basis of the OBR's economic forecast published in the March 2012 *Economic and fiscal outlook*.

B.4 The OBR scrutinises the costings submitted by Government departments that are produced using the methodologies set out in this document. These costings take into account the direct effects of a policy on the component of taxes or spending to which the policy applies, and closely-related components. They do not take into account the indirect effect of policy measures on the wider economy. Any such effects are incorporated in the OBR's economic forecast. Measures with such effects in this Budget are set out from paragraph B.8. This summer, we intend to work jointly with the Government to publish a briefing paper explaining in more detail our joint approach to producing policy costings.

Scrutiny and challenge process

B.5 Along with the officials responsible for producing each costing, the OBR attended a series of Star Chamber meetings, at which the assumptions, judgements and methodology used in each costing were scrutinised by the BRC and OBR staff. The OBR was provided with detailed analysis and had full access to the information used in the costings. In the cases where the BRC felt that a different methodology or judgement was required, changes were made to the costings in line with BRC views, and a further set of discussions took place. Through this iterative process of scrutiny, the BRC was able independently to challenge the Government's costings in detail, and ensure its views were fully reflected in the Treasury's final costings.

Uncertainty

B.6 The OBR emphasises the uncertainty which surrounds forecasts of the public finances. Policy costings are subject to a similar, if not greater, level of uncertainty for a number of reasons. In many cases, costings are highly sensitive to assumptions about the future behavioural responses of taxpayers or benefit recipients. So, for example, capital gains tax policy can have an unpredictable effect on the levels of error, fraud and avoidance in the tax system. In addition, it is difficult to analyse the accuracy of previous policy costings to draw lessons for future costings, as it is analytically complex to separate the eventual cost or yield associated with a particular measure from other changes in total receipts and expenditure and requires a suitable counterfactual. In the case of the additional rate of income tax, this is set out in HMRC's report, published alongside Budget 2012.

B.7 In respect of the specific policy costings at this Budget the OBR identified the following areas of particular uncertainty:

- Reduction in the additional rate of income tax to 45p in 2013-14: the estimate of the impact of this policy is based on the evaluation by HMRC of the revenue raised by the 50 per cent additional rate. As the HMRC report emphasises, the results of this evaluation are highly uncertain. A more detailed discussion of these uncertainties and the implication of the costing for our forecast can be found in our March *Economic and fiscal outlook*.[1]
- Cap on unlimited income tax reliefs: this policy will affect those subject to the additional rate of income tax. Predicting how those affected by this policy will respond to it relies heavily on assumptions as there is limited evidence on which to base these judgements. Furthermore for simplicity this costing assumes that the earnings of the tax payers affected are subject to a marginal rate of income tax of 45 per cent; however in reality tax payers may face lower effective tax rates as they may receive large proportions of their income in dividends. Their effective rates of income tax will also affect how additional rate tax payers respond to this policy.
- Stamp Duty Land Tax avoidance measures: the uncertainties in these costings derive from the difficulty in forecasting the number of properties worth £2 million or above that are transferred to envelopes. Some properties may have been enveloped for reasons other than tax-avoidance so it is difficult to predict how many properties will remain in the envelope and how many will be removed following the introduction of an annual charge. Furthermore the introduction of a stamp duty rate of 7 per cent on properties worth than £2 million interacts with these policy changes, and could affect behaviour of those affected in unforeseen ways.
- Confirmation of announced Controlled Foreign Companies (CFC) rules: this policy, originally introduced at Budget 2011, has been subject to reform and so the OBR was presented with a new estimate of the cost. Since Budget 2011, HMRC has conducted a survey which has provided them with more information on the types of companies affected by this policy. However, considerable uncertainty remains around the behavioural responses by these companies to the rules.
- Machine Games Duty: this measure does not appear in the Treasury's table of Budget policy decisions because the central estimate of the cost is under £5 million a year. However, the measure replaces Amusement Machine Licence Duty (AMLD) and the VAT charge on gaming machines, which together raise about £600 million a year, with a new tax, Machine Games Duty. (MGD). The intention is for the change to be fiscally neutral and the tax rates for MGD were chosen accordingly, but the actual yield of MGD will depend on the behavioural responses of gaming companies and consumers. If their response is different to the assumptions underlying this costing then this policy change could either raise or reduce gaming receipts by a significant amount.
- Paying down the housing debt: This policy is expected to increase property sales which should lead to increased public sector net capital receipts, partially offset by lower net public sector income. However there is particular uncertainty around the level of increased sales that the higher Right to Buy discounts will encourage.

[1] The OBR's March 2012 *Economic and fiscal outlook* is available on the OBR's website: http://budgetresponsibility.independent.gov.uk/

Indirect effects on the economy forecast

B.8 The main effect on the OBR's economy forecast from policy changes is the reduction in the main rate of corporate tax. We estimate that this will reduce the cost of capital faced by firms and increase the level of business investment by around 1 per cent by the end of the forecast period. This judgement is the same as was reached by the interim OBR with regards to the cut in corporation tax in the June 2010 Budget. We have also adjusted the inflation forecast to reflect the impact of measures on VAT and tobacco. We have made no other material adjustments to the economy forecast as a result of Budget 2012 policy announcements.

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This document can be found in full on our website: http://www.hm-treasury.gov.uk

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