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## BRIEFING PAPER

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# Spring Budget 2017: A summary

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# Summary: Spring Budget 2017 at a glance

[Spring Budget 2017](#) was presented by the Chancellor of the Exchequer to Parliament on 8 March. At the same time the Office for Budget Responsibility (OBR) published updated forecasts in its [economic and fiscal outlook](#).

## Government announcements

### Tax

- The **main rate of self-employment Class 4 National Insurance contributions to rise** from 9% to 10% in April 2018 and 11% in April 2019. The Class 4 rate is currently levied on self-employment profits above £8,060. This change raises between £325 million and £645 million a year. **This change and the Chancellor's decision to reverse it are discussed in section 3 of this briefing.**
- The **tax-free allowance for dividend income to be reduced** from £5,000 to £2,000 from April 2018. This change raises over £800 million a year from 2019/20. **This change is discussed in section 3 of this briefing.**
- Local authorities to receive around £300 million over the next three years to provide discretionary **support for businesses** facing increases in business rates bills following April 2017's **business rates revaluation in England.**
- Additional funding of £20-25 million a year to **support some businesses that no longer receive small business rate relief after the revaluation.**
- A **25% charge** to be introduced targeted at those seeking to reduce the tax payable by **moving their pension wealth to another jurisdiction.** This change raises around £60 million a year.
- **UK VAT of 20% will apply to mobile phone use by UK residents when outside the EU.** Currently VAT is applied when UK residents use their mobile phone inside the EU, but not when outside. The change ensures mobile phone companies cannot use the inconsistency to avoid UK VAT. This change raises around £65 million a year.

### Spending

- Local authorities in England to receive **£2 billion** of additional funding over the next three years to **spend on adult social services.**
- **NHS in England** to receive an additional **£100 million** in 2017/18 for capital investment in **A&E departments.** The funding will support up to 100 new GP triage projects.
- **NHS in England** to receive **£325 million** over the next three years to invest in local Sustainability and Transformation Plans

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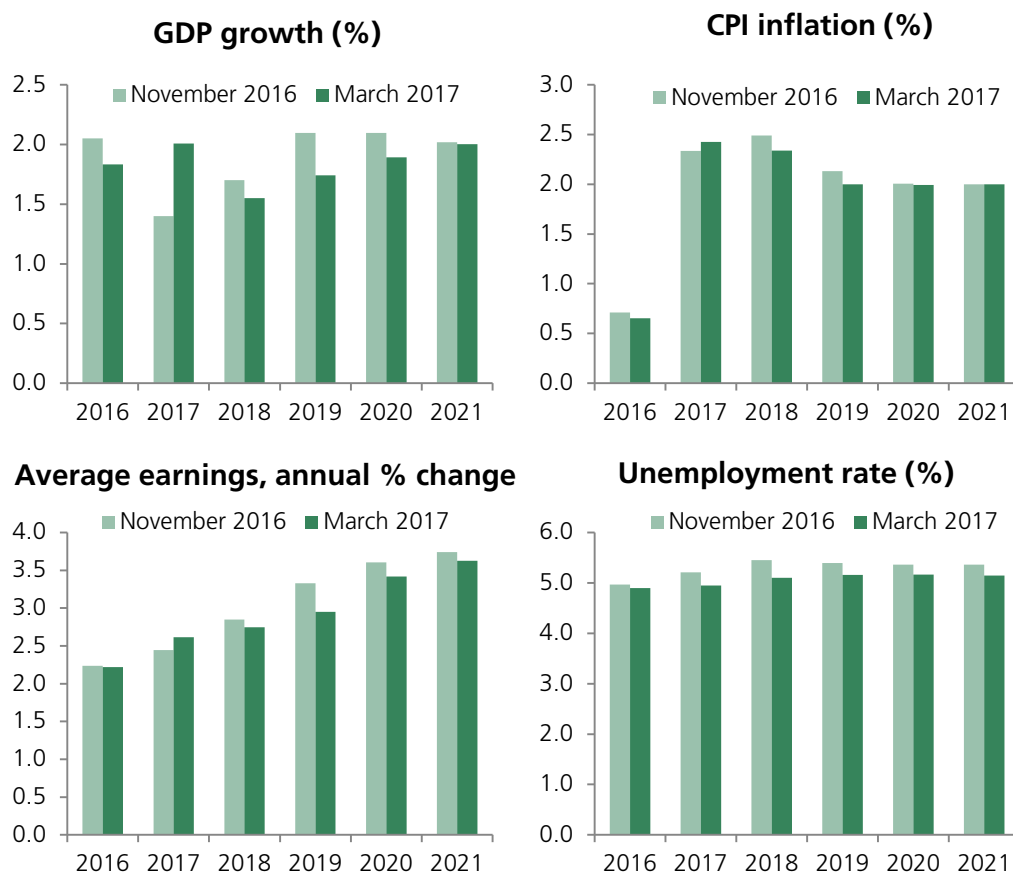
(STPs). STPs are locally developed proposals to improve local health and care.

- **£320 million** of additional spending this Parliament to extend the **free schools programme** introducing new schools in England, including selective schools. Over **£500 million** will be provided in 2021/22.
- Additional funding for **16-19 technical education** in England. New T-levels, offering technical training routes, will be introduced from 2019/20. Around £300 million will be provided during this Parliament.
- An additional **£216 million** spread over 2018/19 and 2019/20 for **school maintenance**.
- The **Scottish Government** (£350 million), **Welsh Government** (£200 million) and **Northern Ireland Executive** (£120 million) receive additional funding through the Barnett formula.

# 1. OBR forecasts for the economy

In its March 2017, forecasts compared with its November 2016 forecasts, the OBR:

- expects annual GDP growth to be higher in 2017 but lower in 2018, 2019 and 2020. The forecast for the overall level of GDP from 2019 is very similar;
- has left its CPI inflation forecasts broadly unchanged;
- has raised average annual earnings growth forecasts for 2017 but lowered them in every year afterwards;
- has lowered its unemployment rate forecasts in each year.



## OBR forecasts: economy

	2015	2016	2017	2018	2019	2020	2021
<b>GDP growth (%)</b>							
November 2016	2.2	2.1	1.4	1.7	2.1	2.1	2.0
<b>March 2017</b>	<b>2.2</b>	<b>1.8</b>	<b>2.0</b>	<b>1.6</b>	<b>1.7</b>	<b>1.9</b>	<b>2.0</b>
<b>CPI inflation (%)</b>							
November 2016	0.0	0.7	2.3	2.5	2.1	2.0	2.0
<b>March 2017</b>	<b>0.0</b>	<b>0.7</b>	<b>2.4</b>	<b>2.3</b>	<b>2.0</b>	<b>2.0</b>	<b>2.0</b>
<b>ILO unemployment rate, %</b>							
November 2016	5.4	5.0	5.2	5.5	5.4	5.4	5.4
<b>March 2017</b>	<b>5.4</b>	<b>4.9</b>	<b>4.9</b>	<b>5.1</b>	<b>5.2</b>	<b>5.2</b>	<b>5.1</b>
<b>Average earnings, % change on previous year</b>							
November 2016	1.8	2.2	2.4	2.8	3.3	3.6	3.7
<b>March 2017</b>	<b>1.9</b>	<b>2.2</b>	<b>2.6</b>	<b>2.7</b>	<b>3.0</b>	<b>3.4</b>	<b>3.6</b>

## 2. OBR forecasts for the public finances

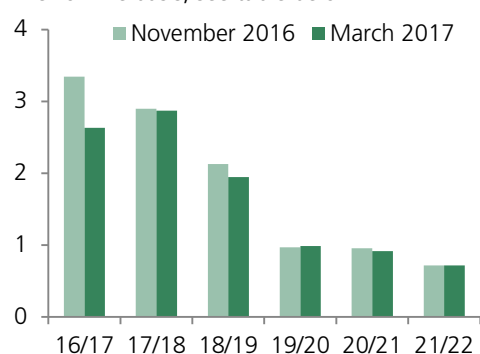
In its March 2017 forecasts, compared with its November 2016 forecasts, the OBR:

- lowered its forecast for borrowing in 2016/17 by £13.4 billion (on a like-for-like basis) to £51.7 billion, or from 3.3% of GDP to 2.6%;
- expects broadly similar borrowing in each year from 2017/18 to 2021/22, which means the deficit will rise in 2017/18 compared with 2016/17 before falling in future years;
- forecasts debt as a proportion of GDP to be lower in all years.

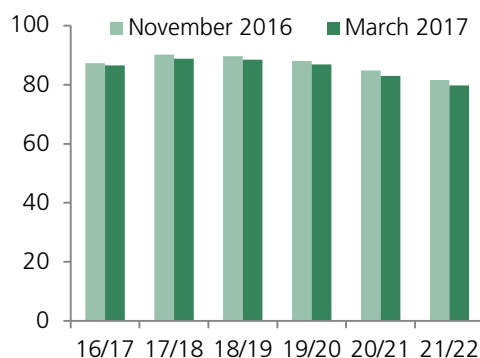
The OBR assesses that the Government is more likely than not to meet its fiscal targets for: (i) the cyclically-adjusted, or structural, deficit to be below 2% of GDP by 2020/21, and (ii) debt to be falling as a percentage of GDP by 2020/21.

### Public sector net borrowing, % of GDP

Like-for-like basis, see table below



### Public sector net debt, % of GDP



### OBR forecasts: public finances

	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22
<b>Net borrowing*, £ billion</b>							
November 2016	74.7	65.2	58.0	44.3	21.0	21.5	16.8
<b>March 2017</b>	<b>71.7</b>	<b>51.7</b>	<b>58.3</b>	<b>40.8</b>	<b>21.4</b>	<b>20.6</b>	<b>16.8</b>
<b>Net borrowing*, % of GDP</b>							
November 2016	4.0	3.3	2.9	2.1	1.0	1.0	0.7
<b>March 2017</b>	<b>3.8</b>	<b>2.6</b>	<b>2.9</b>	<b>1.9</b>	<b>1.0</b>	<b>0.9</b>	<b>0.7</b>
<b>Cyclically adjusted net borrowing, % of GDP</b>							
November 2016	3.8	3.3	2.6	1.8	0.8	0.8	0.7
<b>March 2017</b>	<b>3.6</b>	<b>2.6</b>	<b>2.9</b>	<b>1.9</b>	<b>0.9</b>	<b>0.9</b>	<b>0.7</b>
<b>Net debt, £ trillion</b>							
November 2016	1.61	1.72	1.84	1.90	1.95	1.95	1.95
<b>March 2017</b>	<b>1.61</b>	<b>1.73</b>	<b>1.83</b>	<b>1.89</b>	<b>1.92</b>	<b>1.90</b>	<b>1.90</b>
<b>Net debt, % of GDP</b>							
November 2016	84.2	87.3	90.2	89.7	88.0	84.8	81.6
<b>March 2017</b>	<b>83.6</b>	<b>86.6</b>	<b>88.8</b>	<b>88.5</b>	<b>86.9</b>	<b>83.0</b>	<b>79.8</b>

\* Like-for-like basis adjusting the Nov'16 forecast for ONS accounting treatment change

## 3. Personal tax measures

### Summary

In the Budget the Chancellor announced two reforms to personal taxation:

- The main rate of Class 4 NICs, paid by the self-employed, will increase from 9% to 10% from April 2018, and from 10% to 11% from April 2019. This is forecast to raise £325m in 2018/19, rising to £645m in 2019/20.<sup>1</sup>
- The dividend allowance – the annual amount of dividend income that individuals may receive tax free – will be reduced from £5,000 to £2,000 from April 2018. This is forecast to raise £870m in 2019/20.<sup>2</sup>

[In his Budget speech](#) Mr Hammond set out his case that these changes were necessary, to reduce the differential between the taxation of employees and the self-employment, and between both employees and the self-employment and those working through a company. In the former case, HM Revenue & Customs have estimated that the foregone NI revenue from the lower rates of NICs paid by the self-employed, compared with employees, will cost the public finances £5.1bn in 2016/17.<sup>3</sup> In the latter case, last year the Office for Budget Responsibility published estimates showing the Exchequer cost of individuals shifting towards working through a small company rising from £1.0bn in 2016/17 to £3.5bn by 2020/21.<sup>4</sup>

In his speech the Chancellor noted that the Government had already announced that from April 2018 it would abolish Class 2 NICs, the flat rate charge also paid by the self-employed. This reform is forecast to cost £405m in 2018/19, rising to £430m in 2019/20.<sup>5</sup> The Budget report estimates that taken together, these changes to self-employed NICs would mean that individuals would pay more in NICs if their annual profits exceed £16,250 in 2019/20.<sup>6</sup>

In the Autumn Statement last November the Chancellor had said the Government would “consider how we can ensure that the taxation of different ways of working is fair between different individuals doing essentially the same work, and sustains the tax base as the economy undergoes rapid change.”<sup>7</sup> The Budget report confirmed that there would be a consultation on reforming the taxation of accommodation benefits, and that the Government will gather evidence on the tax rules as they apply to benefits in kind and employee expenses.<sup>8</sup>

However on 15 March the Chancellor announced that the Government would *not* proceed with the first of these reforms: in a letter to the Chair of the Treasury Select Committee Mr Hammond stated that there “would be no increases in NIC rates in this Parliament” though the Government would “continue with the abolition of Class 2 NICs from April 2018.” The cost of reversing this measure “will be funded by measures to be announced in the Autumn Budget.”<sup>9</sup>

<sup>1</sup> *Spring Budget 2017*, HC 1025, March 2017 p 26 (Table 2.1 – item 15). Receipts are forecast to fall in later years: £595m in 2020/21, and £495m in 2021/22.

<sup>2</sup> *Spring Budget 2017*, HC 1025, March 2017 p 26 (Table 2.1 – item 16). Receipts in later years are forecast to be: £825m in 2020/21, and £930m in 2021/22.

<sup>3</sup> See, HMRC, *Estimated costs of main tax reliefs*, January 2017

<sup>4</sup> OBR, *Economic & Fiscal Outlook*, Cm 9346, November 2016 p121 ([Box 4.1](#))

<sup>5</sup> *Spring Budget 2017*, HC 1025, March 2017 p 29 (Table 2.2 – item am). The cost of this measure is forecast to fall in later years: £380m in 20/21, and £350m in 21/22.

<sup>6</sup> *Spring Budget 2017*, HC 1025, March 2017 para 3.5. see also, HM Treasury, [NI and the self-employed factsheet](#), March 2017 para 1.23-4

<sup>7</sup> [HC Deb 23 November 2016 c907](#)

<sup>8</sup> *Spring Budget 2017*, HC 1025, March 2017 para 3.7

<sup>9</sup> HM Treasury, [Letter from the Chancellor to the Chair of the Treasury Select Committee](#), 15 March 2017. See also, [HC Deb 15 March 2017 cc420-1](#)

### 3.1 National Insurance contributions - current structure

National insurance benefits are funded by a system of compulsory contributions on earnings, paid by employees, employers and the self-employed. Receipts from these contributions – NICs, for short – are paid into the National Insurance Fund, kept separate from all other revenue raised by national taxes. A fixed proportion of NI receipts are not paid into the Fund but go to the National Health Service. The National Insurance Fund is used exclusively to pay for contributory benefits, and operates on a ‘pay as you go’ basis: broadly speaking, this year’s contributions pay for this year’s benefits.<sup>10</sup>

National Insurance contributions (NICs) raised an estimated £125bn in 2016/17. This compares with estimated Exchequer receipts from income tax of £175bn, and £121bn from VAT.<sup>11</sup>

**Employees** are liable to pay National Insurance contributions (NICs) on their earnings if they exceed the lower earnings limit (LEL). The LEL is set at £113 per week for 2017/18.

A zero rate of NICs is charged on earnings between the LEL and the primary threshold (PT), which is set at £157 per week. A notional primary Class 1 NIC is deemed to have been paid in respect of earnings between LEL and PT to protect benefit entitlement.

Earnings above the PT are charged NICs at a rate of 12%, subject to a cap at the upper earnings limit (UEL), which is set at £866 per week. Earnings *above* the UEL are charged NICs at a rate of 2%.

Prior to 6 April 2016 employees were charged a reduced rate of NICs if they had contracted out of the state second pension (S2P). These arrangements have ended with the introduction of the new ‘single-tier’ state pension, and the closure of the additional state pension.<sup>12</sup>

**Employers** pay NICs on employee earnings at a rate of 13.8% on earnings above the secondary threshold (ST). The ST is set at £157 a week for 2017/18.

In the 2013 Autumn Statement the Government announced that from April 2015 it would abolish employer NICs on earnings for employees under 21, on earnings up to the higher rate threshold.<sup>13</sup> From this date a zero rate has applied to earnings on this category of employee up to the ‘upper secondary threshold’ (UST), set in line with the UEL.

<sup>10</sup> For more background on the operation of NI see, [National Insurance contributions: an introduction](#), Commons Briefing paper SN4517, 21 December 2015

<sup>11</sup> OBR, *Economic & Fiscal Outlook*, Cm 9419, March 2017 p104 ([Table 4.6](#))

<sup>12</sup> For details see, [The new ‘single-tier’ State Pension](#), Commons Briefing paper SN6525, 30 August 2016.

<sup>13</sup> [Autumn Statement, Cm 8747, December 2013](#) para 1.195



In December 2014 the Government announced that it would abolish employer NICs up to the UEL for apprentices aged under 25, with effect from April 2016.<sup>14</sup> Consequently a zero rate also applies to earnings on this second category of employees up to a new 'apprentice upper secondary threshold' (AUST), which is also aligned with the UEL. The UST and AUST are set at £866 per week for 2017/18.

**Self-employed people** pay a weekly flat rate Class 2 NIC (set at £2.85). They may apply for exemption from paying class 2 contributions if their annual profits are less than the level of the 'small profits threshold' (SPT), set at £6,025. In addition they may be liable to pay a separate Class 4 profits related contribution. Class 4 NICs are charged at a rate of 9% on profits between a lower annual profits limit (£8,164) and an annual upper profits limit (£45,000 – all figures for 2017/18). Profits above the upper limit are charged NICs at a rate of 2%.

**Further to these categories, individuals** may be entitled to make voluntary Class 3 contributions to ensure that they qualify for basic retirement pension and bereavement benefits. Class 3 NICs are charged at a weekly flat rate, set at £14.25 for 2017/18.<sup>15</sup>

### 3.2 The 'Tax Lock'

In its 2015 General Election manifesto the Conservative Party stated that, in government, it would "not increase the rates of VAT, Income Tax or National Insurance in the next Parliament."<sup>16</sup> In a speech the Prime Minister David Cameron confirmed that this 'tax lock' also meant that there would not be any extension to the scope of VAT, or an increase in the ceiling set for the main rate of National Insurance contributions (NICs) by employees - the 'Upper Earnings Limit' (UEL).<sup>17</sup>

For its part, in its manifesto the Labour Party stated that, in government, it would "not increase the basic or higher rates of Income Tax or National Insurance. Nor will we raise VAT", though it confirmed that it would reverse the Coalition Government's decision to cut the additional rate of income tax from 50p to 45p.<sup>18</sup>

In its analysis of the parties' tax and spending proposals the Institute for Fiscal Studies (IFS) noted that these commitments did not rule out increases in these taxes through other measures:

The Conservatives ... have pledged not to increase the rates of income tax, National Insurance contributions (NICs) or value added tax (VAT) during the next parliament ... Like the Conservative Party, Labour has pledged *not* to implement certain kinds of tax rises ... their manifesto rules out increases to the basic and higher rates of income tax or rates of National Insurance; and it rules out increasing rates of VAT, as well as extending the VAT base to include food, children's clothes, books, newspapers or public transport fares.

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<sup>14</sup> [Autumn Statement, Cm 8961, December 2014 para 2.53](#)

<sup>15</sup> Government Actuary's Department, [Report to Parliament on the 2017 re-rating and up-rating orders](#), January 2017 pp22-23

<sup>16</sup> Conservative Party, [2015 General Election Manifesto](#), April 2015 p27

<sup>17</sup> "Cameron pledges to ban tax rises until 2020", *Financial Times*, 29 April 2015. Mr Cameron also publicised this commitment [on Twitter](#).

<sup>18</sup> Labour Party, [2015 General Election Manifesto](#), April 2015 p18, p27

This does not rule out raising more revenue from these taxes in other ways: they could, for example, change income tax or National Insurance thresholds, or implement further restrictions to income tax relief on pension contributions. These could affect many of the same people, via the same tax, as the hypothetical tax rises that they have ruled out.<sup>19</sup>

Writing in the *Financial Times*, the paper's economics editor, Chris Giles, argued that such pledges were "positively dangerous":

Britain's income tax already bears the hallmarks of commitments not to increase the main rates. Labour and Tory-led governments since 2000 have complicated the levy, introducing higher rates over large slices of income, necessary to remove the financial benefits of child benefit and the personal allowance from richer people.

Income taxation is further complicated by national insurance, an income tax in all but name, from which pensioners are exempt and which uses a different definition of income: all of which encourages the tax avoidance industry that politicians say they abhor. When individuals arrange their affairs quite legitimately to avoid taxation, it is no surprise productivity suffers as they waste time minimising tax bills rather than doing something more productive.<sup>20</sup>

Following the General Election, the then Chancellor George Osborne presented the Conservative Government's first Budget on 8 July. In his Budget speech Mr Osborne confirmed that "in the coming weeks" the Government would legislate to "prohibit any increase in the main rates of income tax, national insurance and VAT for the next five years."<sup>21</sup> The Budget report explained that provision to this effect would be included in a Summer *Finance Bill*, to be presented on the conclusion of the Budget debates:

The government will legislate to set a ceiling for the main rates of income tax, the standard and reduced rates of VAT, and employer and employee (Class 1) NICs rates, ensuring that they cannot rise above their current (2015-16) levels. The tax lock will also ensure that the NICs Upper Earnings Limit cannot rise above the income tax higher rate threshold; and will prevent the relevant statutory provisions being used to remove any items from the zero rate of VAT and reduced rate of VAT for the duration of this Parliament. (Summer Finance Bill 2015).<sup>22</sup>

Alongside the Finance Bill, the Government also published a second Bill to set the tax lock with regards to National Insurance.<sup>23</sup>

Statutory provisions regarding NI cannot be included in the annual Finance Bill. This is because the Bill's remit – as set out in its long title – specifically excludes any tax that does not raise money for financing

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<sup>19</sup> [Taxes and Benefits: The Parties' Plans - IFS Briefing Note BN172](#), April 2015 p12, p29. See also, "Triple tax lock puts other revenue sources in spotlight", *Financial Times*, 28 May 2015.

<sup>20</sup> "The battle for Britain's most reckless tax pledge", *Financial Times*, 8 April 2015; see also, "Cameron's pledges unwise or costly or both, says Lawson", *Financial Times*, 29 April 2015

<sup>21</sup> [HC Deb 8 July 2015 c336](#)

<sup>22</sup> *Budget 2015*, HC 264, March 2015 [para 2.53](#). In turn provision was made by ss1-2 of the *Finance (No.2) Act 2015*.

<sup>23</sup> Details of the scrutiny given the [National Insurance Contributions \(Rate Ceilings\) Act 2015](#) are on its [Parliament Bill page](#). See also, [Commons Library Briefing CBP7260](#), 29 February 2016.

central government *as a whole*. Usually the long title of the Finance Bill is of the form, “a Bill to grant certain duties, to alter other duties, and to amend the law relating to the National Debt and the Public Finance, and to make further provision in connection with finance.” As a consequence the Bill cannot include provisions relating to NICs, as those NI receipts paid into the National Insurance Fund may only be used to meet the costs of contributory benefits.<sup>24</sup>

Notably the most recent change in the rates of NICs – the 1% point increase in NI rates for employees, employers and the self-employed, from April 2011 – was introduced by the [National Insurance Contributions Act 2011](#).

### 3.3 Abolition of Class 2 NICs

In his Budget statement in March 2015 the then Chancellor George Osborne announced that “to support 5 million people who are self-employed and to make their tax affairs simpler, we will, in the next Parliament, abolish entirely Class 2 National Insurance contributions for the self-employed.”<sup>25</sup> In December 2015 the Government launched [a consultation](#) on the design of new contributory tests, so that the self-employed would continue to have access to contributory benefits when Class 2 NICs were abolished. In the Autumn Statement in November 2016 the Government confirmed it would proceed with its plans to abolish Class 2 NICs, with effect from April 2018.<sup>26</sup>

Further details were published the following month.<sup>27</sup> From April 2018 the self-employed would gain access to contributory benefits based on a profits test in Class 4 NICs. A new zero-rate band would be introduced into Class 4 NICs on profits between the Small Profits Limit (replacing the Class 2 Small Profits Threshold) and the Lower Profits Limit:

In April 2018, Class 4 will be reformed to confer entitlement to the new State Pension and other contributory benefits.

- The contribution conditions attached to the new State Pension and other contributory benefits will be changed to enable Class 4 NICs to count towards benefit entitlement.
- A new zero-rate band of Class 4 NICs will apply on annual profits between a threshold to be known as the Small Profits Limit (SPL) and the Lower Profits Limit (LPL, the point beyond which Class 4 NICs become payable).
- This means that self-employed individuals with annual profits at or over the SPL will be able to gain qualifying years (QYs) for benefit entitlement.
- The SPL will be aligned with the annual equivalent of the Lower Earnings Limit (LEL) in Class 1 employee NICs.

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<sup>24</sup> For more details on these procedures see, [The Budget and the annual Finance Bill](#), Commons Briefing Paper SN813, 13 February 2017.

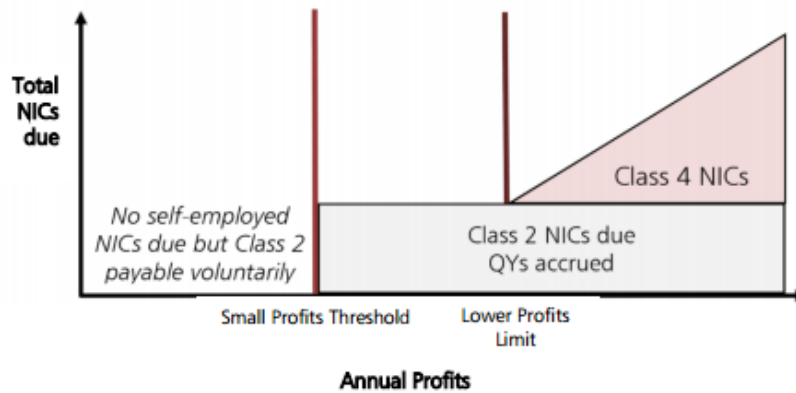
<sup>25</sup> HC Deb 18 March 2015 c777

<sup>26</sup> *Autumn Statement*, Cm 9362, November 2016 para 4.8

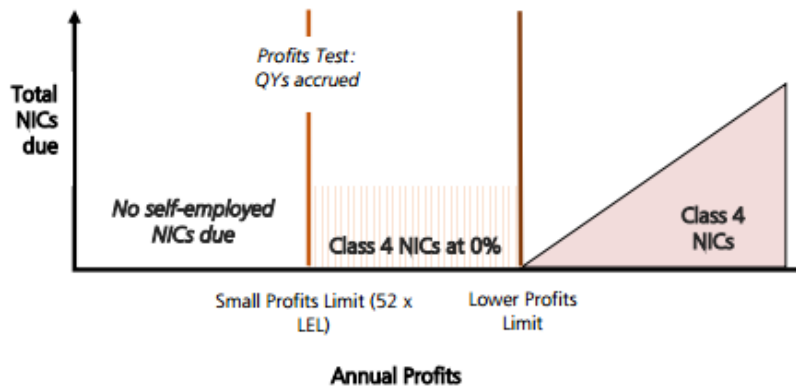
<sup>27</sup> HM Revenue & Customs, [Abolition of Class 2 National Insurance contributions: tax information & impact note](#), December 2016

The existing and proposed systems are shown in Figures 2.A and 2.B.

**Figure 2.A: The existing Class 2 and 4 NICs structure**



**Figure 2.B: The proposed Class 4 NICs structure**



(QY = Qualifying Year towards the State Pension)

This reform means that self-employed individuals will gain access to benefits if their profits are over the SPL, even though Class 4 NICs are only paid on profits over the LPL. This is consistent with the rules in place for employees, who are treated as having paid Class 1 NICs with earnings between the LEL and the Primary Threshold in an earnings period. By aligning the way in which employees and the self-employed gain access to benefits based on their earnings or profits, this reform also makes the NICs system simpler and more equitable for all.<sup>28</sup>

Individuals whose profits fall below the Small Profits Limit would be able to protect their entitlement to the State Pension by taking up the option of paying Class 3 NICs. As noted above, employees whose earnings are too low to be liable for NICs may protect their benefit entitlement by paying Class 3 NICs, though at present the rate of Class 3 is considerably higher than the rate of Class 2.

Many respondents to the Government’s consultation paper raised concerns that people who were paying Class 2 NICs voluntarily would have to pay considerably more in tax if they wish to protect their entitlement to the State Pension. In its response the Government argued

<sup>28</sup> [Abolishing Class 2 and reforming Class 4 National Insurance contributions: response to the consultation](#), December 2016 pp7-8

that relatively few individuals in this position would have to pay Class 3 NICs...

The government wants to ensure that self-employed individuals who have profits below the SPL can continue to gain access to the new State Pension. There is already protection in the NICs system for these individuals to do this:

- government analysis suggests that in 2018-19, around 77%<sup>29</sup> of all self-employed individuals expected to have profits below the SPL will see their State Pension record protected by NI contributions from employment alongside self-employment, by NI credits or will already have a full State Pension record<sup>30</sup>
- the remainder will still be able to pay Class 3 voluntary NICs to gain access to the new State Pension for those years in which their profits were below the SPL. Class 3 NICs can usually be paid for up to six years after the year in which an individual did not achieve a qualifying year. Individuals are able to check their National Insurance record on their Personal Tax Account (via GOV.UK) before deciding whether to pay Class 3 voluntary NICs<sup>31</sup>
- an individual needs 35 years of NICs and/or NI credits to qualify for the full rate of the new State Pension. NICs are currently payable by those aged between 16 and State Pension age, which means that an individual could have up to 15 years of gaps in their National Insurance record without their State Pension award being affected
- the median duration of self-employment is between six and ten years (Department for Work and Pensions analysis). This means that those with profits below the SPL are unlikely to rely solely on their profits for their entire working lives

Analysis suggests that those expected to pay Class 3 NICs in any one year following the abolition of Class 2 would represent only 5% of those with profits below the SPL in 2018-19, and around 2% of all self-employed individuals who may have self-employment profits.<sup>32</sup>

... and that the introduction of the new State Pension will mean that the self-employed will be able to gain a greater amount of pension than they had in the past:

#### **Box 2.A: The self-employed and the new State Pension**

The new State Pension allows self-employed individuals to gain a greater amount of State Pension than they were able to in the past. Under the old system, Class 2 NICs counted towards the basic State Pension (a maximum of £119.30 a week in 2016-17, for 30 years of contributions). However, Class 2 NICs did not count for the earnings-related additional State Pension. This meant that in general, each qualifying year based on Class 2 NICs

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<sup>29</sup> This is based on HMRC forecasts. This figure also includes those who have already achieved the maximum number of qualifying years towards the State Pension.

<sup>30</sup> NI credits are available to individuals in certain circumstances and help to protect their future entitlement to contributory benefits. More information is available here: <https://www.gov.uk/national-insurance-credits/overview>.

<sup>31</sup> More information is available on how to check your National Insurance record is available here: <https://www.gov.uk/check-national-insurance-record>

<sup>32</sup> This is based on HMRC forecasts showing that there will be over 5 million self-employed individuals who may be liable to NICs in 2018-19.

in the 'old' system would only have been worth £3.98 of State Pension per week every year.

Under the new State Pension, all contribution years after 6 April 2016 will add a year of new State Pension in the same way for all classes of NICs and credits. That is 1/35 of the full amount for each post-2016 year. The full new State Pension is £155.65 a week in 2016-17, for 35 years of contributions.

Therefore, a qualifying year gained under the new system, including those by self-employed individuals, is worth £4.45 of State Pension per week. As a result, it will be possible for self-employed individuals to gain a much higher State Pension (with 35 years of any NI contributions) under the new State Pension system, than they could in the previous system (with 30 years of Class 2 NICs).<sup>33</sup>

### 3.4 Budget 2017: increases in rates of Class 4 NICs

In his Budget speech the Chancellor observed, "we have seen a dramatic increase in the number of people working as self-employed or through their own companies", but went on to argue, "people should have choices about how they work, but those choices should not be driven primarily by differences in tax treatment." Mr Hammond acknowledged that, historically, the lower rate of NICs paid by the self-employed reflected their limited access to social security benefits, but suggested the size of this disparity was no longer justified:

An employee earning £32,000 will incur, between him and his employer, £6,170 of national insurance contributions. A self-employed person earning the equivalent amount will pay just £2,300—significantly less than half as much. Historically, the differences in NICs between those in employment and the self-employed reflected differences in state pension entitlement and contributory welfare benefits, but with the introduction of the new state pension last year, these differences have been very substantially reduced ...

The most significant remaining area of difference is in relation to parental benefits, and I can announce today that we will consult in the summer on options to address the disparities in this area...

Such dramatically different treatment of two people earning essentially the same undermines the fairness of the tax system. Employed and self-employed alike use our public services in the same way, but they are not paying for them in the same way. The lower national insurance paid by the self-employed is forecast to cost our public finances over £5 billion this year alone. This is not fair to the 85% of workers who are employees.<sup>34</sup>

Mr Hammond noted that the size of this disparity would increase with the abolition of Class 2 NICs, and announced that in the light of this, the rate of Class 4 NICs would be increased to 11% by April 2019:

The abolition of class 2 NICs for self-employed people ... due to take effect in 2018 would further increase the gap between employment and self-employment. To be able to support our

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<sup>33</sup> [Abolishing Class 2 and reforming Class 4 National Insurance contributions: response to the consultation](#), December 2016 pp 9-10

<sup>34</sup> HC Deb 8 March 2017 cc813-4

public services in this Budget, and to improve the fairness of the tax system, I will act to reduce the gap to better reflect the current differences in state benefits.

I have considered the possibility of simply reversing the decision to abolish class 2 contributions, but the class 2 NIC is regressive and outdated—it is absolutely right that it should go—so, instead, from April 2018, when the class 2 NIC is abolished, the main rate of class 4 NICs for the self-employed will increase by 1% to 10%, with a further 1% increase in April 2019.

The combination of the abolition of class 2 and the class 4 increases I have announced today raises a net £145 million a year for our public services by 2021-22. That is an average of around 60p a week per self-employed person in this country. Since class 2 contributions are payable at a flat rate while class 4 is chargeable as a proportion of profits, all self-employed people earning less than £16,250 will still see a reduction in their total NICs bill.<sup>35</sup>

Further to the Chancellor's comments, the Budget report underlined that the Government would "consider whether there is a case for greater parity in parental benefits between the employed and self-employed", alongside the review of employment practices being undertaken by Matthew Taylor.<sup>36</sup> In October last year the Prime Minister appointed Mr Taylor (Chief Executive of the Royal Society of the Arts) to lead a review "to consider how employment practices need to change in order to keep pace with modern business models."<sup>37</sup>

In his speech the Chancellor noted that Mr Taylor's final report was expected in summer 2017, though "he is clear that differences in tax treatment are a key driver behind the trends we are observing—a conclusion shared by the Institute for Fiscal Studies and the Resolution Foundation."<sup>38</sup> Subsequently the Prime Minister was asked about this aspect of the Budget at the EU Council meeting on 9 March when she confirmed that the legislation to implement these reforms would be introduced in the autumn:

We've been very clear, the government was very clear that when the tax lock legislation was passed that it related to the class 1 national insurance contributions. Now of course it's class 1 that covers 85% of workers. The legislation was clear that it was honouring the 2015 manifesto and no amendments or concerns were raised at the time.

...The change to national insurance will require legislation of its own, it won't be part of the Finance Bill, that's always what happens with national insurance changes and those elements of the package will be brought forward by the autumn, as I say making lower paid self employed workers better off and we will publish a paper which will explain the full effects of the changes to class 2 and class 4, along with some changes we plan to make on rights and protections for self employed workers including on issues like pension rights and parental rights and maternity pay.<sup>39</sup>

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<sup>35</sup> HC Deb 8 March 2017 c814

<sup>36</sup> *Spring Budget 2017*, HC 1025, March 2017 para 3.5

<sup>37</sup> Details on the Review [are on Gov.uk](#).

<sup>38</sup> HC Deb 8 March 2017 c813

<sup>39</sup> No.10 Downing Street, [PM statement at European Council Meeting](#), 9 March 2017. See also, "Theresa May delays vote on self-employment tax rise", *Financial Times*, 10 March 2017



The Treasury published a number of examples of how these reforms would affect individuals on different profit levels, taking into account the projected increases in both the personal allowance and the higher rate threshold; an extract is reproduced below:<sup>40</sup>

**1.26** Chart 1.B shows the difference in tax and NICs paid at different profit levels between the start of the Parliament (2015-16) and when the changes to self-employed NICs take full effect in April 2019. Those on £17,500, £25,000 and £50,000 will gain overall, whereas the individual on £150,000 will not.



### 3.5 Budget 2017: reduction in the dividend allowance

Historically, income from dividends has been taxed differently to income from earnings or pensions, to take account of the fact that corporate profits will be subject to corporation tax, *and then* paid out in dividends or retained within the company. Prior to April 2016, dividend income was taxed at 10% up to the basic-rate limit, 32.5% between the basic-rate limit and the additional-rate limit, and 37.5% above that. However, this was offset by a dividend tax credit, which reduced the effective rates to 0%, 25% and 30.6% respectively.

In the Summer 2015 Budget the then Chancellor George Osborne, announced a major change in the taxation of dividend income:

We cut corporation tax from 28% to 20% over the last Parliament—one of the biggest boosts British business has ever seen. We cannot take it lower than that while such strong incentives are created for people to self-incorporate and pay the lower rates of tax due on dividends. The dividend tax system was designed partly to offset double taxation on profits, but the

<sup>40</sup> HM Treasury, [NI and the self-employed factsheet](#), March 2017 p6. Rates and thresholds are based on OBR projections for 2018-19 onwards. The government has committed to increase the income tax personal allowance to £12,500 and higher rate threshold to £50,000 by the end of the Parliament. All case studies apply to England, Scotland and Northern Ireland only, as the main rates and thresholds are devolved to Scotland.



system has not changed despite sharp reductions in corporation tax ...

I am today undertaking a major and long-overdue reform to simplify the taxation of dividends. The dividend tax credit will be replaced with a new tax-free allowance of £5,000 of dividend income for all taxpayers. The rates of dividend tax will be set at 7.5%, 32.5% and 38.1%—an increase of 7.5% where dividend income exceeds £5,000.

Dividends paid within pensions and ISAs will remain tax free and unaffected by these changes. Those who either pay themselves in dividends or have large shareholdings worth typically over £140,000 will pay more tax; 85% of those who receive dividends will see no change or will be better off; and over a million people will see their tax cut.<sup>41</sup>

Although there was relatively little comment on this reform at the time,<sup>42</sup> it was projected to raise considerable amounts of money.<sup>43</sup> It is to be expected that taxpayers will respond to a pre-announced tax increase by taking steps to mitigate its impact. In this case the scale of 'forestalling' appears to have been considerable, as noted in the OBR's *Economic & Fiscal Outlook* published alongside the 2017 Budget:

[The reforms to dividend taxation announced in the July 2015 Budget] came into effect in April 2016, giving those affected a period in which to bring forward dividend income into 2015-16 so that it was taxed at the lower rate. Dividends are subject to income tax (with the same thresholds but different rates) mainly via self assessment (SA), so 2015-16 liabilities were mostly paid in January and February 2017.

The original costing estimated that £7.6 billion of income would be brought forward to 2015-16, about two-thirds of this by additional rate taxpayers with incomes over £150,000 ... Preliminary HMRC analysis of 2015-16 SA returns suggests that forestalling of this change was underestimated by a significant amount. It is now estimated that £10.7 billion of dividend income (around 40 per cent more than originally predicted) was brought forward into 2015-16 ...

Our latest estimate is that dividend income shifting increased 2016-17 SA receipts by £4.0 billion (higher than the initial estimate of £2.6 billion) but will reduce future receipts by £4.8 billion. This implies that pre-announcing the policy allowed taxpayers to reduce their bills by around £0.8 billion at the same cost to the Exchequer. HMRC analysis suggests that around one pound in seven of that saving benefited just 100 individuals who were able to withdraw dividends averaging £30 million each from their companies before the higher tax rate took effect.<sup>44</sup>

Writing in the *Times*, Paul Johnson, director of the IFS observed, "this [analysis] tells us three important things. First, people really do respond to incentives created by the tax system where they can. Second, a small number of people pay a very large amount of tax (and we are quite

<sup>41</sup> [HC Deb 8 July 2015 cc331-2](#). See also, [Budget 2015, HC 264, July 2015 pp44-5](#)

<sup>42</sup> See, House of Lords Economic Affairs Committee, *The Draft Finance Bill 2016*, HL Paper 108, 4 March 2016 (see in particular, [para 65-86 of the report](#)).

<sup>43</sup> *Budget 2016*, HC 901, March 2016 p88 ([Table 2.2 – item ae](#)), and, HMRC, [Income tax: changes to dividend taxation – tax information & impact note](#), June 2016.

<sup>44</sup> OBR, *Economic & Fiscal Outlook*, Cm 9419, March 2017 [pp111-3 \(Box 4.3\)](#)

dependent on them to keep doing so). And third, there are some seriously wealthy people out there.”<sup>45</sup>

After setting out the Government’s proposals to increase the rate of Class 4 NICs, the Chancellor went on to announce a cut in the dividend allowance, arguing that there was “a parallel unfairness in the treatment of those working through their own companies”:

The gap in total tax and NICs between an employed worker and one who has set up his own company will normally be greater even than the gap with the self-employed, and there are several perfectly legal ways in which that gap can be made bigger still. This is not fair, and it is not affordable ...

The dividend allowance has increased the tax advantage of incorporation. It allows each director/shareholder to take £5,000 of dividends out of their company tax-free, over and above the personal allowance. It is also an extremely generous tax break for investors with substantial share portfolios.

I have decided to address the unfairness around director/shareholders’ tax advantage, and at the same time raise some much-needed revenue ... by reducing the tax-free dividend allowance from £5,000 to £2,000 with effect from April 2018. About half the people affected by this measure are director/shareholders of private companies. The rest are investors in shares with holdings typically worth over £50,000 outside individual savings accounts.<sup>46</sup>

The Budget report noted that a £2,000 allowance “will continue to mean that 80% of general investors pay no dividend tax, including those with sizeable investments (typically, up to £50,000).<sup>47</sup>

### 3.6 Initial reactions

There were a variety of reactions to the Government’s proposed reforms.

In the first day of the Budget debates after the Budget speech, the Leader of the Opposition, Jeremy Corbyn noted, “we have long argued for a clampdown on bogus self-employment, but today the Chancellor seems to have put the burden on self-employed workers instead. There has to be a something-for-something deal, so I hope the Chancellor will bring forward extra social security in return.”<sup>48</sup> Andrew Tyrie, Chair of the Treasury Committee, noted the Chancellor’s “strong argument for matching what people get out of NICs on the receipt side to the contribution side”, though on the question of whether the rise in Class 4 contravened the tax lock he added, “I will no doubt have a further discussion [with the Chancellor] when he comes before the Treasury Committee.”<sup>49</sup>

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<sup>45</sup> [“Dividend windfall shows high earners can be induced to pay”](#), *Times*, 8 March 2017. See also, “Chart that tells a story: Dividends bonanza was prompted by tax reforms”, *Financial Times*, 16 March 2017

<sup>46</sup> HC Deb 8 March 2017 cc814-5

<sup>47</sup> *Spring Budget 2017*, HC 1025, March 2017 para 3.6

<sup>48</sup> [HC Deb 8 March 2017 c825](#)

<sup>49</sup> [HC Deb 8 March 2017 c829](#)

Jonathan Edwards observed, “self-employed people do not have equal access to in-work benefits such as holiday pay, sick pay, auto-enrolment and parental leave. How, then, can it be right to put up the tax on self-employed people?”<sup>50</sup> Similarly Chris Leslie argued, “the self-employed do not have the same security [as employees], which is why we have had the discrepancy in the levels of taxation historically.”<sup>51</sup> By contrast Charlie Elphike said, “It is also important to have a level playing field for workers, be they employed or self-employed ... we have legislated to place a lock on class 1 national insurance contributions, VAT and income tax, but I think that class 4 contributions—as part of creating a more level playing field—are a different matter. For me, it is about fairness and pragmatism.”<sup>52</sup>

Much of the comment in the press focused on the Government apparently breaking its manifesto commitment regarding the ‘tax lock’.<sup>53</sup> An editorial in the *Daily Telegraph* argued, “since the country will rely more than ever upon its entrepreneurs and risk-takers it seemed at odds with that aim to increase tax on the self-employed, not least when such a move was specifically ruled out in the manifesto on which the Tories won the 2015 election.”<sup>54</sup> By contrast the *Guardian* took the view that “Mr Hammond’s contradiction of a promise in the 2015 Tory manifesto” was “courageous”, a sensible response to the “rapid, tax-incentivised growth of self-employment”, and, “[as the Resolution Foundation pointed out, a progressive move](#) partly because many highly paid professionals work as partners in firms and are treated as self-employed.”<sup>55</sup>

The *Times* expressed the view that, “it is reasonable ... for the Treasury to focus on those who have been gaming the system to pay less tax as “self-employed” than people doing similar work as employees. However, the self-employed also include millions of small business owners who are the foundation of an entrepreneurial culture that any Conservative government should be careful to incentivise, not penalise.”<sup>56</sup> The *Financial Times* observed that the rise in NICs would be “especially contentious”, and “all the more difficult because Mr Hammond is breaching a Conservative manifesto pledge”, although “politics aside, his decision is the right one ... If the government can find ways to put self-employed people on a more equal footing on

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<sup>50</sup> [HC Deb 8 March 2017 c847](#)

<sup>51</sup> [HC Deb 8 March 2017 c852](#)

<sup>52</sup> [HC Deb 8 March 2017 c847](#)

<sup>53</sup> “Hammond defends Budget rise in national insurance for self-employed”, *Financial Times*, 9 March 2017. See also, “[Spring Budget 2017 tax rise: What's the fuss about?](#)”, *BBC News*, 9 March 2017

<sup>54</sup> “[Leader: We still await a Budget for Brexit](#)”, *Daily Telegraph*, 9 March 2017. On similar lines see, “The Treasury and the self-employed”, [Adam Smith Institute blog](#), 10 March 2017.

<sup>55</sup> “[Editorial: The Guardian view on the spring budget: not enough](#)”, *Guardian*, 9 March 2017

<sup>56</sup> “Leader: Calculated risk”, *Times*, 9 March 2017

parental leave and other benefits, there may even be a case to go further.”<sup>57</sup>

Writing in the paper columnist Martin Wolf noted “the logic of equalisation is persuasive although [the Chancellor’s] backbenchers might well object,” while his colleague Janan Ganesh argued the rate rise “jars with the Conservative commitment to entrepreneurship. It is provocative in a country in which a large share of voters work for themselves, and hard to reconcile with promises made in the party’s 2015 election manifesto.”<sup>58</sup>

In an opinion piece the next day Judith Freedman, Pinset Masons professor of tax law at Oxford University, argued that critics of the NICs increase “may have fallen for three myths about changing working practices and around self-employment that risk undermining the reform process.”

First is the myth that it is desirable to encourage self-employment indiscriminately through the tax system. The “self-employed” ... [vary considerably in circumstance and income, and] untargeted, general tax reliefs cannot be calibrated to reflect all these situations ... The second myth is that tax and employment law changes are somehow necessitated by the recent rise of the so-called gig economy. Yet the structural problems have been with us for many years ...

The third myth is that tax and employment law operate on a unified basis ... Traditionally, tax classification has followed employment status. This is no longer necessarily the case: while tax law has stuck with a binary system (you are either self-employed or employed), employment law has developed a third, intermediary category (confusingly called “the worker”), which gives entitlement to basic protection including minimum wage and discrimination law.

Professor Friedman concluded “there is a real danger that if these myths are not debunked, the fundamental reform that is needed will become impossible politically.”<sup>59</sup>

The Chartered Institute of Taxation (CIOT) argued that the decision was ‘understandable’ but left wider questions about tax reform unaddressed:

If the Government truly intend to level the playing field the big factor is employer’s national insurance contributions. That is the ‘elephant in the room’ which went unmentioned by the Chancellor today. And at 13.8% this is a material cost for employers at a time when there is widespread concern about the impact on jobs of automation, offshoring and general economic uncertainty.<sup>60</sup>

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<sup>57</sup> “Editorial: Hammond has done what he can to prepare Britain’s defences for Brexit”, *Financial Times*, 9 March 2017. See also, “Self-employed give thumbs down to Hammond”, *Financial Times*, 10 March 2017

<sup>58</sup> “Budget 2017: An act of well-judged caution in risky times” & “Hammond risks a jab at the self-employed in the Budget of 2017”, *Financial Times*, 9 March 2017

<sup>59</sup> “Three myths about tax and the self-employed”, *Financial Times*, 10 March 2017

<sup>60</sup> CIOT press notice, [Budget 2017 – self-employed tax: time to open up the debate](#), 8 March 2017

In a second press notice the CIOT also raised concerns about the cut in the dividend allowance: "Clearly the 2015 reform of dividend taxation did not achieve its intended objective. We believe the key lesson is that there should be consultation in advance of such major changes, to ensure that the public understand the reasons for them, and that with the benefit of a proper debate, the Government are able to get the reforms right."<sup>61</sup>

There was also a division of opinion among business groups. Carolyn Fairbairn, director-general of the CBI Director-General said, "We understand the decision to introduce a simpler tax system by reducing the difference between employee and self-employed National Insurance Contributions, but it must continue to incentivise entrepreneurship."<sup>62</sup> By contrast, Mike Cherry, national chairman of the Federation of Small Businesses was strongly critical:

The genuinely self-employed are fundamentally different to employees – they are the risk takers that spearhead growth and productivity in our economy. ... this measure is a tax grab on middle income self-employed people, who are just about managing. ... Millions of self-employed will now face this tax hike, including plumbers, hairdressers, designers, musicians and many others in all our local communities.<sup>63</sup>

Finally the Resolution Foundation and the Institute for Fiscal Studies, which have both published recent work on the trends in self-employment and incorporation, and the tax drivers underpinning these trends,<sup>64</sup> commented on the impact of these reforms in their post-Budget analysis.

In the former case the Foundation described the abolition of Class 2 and the rise in Class 4 rates as a "sensible and modest tax change":

The greatest losers [from this reform] would be anyone earning above £47,000 – who would pay a little over £600 more tax each year. Given the way it's been reported, it might be worth repeating: most of the self-employed, and all of those on low earnings, will be better off at the end of this decade as result of these NI changes. If it's a tax hike it's not a very good one.<sup>65</sup>

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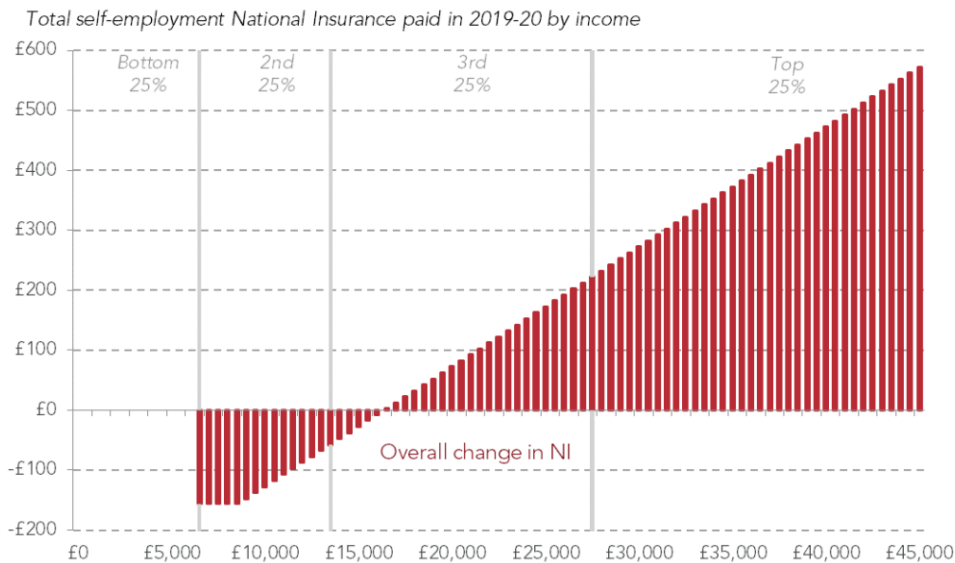
<sup>61</sup> CIOT press notice, [Changes to dividend tax allowance will not stop tax-motivated incorporation](#), 8 March 2017

<sup>62</sup> CBI press notice, [Our full reaction to the Budget](#), 8 March 2017

<sup>63</sup> FSB press notice, [Budget relief on rates but a tax grab on the self employed](#), 8 March 2017

<sup>64</sup> Resolution Foundation, [A tough gig? The nature of self-employment in 21st Century Britain and policy implications](#), February 2017 & Institute for Fiscal Studies, [Tax, legal form and the gig economy](#), 2 February 2017

<sup>65</sup> ["A small and sensible National Insurance rise for the self-employed is not the real strivers tax"](#), *Resolution Foundation blog*, 10 March 2017



In a separate blog post the director of the Foundation, Torsten Bell, argued that because, in his view, the amounts raised by this reform were “so tiny” that “it’s worth reflecting on why the Chancellor is acting”:

It can’t be just to raise revenue, because there are hundreds of easier ways to do that like scrapping expensive and unwise corporation tax cuts between now and 2020 that would raise £5bn. So the Chancellor’s action is not about the revenue raised but the incentives changed. He and many others rightly recognise that fast growing self-employment combined with a much lower tax take for each person that is self-employed is posing an ever growing risk to our public finances. Or to put it another way, to everyone else’s tax bill and public services.<sup>66</sup>

In his presentation on the 2017 Budget, the director of the IFS, Paul Johnson, identified the reforms to NICs, and the cut in the dividend allowance as, the “only two tax changes of any substance” that had been announced by the Chancellor:

The former is a modest but welcome change designed to shore up the tax base and create a slightly less unequal playing field between the self-employed and employees. The latter reflected the concern that if you increase tax on the self-employed you increase their incentive to incorporate. It undoes most of a change introduced less than a year ago.<sup>67</sup>

Mr Johnson went on to argue that the reforms were “baby steps in the right direction”, but was strongly critical that the Government had made its ‘tax lock’ commitment in the first place:

The 2% increase in NICs for the self-employed closes a small fraction of the gap between employees and the self-employed ...The tax advantage to being self-employed will still run into the thousands of pounds. The really big difference in treatment is the fact that employers pay 13.8% NI on anything they pay to their employees and nothing on anything they pay to self-employed contractors.

<sup>66</sup> [“Reforming tax for the self-employed should be welcomed by progressives and fiscal hawks alike”, Resolution Foundation blog, 9 March 2017](#)

<sup>67</sup> [Spring Budget 2017: IFS Director Paul Johnson’s opening remarks, 9 March 2017 p1](#)

A tax system which charges thousands of pounds more in tax for employees doing the same job as someone else needs reform. It distorts decisions, creates complexity and is unfair ...

You'll note that the Chancellor at the same time announced that the £5,000 tax free dividend allowance, introduced less than a year ago, would be cut to £2,000 ... It happened because he worries that by increasing tax on the self-employed he increases the incentive to incorporate. He is right to worry. Rates of incorporation have been rising and they are sensitive to the tax treatment. All in all these feel like baby steps in the right direction. But they are sticking plasters not the fundamental look at the tax base as well as tax rates that is required ...

Part of the problem of course is that the increase in class 4 NICs does look like a breaking of the manifesto commitment not to raise NI. Just as the last Labour government broke its manifesto pledge not to raise the basic or top rates of income tax when it increased the top rate to 50%. As we said at the time these were silly pledges. To commit yourself to not raising the three main taxes – income tax, NI and VAT – ties your hands to an absurd extent. No party should repeat these sorts of promises.<sup>68</sup>

In addition to Mr Johnson's comments, Helen Miller, associate director of the IFS, gave [a presentation on business taxes](#), which discussed both of these changes, and provided some distributional analysis of the NICs reforms.<sup>69</sup>

### 3.7 Decision to reverse proposed increase in Class 4 NICs

On 15 March the Chancellor announced that the Government would *not* proceed with the proposed increase in Class 4 NICs, first in a letter to the Chair of the Treasury Select Committee,<sup>70</sup> and later that day in a statement to the House – part of which is reproduced below:

The measures I announced in the Budget sought to reflect more fairly the differences in entitlement in the contributions made by the self-employed. The Government continue to believe that addressing this unfairness is the right approach. However, since the Budget, parliamentary colleagues and others have questioned whether the proposed increase in class 4 contributions is compatible with the tax lock commitments made in our 2015 manifesto.

Ahead of last year's autumn statement, the Prime Minister and I decided that however difficult the fiscal challenges we face, the tax lock and spending ring fence commitments we have made for this Parliament should be honoured in full ... As far as national insurance contributions are concerned, the locks were legislated for in the National Insurance Contributions (Rate Ceilings) Act 2015. When the Bill was introduced, it was made clear by Ministers that the lock would apply only to class 1 contributions

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<sup>68</sup> [Spring Budget 2017: IFS Director Paul Johnson's opening remarks](#), 9 March 2017 pp4-5. An editorial in the *Financial Times* the following day made a similar point: "Leader: Stand your ground on the tax rise, Chancellor", 10 March 2017.

<sup>69</sup> [Spring Budget 2017: Business Taxes presentation](#), 9 March 2017 ([see slide 7](#)).

<sup>70</sup> HM Treasury, [Letter from the Chancellor to the Chair of the Treasury Select Committee](#), 15 March 2017



... However, it is clear from discussions with colleagues over the last few days that this legislative test of the manifesto commitment does not meet a wider understanding of the spirit of that commitment.

It is very important both to me and to my right hon. Friend the Prime Minister that we comply with not just the letter but the spirit of the commitments that were made. Therefore ... I have decided not to proceed with the class 4 NICs measures set out in the Budget. There will be no increases in NIC rates in this Parliament. For the avoidance of doubt, and as I set out in the Budget, we will go ahead with the abolition of class 2 national insurance contributions from April 2018. Class 2 is an outdated and regressive tax, and it remains right that it should go. I will set out in the autumn Budget further measures to fund, in full, today's decision.

I undertook in the Budget speech to consult over the summer on options to address the principal outstanding area of difference in benefit entitlement between the employed and the self-employed: parental benefits. We will go ahead with that review, but we now intend to widen the exercise to look at the other areas of difference in treatment, alongside the Government's consideration of the forthcoming report by Matthew Taylor ... on the implications for employment rights of different ways of working in a rapidly changing economy. Once we have completed these pieces of work, the Government will set out how we intend to take forward and fund reforms in this area.<sup>71</sup>

In response Shadow Chancellor John McDonnell argued that the proposed increase in NICs rates was "a £2 billion tax hike for many low and middle earners, and a clear-cut and cynical breaking of a manifesto promise":

The £2 billion that would have been raised was to go some way to tackling the social care crisis. We need to know where these desperately needed funds will come from now. We need guarantees from the Chancellor that no working people will be hit, either now or in the autumn statement, with stealth or other tax rises, and that there will be no further cuts to public services to pay for this blunder.<sup>72</sup>

Andrew Tyrie, Chair of the Treasury Committee, said the announcement was "doubly welcome" as it "bolsters trust in the Government's other commitments, and removes the perception of a cigarette paper between No. 10 and No. 11", but went on to ask whether the Chancellor agreed that "a differential should, none the less, remain in the long run to reflect the additional risk taken by the self-employed when they are doing their job?" In response Mr Hammond said:

In the Budget speech last week, I made very clear that we were seeking to close the gap a little. We were not seeking to equalise the contributions treatment of the employed and self-employed, as there are very good reasons why there may well need to be a gap. That is why we will look at this in the round—contributions, entitlements and the way the whole package works for the self-employed. Let us come back to this once we have completed the

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<sup>71</sup> [HC Deb 15 March 2017 cc420-1](#)

<sup>72</sup> [HC Deb 15 March 2017 c421](#)



review, have the Matthew Taylor work and can look at the problem in the round.<sup>73</sup>

Speaking for the SNP Stewart Hosie welcomed the decision, “not least because about 140,000 Scottish self-employed people would have been affected by it”, and other Members who spoke on this occasion were also supportive of this change.<sup>74</sup>

Reactions in the press have been more varied.<sup>75</sup> The *Daily Telegraph* described the decision as “an abject humiliation for Philip Hammond, the Chancellor of the Exchequer, and an acute embarrassment for the Government as a whole.”<sup>76</sup> The *Times* suggested that “a relatively minor budgetary issue has been allowance to take a life of its own because of political misjudgement and poor communication between the two most important members of government.”<sup>77</sup> The *Guardian* argued “increases in NICs were not ... a blow to so-called risk-takers. They were in fact a challenge to those, often very well-off, who avoid their fair share because it can be tax advantageous.”<sup>78</sup> An editorial in the *Financial Times* took the view that “the UK government’s climb-down on national insurance puts politics over good policy”:

This newspaper has argued that Mr Hammond’s mistake was not raising contributions, but rather failing to include the change in a wider package of reforms for self-employment — something that the government is now considering. Mrs May has announced there will be no further changes to NICs until after the next general election, due in 2020.

A serious problem has in effect been put on indefinite hold. The danger now is that the Taylor Review into self-employment due this summer will suffer the same fate.<sup>79</sup>

Among stakeholder groups and commentators, the FSB strongly endorsed the Chancellor’s decision,<sup>80</sup> while the Chartered Institute of Taxation suggested “the Government’s U-turn over the National Insurance increase for the self-employed shows what can happen when Chancellors pull ‘rabbits’ out of the hat on Budget day without consulting or preparing the ground in advance.”<sup>81</sup> Torsten Bell, director of the Resolution Foundation, argued that “the Chancellor’s U-turn on his Budget plan to raise National Insurance for the self-employed is a very unusual one, combining as it does a very firm defence of the need for the policy with the decision to scrap it”:

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<sup>73</sup> [HC Deb 15 March 2017 c423](#)

<sup>74</sup> [HC Deb 15 March 2017 c423](#)

<sup>75</sup> “Tory U-turn as Philip Hammond scraps tax rise on self-employed” & “Self-employed relieved but wary after Hammond’s Budget U-turn”, *Financial Times*, 15 March 2017

<sup>76</sup> “Editorial: Philip Hammond’s embarrassing U-turn points to bigger issues in government”, *Daily Telegraph*, 16 March 2017

<sup>77</sup> “Leader: No way to govern”, *Times*, 16 March 2017

<sup>78</sup> “Editorial: The Guardian view on the budget U-turn: a climbdown that shows where power lies”, *Guardian*, 16 March 2017

<sup>79</sup> “Editorial: Philip Hammond has made the wrong U-turn for the wrong reasons”, *Financial Times*, 16 March 2017

<sup>80</sup> FSB press notice, [NIC’s U-turn is a great victory for FSB’s self-employed members](#), 15 March 2017

<sup>81</sup> CIOT press notice, [National Insurance U-turn shows why Budget ‘rabbits’ are a bad idea](#), 15 March 2017

That we have ended up in that place reflects the undeniable fact that the politics of the increase in self-employed National Insurance contributions (NICs) has been a disaster, while the policy rationale remains absolutely undeniable. To put it another way, whatever the rights and wrongs of breaking the spirit of Manifesto commitments – be it tax rises, migration targets or membership of the single market – the substance of the Chancellor's U-turn on (NICs) means the government has missed an opportunity to correct a big structural flaw in our tax system.<sup>82</sup>

In a letter to the Times IFS director Paul Johnson expressed the view that “some long-term planning and strategy would not go amiss”:

We should learn some lessons. First, it is a mistake to commit in a manifesto to not raising the three most important taxes — that ties the chancellor's hands to an absurd degree. Second, some long-term planning and strategy would not go amiss. The self-employed have been handed two big bonuses in recent years: access to a much enhanced state pension and the abolition of class 2 national insurance contributions. Announcing an increase in the class 4 rate at the same time, rather than as an apparent afterthought, might have made more sense. And finally, we need a more sensible debate about tax and spend. If we really can't raise taxes, then even more (and even deeper) public spending cuts are the only alternative.<sup>83</sup>

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<sup>82</sup> [“U-turn if you don't want to”](#), *Resolution Foundation blog*, 15 March 2017

<sup>83</sup> “Letters: Hammond's U-turn over national insurance”, *Times*, 16 March 2017

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