Office for Budget Responsibility

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Supplementary forecast information release

Costing of changes to the main, BADR and IR rates of capital gains tax

1.1 The OBR is releasing this information following a request for further detail in respect of the costing of changes to the main, business asset disposal relief (BADR) and investors' relief (IR) rates of capital gains tax (CGT) in our October 2024 *Economic and fiscal outlook*. We will, as far as possible, meet any requests to release supplementary forecast information where this will improve the quality of public debate on the public finances. Our full release policy is available on our website.

1.2 This release briefly describes the measure, sets out the data sources and modelling used to estimate the costing, and discusses the main sources of uncertainty around this central estimate, following the OBR's policy costings process.[1] As set out in the *Charter for Budget Responsibility*, the Government is responsible for producing all policy costings. In the case of tax policies the costings are typically produced by HMRC. The OBR's role is to provide independent scrutiny and certification of whether the Government's policy costings are reasonable and central.[2]

Policy description

1.3 Effective from the day of the Budget (30 October 2024), the main rates of CGT were increased from 10 per cent to 18 per cent for basic-rate taxpayers and from 20 per cent to 24 per cent for higher-rate taxpayers.[3] From April 2025, the rate on BADR and IR will rise from 10 per cent to 14 per cent, and from April 2026 will rise to 18 per cent.[4]

Data

1.4 CGT is charged on the profit made upon disposal by an individual or trustee of a qualifying asset. The main source of data for the costing is net 'chargeable' gains for individuals in the 2022-23 tax year held by HMRC. These data are primarily made up of self-assessment returns and payment on property disposals (PPD) and are broken down by tax rate.[5] Data are scaled to account for late filing, liability adjustments, and the average proportion of tax paid by trusts. These adjustments partly offset with a net effect under ten per cent.

[1] See our *Briefing paper No.6: Policy costings and our forecast*, March 2014.
[2] This means that the full datasets underpinning tax policy costings are generally held by HMRC. Therefore, requests for access to any datasets not available at the sources referenced in this note should be directed to HMRC.
[3] CGT applies to 'chargeable assets' other than residential property and carried interest, which have their own CGT rates. In practice this generally means gains on financial assets, like shares. For more information see HMRC, *Capital Gains Tax – rates of tax*, October 2024.
[4] BADR and IR allow for a reduced CGT rate for the disposal of all of part of a business, and of shares in a trading company not listed on a stock exchange, respectively. Take-up of IR has been low and as such changes to IR are not material to the costing.
[5] This data is held by HMRC. See HMRC, *Capital Gains Tax statistics*, August 2024.

1.5 To estimate the interaction between CGT and stamp duty land tax (SDLT) receipts, the costing uses CGT survey data and self-assessment returns for 2020-21 to identify non-residential property disposals, which are liable for both SDLT and the main rate of CGT.

Modelling

Static costing

1.6 The tax base for this measure consists of 'chargeable' gains that qualify for the main, BADR, or IR rates of CGT. The baseline for the costing is HMRC's CGT Integrated Model (CGTiM), which takes the 2022-23 HMRC data for main rate gains and projects it forward using the relevant element of the CGT forecast (see Table 1.2).[6] Gains are adjusted for the time accruals take to be realised as receipts (normally over a year), and additionally calibrated to align to early indications from the latest receipts data. The calibration changes are small as early data on CGT is very limited. The baseline accounts for forestalling expected in advance of the Budget.[7]

1.7 The static costing of this measure amends the CGTiM to incorporate the changes in rates detailed above. The resulting receipts are compared to the baseline estimate of CGT receipts, and the increase in CGT revenue constitutes the static costing.

Behavioural response

1.8 The following behavioural responses were considered within the costing:

- **Forestalling**, which refers to people bringing gains forward to avoid additional tax. As mentioned above, some forestalling was included in the baseline forecast due to speculation ahead of the Budget about possible policy changes. No post-announcement forestalling in response to the change in the main rate of CGT was possible because the change took effect on the day of announcement; forestalling in response to the staggered change in the BADR rate is discussed below.

- **Holding assets for a longer period**, for example, until death, emigration, or a later possible reversal of the policy change, such that HMRC never receives the revenue. In other cases, the gain would still be taxed at a later date.

- **Shifting investments into assets with a lower tax rate**, for example, incorporating as a business or investing more in a pension. The alignment of the higher main rate of CGT with the higher rate for residential property eliminates some of these incentives.

- **Reduced income-to-gains shifting**. There is evidence that some taxpayers structure their affairs to present labour income as a capital gain to benefit from a lower tax rate. With

[6] For more information on the OBR's CGT forecast, see OBR, *Forecast in-depth: Capital gains tax*, [April] 2024. The CGTiM is similar to HMRC's CGT forecast model but is split by chargeable rate rather than by asset type.
[7] This forestalling was in advance of anticipated policy changes, see paragraph 4.28 in our *Economic and fiscal outlook*, October 2024. This increased 2024-25 receipts by around £2 billion.

the gap between capital gains tax rates and employment tax rates reduced, this policy reduces the incentive for this behaviour.

- Other **tax avoidance** activity.

1.9 For the increase in the main rates of CGT, a retention rate elasticity of 3.6 was used to capture these behaviours in combination. This implies a reduction in realised gains of 3.6 per cent for every 1 per cent reduction in the proportion of post-tax gains retained by the taxpayer. For the increase in BADR rates, a retention rate elasticity of 1.4 was used. This was based on analysis of the BADR population and the shares of repeat and one-time filers.

1.10 This is lower than the elasticity of 4.0 for shares and non-residential property that was agreed with the OBR in 2020 following HMRC analysis of realised gains in the UK in the period from 1998 to 2018.[8] The reasons for lowering the elasticity for this measure were:

- the alignment of main rates with those on residential property and the raising of the BADR rate limiting some of the behavioural options for taxpayers;
- the incorporation of forestalling in the baseline forecast (and no opportunity for post-announcement forestalling in response to main rate changes) limiting scope for further timing-based behavioural responses; and
- international evidence showing that the UK effective tax rate remained toward the average of advanced economies after the measure.[9]

1.11 The increase in capital gains tax rates also affects income tax (IT) and stamp duty land tax (SDLT) receipts (see Table 1.2):

- Income tax receipts are expected to increase due to a reduction in income-to-gains shifting based on the change in the relative attractiveness of structuring earnings as income or gains. The costing assumed that 12.5 per cent of the behavioural response to the decrease in the gap between IT and CGT rates reflected reduced income-to-gains shifting.[10]
- SDLT receipts are expected to decrease because some of the reduction in realised capital gains will relate to non-residential property, which is liable for CGT and SDLT. This was estimated by taking non-residential SDLT relating to CGT disposals and growing it with the non-residential SDLT forecast over the forecast period.[11] The costing applied the change in realised gains from the elasticities detailed in paragraph 1.9 to this profile, assuming (based on the latest CGT survey) that 38 per cent of disposals

[8] We also considered external evidence, much of it US based, notably Agersnap, O., and O. Zidar, *The tax elasticity of capital gains and revenue-maximising rates*, 2020.
[9] See Box 3.1 in our *Economic and fiscal outlook*, October 2024.
[10] Estimates are based on literature, including on the introduction of the Additional Rate of IT in 2010, and HMRC's estimate of the response to Scottish IT changes in 2018. Within the CGT model, HMRC assumes that a quarter of the change in IT in response to a 1 percentage point increase in these marginal tax rates relates to avoidance, of which one half is income-to-gains shifting.
[11] For more information on the OBR's SDLT forecast, see OBR, *Forecast in-depth: Property transaction taxes*, [April] 2024.

are made at BADR rates. Finally, the SDLT impact was scaled down by 20 per cent to account for the likelihood that some gains relate to foreign land and buildings that do not attract an SDLT charge. The reduction in SDLT receipts has only a very small impact on the final costing (Table 1.3).

1.12 The profile of disposals of business assets in the static costing was adjusted to account for forestalling in response to the staggered increase in the BADR rate – over and above the forestalling in the pre-measures CGT forecast. The costing assumes an increase in realised gains of business assets that qualify for BADR of around 60 per cent in 2024-25, when the BADR rate remains at 10 per cent. This then unwinds with lower disposals over the rest of the forecast: around 15 per cent lower in 2025-26, 30 per cent lower in 2026-27 and around 5 per cent lower thereafter.[12]

[12] The reduction in realised gains is greater in 2026-27 than 2025-26 because there are still opportunities to forestall disposals at a BADR rate of 14 per cent, rather than 18 per cent, in 2025-26. But the vast majority of forestalling is assumed to take place in 2024-25.

Table 1.1: Key parameters

Parameter	Value	Description
CGT tax rates (per cent)		
Change in main rate (basic rate taxpayers)	10-18	Tax rate on assets excluding residential property and carried interest before and from October 30, 2024.
Change in main rate (higher rate taxpayers)	18-24	Tax rate on assets excluding residential property and carried interest and not qualifying for BADR before and from October 30, 2024.
Change in BADR and IR rate from April 2025	10-14	Tax rate on disposals qualifying for BADR or IR in 2024-25 and 2025-26.
Change in BADR and IR rate from April 2026	14-18	Tax rate on disposals qualifying for BADR or IR in 2025-26 and 2026-27.
Tax base (per cent)		
Share of 2024-25 gains in scope	35	The share of gains in the 2024-25 tax year realised after the announcement of the policy.
Behavioural assumptions		
Retention rate elasticity (main rates)	3.6	The elasticity of realised main rate gains with respect to the share of retained gains.
Retention rate elasticity (BADR)	1.4	The elasticity of realised BADR gains with respect to the share of retained gains.
Gains-to-income response share from reducing rate differential (per cent)	12.5	The share of overall behaviour that is assumed to represent CGT shifted into income tax following a 1 percentage point reduction in the gap between IT and CGT tax rates.
Proportion of CGT liable non-residential property gains charged at BADR rates (per cent)	38	The amount of reduced CGT gains on non-residential property that would have been charged at BADR rates rather than main rates.
Foreign land and buildings share (per cent)	20	The share of non-residential property held abroad and so not attracting an SDLT charge.
Approximate BADR forestalling in 2024-25 (per cent)	+60	Assumed change in qualifying disposals in advance of the increase in the BADR rate from 10 to 14 per cent.
Approximate BADR forestalling in 2025-26 (per cent)	-15	Assumed change in qualifying disposals in advance of the increase in the BADR rate from 14 to 18 per cent.
Approximate BADR forestalling in 2026-27 (per cent)	-30	Assumed reduction in qualifying disposals in the year the BADR rate rises to 18 per cent.
Approximate BADR forestalling from 2027-28 to 2029-30 (per cent)	-5	Assumed reduction in qualifying disposals over the rest of the forecast.

Source: OBR

Table 1.2: OBR determinants used in costing

	Forecast					
	2024-25	2025-26	2026-27	2027-28	2028-29	2029-30
Pre-measures CGT forecast (£ billion)	15.7	21.5	21.1	24.2	26.8	29.3
Non-residential SDLT (£ billion)	3.0	3.4	3.8	4.3	4.8	5.3
Equity prices (FTSE all-share index)	4,537	4,742	4,918	5,092	5,271	5,461

Note: The difference between the pre-measures and post-measures CGT forecast is the direct effect of measures, such as the changes to CGT rates, plus the indirect effect of the policy package on determinants that affect the CGT forecast.
Source: OBR

Final costing

1.13 The central estimate for the costing is an increase in revenue of £2.5 billion by 2029-30, with the behavioural impact reducing the static yield by around 58 per cent. £1.5 billion of yield comes from increased income tax, while around £1.0 billion comes from net CGT.

Table 1.3: Costing of changes to the main, BADR and IR rates of CGT

	£ billion					
	Forecast					
	2024-25	2025-26	2026-27	2027-28	2028-29	2029-30
Static costing	0.0	-0.9	-3.3	-4.8	-5.3	-5.9
Behavioural response	-0.1	-0.5	2.1	3.5	3.2	3.5
Post-behavioural costing	-0.1	-1.4	-1.4	-1.3	-2.2	-2.5
of which:						
CGT	0.0	-1.0	-0.1	0.1	-0.8	-1.0
Income taxes	0.0	-0.4	-1.3	-1.4	-1.4	-1.5
SDLT	0.0	0.0	0.1	0.1	0.1	0.1
Block grant adjustments	0.0	0.0	-0.1	-0.1	-0.1	-0.1

Note: This table uses the convention that a negative figure means a reduction in PSNB.
Source: OBR

1.14 This policy costing was assigned a 'high' uncertainty rating.[13] This is mainly due to uncertainty over the size of the behavioural response captured in the elasticity judgement. There is also moderate uncertainty over the data and the modelling. These are both upside and downside risks, notably the amount of forestalling in the baseline and the size of the behavioural response. We expect this costing to be roughly in steady state by the end of the forecast period.

[13] See the 'Policy costings uncertainty ratings database – October 2024' spreadsheet at OBR, *Policy costings*, November 2024.