Effects of AIA thresholds on aggregate investment

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Holding the AIA at £500k could increase UK capital stock by about 6%

The Chancellor has announced that the AIA threshold will not be cut back to £25,000 in 2016 but it will be set at a much more generous rate were he to stay in government. The new threshold has not been announced. We calculate the effect of different thresholds.

The AIA only affects investment below its threshold. This implies that the higher the threshold, the larger the effect on aggregate investment and capital stock.

With respect to the £25,000 threshold, if the AIA stays at £500,000, UK capital stock could increase by about 6% in the long run. At the margin, the higher threshold will reduce the effective tax rate on investment by around 30% mainly for firms between 50 and 299 employees. They carry out about 27% of aggregate investment. This will cost a little over £1 billion.

With respect to the £25,000 threshold, a threshold at £250,000 could increase UK capital stock by about 2% in the long run. The higher threshold will reduce the effective tax rate on investment by around 30% mainly for firms between 50 and 99 employees. They carry out about 9% of aggregate investment. This will cost a little over £400 million.

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