

# THE NATIONAL INSTITUTE MODEL FOR LIFETIME INCOME DISTRIBUTIONAL ANALYSIS, LINDA

This manual provides practical guidance in the use of LINDA, a dynamic microsimulation model that projects a reference population cross-section through time, subject to endogenous savings and labour supply decisions.

*User Manual  
version 3.22*

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19 March, 2020

# The National Institute Lifetime INcome Distributional Analysis model LINDA

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## *User Manual*

### **Table of Contents**

1. Introduction .....	4
2. Model set-up on a dedicated workstation.....	6
System requirements.....	6
Loading the model onto a new computer .....	6
Extracting base data from the Wealth and Assets Survey .....	8
Creating a simulation base.....	8
Using MPI integrations.....	10
Setup .....	10
Running the model using MPI .....	10
3. Using the model on a cloud service .....	12
Cloud computing providers and LINDA.....	12
Step 1: Set-up a stand-alone simulation on a local computer .....	13
Local system requirements .....	13
Model set-up on the local computer .....	13
Step 2: Start a cloud instance .....	15
Step 3: Upload the stand-alone model onto the cloud instance.....	26
Step 4: Run the model on the cloud .....	29
Step 5: Download results to the local computer .....	30
Step 6: Terminate the instance.....	30
Step 7: Analyse model output – creating a new simulation base.....	31
Final points of note .....	31
4. Altering Parameters .....	32
FORM 0: SIMULATION TASK.....	33
FORM 1: KEY PARAMETERS.....	35
FORM 2: ANALYSE EXISTING SIMULATION .....	37
FORM 3: FERTILITY ASSUMPTIONS .....	39
FORM 4: SELECTED EMPLOYMENT PARAMETERS .....	41
FORM 5: SELECTED DISABILITY PARAMETERS .....	42

FORM A1: INCOME TAX AND NATIONAL INSTURANCE (2010/11) .....	45
FORM A2: TAX CREDITS – WORKING LIFETIME.....	46
FORM A3: HOUSING RELATED BENEFITS .....	47
FORM A4: BENEFITS FOR NON-DISABLED.....	48
FORM A4: DISABILITY BENEFITS.....	49
FORM A6: AGE THRESHOLDS .....	50
FORM A7: UNIVERSAL CREDIT .....	51
FORM A8: INDIRECT TAXATION .....	52
FORM C1: STATE CONTRIBUTORY PENSIONS .....	53
FORM C2: NON-PENSION WEALTH .....	54
FORM C3: PRIVATE PENSIONS .....	55
FORM C4: VARIATION OVER PRIVATE PENSION ELIGIBILITY .....	57
FORM C5: PRIVATE PENSIONS (cont.).....	58
FORM C6: ESCALATION .....	59
FORM C7: SELF-EMPLOYMENT .....	60
FORM C8: EDUCATION .....	61
FORM D1: SHORT-RUN ANALYSIS .....	62
FORM D4: ANALYSIS OF TAX FUNCTION.....	63
FORM Z: RUN MODEL .....	64
5. Running the model on a local computer.....	65
Stacking simulation counterfactuals.....	65
6. Simulation Output.....	67
Benefit unit level micro-data .....	67
Default summary statistics.....	70
High-level summary statistics - hi_level_statistics.xls .....	70
Optional summary statistics .....	71
High level analysis of population cross-sections and birth cohorts.....	71
Poverty statistics .....	71
Decile-level summary statistics for population cross-sections and birth cohorts.....	72
7. Best Practice Methods of Use .....	74
Step 1: specify policy parameters .....	74
Checking differences with base simulation .....	74
Validating the tax function.....	74
Example.....	75

Step 2: run model and generate output .....	82
Example.....	82
Step 3: think about likely incentive effects.....	83
Example.....	83
Step 4: analyse model output .....	83
High level analysis .....	83
Detailed statistical analysis .....	83
What to do when results do not conform to expectations .....	84
Example.....	84
Step 5: package output .....	87
8. Adjusting the Program Code.....	88
Programming basics.....	88
Basic Code Structure .....	88
Common programming steps .....	90
Programming a new Tax and Benefits Regime .....	93
Organisation of the Tax and Benefits Code .....	93
Introducing user-defined tax schemes .....	94
Adjusting number of tax outputs.....	98
Appendix A: End User License.....	100
Appendix B: The Utility Function .....	101
Appendix C: Pre-programmed tax and transfer systems for the UK .....	102
Appendix C.1: Transfer system applicable in April 2011.....	102
Appendix C.1.1 Taxes .....	102
Appendix C.1.2 Benefits .....	103
Appendix C.2: Transfer system applicable in April 2016.....	110
Appendix C.2.1 Taxes .....	110
Appendix C.1.2 Benefits .....	110
Appendix C.3: Universal credit.....	113

# 1. Introduction

This manual describes use of the National Institute's *Lifetime INcome Distributional Analysis* model, *LINDA*, which is designed to explore the effects of changes to the tax and benefits structure on household circumstances through time. The model generates panel data for the evolving population cross-section, and a series of summary statistics for each considered policy environment.

LINDA is complementary to other analytical approaches that are now in use. Current large-scale microsimulation models are able to provide detailed information regarding the immediate financial implications of policy change. However, such models are not well adapted to consider how savings, employment and consumption can be expected to adapt to altered financial incentives. Econometric analyses can go some way to filling in this missing detail, but not where uncertainty is likely to influence decision making. LINDA is specifically designed to explore savings and employment responses to policy change in context of important aspects of uncertainty that individuals face. The cost of this approach is that it is unable to reflect the degree of detail that is commonly taken into account by the two alternative analytical approaches that are referred to above. Thus, a thorough basis for balanced policy advice is best achieved at present by considering the same issue from alternative analytical perspectives.

LINDA is comprised of a series of Excel files that describe model parameters, and a central executable program that undertakes all of the requested analyses. Alteration of the model parameters is facilitated through an Excel “front-end”, via a series of “user forms”. One purpose of this manual is to describe how to use this Excel front-end. But before we move on to that, it is worth describing at a very high level of detail how the model works.

The model starts from cross-sectional data for the benefit units of a sample of reference adults drawn from the Wealth and Assets Survey. As such, use of the model is limited to individuals who have been granted access to the Wealth and Assets Survey microdata.<sup>1</sup> A benefit unit is defined as one or two adults (living together as a couple) plus any dependent children living with them. The user is first directed to run a simulation that projects the circumstances for the reference population cross-section back through time, and the evolving population cross-section forward through time. This base simulation allows the model to describe the complete life-history of each adult represented in the reference cross-section. The micro-data generated by the model are saved by the model, and used as the “base” data from which subsequent policy-specific projections are made. It is possible to update the “base” data used by the model at any time, as is described later in this manual.

A simulation for a given policy environment typically involves 3 stages. 1) Specify model parameters through an Excel spread sheet. 2) Run the executable program, which automatically loads the model parameters, projects associated panel data starting from the prevailing simulation “base” (output in a standard format, csv), and calculates a set of associated summary statistics (output to Excel). 3) Analyse the model output.

The model is delivered with all of the files – other than the WAS micro-data – that are necessary to run a simulation, including source code describing taxes and benefits.<sup>2</sup> This manual also provides a brief description of how the tax and benefit code considered by the model can be altered. Source

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<sup>1</sup> See the UK Data Service, Catalogue number 7215; “Wealth and Assets Survey, Waves 1-5, 2006-2016”.

<sup>2</sup> Source code for selected aspects of the model is available from the author upon request.

code for the complete model is available upon request; please send an email to [enquiries@simdynamics.org](mailto:enquiries@simdynamics.org).

LINDA is at the prevailing technological frontier. Nevertheless, it is important to recognise the model's limitations from the very outset. This is especially important, because the style of output generated by LINDA can result in mis-conceptions concerning the accuracy of projections; for example, consumption is projected by the model for each family unit down to the last pence (and even beyond that), giving the illusion of a very high degree of accuracy. Technical and theoretical limitations, however, mean that any projection of the future that we make today should not be interpreted as either a forecast or a prediction. Rather, such projections are useful because they reveal the logical implications of alternative policy environments that could only otherwise be guessed at, given a set of explicit (albeit, unavoidably imperfect) assumptions concerning how the future will evolve.

Beyond this manual, a wide range of resources exist to aid in the use of the model. These resources, which include access to aspects of the underlying model code, video tutorials, and a user forum, can all be accessed at the dedicated website: [www.simdynamics.org](http://www.simdynamics.org). An overview of the model is reported in van de Ven (2017a)<sup>3</sup>, and we request that all analyses based on model output reference this article. Furthermore, details about how the model parameters have been calibrated to survey data is reported in van de Ven (2017b)<sup>4</sup>.

This manual is divided into seven sections. Section 2 describes how the model should be set-up for the first time on a dedicated workstation, which includes use of the Excel front-end. Workstations tend to be expensive investments, at least for independent researchers. The model has consequently been adapted to run on cloud computing services, which permit individual simulations to be run at very little cost. Section 3 describes how to set the model up to run on a cloud computing service. Section 4 describes how to use the Excel front-end, which is designed to guide a user through adjustment of selected model parameters. Section 5 describes the output generated by the model. Section 6 provides an overview of how to use the model to conduct policy analyses. Section 7 provides some pointers for those interested in altering the tax and benefit programming code.

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<sup>3</sup> van de Ven, J. (2017a), "SIDD: An adaptable framework for analysing the distributional implications of policy alternatives where savings and employment decisions matter", *Economic Modelling*, 63, pp. 161-174.

<sup>4</sup> van de Ven, J. (2017b), "Parameterising a detailed dynamic programming model of savings and labour supply using cross-sectional data", *International Journal of Microsimulation*, 10.

## 2. Model set-up on a dedicated workstation

### System requirements

LINDA is designed to operate on desktop workstations that use Intel processors and the *Microsoft Windows* operating system. We recommend minimum system specifications of a 64-bit operating system, computing processor(s) with at least 6 physical cores, 32GB of RAM, and 1TB of hard disk space.<sup>5</sup> *Microsoft Excel* is required to generate parameter alternatives and analyse summary statistics reported by the model. *Stata* is required to run a file that we have written to extract the required micro-data from the Wealth and Assets Survey, and supplementary routines we have written to aid analysis of generated microdata. Users who intend to alter the tax and benefits structure beyond simple parameter adjustments, will also require *Intel Fortran Studio XE* or *Intel Parallel Studio XE*. A computer monitor not less than 17" in diagonal dimension is also required.

### Loading the model onto a new computer

The model is delivered as a single \*.exe file. Double click on the file, and work through a standard set of install options. The user license agreement is included in Appendix A to this document. Minor issues to note include:

- The model can be installed onto any directory of your choosing, subject to the limitation that the directory name should not include the character "."
- Model updates are delivered in the same fashion as the full model install. If an update is installed in the same directory as the original model, then it will over-write all pre-existing model files except those that have been generated by the user. This means that all of the simulations that you have generated via a previous version of the model will not be deleted when you up-date the model.

The installer creates three subdirectories: 00 DOCUMENTATION, 01 FORTRAN, and 02 MODEL.

- The 00 DOCUMENTATION subdirectory includes the model's user manuals.
- The 01 FORTRAN subdirectory includes the programming code for the TAX routines that are provided with the model.
- The 02 MODEL subdirectory includes all of the files that are required to run the model.

The MODEL subdirectory contains four subdirectories in addition to a set of model files. The subdirectory ANALYSIS\_FILES contains a set of Excel files that are used by the model's in-built analysis routines, and an additional subdirectory that stores some related statistics. The subdirectory BASE\_FILES contains a separate subdirectory for each "base" specification that you create with the model, in which files that are required for the respective base specification are stored (discussed in the section concerned with "FORM 0" that we return to below). The subdirectory SIMULATIONS will contain a separate subdirectory for each simulation that you run, in which are stored the panel data generated by the model, model parameters, and excel simulation

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<sup>5</sup> The model is delivered on the assumption that you have a 64 bit operating system. Please contact the NIESR if you require files to run on a 32 bit system. Note also that these minimum system requirements are for the base model specification, and are not sufficient for every feasible model specification. Please contact NIESR for further assistance.

output. The STATA subdirectory includes some routines that we have pre-programmed to help you analyse simulated data.

Please follow these steps when installing the model on a new computer:

1. Run the file setup.exe, as referred to above

**USERS WITH FORTRAN PROCEED TO STEP 2 – ALL OTHERS SKIP TO THE SUBSECTION ENTITLED “Extracting base data from the Wealth and Assets Survey” ON THE NEXT PAGE**

2. In the FORTRAN subdirectory, open up the TAXES subdirectory, and double-click on TAXES.sln
  - a. This should open the Visual Studio program environment
3. If you can see the “solution explorer” window, then select the “TAXES” box under the “Solution ‘TAXES’” project
  - a. If you cannot see the “solution explorer” window, then open it through the “View” drop-down menu
4. In the “Project” drop-down menu at the top of Visual Studio, select “Properties”
5. In the “Configuration” drop-down menu select “All configurations”
6. In the “Platform” drop-down menu select “x64” (the only option available)
7. Under “Configuration Properties”, select the “General” category
8. Under “Configuration Properties”, select the “Debugging” category
9. Against “Command”, enter the location of the file “SIDD.exe”; eg:  
“C:\MyFiles\MODEL\_LAB\MODEL 02\SIDD.EXE”
10. Against “Working Directory”, enter “..\..\02 MODEL\”
11. Press the “Apply” button, and then the “Ok” button
12. Under the “File” drop-down menu select “Save All”
13. Under the “Build” drop-down menu select “Configuration Manager”
14. Under the “Active Solution Configuration” select “release”
15. Under the “Active Solution Platform” select “x64” and press the “Close” button
16. Under the “Build” drop-down menu select “Rebuild Solution”



You should then see some text like, indicating that everything has worked:

```
1>----- Rebuild All started: Project: TAXES, Configuration: release x64 -----
1>Deleting intermediate files and output files for project 'TAXES', configuration 'release|x64'.
1>Compiling with Intel(R) Visual Fortran Compiler XE 15.0.4.221 [Intel(R) 64]...
1>2_global.f90
1>UK_3.f90
1>UK_4.f90
1>1_TaxTools.f90
1>UK_2.f90
1>AUS_1.f90
1>IT_1.f90
1>IE_1.f90
1>UK_1.f90
1>0_app_taxes.f90
1>Linking...
1> Creating library C:\MyFiles\MODEL_LAB\MODEL 02\TAXES.lib and object C:\MyFiles\MODEL_LAB\MODEL
02\TAXES.exp
1>
1>Build log written to "file://C:\MyFiles\MODEL_LAB\FORTRAN\TAXES\x64\release\BuildLog.htm"
1>TAXES - 0 error(s), 0 warning(s)
===== Rebuild All: 1 succeeded, 0 failed, 0 skipped =====
```

## Extracting base data from the Wealth and Assets Survey

As noted in the introduction, the model starts with data reported by the Wealth and Assets Survey (WAS) for a population cross-section of reference adults. A Stata program (e.g. `derive_WAS 2015.do`) is provided in the model subdirectory “\MODEL 02\base\_files\” to extract and format the WAS data, ready for importing into the model. Unless otherwise stated, the model has been specified to use the standard End User License version of the WAS available through the UK Data Archive, since 2015.<sup>6</sup> Please open the file “`derive_WAS 2015.do`”, edit the directory locations as indicated by comments at the top of the file, and run it to generate the base dataset.

## Creating a simulation base

As noted in the introduction, the model starts with data reported by the Wealth and Assets Survey for a population cross-section of reference adults. The model parameters have been calibrated to match the model to a wide range of summary statistics calculated from survey data sources, with the calibration structured around the year in which the reference population was observed (see van de Ven, 2017, for details). The model comes packaged, ready to project the circumstances of the population cross-section forward and backward through time, to build up a complete life history for each reference individual. It is recommended that this be done, and that the associated data should be defined as the “base” for subsequent simulations. This can be done by following steps 18 to 28 below.

17. Open the MODEL subdirectory, and then open “Job File.xls”
  - a. note that a “Security Warning” may appear in Excel if macros have been disabled
18. Ensure that you allow macros to work in Excel
  - a. please ask your system administrator if you require assistance with this
19. Press ALT+F8
20. Select “SIDD” and press the RUN button
21. Press the “RUN EXISTING JOB FILE” button

---

<sup>6</sup> Prior to 2015, the model used the Special User Licenses of the WAS, which was withdrawn for public use by the Office for National Statistics from October 2016.

- a. A warning message may appear if the model identifies the potential for insufficient system memory. If system memory is a problem, then it is possible to proceed using cloud computing services, as discussed in Section 3 of this manual

A window showing the model execution should open, and provide information to let you know what the model is doing. When the model simulation is complete, a total time for execution should be reported, and you should see a cursor indicating that the window is ready for a new command.

22. Close the execution window
23. Re-open "Job File.xls"
24. Press ALT+F8
25. Select "SIDD" and press the RUN button
26. Enter "2015p\_base" into the text-box with the title "name of run to adopt as new base"
27. Enter "2015p\_base" into the text-box with the title "directory name for new base"
28. Press the "CONVERT RUN TO NEW BASE" button

Excel will then work away for a short while, after which you should receive a message confirming that the new base has been created. If you look in the BASE\_FILES subdirectory, you should now see a new subdirectory with the name "2015p\_base", which includes all of the files defining the base simulation specification.

To test that the model set-up has been successfully completed:

29. Re-open "Job File.xls"
  - a. This file has been changed since step (23), so that it now references the new base model directory by default.
30. Press ALT+F8
31. Select "SIDD" and press the RUN button
32. Press the "NEW SIMULATION FOR UK" button
33. Type "test" in the text-box with the title "Simulation Name"
34. Press the "ENTER" button
35. Tick the box to direct the model to calculate "statistics for equivalised income deciles"
36. Tick the box to indicate that "comparative statistics with the population base" should be evaluated
37. Press the "ENTER AND RUN" button
38. Press the "LAUNCH MODEL" button

The model should then run through once again. This time, however, the simulations will project only forward through time, taking the population characteristics back in time from the base specification. When the model is complete, please open the analysis\_dec.xls file that is created in the "test" simulation directory, and check that all of the statistics reported in the "differences with base" sheet are close to zero.

## Using MPI integrations

If the model is run on a computer with two or more physical processors<sup>7</sup>, as is currently available in workstations and a feature of HPC (High Performance Computing) clusters, then substantial reductions in computation time can be realised by taking advantage of the MPI integration that has been built into the model. It is necessary to perform a number of additional steps to set the model up for use with MPI integrations.

### Setup

The Intel MPI run-time libraries must be installed to take advantage of MPI integrations. These run-time libraries are freely available from the Intel website.

After the Intel MPI libraries are installed, it is necessary to register a user-name and password with the MPI libraries, which are encrypted and stored by the system to permit the creation of MPI processes. This is done by opening a Command Prompt window (type cmd in the windows search box), and typing “mpiexec -register”.

### Running the model using MPI

Two additional things are then required each time you want to run the model using MPI integrations. First, the prevailing model parameters need to be TRANSLATED for suppressing communications with Excel. To do this:

1. Open the MODEL subdirectory, and then open “Job File.xls”
2. Ensure that you allow macros to work in Excel
  - a. please ask your system administrator if you require assistance with this
3. Press ALT+F8
4. Select “TRANSLATE” and press the RUN button

A series of Excel macros will then run through, ending in a message to indicate that model parameters have been successfully translated for reading in without recourse to Excel.

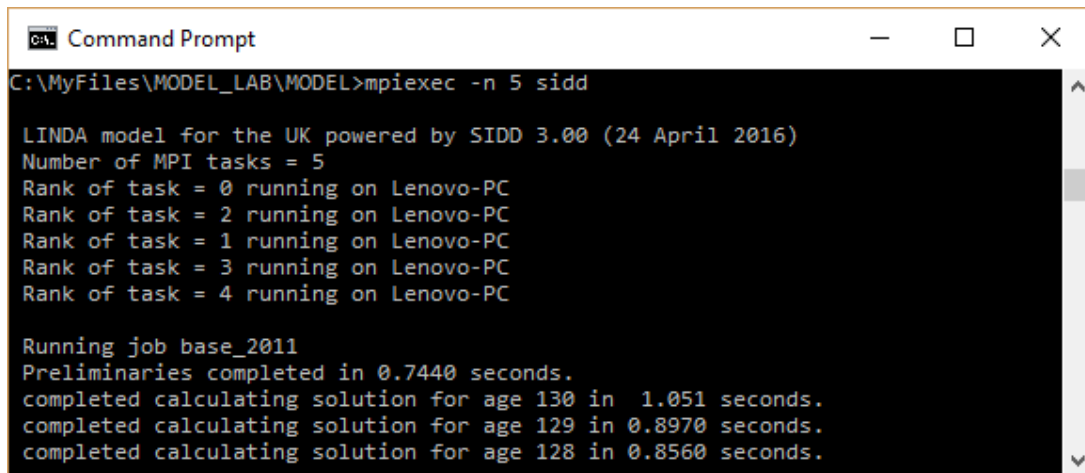
Secondly, open a Command Prompt window, navigate to the directory that the model is stored in (by typing cd XXX, where “XXX” is replaced by the location of the main model directory; e.g. “C:\MyFiles\MODEL\_LAB\MODEL”), and type:

```
mpiexec -n X sidd
```

and hit the RETURN key. “X” here defines the number of MPI processes, and should be replaced by the desired figure. As a general rule, set X to the number of CPU’s in your system. You should then see some output like the following:

---

<sup>7</sup> A ‘physical processor’ refers to a Central Processing Unit or CPU. Each CPU may include multiple (physical) computing ‘cores’



```
Command Prompt
C:\MyFiles\MODEL_LAB\MODEL>mpiexec -n 5 sidd

LINDA model for the UK powered by SIDD 3.00 (24 April 2016)
Number of MPI tasks = 5
Rank of task = 0 running on Lenovo-PC
Rank of task = 2 running on Lenovo-PC
Rank of task = 1 running on Lenovo-PC
Rank of task = 3 running on Lenovo-PC
Rank of task = 4 running on Lenovo-PC

Running job base_2011
Preliminaries completed in 0.7440 seconds.
completed calculating solution for age 130 in 1.051 seconds.
completed calculating solution for age 129 in 0.8970 seconds.
completed calculating solution for age 128 in 0.8560 seconds.
```

The second line of output should indicate that the number of MPI tasks is set to “X”, after which “X” lines should appear indicating the index and computer name of each MPI task.

### 3. Using the model on a cloud service

LINDA is computationally intensive, and as such can impose a heavy demand on computing resources. The model has consequently been adapted to take advantage of modern computing technology, including the possibility of running it entirely on a cloud computing service. Running the model on a cloud service has the distinct advantage that it permits the user to rent access to specialist computing services, which they may not need on a day-to-day basis. The model is designed to take advantage of both “shared memory” systems (as present in a single personal computer, workstation, or computational “instance” discussed below), and “distributed memory” systems (as present in High-Performance Computing, or supercomputer, clusters). This section walks through the steps required to run the model on a single computation “instance” in a cloud service. How to establish and run the model on a computer cluster (comprised of multiple “instances”) is beyond the scope of this manual.

#### Cloud computing providers and LINDA

There are currently a large number of cloud computing providers, consistent with an industry-wide view that cloud computing is likely to account for an increasing share of computational demand in the future. Each provider has its own strengths and weaknesses, which evolve at a rapid pace. This section refers to services provided by Amazon through its *Elastic Compute* facility (EC2), though it could just as easily have referenced Google’s *Compute Engine*, or Microsoft’s *Azure*. The user is advised to seek out the option that best suits their needs.

Cloud computing services are organised around “instances”, which can be thought of as individual (virtual) computers. Each instance is assigned an explicit set of compute resources, including “virtual central processing units”, vCPUs, memory, RAM, and physical disk space. Costs are typically charged per minute or hour, and vary with the scale of the resources that are rented.

It is possible to access instances individually, or as a group. A group of instances that has been organised to work together is sometimes referred to as a “cluster”. Individual instances are typically limited to the specifications of a prevailing high-end desktop workstation. Clusters, in contrast, offer potentially unlimited resources. While the number of vCPUs currently accommodated on an instance is limited to 40, clusters comprised of up to 156,000 vCPUs (cores) have been used. In this regard, it is useful to bear in mind that the computational time of a simulation is generally inversely proportional to the number of cores. Hence, a problem that would take a week to compute on a single vCPU, would take 4.2 hours to compute on a 40 vCPU instance, and just under 4 seconds to compute on a 156,000 vCPU cluster.

An important point to note is that LINDA is currently limited to accessing a single instance at any one time. The current description is consequently limited to discussion of how to launch and use a single instance, noting that an additional layer of complexity is associated with the establishment and use of a cluster.

Most cloud computing services that currently exist supply instances with minimal pre-installed software. There are two ways to use LINDA in context of these software limitations.

In the first alternative, a dedicated instance can be started, and the user can load all of the software required to run the model onto the instance. As all data loaded onto an instance are lost when an instance is terminated, this approach lends itself to renting an instance for the entire duration of an

analysis of interest. In this case, the model set-up would proceed in a similar fashion to that described in Section 2 for a dedicated workstation.

The second alternative involves renting an instance only for the duration of a single simulation. In this case, it is necessary to:

- 1) Use a local computer to set up a stand-alone model specification that is designed to minimise software pre-requisites
- 2) Start a cloud instance
- 3) Upload the stand-alone model specification onto the instance
- 4) Run the model specification
- 5) Download results to the local computer
- 6) Terminate the instance
- 7) Analyse results on the local computer

The remainder of this section walks through each of the seven steps that are listed here.

## **Step 1: Set-up a stand-alone simulation on a local computer**

### **Local system requirements**

Setting-up a stand-alone model specification requires a computer with any operating system, a monitor not less than 19" in diagonal dimension, an internet connection (to access the cloud), and two pieces of off-the-shelf software. Microsoft Excel is needed to generate parameter alternatives and analyse summary statistics. Stata is required to run a file that we have written to extract the required micro-data from the Wealth and Assets Survey, and to use supplementary routines that we have written to aid analysis of simulated microdata. Users who intend to alter the tax and benefits structure beyond simple parameter adjustments will also require a 64-bit Microsoft Windows operating system, and *Intel Fortran Studio XE* or *Intel Parallel Studio XE*.

### **Model set-up on the local computer**

Setting-up the model on a local computer is described at length in Section 2. Please follow the directions outlined in the three subsections of Section 2 preceding the subheading "Creating a simulation base".

In common with the procedure of setting up a model on a dedicated workstation, we recommend that analysis start by setting up a base simulation. This base simulation projects data forward and backward through time using a base parameter specification, building up a description for the complete life-course of individuals present in a reference population cross-section. The model parameters necessary to undertake this simulation come pre-packaged with the model. The remainder of this section describes how to run this base simulation on Amazon's EC2. Please note that a similar set of steps to those described below is required to run subsequent simulations.

A stand-alone specification for the model using the pre-packaged parameters can be generated via the following steps:

5. Open the MODEL subdirectory, and then open "Job File.xls"
6. Ensure that you allow macros to work in Excel
  - a. please ask your system administrator if you require assistance with this

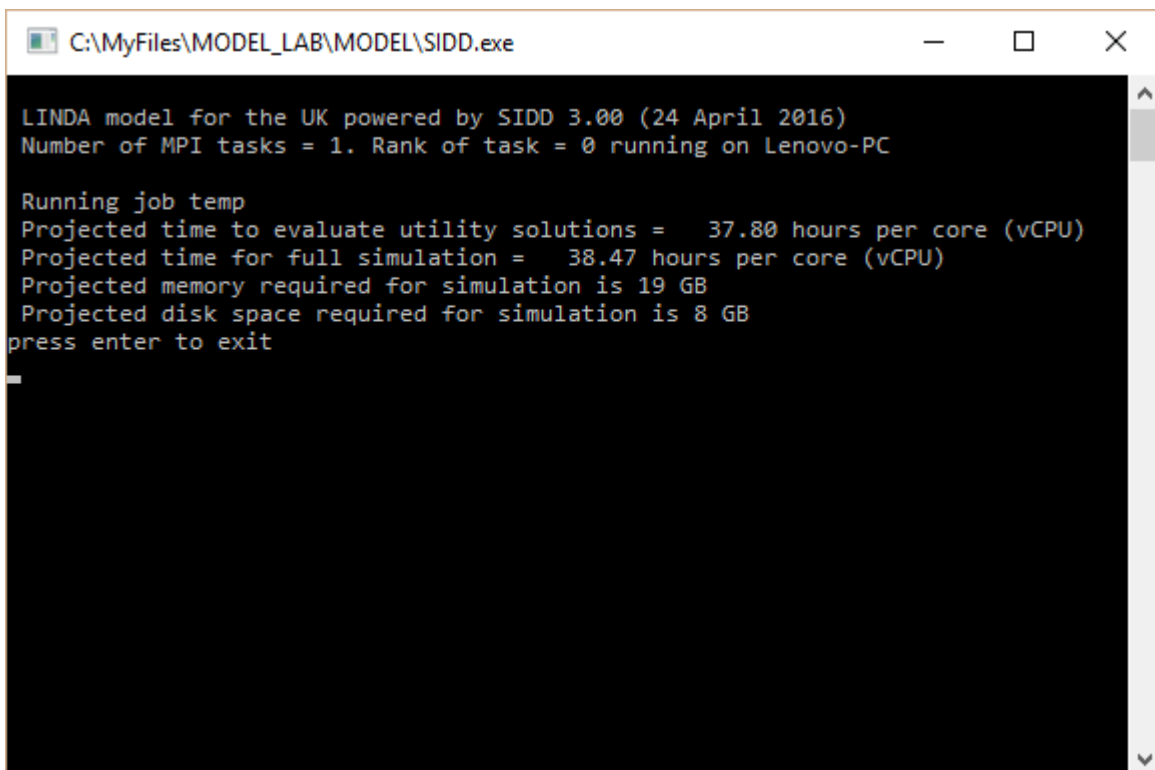
7. Press ALT+F8
8. Select “TRANSLATE” and press the RUN button

A series of Excel macros will then run through, ending in a message to indicate that model parameters have been successfully translated for reading in without recourse to Excel. The model is now ready for copying to an instance on the cloud.

Individuals who have access to a 64bit Windows operating system can now use the model on their local machine to generate useful statistics for determining the cloud resources that they need. This can be done by following these steps:

1. Open the MODEL subdirectory, and then open “Job File.xls”
2. Ensure that you allow macros to work in Excel
  - a. please ask your system administrator if you require assistance with this
3. Press ALT+F8
4. Select “SIDD” and press the RUN button
5. Press the “NEW SIMULATION FOR UK” button
6. Type “temp” in the text box next to “simulation name”
7. Press the “ENTER” button
8. Select the checkbox next to “generate advisory statistics...”
9. Press the “ENTER AND RUN” button
10. Press the “LAUNCH MODEL” button

You should then see output similar to the following:



```
C:\MyFiles\MODEL_LAB\MODEL\SIDD.exe

LINDA model for the UK powered by SIDD 3.00 (24 April 2016)
Number of MPI tasks = 1. Rank of task = 0 running on Lenovo-PC

Running job temp
Projected time to evaluate utility solutions = 37.80 hours per core (vCPU)
Projected time for full simulation = 38.47 hours per core (vCPU)
Projected memory required for simulation is 19 GB
Projected disk space required for simulation is 8 GB
press enter to exit
```

The first line of output following “Running job temp” indicates that selecting a single vCPU instance will solve the utility maximisation problem in approximately 37.8 hours, and the full simulation

output in approximately 38.5 hours. Note that the time taken to evaluate the utility maximisation problem declines approximately proportionally with the number of vCPUs, while the time taken for the remainder of the simulation is broadly unaffected by the number of vCPUs. Hence, the above statistics imply that selecting a cloud instance with 10 vCPUs should run in approximately 4.5 (= 3.78 + 0.7) hours. The model output also indicates that the problem will require approximately 19GB of RAM, and 8GB of physical disk space.

## **Step 2: Start a cloud instance**

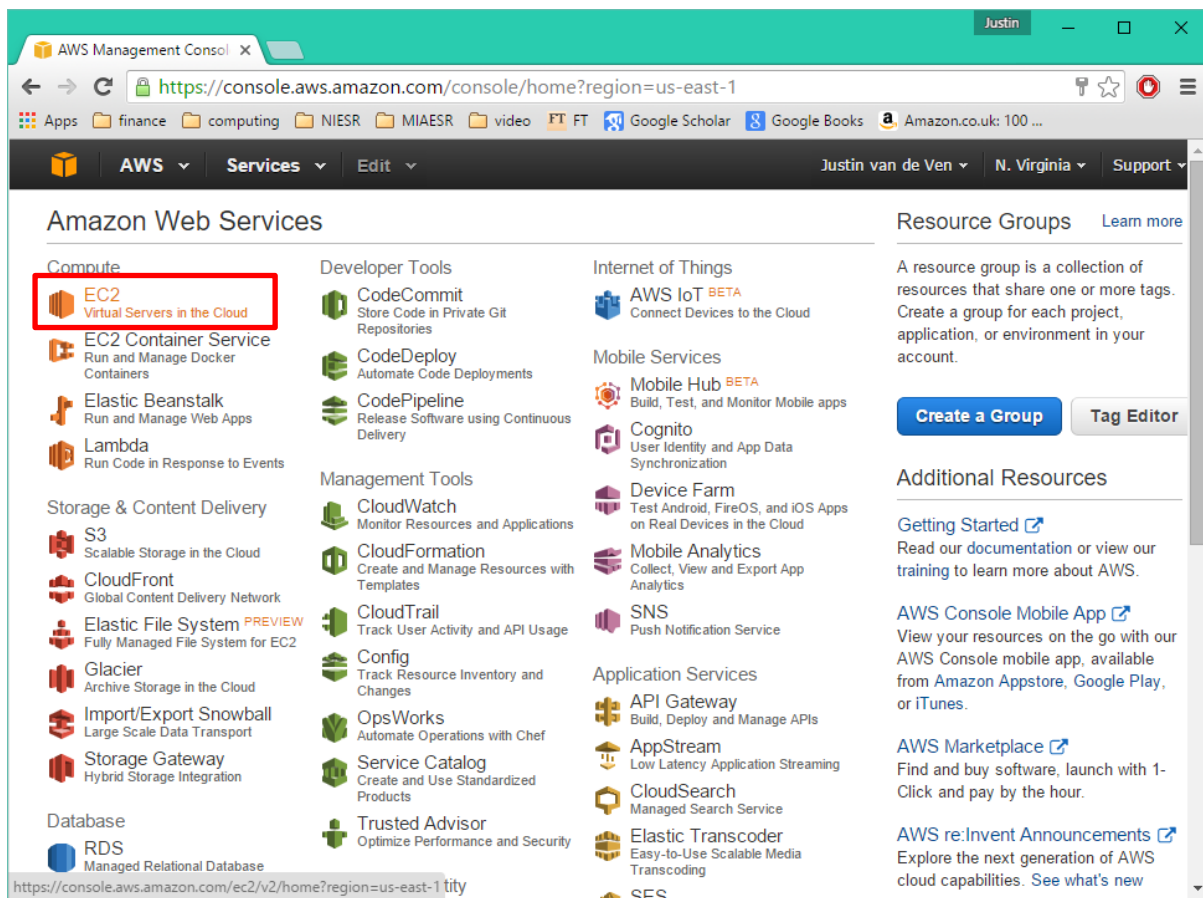
Amazon Web Services (AWS) offer a very wide variety of cloud computing services. Users should refer to the website <https://aws.amazon.com/> for full details concerning how to set-up a user account, and what facilities are on offer.

Like most cloud computing options that are currently available, there are no sign-on costs for AWS, no fixed costs, and no mandatory contract periods; you only pay for what you use. The description here is limited exclusively to the steps involved in initialising and running the model on EC2 available through AWS, assuming that an account has been set up.

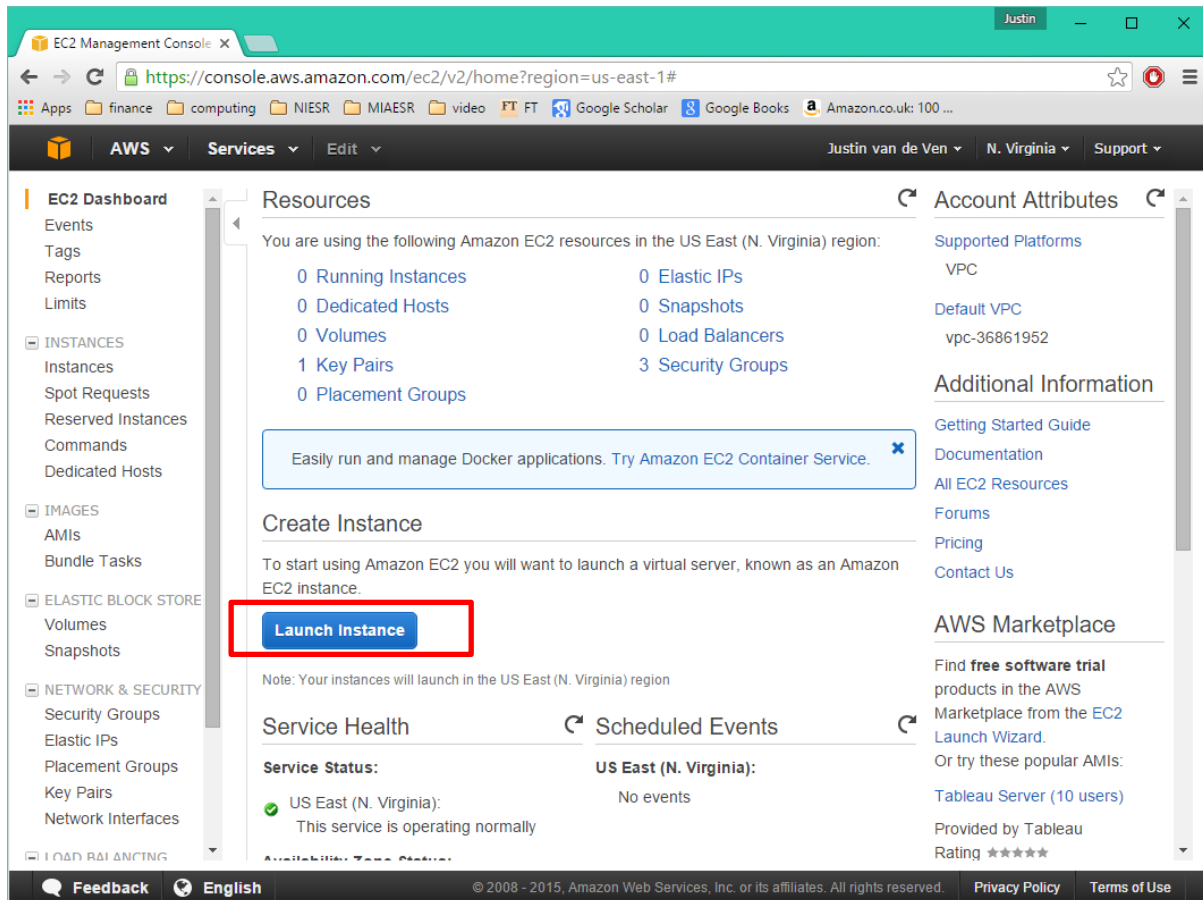
- 1) Sign in to the AWS console using your account credentials.



## 2) Select EC2 from the main menu



- 3) Select “Launch an instance”
  - a. We recommend using a “on-demand” instance



- 4) Select an Amazon Machine Image (AMI) that has Microsoft Windows Server installed.
- a. Note: do not select a server with SQL included, as SQL is not needed by the model and the associated AMIs are more expensive to rent

The screenshot shows the AWS Management Console's 'Launch Instance Wizard' at the 'Choose AMI' step. The console lists four AMIs:

- Ubuntu Server 14.04 LTS (HVM), SSD Volume Type** (ami-d05e75b8): 64-bit, Free tier eligible. Annotation: "e.g. use this one".
- Microsoft Windows Server 2012 R2 Base** (ami-e171098b): 64-bit, Free tier eligible. Annotation: "e.g. use this one".
- Microsoft Windows Server 2012 R2 with SQL Server Express** (ami-86760eec): 64-bit. Annotation: "not this one".
- Microsoft Windows Server 2012 R2 with SQL Server Web** (ami-ca770fa0): 64-bit. Annotation: "not this one".

Each AMI entry includes a 'Select' button and details about the root device type (ebs) and virtualization type (hvm).

- 5) Select an instance type
  - a. we typically focus on the compute optimised options,
  - b. Ensure that there are sufficient vCPUs (A) and RAM (B)
  - c. press Next

The screenshot shows the AWS Management Console's 'Launch Instance Wizard' at Step 2: Choose an Instance Type. The wizard is for the 'us-east-1' region. The instance type 'c4.8xlarge' is selected, which is highlighted with a red box. This instance type has 36 vCPUs (labeled 'A') and 60 GB of RAM (labeled 'B'). It is a 'Compute optimized' instance with 'EBS only' storage and a '10 Gigabit' network interface. The 'Next: Configure Instance Details' button is also highlighted with a red box.

Instance Type	Category	vCPUs (A)	RAM (B)	Storage	Network
c4.large	Compute optimized	2	3.75	EBS only	Moderate
c4.xlarge	Compute optimized	4	7.5	EBS only	High
c4.2xlarge	Compute optimized	8	15	EBS only	High
c4.4xlarge	Compute optimized	16	30	EBS only	High
c4.8xlarge	Compute optimized	36	60	EBS only	10 Gigabit
c3.large	Compute optimized	2	3.75	2 x 16 (SSD)	Moderate
c3.xlarge	Compute optimized	4	7.5	2 x 40 (SSD)	Moderate
c3.2xlarge	Compute optimized	8	15	2 x 80 (SSD)	High
c3.4xlarge	Compute optimized	16	30	2 x 160 (SSD)	High
c3.8xlarge	Compute optimized	32	60	2 x 320 (SSD)	10 Gigabit

Buttons: Cancel, Previous, Review and Launch, Next: Configure Instance Details

6) Default instance details are fine for us, click next

The screenshot shows the AWS Management Console interface for the 'Launch Instance Wizard'. The browser address bar displays the URL: <https://console.aws.amazon.com/ec2/v2/home?region=us-east-1#LaunchInstanceWizard>. The console header includes the AWS logo, 'Services', and user information 'Justin van de Ven' in 'N. Virginia'. The wizard progress bar shows seven steps: 1. Choose AMI, 2. Choose Instance Type, 3. Configure Instance (active), 4. Add Storage, 5. Tag Instance, 6. Configure Security Group, and 7. Review.

### Step 3: Configure Instance Details

Configure the instance to suit your requirements. You can launch multiple instances from the same AMI, request Spot instances to take advantage of the lower pricing, assign an access management role to the instance, and more.

Number of instances	<input type="text" value="1"/>	<a href="#">Launch into Auto Scaling Group</a>
Purchasing option	<input type="checkbox"/> Request Spot instances	
Network	<input type="text" value="vpc-36861952 (172.31.0.0/16) (default)"/>	<a href="#">Create new VPC</a>
Subnet	<input type="text" value="No preference (default subnet in any Availability Zo)"/>	<a href="#">Create new subnet</a>
Auto-assign Public IP	<input type="text" value="Use subnet setting (Enable)"/>	
Placement group	<input type="text" value="No placement group"/>	
Domain join directory	<input type="text" value="None"/>	<a href="#">Create new directory</a>
IAM role	<input type="text" value="None"/>	<a href="#">Create new IAM role</a>
Shutdown behavior	<input type="text" value="Stop"/>	
Enable termination protection	<input type="checkbox"/> Protect against accidental termination	
Monitoring	<input type="checkbox"/> Enable CloudWatch detailed monitoring	

At the bottom of the configuration section, there are four buttons: 'Cancel', 'Previous', 'Review and Launch', and 'Next: Add Storage'. The 'Next: Add Storage' button is highlighted with a red rectangular box.

The footer of the console includes a 'Feedback' link, 'English' language selection, copyright information '© 2008 - 2015, Amazon Web Services, Inc. or its affiliates. All rights reserved.', and links to 'Privacy Policy' and 'Terms of Use'.

7) Add sufficient storage for the simulation.

- a. The model advised that we require at least 8GB of storage space for the simulation. The basic system supplied with the instance takes up just over 21GB and the model takes up 0.5 GB. The model will return an error code if it runs out of storage space, and require re-launching. We consequently suggest that at least 10GB of storage beyond the very minimum is requested. In our context, this is 40GB (=21 + 8 + 0.5)

EC2 Management Console X Justin

https://console.aws.amazon.com/ec2/v2/home?region=us-east-1#LaunchInstanceWizard:

Apps finance computing NIESR MIAESR video FT FT Google Scholar Google Books Amazon.co.uk: 100 ...

AWS Services Edit Justin van de Ven N. Virginia Support

1. Choose AMI 2. Choose Instance Type 3. Configure Instance 4. Add Storage 5. Tag Instance 6. Configure Security Group 7. Review

### Step 4: Add Storage

Your instance will be launched with the following storage device settings. You can attach additional EBS volumes and instance store volumes to your instance, or edit the settings of the root volume. You can also attach additional EBS volumes after launching an instance, but not instance store volumes. [Learn more](#) about storage options in Amazon EC2.

Volume Type ⓘ	Device ⓘ	Snapshot ⓘ	Size (GiB) ⓘ	Volume Type ⓘ	IOPS ⓘ	Delete on Termination ⓘ	Encrypted ⓘ
Root	/dev/sda1	snap-0f48ba6b	40	General Purpose ▾	90 / 3000	<input checked="" type="checkbox"/>	Not Encrypted
Instance Store 0 ▾	xvdc	N/A	N/A	N/A	N/A	N/A	Not Encrypted ✕
Instance Store 1 ▾	xvdc	N/A	N/A	N/A	N/A	N/A	Not Encrypted ✕

[Add New Volume](#)

Free tier eligible customers can get up to 30 GB of EBS General Purpose (SSD) or Magnetic storage. [Learn more](#) about free usage tier eligibility and usage restrictions.

[Cancel](#) [Previous](#) [Review and Launch](#) [Next: Tag Instance](#)

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8) There is no need to tag our instance – press next

The screenshot shows the AWS Management Console interface for the EC2 Launch Wizard. The browser address bar displays the URL: <https://console.aws.amazon.com/ec2/v2/home?region=us-east-1#LaunchInstanceWizard>. The console header includes the AWS logo, navigation tabs (AWS, Services, Edit), and user information (Justin van de Ven, N. Virginia, Support).

The wizard progress bar shows seven steps: 1. Choose AMI, 2. Choose Instance Type, 3. Configure Instance, 4. Add Storage, 5. Tag Instance (current step), 6. Configure Security Group, and 7. Review.

### Step 5: Tag Instance

A tag consists of a case-sensitive key-value pair. For example, you could define a tag with key = Name and value = Webserver. [Learn more](#) about tagging your Amazon EC2 resources.

Key (127 characters maximum)	Value (255 characters maximum)
<input type="text" value="Name"/>	<input type="text"/>

(Up to 10 tags maximum)

At the bottom of the wizard, there are four buttons: [Cancel](#), [Previous](#), [Review and Launch](#), and [Next: Configure Security Group](#). The [Next: Configure Security Group](#) button is highlighted with a red rectangular box.

The footer contains links for [Feedback](#), [English](#), copyright information (© 2008 - 2015, Amazon Web Services, Inc. or its affiliates. All rights reserved.), [Privacy Policy](#), and [Terms of Use](#).

## 9) Edit security groups, and press review and launch

EC2 Management Console X Justin

https://console.aws.amazon.com/ec2/v2/home?region=us-east-1#LaunchInstanceWizard:

Apps finance computing NIESR MIAESR video FT Google Scholar Google Books Amazon.co.uk: 100 ...

AWS Services Edit Justin van de Ven N. Virginia Support

1. Choose AMI 2. Choose Instance Type 3. Configure Instance 4. Add Storage 5. Tag Instance 6. Configure Security Group 7. Review

### Step 6: Configure Security Group

A security group is a set of firewall rules that control the traffic for your instance. On this page, you can add rules to allow specific traffic to reach your instance. For example, if you want to set up a web server and allow Internet traffic to reach your instance, add rules that allow unrestricted access to the HTTP and HTTPS ports. You can create a new security group or select from an existing one below. [Learn more](#) about Amazon EC2 security groups.

**Assign a security group:** ☒ Create a **new** security group  
☐ Select an **existing** security group

**Security group name:** launch-wizard-3

**Description:** launch-wizard-3 created 2015-12-16T17:10:03.158+11:00

Type	Protocol	Port Range	Source
RDP	TCP	3389	My IP 120.148.90.240/32

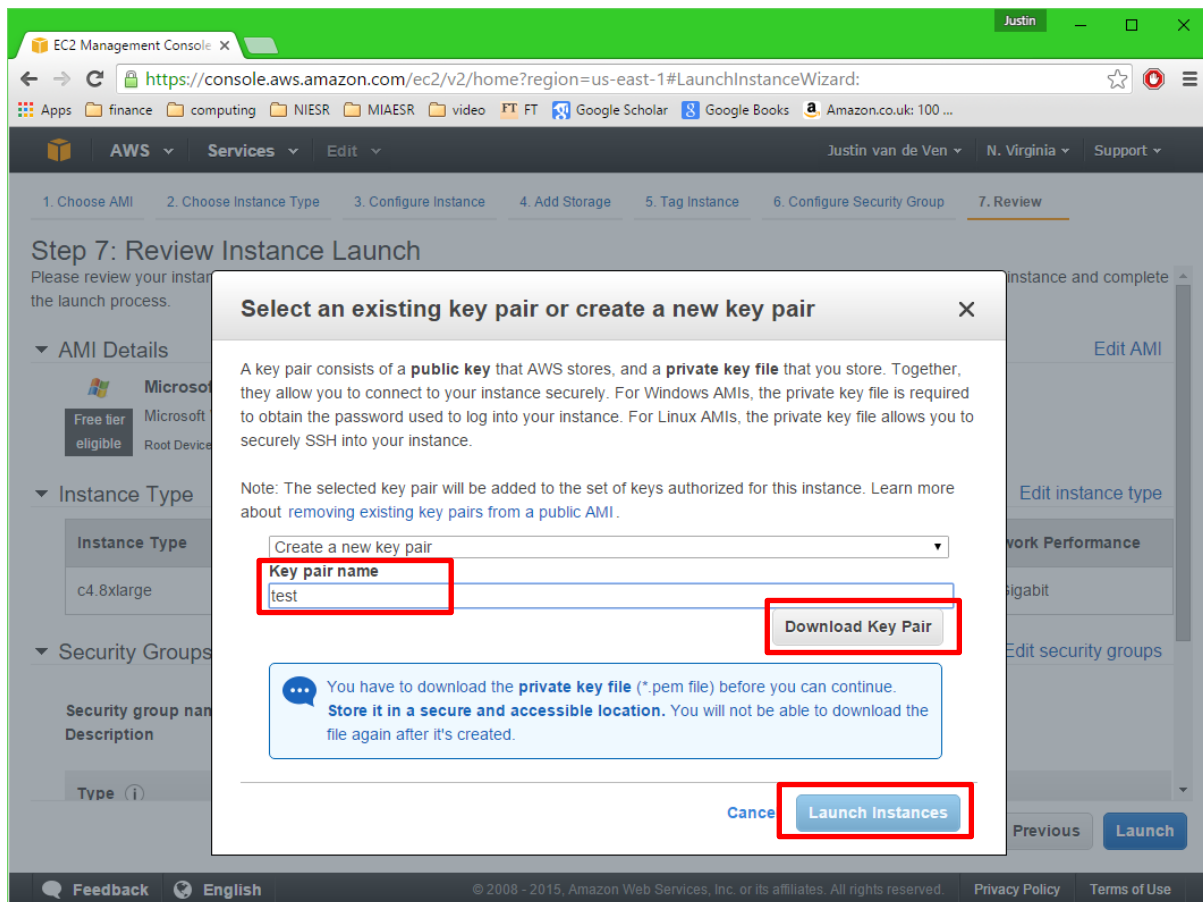
Add Rule

Cancel Previous **Review and Launch**

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- 10) Create a new key pair, download the key, and launch
- You start paying for the instance from the time that you press the Launch button.



11) Go to the instances monitoring page, and wait for the new instance to initialise

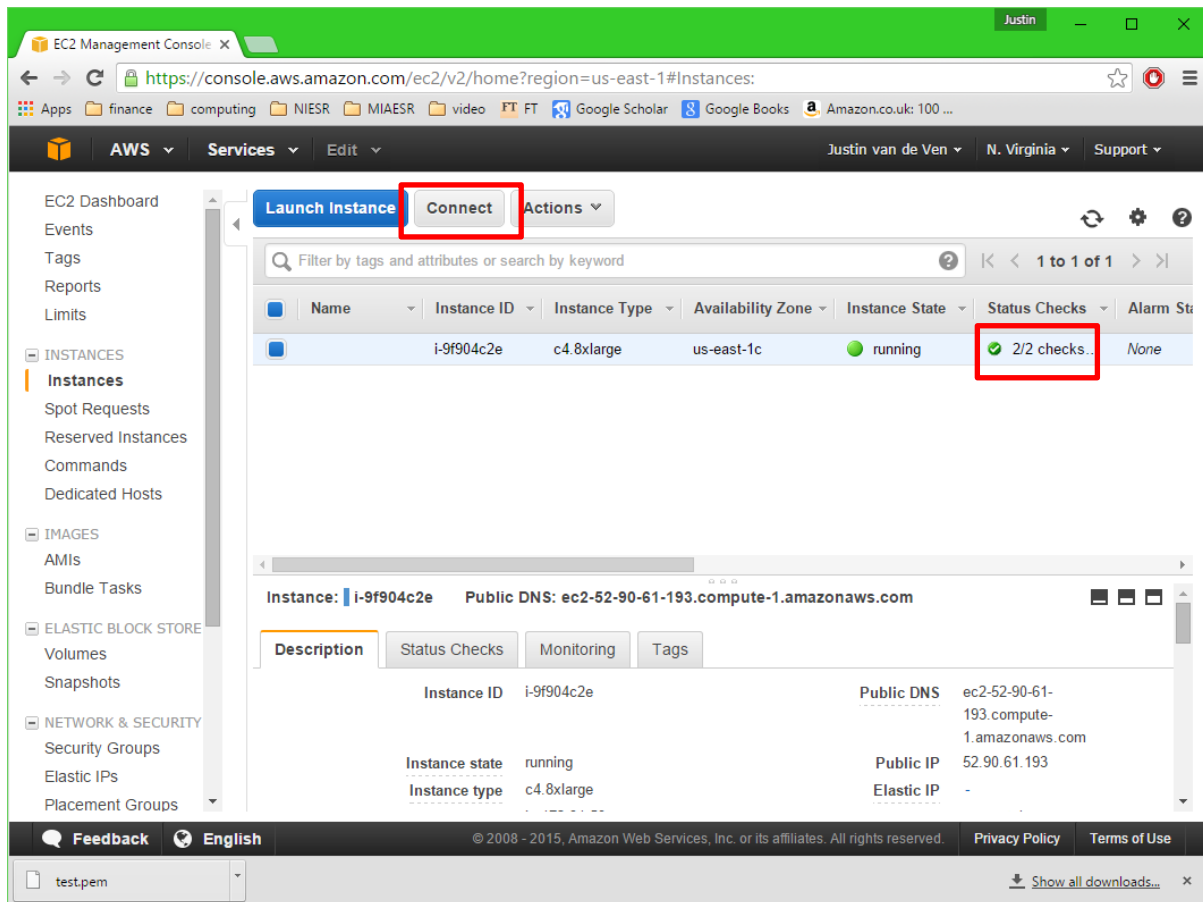
The screenshot displays the AWS Management Console for the EC2 service. The left-hand navigation pane shows the 'INSTANCES' section selected, with 'Instances' highlighted. The main content area shows a table of instances. A single instance is listed with the following details:

Name	Instance ID	Instance Type	Availability Zone	Instance State	Status Checks	Alarm Status
	i-9f904c2e	c4.xlarge	us-east-1c	running	Initializing	None

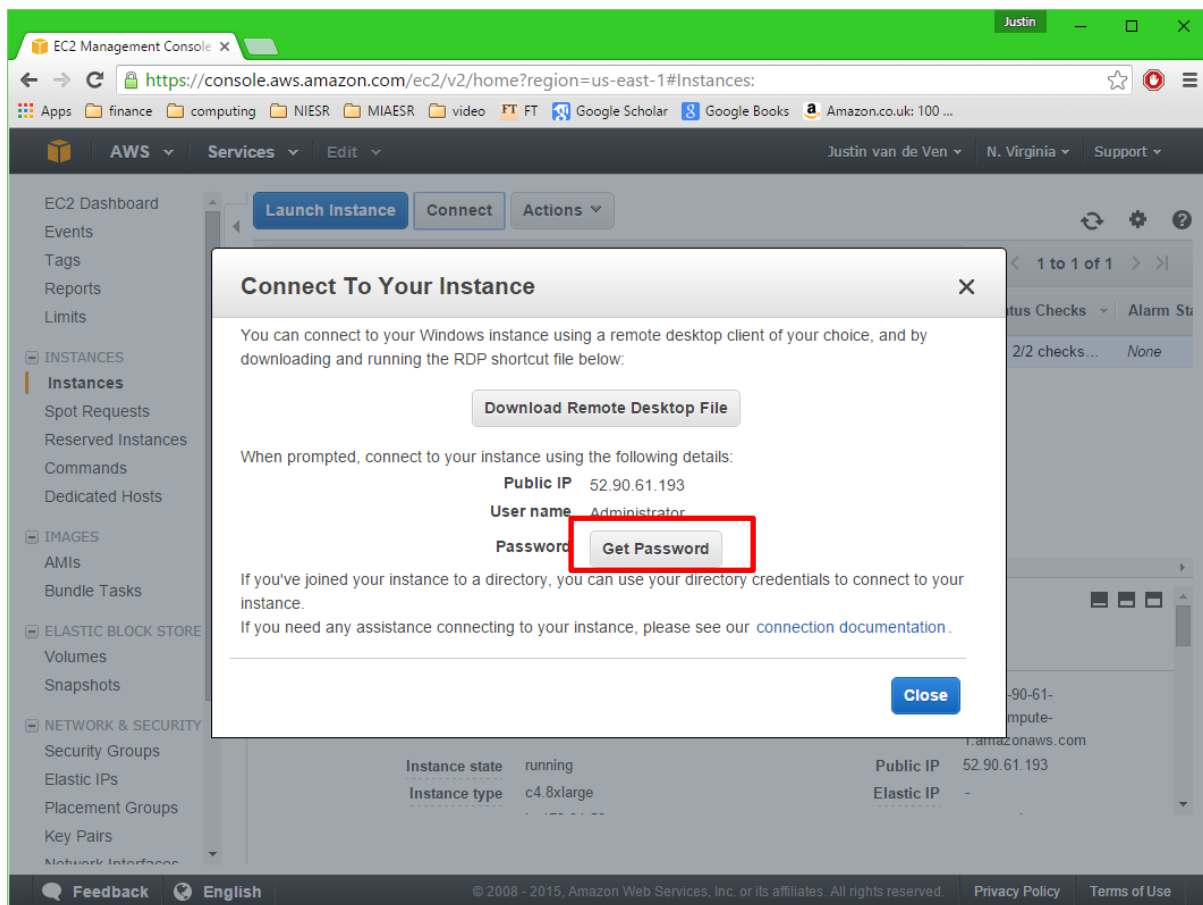
The 'Initializing' status in the 'Status Checks' column is highlighted with a red rectangle. Below the table, the details for the selected instance (i-9f904c2e) are shown, including the 'Public DNS' address: ec2-52-90-61-193.compute-1.amazonaws.com. The console also shows the 'Launch Instance' button and various navigation links at the top.

### Step 3: Upload the stand-alone model onto the cloud instance

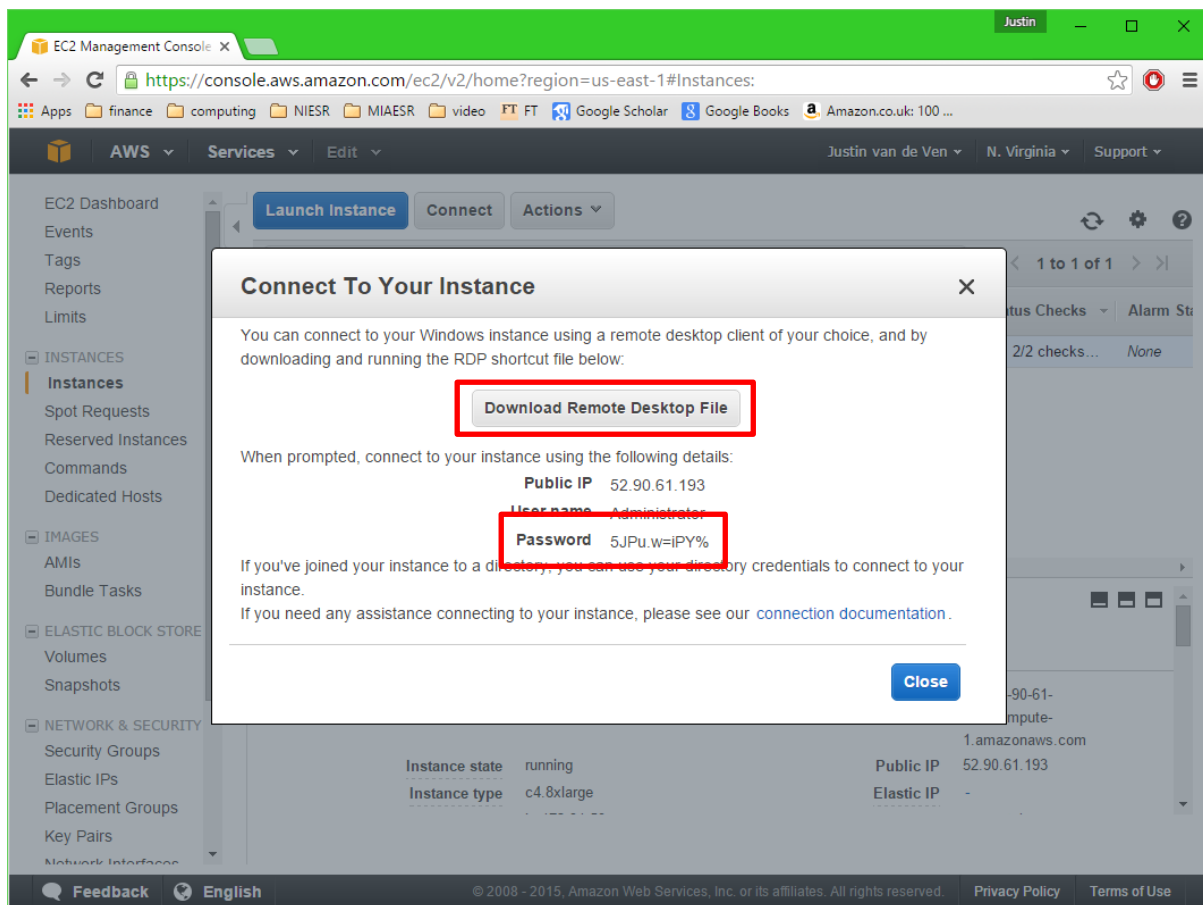
- 10) Put all of the files in the \MODEL subdirectory into a zipped folder
- 11) Connect to your instance once it is ready:



12) Use the key pair that was created at step 8 to obtain a password:



13) Store the password for future reference and download remote desktop file:



14) Open the remote desktop download, and connect using the password obtained in the preceding step.

15) After a moment for the initialisation, you should be able to see the desktop of your instance.

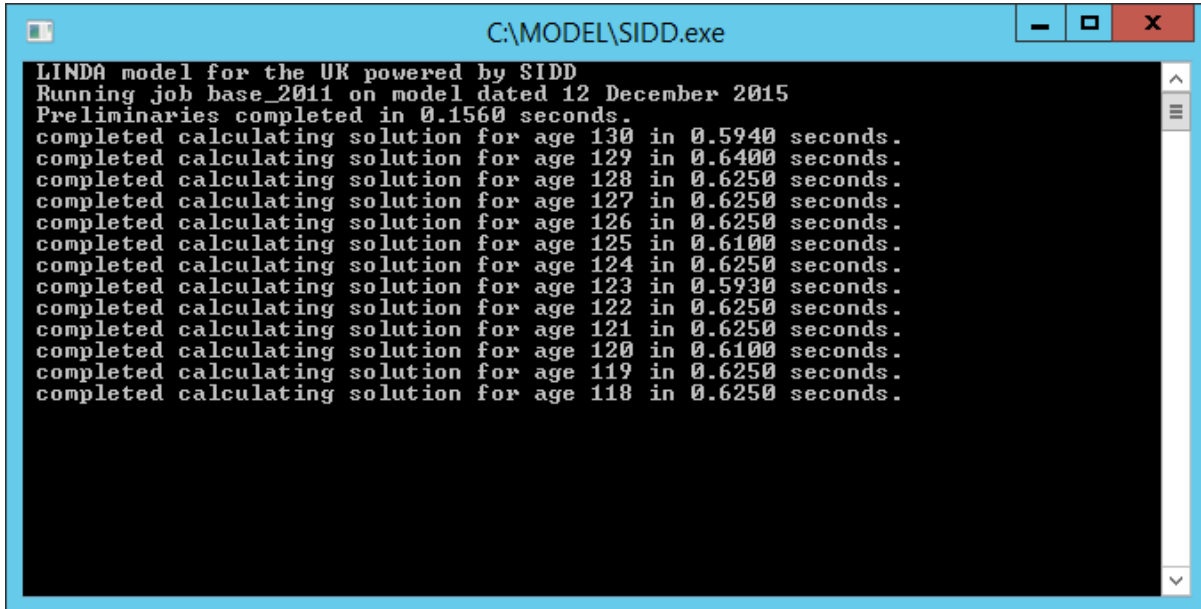
16) Copy the zip folder with the model onto your instance.

- a. Note that the time this takes will depend upon the speed of your internet connection
- b. Note also, that you should not copy or paste anything on your computer while the download is taking place, or it may fail

#### Step 4: Run the model on the cloud

- 17) When the download is complete, extract the model from the zip folder using Windows explorer to a folder of your choosing on the instance
- 18) Double click on SIDD.exe in the \MODEL subdirectory on the instance.

*The model should now run through to completion, providing a message when it is complete*



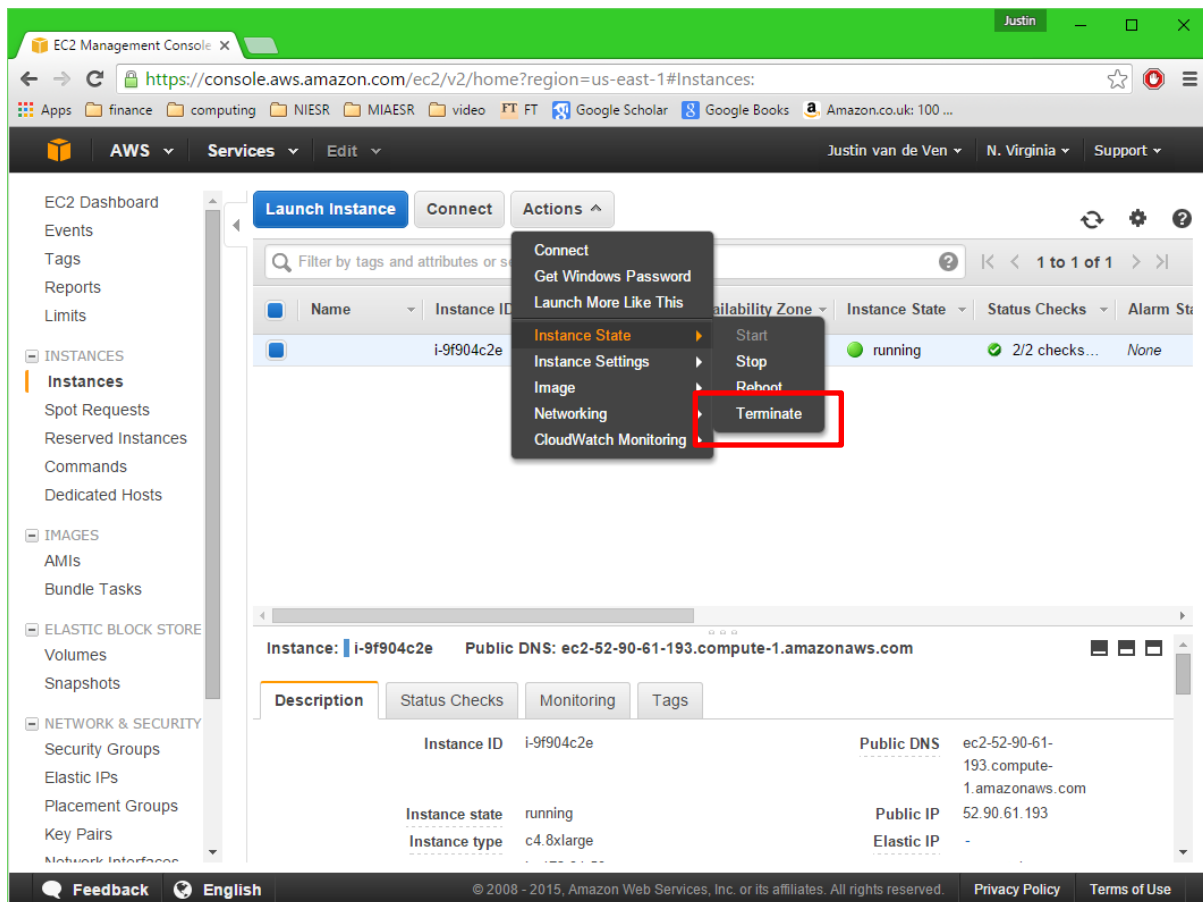
```
C:\MODEL\SIDD.exe
LINDA model for the UK powered by SIDD
Running job base_2011 on model dated 12 December 2015
Preliminaries completed in 0.1560 seconds.
completed calculating solution for age 130 in 0.5940 seconds.
completed calculating solution for age 129 in 0.6400 seconds.
completed calculating solution for age 128 in 0.6250 seconds.
completed calculating solution for age 127 in 0.6250 seconds.
completed calculating solution for age 126 in 0.6250 seconds.
completed calculating solution for age 125 in 0.6100 seconds.
completed calculating solution for age 124 in 0.6250 seconds.
completed calculating solution for age 123 in 0.5930 seconds.
completed calculating solution for age 122 in 0.6250 seconds.
completed calculating solution for age 121 in 0.6250 seconds.
completed calculating solution for age 120 in 0.6100 seconds.
completed calculating solution for age 119 in 0.6250 seconds.
completed calculating solution for age 118 in 0.6250 seconds.
```

## Step 5: Download results to the local computer

- 19) Put all of the files in the “\MODEL 02\simulations\2011\_base” subdirectory on your instance into a zip folder, including the “anals” and “long\_file” subdirectories, but omitting the “grids” subdirectory
- 20) Copy this zip file and paste it to your local computer
- 21) Extract the files and folders to a “2011\_base” folder in your “\MODEL 02\simulations” subdirectory.

## Step 6: Terminate the instance

- 22) You stop paying for the instance when the instance is terminated:



## **Step 7: Analyse model output – creating a new simulation base**

1. Re-open “Job File.xls”
2. Press ALT+F8
3. Select “SIDD” and press the RUN button
4. Enter “base\_2011” into the text-box with the title “name of run to adopt as new base”
5. Enter “base\_2011” into the text-box with the title “directory name for new base”
6. Press the “CONVERT RUN TO NEW BASE” button

Excel will then work away for a short while, after which you should receive a message confirming that the new base has been created. If you look in the BASE\_FILES subdirectory, you should now see a new subdirectory with the name “base\_2011”, which includes all of the files defining the base simulation specification.

### **Final points of note**

Up-load and down-load times can be non-trivial when working with the model. It may be possible to economise these costs by storing data in the cloud with your provider.

Another point that may help to economise data up-load and down-load times concerns the information that the model requires to run a simulation. In this case, the model requires all files in the \MODEL subdirectory, including its child subdirectories, except the following:

- No subdirectories are required under the “MODEL\simulations” directory
- The model only requires the files in the “MODEL\base\_files\XXX” subdirectory, where XXX refers to the name given to your prevailing simulation base (base\_2011 in the above example). All other subdirectories in “MODEL\base\_files\” can be omitted.



## 4. Altering Parameters

Most of the key model parameters are stored in the spread sheet “Job File.xls”. Altering this file name may prevent the main executable file SIDD.exe from locating the model parameters.<sup>8</sup> “Job File.xls” is comprised of a number of worksheets. The parameters which drive the model are present in the worksheet *input*. Parameter values of the base simulation are stored in the sheet *inputA*. Expert users can make changes directly to the parameters described in the *input* worksheet, without recourse to the user front-end. Alternatively, the front-end system of forms that is included with the spread sheet can be used to alter a selected set of model parameters. Differences between the data stored in the *input* and *inputA* sheets are identified by 1s in the *check* sheet. Any other sheets included in “Job File.xls” are beyond the scope of this manual, and should not be altered by the user.

To use the front-end, users should open “Job File.xls” and run the macro “*SIDD*”, visible in the Tools/Macros window (Alt+F8). This displays Form 0.

---

<sup>8</sup> The only exception is in the case when the user would like to “stack” a series of simulations for consecutive (automated) execution. In this case, the “job file” associated with each alternative simulation should be numbered in their order of execution – e.g. “job file1.xls”, “job file2.xls”, “job file3.xls”...

## FORM 0: SIMULATION TASK

FORM 0: SIMULATION TASK

NEW SIMULATION FOR UK

location of existing job file to load model parameters from  
(e.g. c:\new\_base\job file.xls) leave blank by default

NEW SIMULATION FOR ITALY

RUN EXISTING JOB FILE

name to adopt for existing job file  
2015p\_base

ANALYSE TAX FUNCTION

ANALYSE EXISTING SIMULATION

name of run to analyse

name of run to adopt as new base

starting year for new base simulations  
2015

directory name for new base (e.g. base\_2006)

CONVERT RUN TO NEW BASE

LOAD EXISTING JOB FILE

location of existing job file to load parameters from  
(e.g. c:\new\_base\job file.xls)

UNDERTAKE SHORT RUN ANALYSIS

ADJUST NUMBER OF TAX OUTPUTS

UPDATE FERTILITY PROBABILITIES

Form 0 offers the user a series of alternative options for running LINDA.

### *Setting up a New Simulation*

This function allows the user to define and run a new simulation from scratch. Pressing the “NEW SIMULATION FOR UK” button will lead to a series of alternative user forms, which are designed to guide the user through the process of altering a selected set of model parameters. The related forms are described below.

### *Run Existing Job File*

An existing job specification (as described by the parameters on the existing *input* sheet) can be run by clicking the “RUN EXISTING JOB FILE” button. The name of the simulation will be auto-populated with whatever name exists in cell A2 of the current *input* sheet. The user may alter this name to an alpha-numeric combination of their choosing. The model will then run, and save all associated results into a subdirectory with the name given to the simulation.

### *Analysing the Tax Function*

It is often useful to “eyeball” the influence of simulated taxes and benefits on benefit units. The model includes two analysis routines for this purpose, which can be accessed by pressing the

“ANALYSE TAX FUNCTION” button. The associated analysis routines are described under “Form D4” later in this manual.

#### *Analyse Existing Simulation*

The model permits a series of supplementary analyses to be run after a given simulation is complete. Pressing the “ANALYSE EXISTING SIMULATION” button will open a new form that allows the user to choose which additional analyses will be performed. This alternative is returned to under “Form 2” below.

#### *Convert Run to New Base*

As discussed in the introduction, the model projects a population through time assuming a series of “base” parameters. The base from which model projections are made can be re-specified to reflect any simulation that the user has previously run by listing the simulation name in the “NAME OF EXISTING RUN TO ADOPT AS BASE” text box, and pressing the “CONVERT RUN TO NEW BASE” button. A name for the new base must also be entered, and all associated files will subsequently be stored under the given name in the subdirectory “base\_files” of the main model directory. The model will subsequently use the specified simulation as its base for simulating a population forward through time.

#### *Load Existing Job File*

It may sometimes be useful to load in parameters from an existing job file for subsequent analysis. This can be achieved using the “LOAD EXISTING JOB FILE BUTTON”.

#### *Undertake Short-run Analysis*

The model will usually project the circumstances of a population forward through time from the base year, assuming a single policy environment. The “UNDERTAKE SHORT RUN ANALYSIS” button allows the population to be simulated forward assuming multiple policy environments. We return to describe this option further under “Form D1” below.

#### *Adjust Number of Tax Outputs*

The user can define a series of outputs relating to the tax and benefits structure that the model will save by default. We describe how to define additional transfer statistics in Section 8 of this manual. Where new outputs are desired, then the model parameters can be adjusted to accommodate these by pressing the “ADJUST NUMBER OF TAX OUTPUTS” button.

#### *Update Fertility Probabilities*

This is only necessary when the terms of fertility, as assumed in the model, are altered. If this is the case, then please contact the NIESR for further assistance.

## FORM 1: KEY PARAMETERS

FORM 1: KEY PARAMETERS

×

simulation name

start year of simulation

2015

maximum population size

200000

?

end year of simulation

2044

Tax function to simulate from

☒ 2016 tax and benefit structure
 

tax function reference year

2016

☐ 2011 tax and benefit structure
 

number of additional outputs generated by tax function

0

☐ user-defined tax structure
 

reference number for user tax structure

6

price reference year for simulated output

2015

?

☒ allow for Universal Credit

first year of Universal Credit

2017

?

Note that all financial terms are defined in prices for the tax function reference year

?

☐ reset all variables following start year of simulation

?

ENTER

ENTER and RUN

RESET

BACK

**TIP: Explanatory notes can be found by pressing the “?” buttons.**

### *Simulation Name.*

The user must provide name for each simulated scenario. The name can be flexibly defined, but should not include any of the following characters: < > : “ / \ | ? \*. The results of the simulation are stored in a sub-directory with the supplied name. We also recommend avoiding very long simulation names.

### *Start year of simulation*

The model will project forward, starting from data described for the year defined in this form.

### *End year of simulation, maximum population size, and maximum year of birth of any simulated cohort*

The model is designed to project the evolving population cross-section forward through time. Projecting a population cross-section forward through time involves expanding the simulated population size, to accommodate entry into the sample of immigrants and the maturation of dependent children. The model will augment the simulated population in every year that it projects

forward until it encounters any one of the following three conditions: (i) it reaches the end of the simulated time horizon, (ii) it reaches the maximum population size, or (iii) it encounters maturing children born after the maximum year defined here. Thereafter, no additional individual is added to the simulated population.

#### *Tax function to simulate from*

LINDA is supplied with a number of pre-programmed tax and transfer systems (see Appendix C for related detail). Users should use the radio buttons in Form 1 to select the tax system that they wish to apply. Specific parameters characterising these systems are specified in later forms. It is also possible to direct the model to use an alternative tax schedule that they have written themselves. Details about how to specify an entire tax schedule are discussed in Section 8.

#### *User-defined tax output*

The model is set-up to permit the user to define specific tax and benefits statistics that the model will generate for each simulated individual. How these statistics are defined is discussed in Section 8. The number of statistics that the user has defined should be provided in the associated text box on this form.

#### *Price reference year for simulated output*

The simulated output includes a wide range of financial statistics, all of which are defined as real (inflation adjusted) relative to a given reference year. The reference year that the model uses to generate these statistics is defined here.

#### *Reset all variables following start year of simulation*

Comparisons between simulations are facilitated by ensuring that selected demographic characteristics are the same as projected under the base simulation. The model is set-up to do this by default, which can be over-ridden by selecting the option displayed here. The related demographic characteristics include timing of death, cohabitation, fertility, migration, and health. The option provided here should be selected whenever analysing counterfactual assumptions regarding the transition rates of any of these demographic characteristics.

## FORM 2: ANALYSE EXISTING SIMULATION

FORM 2: USER DEFINED ANALYSIS ROUTINES

×

Population summary statistics of selected years

?

year 1

year 2

year 3

year 4

year 5

year 6

High-level analysis of population cross-sections

?

year 1

year 2

year 3

year 4

year 5

year 6

High-level analysis of individual birth cohorts

?

birth year 1

birth year 2

birth year 3

birth year 4

birth year 5

birth year 6

☐ tick if calculate statistics for equivalised income deciles

?

?

☐ analyse population cross-section

min cross-section / birth year

1965

☒ analyse birth cohort

max cross-section / birth year

1975

☐ generate long-file format data optimised for importing into Stata

?

ANALYSE TAXES

ENTER

ENTER and RUN

BACK

The user can request that the model run a series of alternative pre-programmed analysis routines, in addition to those that it runs for each simulation by default. All routines report statistics either to the screen or specific excel files after a model run has completed. The Excel files are saved in a subdirectory with the name given to the simulation scenario (as defined in Form 1).

### *Population summary statistics*

This routine produces summary statistics designed to reflect the cross-sectional state of the economy. Results are saved in Excel files named 'hi\_level\_statsYYYY.xls' where YYYY denotes the considered year.

### *High-level analysis of population cross-sections / birth cohorts*

This routine reports a broad range of summary statistics for the specified population cross-sections and birth cohorts, including rates of employment, means and variances of income, consumption, wealth, and rates of pension scheme participation. These statistics are reported in files with names “YYYYcs.xls” for cross-sectional statistics, and files ending “YYYYby.xls” for birth cohorts, where “YYYY” refers to the relevant year.

### *Calculate statistics for equivalised income deciles*

The model can be directed to produce simulated averages for population deciles, specified by equivalised disposable benefit unit income. The revised OECD equivalence scale is used to adjust disposable incomes. If the model is directed to analyse data for a population cross-section, then the relevant year should be included in the form as directed. Otherwise, the birth year of the cohort of interest should be provided.

### *Generate long-file format*

The model can be directed to save the microdata generated for the population in a format that is designed to facilitate importing into secondary statistical packages, including Stata.

The “ANALYSE TAXES” button in this sheet is provided to allow a second chance (in addition to that provided on FORM 0) to explore the properties of the assumed tax and benefits system, rather than run a full simulation. We have found it useful to include this option here to facilitate the development of user defined tax and benefit schemes, as is discussed in Section 8.

## FORM 3: DECISION MAKING

FORM 3: DECISION MAKING

×

☐ use description of utility maximising decisions from another simulation

name of simulation to use to project decisions

temp

*Preference parameters*

relative risk aversion (1/gamma)

1.55

utility price of leisure (alpha)

2.2

elasticity btw cons and leisure (epsilon)

0.6

discount Factor (delta), singles

0.97

short-run discount factor (beta)

1

discount Factor (delta), couples

0.93

*Reduced-form decisions*

☐ project decisions using reduced form wherever possible

☐ project employment decisions using reduced-form

☐ project consumption decisions using reduced-form regression

2006

2011

?

ENTER

ENTER and RUN

RESET

BACK

Projections made by LINDA typically proceed in two discrete stages. In the first stage, the model evaluates a look-up table that describes utility maximising decisions for all feasible simulated combinations of individual specific circumstances (the model state-space). In the second stage, starting from micro-data for a representative population cross-section, LINDA projects panel data at annual intervals for the evolving population cross-section. These panel data are generated using statistical descriptions for the intertemporal evolution of individual specific characteristics and the behavioural descriptions evaluated in the first stage. Importantly, the utility maximising decisions evaluated in the first stage are based on the same statistical descriptions for intertemporal evolution as are used in the second stage of the projection. It is this feature that makes the projected decisions ‘rational’.

The two-stage procedure described in the preceding paragraph is necessary to capture ‘rational’ decision making. It can, however, lead to simulation run-times that limit flexibility of the analyst. In many practical contexts, the analyst may find that the costs of ‘rational projections’ in terms of the implied run-times outweigh the benefits of ensuring that decisions are consistent with the intertemporal incentives that people face. The model has consequently been designed to allow the analyst to choose to avoid the first-stage of the model projection.

There are two ways to avoid calculating a look-up table for utility maximising decisions when making projections using LINDA. One approach is to project decisions using ‘reduced form’ equations that have been estimated on historical survey data. The alternative approach involves projecting decisions



using a look-up table evaluated for an alternative simulation. Either one of these options can be selected via Form 3

### *Preference Parameters*

The preference relation assumed for the model is described in Appendix B of this manual. Key parameters governing the nature of the preference relation can be altered within this sheet. Please note that the preference parameters that are supplied with the model are the product of a detailed (and complex) calibration process (see Lucchino and van de Ven, 2013, for a description of how these parameters were calibrated). *It is advised that these parameters should be altered only for the purpose of exploring model sensitivity to alternative assumptions.*

### *Reduced-form decisions*

The model can be directed to project a selected set of decisions using either a reduced-form or structural approaches. It is also possible to mix the approaches, in the sense that one set of decisions can be simulated using reduced forms, and another set using a structural framework.

Reduced-form and structural frameworks of decision making share a great deal in common. Both approaches are based upon the assumption that past behaviour can be used as a basis for anticipating behaviour in the future. Both approaches typically describe past behaviour as a function of a set of observable characteristics. Furthermore, the precise nature of the relationships between decisions of interest and observable characteristics is commonly evaluated statistically drawing on survey data sources, whether a model is based on a reduced-form or structural framework. The key distinguishing feature is that a reduced-form approach to model behaviour is based only on correlations between decisions and (observable) explanatory variables, whereas a structural approach is designed to interpret (observable) correlations through the lens of a theory concerning how decisions are made.

A structural model assumed for LINDA is expressly designed so that changes in incentives feed through to behaviour in a logical fashion, guided by so-called “deep parameters”, which are assumed to be invariant to changes in either time or the policy environment. A reduced-form approach, in contrast, is ill-equipped to reflect behavioural variation to altered incentives. There are, however, (at least) two important drawbacks of the structural approach. First, the structural approach is more computationally demanding, implying longer simulation run-times, and complicating associated parameterisation. Secondly, a structural model can increase the difficulty of interpreting simulated effects of policy change, as behaviour may adapt to altered incentives in complex ways. These two drawbacks suggest that it may be preferable to adopt a reduced form analytical approach when undertaking preliminary analysis of potential policy reforms. A reduced form approach will also be preferred when interest is focussed on impact effects (omitting behavioural responses) of policy change. In contrast, a structural approach becomes essential when projections of interest need to adapt to the altered incentives associated with a policy counterfactual.

In context of the current model, it is the view of the model’s developers that behavioural rigidities make reduced form projections preferred for near-term time horizons (up to 5 years), and the importance of capturing the influence of changing incentives make structural projections preferable for medium to long-term time horizons (5 years and over).

## FORM 4: SELECTED EMPLOYMENT PARAMETERS

FORM 4: SELECTED EMPLOYMENT PARAMETERS

×

☒ part-time / full-time / not employed
   
☐ full-time / not employed
   
☐ user defined employment options
 

number of labour options  
(where user defined)

  
☐ distinguish private and public sectors
   
☒ impose minimum hourly wage rate(s)
 

lower age bound	age of maturity	<input type="text" value="21"/>	<input type="text" value="25"/>	<input type="text" value="90"/>
minimum wage rate (£ p.h.)		<input type="text" value="5.299999"/>	<input type="text" value="6.700000"/>	<input type="text" value="6.700000"/>
growth rate into future (% real)		<input type="text" value="1.5"/>	<input type="text" value="1.5"/>	<input type="text" value="1.5"/>

### *Employment options*

Here the user can choose between alternative specifications for the simulated labour supply decision of each adult: full-time/not employed; full-time/part-time/not employed; and an option that allows the user to define an arbitrary number of labour supply alternatives. When the third of these options is chosen, then the model assumes that the same hourly wage rate applies to all labour alternatives. If the full-time/part-time option is chosen, then hourly wage rates may vary by the labour decision.

### *Public and private sector employees*

The model can be directed to distinguish between public and private sector employees, which can differ from one another in relation to their occupational pension arrangements, wage profiles, and likelihood of involuntary unemployment.

### *Minimum hourly wages*

Tick this box to impose minimum hourly wage rates. Minimum hourly wage rates can be defined to vary over four age bands, and values should be set for the year from which the respective minimum applies. The model applies the NMW by assuming that any individual who's underlying productivity implies a lower hourly wage rate at a given employment option (e.g. full-time / part-time) than the prevailing minimum wage cannot find work at the respective employment option. The temporal growth rates to assume for minimum wage rates in forward projections are also be defined here

## FORM 5: FERTILITY ASSUMPTIONS

FORM 5: FERTILITY ASSUMPTIONS

☒ explicitly model number and age of dependent children in each household

number of child birth ages
3
?
age at which child matures
17

	<i>parent age at birth</i>	<i>max. no. of births</i>		<i>parent age at birth</i>	<i>max. no. of births</i>
child birth age 1	20	2	child birth age 11	41	2
child birth age 2	29	2	child birth age 12	42	1
child birth age 3	37	2	child birth age 13	43	1
child birth age 4	35	2	child birth age 14	44	1
child birth age 5	28	2	child birth age 15	45	1
child birth age 6	30	2	child birth age 16	46	1
child birth age 7	32	2	child birth age 17	47	1
child birth age 8	36	2	child birth age 18	48	1
child birth age 9	38	2	child birth age 19	49	1
child birth age 10	40	2	child birth age 20	50	1

ENTER
ENTER and RUN
RESET
BACK

To ensure that the model will solve within the desired timeframe, it is currently necessary to restrict child “births” to a small set of “child birth ages” (e.g. 3). To offset this stylisation, the model allows for multiple births at each child birth age. The parameters in this form allow the number and timing of child birth ages to be defined, the number of children that can be born at each age, and the number of years that children are considered to remain dependents. It is also possible to suppress explicit consideration of children through this user form, which will allow the model to complete a simulation in appreciably less time.

## FORM 6: SELECTED DISABILITY PARAMETERS

FORM 6: SELECTED DISABILITY PARAMETERS

×

☐ distinguish between disability states

?

☐ limit consideration of disability to "older adults"

youngest age of "older adults"

61

☐ permit carry over of DLA/PIP post state pension age
☒ distinguish carers
☐ distinguish child disability

☒ model disability benefits even though disability state not explicit?

?

ENTER

ENTER and RUN

RESET

BACK

The model can be directed to generate disability states for the simulated population. Four disability states are included in the base model specification, and simulated adults are assumed to be able to transition to any one of the four disability states from one year to the next, subject to transition probabilities that vary by age and prevailing disability status:

- 1) *Non-disabled*: This is the default condition, in which individuals are assumed to be physically capable of work, not to require any care, and subject to 'normal' living costs.
- 2) *Moderate work-limiting disability*: This disability state is assumed to impede work effort, and to receive recognition through the transfer system via eligibility for ESA work related activity benefits. Affected individuals are assumed to be physically capable of work, not to require any care, and subject to 'normal' living costs.
- 3) *Significant work-limiting disability*: This disability state is assumed to impede work effort, and to receive recognition through the transfer system via eligibility to both ESA support and PIP benefits. Affected individuals are assumed to be capable of limited work effort, may require care up to but not exceeding the day or night but not both. Individuals with significant work-limiting disabilities are also assumed to be subject to higher living costs, reflecting the value of DLA/PIP.
- 4) *Severe impairment*: This disability state is assumed to prevent any work effort, and to receive recognition through the transfer system via ESA support and PIP benefits. Affected individuals are assumed to require care during both the day and the evening, and are subject to increased living costs.

Modelling disability states is computationally intensive. This computational burden can be reduced by limiting consideration of disability to people of older ages. Alternatively, it is also possible to direct the model to project disability states for dependent children.

If disability states are accommodated, then the model can be directed to track receipt of disability related benefits from pre-state pension age, thereby allowing DLA recipients to maintain their benefits into older age.

It is possible to direct the model to identify benefit units that include adults who care for disabled individuals. This aspect of the model is designed to reflect the incidence of Carer's Allowance.

If disability states are not explicitly accommodated by the model, it is still possible to reflect the effects of disability related benefits in the simulation. In this case, benefits are simulated to reflect the average incidence of disability by age reported in survey data.

## FORM A1: INCOME TAX AND NATIONAL INSTURANCE (2010/11)

FORM A1: INCOME TAX AND NATIONAL INSURANCE

×

### Income Tax Rates and Thresholds

<i>Tax thresholds</i>	<i>Tax rates</i>	<i>NIC rates &amp; UEL (LEL=Personal Allowance)</i>
2nd tax threshold <input type="text" value="35000"/> £ p.a.	rate 1 <input type="text" value="20"/> %	rate 1 <input type="text" value="12"/> %
3rd tax threshold <input type="text" value="150000"/> £ p.a.	rate 2 <input type="text" value="40"/> %	rate 2 <input type="text" value="2"/> %
4th tax threshold <input type="text" value="200000"/> £ p.a.	rate 3 <input type="text" value="50"/> %	primary threshold <input type="text" value="139"/> £ p.w.
5th tax threshold <input type="text" value="250000"/> £ p.a.	rate 4 <input type="text" value="50"/> %	upper earnings limit <input type="text" value="817"/> £ p.w.
6th tax threshold <input type="text" value="300000"/> £ p.a.	rate 5 <input type="text" value="50"/> %	
	rate 6 <input type="text" value="50"/> %	

### Personal Allowances

<i>Working lifetime</i>	<i>From state pension age</i>
personal allowance <input type="text" value="7475"/> £ p.a.	personal allowance <input type="text" value="10015"/> £ p.a.
wdrwl threshold <input type="text" value="100000"/> £ p.a.	1: lower threshold <input type="text" value="24000"/> £ p.a.
PA wdrwl rate <input type="text" value="50"/> %	1: upper threshold <input type="text" value="29080"/> £ p.a.
	wdrwl rate1 <input type="text" value="50"/> %
	2: lower threshold <input type="text" value="100000"/> £ p.a.
	wdrwl rate2 <input type="text" value="50"/> %

ENTER

ENTER and RUN

RESET

BACK

The form reported here is for the 2010 and 2011 tax structures, and a slightly different form is presented for the 2006 tax structure. This form allows the user to specify the structure of income tax and national insurance. Consistent with contemporary tax policy in the UK, income taxes are calculated on individual specific “taxable income”, obtained by subtracting an individual’s Personal Allowance from their gross income. There are six possible tax rates and two national insurance rates. The first tax rate applies to taxable income up to the “2<sup>nd</sup> Tax Threshold”, the second tax rate to the “3<sup>rd</sup> Tax Threshold”, and so on. Similarly, “Rate 1” NICs are applied to taxable income between the “Primary Threshold” and the “Upper Earnings Limit”, and “Rate 2” applied to taxable income in excess of the Upper Earnings Limit.

Individuals under state pension age and with a taxable income in excess of a “Wdrwl Threshold” have their Personal Allowance reduced at the rate “PA Wdrwl Rate”. The adjustment of the Personal Allowance for people over state pension age is somewhat more complex. In this case, the Personal Allowance is withdrawn at “Wdrwl Rate1” on taxable income between “1: lower threshold”, and “1: upper threshold”, and is withdrawn at “Wdrwl Rate2” on taxable income in excess of “2: lower threshold”.

## FORM A2: TAX CREDITS – WORKING LIFETIME

FORM A2: TAX CREDITS - WORKING LIFETIME

×

Working Tax Credit

Benefit rates

basic element

1920

£ p.a.

couples / lone parent addition

1950

£ p.a.

30 hour element

790

£ p.a.

minimum benefit

0

£ p.a.

minimum age for receipt

25

Allowable child care

one child

175

£ p.w.

two or more children

300

£ p.w.

cost covered

70

%

Thresholds and withdrawal rates

?

first threshold

6420

£ p.a.

first withdrawal rate

41

%

second threshold

26000

£ p.a.

second withdrawal rate

41

%

Child Tax Credit

Benefit rates

family element

545

£ p.a.

child element

2555

£ p.a.

child element max children

10

Thresholds and withdrawal rates

?

first threshold

15860

£ p.a.

first withdrawal rate

41

%

second threshold

26000

£ p.a.

second withdrawal rate

41

%

ENTER

ENTER and RUN

RESET

BACK

The parameters of the Working Tax Credit and the Child Tax Credit can be altered via Form A2. The 30 hour element of the WTC is considered to be awarded in respect of full-time employment of at least one adult benefit unit member. In the case of both the WTC and the CTC, the first withdrawal rate applies to gross income earned between the first and second thresholds, and the second withdrawal rate to gross income earned in excess of the second threshold until the respective benefit is exhausted.

If Universal Credit is selected for analysis in Form 1, then only those parameters that are relevant to the simplified tax structure are displayed.

46 | Page

## FORM A3: HOUSING RELATED BENEFITS

FORM A3: HOUSING RELATED BENEFITS

×

	<i>Eligible rent</i>		<i>Council tax single adults</i>		<i>Council tax couples</i>	
1 bedroom	<input type="text" value="162.5"/> £ p.w.		<input type="text" value="14.168"/> £ p.w.		<input type="text" value="19.228"/> £ p.w.	<input type="text" value="?"/>
2 bedroom	<input type="text" value="188.5"/> £ p.w.		<input type="text" value="16.192"/> £ p.w.		<input type="text" value="22.264"/> £ p.w.	
3 bedroom	<input type="text" value="221"/> £ p.w.		<input type="text" value="18.216"/> £ p.w.		<input type="text" value="27.324"/> £ p.w.	
4 bedroom	<input type="text" value="260"/> £ p.w.		<input type="text" value="20.24"/> £ p.w.		<input type="text" value="32.384"/> £ p.w.	

<i>Allowances</i>		<i>Premia</i>	
personal allowance	<input type="text" value="67.5"/> £ p.w.	family	<input type="text" value="17.4"/> £ p.w.
lone parent allowance	<input type="text" value="72.3"/> £ p.w.	single pensioner	<input type="text" value="69.85"/> £ p.w.
couples allowance	<input type="text" value="105.95"/> £ p.w.	pensioner couple	<input type="text" value="103.75"/> £ p.w.
children allowance	<input type="text" value="62.33"/> £ p.w.	single incapacity benefit recipient	<input type="text" value="99.85"/> £ p.w.
		couple incapacity benefit recipient	<input type="text" value="138.3"/> £ p.w.

<i>Earnings disregards</i>			
single adult	<input type="text" value="5"/> £ p.w.	HB taper rate	<input type="text" value="65"/> %
lone parent	<input type="text" value="25"/> £ p.w.	HB minimum payment	<input type="text" value="0.5"/> £ p.w.
couple	<input type="text" value="10"/> £ p.w.	CTB taper rate	<input type="text" value="20"/> %
additional	<input type="text" value="17.1"/> £ p.w.	CTB min payment	<input type="text" value="0.01"/> £ p.w.

☒ allow for council tax benefit

ENTER

ENTER and RUN

RESET

BACK

Form A3 defines the housing costs and related benefits assumed by the model. Rental costs are based upon the number of children in a benefit unit, and Council Tax varies by benefit unit relationship status. Matching to survey data suggests that these housing costs should be based on assumptions made by the Department for Work and Pensions in producing the Tax Benefit Model Tables for local authority tenants and not private tenants (as had been assumed in the past). This seems a more sensible assumption for those toward the bottom of the distribution. The “Allowances”, “Premia”, “Earnings Disregards” and taper rates assumed for Housing Benefit and Council Tax Benefit can all be varied here.



## FORM A4: BENEFITS FOR NON-DISABLED

FORM A4: BENEFITS FOR NON-DISABLED

×

Income Support

Benefit Value		Benefit Value		Assets test	
jobseeker allowance personal	71 £ p.w.	jobseeker allowance couple	111.45 £ p.w.	exemption singles	6000 £
jobseeker allowance lone parent	71 £ p.w.	free school meals	6.2 £ p.w.	exemption couples	6000 £
				rate of imputed rent	0.4 %

Carer's Allowance

?

basic rate of benefit	55.55 £ p.w.	premium for ESA / IS	31 £ p.w.	premium for PC	55.3 £ p.w.
first income withdrawal threshold	0 £ p.w.	withdrawal rate	0 %	income cut-off	102 £ p.w.

Pension Credit

Benefit Value		Benefit Value		Assets test	
guarantee credit singles	137.35 £ p.w.	savings credit threshold singles	103.15 £ p.w.	exemption singles	10000 £
guarantee credit couples	209.7 £ p.w.	savings credit threshold couples	164.55 £ p.w.	exemption couples	10000 £
guarantee credit withdrawal rate	100 %	savings credit withdrawal rate	40 %	withdrawal rate	0.2 %

Flat-rate Benefits

child benefit - eldest child	20.3 £ p.w.	flat-rate state pension - single	0 £ p.w.
child benefit - other children	13.4 £ p.w.	flat-rate state pension - couple	0 £ p.w.

ENTER

ENTER and RUN

RESET

BACK

Form A4 allows the user to set the terms for a range of benefits designed to support non-disabled people, including Income Support, Carer's Allowance, Pension Credit, and Child Benefit. This form also permits the user to allow for a hypothetical flat-rate "citizen's pension" to individuals above state pension age.

Universal Credit will replace Jobseeker's Allowance. However, the full form will continue to appear when Universal Credit is selected, as Universal Credit is based on some of the same parameters as Jobseeker's Allowance / Income Support.

In addition to income tests, assets tests can be applied to means tested benefits. In the pre-packaged tax and benefit schemes, assets tests are accommodated by: 1) calculating an implicit rent flowing from benefit unit assets; 2) adding the implicit rent to other benefit unit income; 3) applying the aggregate income to the relevant income test.

## FORM A4: DISABILITY BENEFITS

FORM A5: DISABILITY BENEFITS

### Employment and Support Allowance

Personal Allowances		Premia	£ p.w.	min disability status	
singles	67.5 £ p.w.	work-related activity	26.75	2	
couples	105.95 £ p.w.	support	32.35	3	

Assets test

exemption singles	10000 £	exemption couples	10000 £	imputed rent	0.2 %
-------------------	---------	-------------------	---------	--------------	-------

### Disability Living Allowance / Personal Independence Payment

care comp.	£ p.w.	min disability status	Premia		
lower rate	19.55	3	Child Tax Credit	2800	£
standard rate	49.3	3	WTC standard	2650	£
enhanced rate	73.6	4	WTC enhanced	1130	£

mobility comp.

	£ p.w.	min disability status		single	couple	£ p.w.
lower rate	19.55	3	ESA enhanced	14.05	20.25	£ p.w.
higher rate	51.4	3	ESA severe	55.3	110.6	£ p.w.

### Attendance Allowance

	£ p.w.	min disability status	Premia	single	couple	£ p.w.
lower rate	49.3	3	PC severe	55.3	110.6	£ p.w.
higher rate	73.6	4				

ENTER
ENTER and RUN
RESET
BACK

Three benefit schemes designed to support people with disabilities are pre-programmed in the model: Employment and Support Allowance, Disability Living Allowance / Personal Independence Payment, and Attendance Allowance. The value of each of these benefits, and the minimum disability condition required for eligibility, are defined in this form.

## FORM A6: AGE THRESHOLDS

FORM A5: AGE THRESHOLDS

×

### Incapacity Benefit Age

☒ model Incapacity Benefit as a vehicle to fund early retirement (if no can ignore following parameters)

	back in time	base		forward in time			
age	55	55	55	55	56	57	58
from year	1925	1945	1950	2011	2019	2026	2034

### Pension Credit Qualifying Age

☒ allow age of eligibility for Pension Credit to differ from State Pension Age (if no can ignore following parameters)

	back in time	base		forward in time			
age	60	60	60	61	62	63	64
from year	1925	1945	2009	2011	2012	2014	2016

☒ set eligibility age for Pension Credit to State Pension Age from given year: 2018

### State Pension Age

	back in time	base		forward in time			
age	65	65	65	65	66	67	68
from year	1925	1945	1950	2011	2019	2026	2034

ENTER

ENTER and RUN

RESET

BACK

**Incapacity Benefit Age:** This is the lowest age at which incapacity benefit is assumed to be available as a form of early retirement support. This age can be allowed to vary through time, as indicated by the auto-populated figures.

**Pension Credit Qualifying Age:** This is the lowest age at which the Pension Credit is assumed to be available. The model allows the qualifying age for Pension Credit to differ from State Pension Age, consistent with current legislation. The Pension Credit Qualifying Age can be allowed to vary through time, and any disparity with State Pension Age can be suppressed from an exogenously specified year.

**State Pension Age:** This is the age from which state pensions are taken. Any employment income after State Pension Age is not subject to NICs and all individuals are assumed to be eligible to the Pension Credit from State Pension Age under the pre-programmed tax structures.

## FORM A7: UNIVERSAL CREDIT

FORM A7: UNIVERSAL CREDIT

×

Higher Work Allowance		Lower Work Allowance	
single adult	<input type="text" value="108.38"/> £ p.m.	single adult	<input type="text" value="108.38"/> £ p.m.
lone parent	<input type="text" value="716.7"/> £ p.m.	lone parent	<input type="text" value="256.8"/> £ p.m.
single work limited	<input type="text" value="631.75"/> £ p.m.	single work limited	<input type="text" value="187.47"/> £ p.m.
couple	<input type="text" value="108.38"/> £ p.m.	couple	<input type="text" value="108.38"/> £ p.m.
couple with child	<input type="text" value="523.36"/> £ p.m.	couple with child	<input type="text" value="216.77"/> £ p.m.
couple work limited	<input type="text" value="631.75"/> £ p.m.	couple work limited	<input type="text" value="187.47"/> £ p.m.

taper rate on  
employment inc

%

ENTER

ENTER and RUN

RESET

BACK

This form allows the user to input parameters defining Universal Credit. It only appears if Universal Credit is selected in Form 1.

## FORM A8: INDIRECT TAXATION

FORM A8: INDIRECT TAXATION

×

☒ model consumption taxes

*Indirect tax rates*

VAT full rate

20

%

alcohol

50

%

VAT reduced rate

5

%

tobacco

80

%

insurance premium  
tax - standard rate

6

%

fuels

66

%

insurance premium  
tax - higher rate

20

%

ENTER

ENTER and RUN

RESET

BACK

LINDA can be directed to include an allowance for indirect taxes in the simulated analysis. In this case, the model uses reduced form regression equations to disaggregate aggregate consumption (which is simulated endogenously) into the consumption categories that are subject to alternative tax rates. The model therefore accounts for income effects associated with indirect taxes (ie the reduction in aggregate purchasing power), but not price effects (ie the influence of indirect taxes on relative prices of alternative consumption subgroups). Please contact the NIESR for further details.

## FORM C1: STATE CONTRIBUTORY PENSIONS

FORM C1: STATE CONTRIBUTORY PENSIONS

×

Contributory Pension 1

value of pension depends on years of contributions modelled on basic State Pension

☒ tick if included in simulations
 ☐ tick if simulated endogenously ?

maximum value of pension - single adult  £ p.w.

maximum value of pension - couple  £ p.w.

contrib years for maximum benefit

contribution years to obtain minimum ben

min employment income to qualify  £ p.w.

benefit growth pre state pension age  %

benefit growth from state pension age  %

☒ contributions received in respect of involuntary unemployment

☒ contributions received in respect of child care

Contributory Pension 2

value of pension depends on years of contributions and income modelled on State Second Pension

☐ tick if included in simulations
 ☐ tick if simulated endogenously ?

lower earnings limit  £ p.w.

lower earnings threshold  £ p.w.

upper accrual point  £ p.w.

accrual rate 1  %

accrual rate 2  %

benefit growth pre state pension age  %

benefit growth from state pension age  %

☐ amend terms of Contributory Pension 2 to conform to private pensions? ?

Note: all growth rates are real (inflation adjusted)

Form C1 allows two forms of State contributory pension to be included in the analysis. Contributory Pension 1 offers a flat-rate increase in the pension payable from state pension age for each year that contributions are accredited during the working lifetime, and is designed to reflect the basic State Pension. Contributory Pension 2 provides pension benefits from state pension age that can increase with earnings during the working lifetime, and is designed to reflect the State Second Pension.

## FORM C2: NON-PENSION WEALTH

FORM C2: NON-PENSION WEALTH

×

☐ tick if investment in risky assets

?

☒ tick if unsecured debt allowed

☒ tick if investment in ISAs allowed

annual ISA contribution limit

10200

£

expected rate of return to ISA savings

1.2

%

std. dev. of return to ISAs  
(set this to zero if certain)

0

%

decision cost of ISA account set-up

0

£

ENTER

ENTER and RUN

RESET

BACK

This form defines parameters that determine the types of non-pension assets that the simulated population has access to. The model necessarily includes a basic “liquid asset”, to allow for disparities between consumption and income in any given year. The user can also specify that the simulated population can allocate some of their liquid wealth to a risky investment asset, whether the simulated population has access to (unsecured) credit, or whether they are able to invest in an Individual Savings Account (ISA).

If ISAs are included for analysis, then parameters governing the terms of this asset class can also be amended.

## FORM C3: PRIVATE PENSIONS

FORM C3: PRIVATE PENSIONS

×

Private Pension (Superannuation) Parameters

☒ tick if any private pension available

lower income threshold

0

£ p.w.

no. of pensions available (up to 5)

1

☒ pension participation endogenous

☐ project participation decision using reduced form

2006

2011

?

☐ contribution rate endogenous

☐ project contribution rate using reduced form

☐ project timing of pension access using reduced form

☐ model decision costs for pension decisions

☐ allow alternative employee/employer contributions

	Private Pension 1	Private Pension 2	Private Pension 3	Private Pension 4	Private Pension 5
(minimum) employee contribution rate (%)	8	8	8	0	0
employer contribution rate (%)	14	12	16	0	0
alternative employee contribution rate (%)	6	8	8	0	0
alternative employer contribution rate (%)	17	12	8	0	0
annual management costs (% of capital)	0	0	0	0	0
opt out of contrib pens	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
default to opt-in	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
proportion of pension taken as lump-sum	25 %				
rate of return (expected)		3.5 % p.a.			
std dev of return			13 % p.a.		
				<input type="checkbox"/> tick if returns uncertain	

ENTER

ENTER and RUN

BACK

RESET

Form C3 allows the parameters of personal pension schemes available in the model to be set. It is necessary to ensure that the check-box “tick if any private pension available” is set to allow for private pensions in the model simulations.

If private pensions are accommodated in the simulations, then it is possible to allow for endogenous decisions regarding pension participation, allow the contribution rate to be endogenous, and to limit decisions concerning the contribution rate to be made between two discrete alternatives. It is also possible to allow for multiple private pension types in the simulation, which differ from one another over a range of details including (minimum) employee and (fixed) employer contribution rates, and management investment charges (that reduce total annual returns). Pension contributions are specified as a percentage of labour income, and only if labour income exceeds the lower threshold defined in this form.

If pension participation is made endogenous, then it is possible to simulate this decision using a reduced-form equation. If the decision is not simulated using a reduced form equation, then the utility maximisation problem can be associated with a “decision cost”, designed to account for the importance of default options as indicated by the available empirical literature. If “decision costs



over pension decisions” are included for analysis, then it is also necessary to indicate whether the default option is to opt-in to private pensions.

The form also allows you to indicate whether participating in a private pension implies “opting out” of the second state contributory pension (see Form C1).

Parameters defining the rate of return to private pensions, and whether these returns are uncertain can also be specified. If uncertain returns are considered the box should be ticked and the standard deviations of the rates of return set.

The parameters that have been included here by default are designed to approximate occupational pensions, as these stood in 2011. A single pension type is assumed to limit computation time. The 14% employer contribution rate reflects a strong (single) mode of employer contributions as reported by the Family Resources Survey, and the 8% employee contribution rate is referred to as ‘normal’ in the guidance to interviewers for the Family Resources Survey.

## FORM C4: VARIATION OVER PRIVATE PENSION ELIGIBILITY

FORM C4: VARIATION OVER PRIVATE PENSION ELIGIBILITY

×

Private Pension Variation from One Year to the Next

	Income Regime 1	Income Regime 2	Income Regime 3	
upper income threshold	315	99999	all incomes in excess of regime 2	£ p.w.
probability of job change	15	15	15	%
Probability of pension scheme eligibility, given job change				
private pension 1	70	10	45	%
private pension 2	20	60	30	%
private pension 3	10	30	25	%
private pension 4				%
private pension 5				%

ENTER

ENTER and RUN

BACK

RESET

Form C4 will only appear if, in Form C3, “the number of pensions available” is set to a value between 2 and 5. In this case, benefit units are considered to be eligible to participate in only one private pension scheme in any year. Eligibility to each scheme is identified stochastically with reference to income-dependent probabilities defined in Form C4.<sup>9</sup>

The likelihood that a benefit unit is eligible to a given pension scheme in each year depends upon whether they chose to participate (contribute to) their eligible pension in the preceding year and their income. Individuals who chose not to participate in a given scheme receive a new random draw from the available pensions in the immediately succeeding year. In this case, the probability of drawing a scheme varies over three alternative income regimes. Individuals who chose to participate in a given scheme are automatically assumed to be eligible to the same scheme in the immediately succeeding year, unless they experience a job change. A job change has no influence on the benefit unit’s circumstances, other than to indicate that the pension to which they are eligible is taken as a new random draw (in the same way as it would if they chose not to participate in the preceding year).

<sup>9</sup> The 15% probability of job change assumed here is indicative only – analysis by C. Macaulay, ONS *Labour Market Trends*, November 2003, pp. 514-550, reports that 74% of people working in the private sector remained with the same employer after 12 months in 2001 (83% for public sector workers). This suggests an upper bound for the job-change probability of 26%, which would be appropriate if transitions into employment were ignored.

## FORM C5: PRIVATE PENSIONS (cont.)

FORM C5: PRIVATE PENSIONS (cont.)

×

**State Sponsored Incentives to Save in Private Pensions (Superannuation)**

*Concessional contributions*

tax rate on contributions

0

%

contributions cap

1000000

£p.a. to age

65

contributions cap

1000000

£p.a. to age

70

contributions cap

1000000

£p.a. all higher ages

limits on rates of tax relief

minimum

20

%

maximum

100

%

*Non-concessional contributions*

tax rate on contributions

0

%

contributions cap

1500000

£p.a. to age

70

contributions cap

1500000

£p.a. to age

71

contributions cap

1500000

£p.a. all higher ages

☐ can make contributions after pension take-up

ENTER

ENTER and RUN

BACK

RESET

This form sets the tax treatment of pension contributions and dispersals. Concessional contributions refer to pension contributions that receive some tax relief, in contrast to Non-concessional contributions. Caps on contributions can be administered within three mutually exclusive age bands, and the tax relief given to concessional contributions can also be subject to limits. The bottom panel of this form also allows the terms of pension dispersals to be defined.

## FORM C6: ESCALATION

FORM C6: ESCALATION

tax thresholds	<input type="text" value="1.2"/>	% p.a.	benefit thresholds	<input type="text" value="1.2"/>	% p.a.	<input type="button" value="?"/>
benefits	<input type="text" value="0"/>	% p.a.	pension contribn thresholds	<input type="text" value="1.2"/>	% p.a.	
value of guarantee credit	<input type="text" value="1.2"/>	% p.a.	maximum value of savings credit	<input type="text" value="0"/>	% p.a.	
child-care costs	<input type="text" value="2.2"/>	% p.a.	housing costs	<input type="text" value="1.2"/>	% p.a.	
trend wage growth assumed for model parameterisation (for information only)				<input type="text" value="1.52"/>	% p.a.	

Two sets of model parameters define growth adjustments in the model. Year specific escalation factors for each of the eight categories defined in this form are loaded into the model from the 'model index factors' sheet of the 'FINANCIAL PARAMETERS.xls' spreadsheet, found in the respective base directory (...\\MODEL 02\\base\_files\\[base name]\\). The model requires escalation factors for all eight categories at annual intervals between a given start year and end year. The start and end years in the 'model index factors' sheet can be altered as desired.

Beyond the sample that is explicitly defined in the 'model index factors' sheet, the model projects escalation factors forward through time using the growth rates that are defined in Form C6 here.

Trend wage growth that was assumed when initially defining model parameters is also reported in this form to aid selection of related parameters.

When the form is complete the ENTER button is pressed. The RESET button restores the initial values of all of the parameters.

## FORM C7: SELF-EMPLOYMENT

FORM C7: SELF-EMPLOYMENT

×

☒ tick if self-employment included in the simulated population

☒ allow contributions to own business assets

contribution rate to own business wealth  %

rate of return (expected)  % p.a.

std dev of return  % p.a. ☐ tick if uncertain

*Capital gains taxes (on own business wealth)*

tax free threshold  £ p.a.

capital gains tax basic rate  %

entrepreneurs' relief rate  %

entrepreneurs' relief rate cap  £ p.a.

☐ allow contributions by the self-employed to private pensions

contribution rate to private pensions  %

ENTER

ENTER and RUN

RESET

BACK

This form allows the user to indicate whether the self-employed should be included in the analysis. If the self-employed are included, then the user can also define whether the model should account for own-business assets, and private pension contributions.

## FORM C8: EDUCATION

FORM C8: EDUCATION

×

☒ allow for heterogeneity over education status
   
☒ allow for differences between graduates and non-graduates
   
☒ take tertiary student status into account at entry to simulated population ?
  

proportion type 1 students

0.72

age of completion student type 1

23

failure rate

0.14

age of completion student type 2

27

  
☒ allow for differences between non-graduate education levels ?
  
☒ allow for no qualifications
   
☒ allow for second level qualifications (5+ A\*-C GCSEs)
   
☒ allow for third level qualifications (2+ A-levels)
   
☒ allow for fourth level qualifications (apprentices)
   
☒ apply user defined low wage offers in forward projections ?
  

ENTER and RUN

RESET

BACK

The model can be directed to distinguish the population by up to 5 educational categories, as indicated in the form here. Graduates are distinguished from non-graduates in relation to their wage parameters, rates of (involuntary) unemployment, marital rates, and divorce rates. Individuals holding alternative non-graduate education levels can also be allowed to differ from one another in relation to their wage parameters and rates of unemployment.

For the greater part of the simulated lifetime the qualifications of each reference adult remain time-invariant. The sole exception occurs toward the beginning of the simulated lifetime, when the model can be defined to consider the circumstances of students in tertiary education

A student at entry to the sample is considered to remain a student until their respective graduation age. Graduation ages can take one of two values, where type 1 students are considered to graduate before type 2. All individuals identified as students at entry to the simulated sample, and over the graduation age for type 1, but not type 2, are identified as type 2 students. An exogenously defined fraction of individuals identified as students and under the graduation age for type 1 students are defined as type 1 and the remainder as type 2 students. All individuals identified as students and over graduation age 2 are ignored. Achieving graduate status is uncertain and depends upon an exogenously defined failure rate. These parameters can be set in the top half of form C8.

The statistics for age of completion of education, and the proportion of type 1 students are taken from wave 1 of the Wealth and Assets survey. As the statistical evidence to support the assumed failure rate is reasonably weak, the assumed parameter should be treated as approximate only.

## FORM D1: SHORT-RUN ANALYSIS

The screenshot shows a dialog box titled "FORM D1: SHORT-RUN ANALYSIS" with a close button (X) in the top right corner. The dialog contains the following fields and controls:

- A text input field labeled "Simulation Name".
- A checkbox labeled "tick if 2 transition years (default is 1)".
- A row with two text input fields: "name of simulation to assume for starting environment" and "transition year".
- A row with two text input fields: "name of simulation to assume following first transition year" and an empty field.
- A row with two text input fields: "name of simulation to assume following second transition year" and an empty field.
- Two buttons at the bottom: "ENTER and RUN" and "BACK".

The LINDA model can be used to gain an appreciation of the medium term behavioural implications of a policy change. Specifically, it is possible to consider how a population cross-section will evolve through time if they were confronted by a series of unexpected changes to the policy environment. Up to two policy changes can be considered during any given model run.

To undertake this type of analysis the user should do the following:

- 1) Run each of the policy scenarios that are of interest (as described in "Setting up a New Simulation" below), choosing any run names that you prefer.
- 2) After completing the simulations in (1), re-open "job\_file.xls", start the *SIDD* macro, and press the "UNDERTAKE SHORT RUN ANALYSIS" button.
- 3) Enter the name of the folder in which to store the short-run output in the top text box of Form D1
- 4) Enter the transition year(s) in the text boxes as indicated.
- 5) Enter the run names defined in (1) in the remaining text boxes.
- 6) Press the "START ANALYSIS" button.

## FORM D4: ANALYSIS OF TAX FUNCTION

FORM D4: ANALYSIS OF TAX FUNCTION

Define tax parameters for analysis:

- ☐ tax parameters for prevailing model base
- ☐ tax parameters from prevailing input sheet
- ☐ define tax parameters for analysis
- ☒ tax parameters from another job file

name of simulation to analyse:

Define type of tax analysis:

- ☐ single individual type (tax\_test1)
- ☐ flexible individual type (tax\_test2)
- ☒ static projection from base data

name to save simulated output:

ENTER BACK

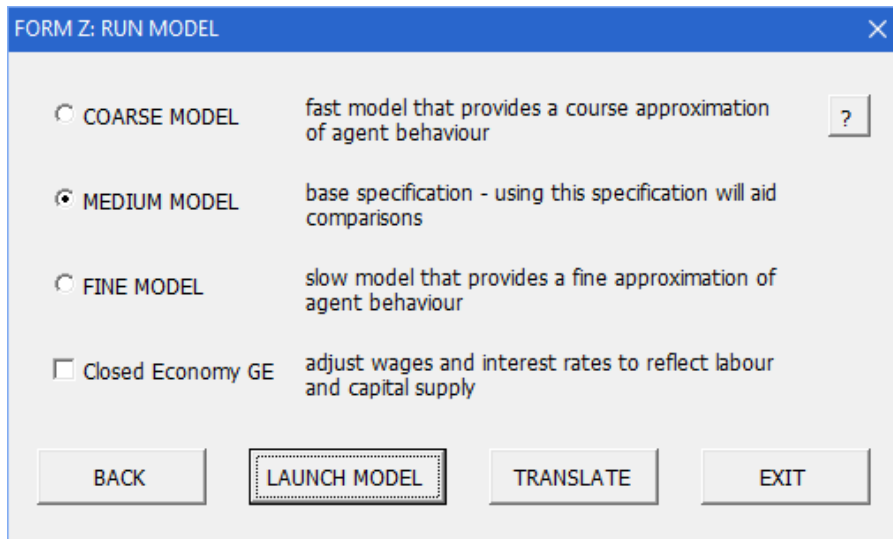
Form D4 defines the terms of the tax analysis routines to run. The top half of this form specifies the tax parameters to consider for analysis. If the option to “define tax parameters” is selected, then pressing enter in this form will jump to Form A1, as described previously in this manual. Selecting “tax parameters from another job file” permits the projections implied by a previously conducted simulation to be explored, in which case the name of the respective simulation must also be defined.

The model includes three methods for analysing the effects of the tax and benefits code. The first method listed here focuses upon a user-defined benefit unit type, in context of a range of alternative measures of private income. The second method listed here considers a set of broad circumstances that are designed to capture a population cross-section. Input statistics, and analytical results for each of these two routines are communicated, respectively, through the files “tax\_test1.xls” and “tax\_test2.xls”, located in the assumed base directory (defined in cell E27 of the *input* sheet of “Job File.xls”).

The third method listed here involves projecting forward the effects of taxes and benefits, taking as given the benefit unit characteristics described by the base population data. The model expects these base data to describe a previously simulated population, rather than the WAS survey data. If the current model specification simulates from the reference cross-sectional data described by the WAS, then the Excel forms will generate a warning message. If this analysis is requested, then it is also necessary to enter a name into which the projected data will be stored.



## FORM Z: RUN MODEL



This final form allows the user to go back to Form C8, to run the model, to export model parameters ready for running the simulation on a cloud instance (see Section 3), or exit the Excel forms. Three options are also provided for running the model. Running the “course model” achieves a fast run-time, but at the cost of numerical accuracy. This option should be used for exploratory analyses only. At the other end of the scale, running the “fine model” implies a relatively long run-time, to obtain a high degree of numerical accuracy. An intermediate option between these two extremes is also provided, and we recommend using the “medium model” specification in general.<sup>10</sup>

The base specification has been set up to balance the competing objectives of accuracy with computation time. It is recommended that this base specification be maintained, and that the alternative model specifications be used for the purpose of sensitivity analysis only.

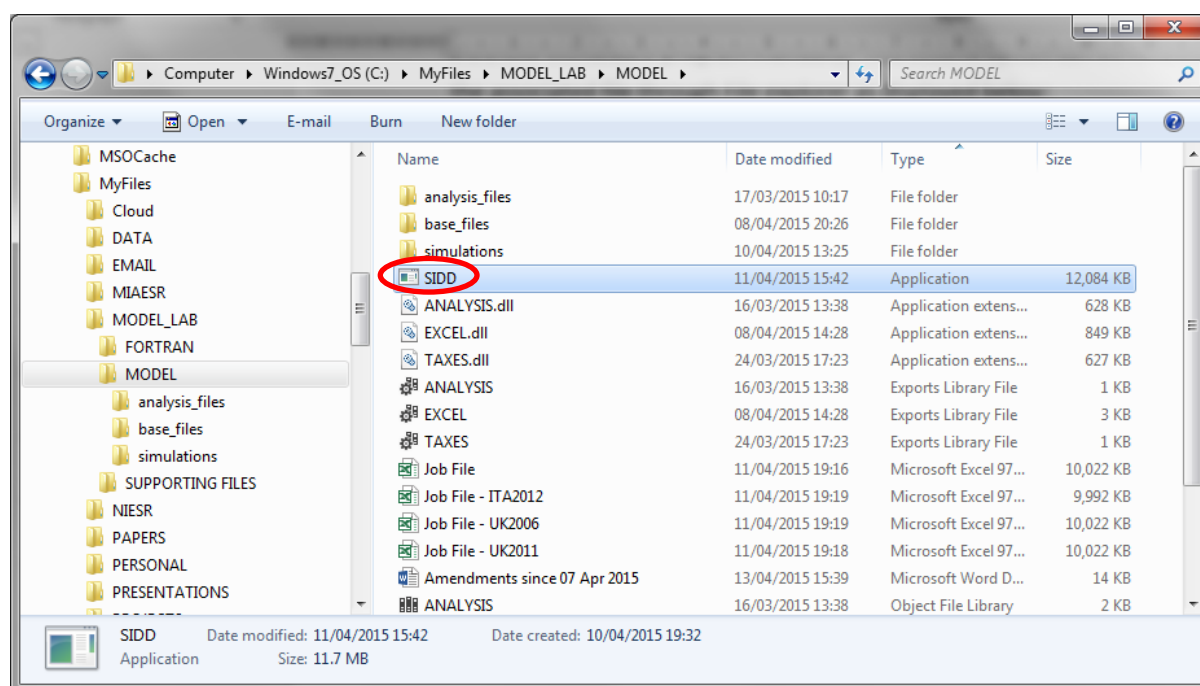
Finally, the user can direct the model to adjust capital and labour prices to reflect a General Equilibrium in a closed economy. This option is discussed at further length in Section 6, under the subheading “High-level summary statistics”.

---

<sup>10</sup> The coarse and medium model specifications both use linear interpolation and Brent’s method for solving in one dimension or Powell’s method for solving in multiple dimensions. These two specifications differ only in the number of “grid points” that are used to approximate the state space. The fine model specification uses cubic interpolation, and then cycles between Brent’s/Powell’s method and a Simplex search routine. The fine model specification also divides the state space into appreciably more points than the coarse and medium model specifications.

## 5. Running the model on a local computer

Having specified model parameters (see Section 3), it is time to set the model running. This can be done either through the model Excel front-end – see Form Z in Section 3 – or by launching the SIDD.exe executable program manually. This second option can be followed, by double-clicking on the associated file through File explorer as displayed below:



### Stacking simulation counterfactuals

It is possible to set the model up so that it will automatically work consecutively through a list of “job file” specifications.

The Excel front-end works on the assumption that a single simulation will be run, with parameters stored in the default file “Job File.xls”. When the model executable file SIDD.exe first starts, however, it looks in the base model subdirectory (where SIDD.exe is saved) for a file named “job file1.xls”. If it finds a file with this name, then it will load in the parameters saved in that file and perform the associated simulation. When that simulation is complete, the model will jettison the parameters described by “job file1.xls”, and search for a file named “job file2.xls”. If it finds “job file2.xls”, then it will load in the parameters saved in that file and perform the associated simulation. The model will then continue working in a similar way, searching for a file named “job file(X+1).xls”, after completing the simulation described by file “job file(X).xls”, until no consecutively higher numbered file is found, at which time the model will stop. If the model fails to find a file named “job file1.xls”, then it will revert to the default file “Job File.xls”, and will stop after the single simulation is complete.

To set-up a series of model simulations to be run in consecutive order, it is possible to work through the Excel front-end described in Section 3 for each simulation in turn, remembering to adopt a different “simulation name” for each specification in FORM 1, and press “EXIT” at FORM Z. Then save the associated excel file with the name “job fileX.xls”, setting X to 1 for the first simulation, 2 to

the second, and so on. When all of the desired files have been set-up, double-click on SIDD.exe as described above, and the model will work its way through the simulations in turn. ***Please remember to delete the numbered files “job fileX.xls” when the stacked simulations have completed.*** Failure to do this will mean that the model will perform undesired simulations when used on subsequent occasions.

## 6. Simulation Output

The model generates by default two levels of statistics for each simulation and saves these in the sub-directory “simulations\xxx\”, where “xxx” refers to the name given to the specific simulation (see discussion on “form 1” above). The model produces, for each benefit unit in the reference population cross-section, simulated panel data for a range of characteristics over the life-course. These “micro-data” are reported in a standard format (csv) that is accessible by widely available statistical packages. Furthermore, the model can be directed to report output in a format that is optimised for importation into the Stata statistical package.

Secondly, the model also generates a core set of summary statistics for each simulation, which are reported in the excel file “hi\_level\_statistics.xls”.

Each of these respective model outputs is discussed separately below.

### Benefit unit level micro-data

The model can be directed to save all of the simulated characteristics projected by each simulation in “Comma Separated Variable” format (CSV), which can be accessed by most statistical software including Excel and Stata. Each simulated characteristic is saved with a separate file name. The data in each file are stored as a two dimensional table, with each row representing a single simulated adult, and each column a single simulated year. The model is designed to economise the use of disk space by only saving those variables that are actually generated by a simulation. The file names that may be produced by a simulation, and a description of the associated data, are listed below.

age:	age of reference adult
alc_dy:	alcohol duty paid (£ per week)
bcohort:	birth cohort
benX:	disaggregated state welfare benefits (£ per week): <ol style="list-style-type: none"><li>1: (Income Support + Employment Support Allowance) or Universal Credit + Flat Rate State Pension + Winter Fuel Payments</li><li>2: Tax Credits</li><li>3: Child Benefit</li><li>4: Council Tax Benefit less Council Tax (negative if Council Tax not fully subsidised)</li><li>5: Housing Benefit</li><li>6: Disability Living Allowance + Personal Independence Payment + Attendance Allowance</li><li>7: Carer Allowance</li></ol>
benagg:	aggregate state welfare benefits less council taxes (excl. state pensions, £ per week)
ben_unit:	benefit unit identifier, equal to the person identifier (psnno) of the reference adult
carer:	one adult carer in the benefit unit
comexcc:	non-discretionary childcare expenditure (£ per week)
comexhl:	non-discretionary healthcare expenditure (£ per week)
comexhs:	non-discretionary expenditure on rent and mortgage interest payments (£ per week)
comexot:	other non-discretionary expenditure (£ per week)
cons:	non-durable discretionary consumption of benefit unit (£ per week)
cons_ind:	non-durable consumption of simulated individual (includes both cons and non-discretionary expenditure, £ per week)
cp1:	number of contribution years for rights to the first state contributory pension (BSP)
cp2:	second state contributory pension (S2P) (£ per week)
cpinc:	state pension income (cp1/2) received (£ per week)

death_age:	age at which reference adult dies
donor:	psnno of adult used to initialise characteristics (for maturing children and immigrants)
dppart:	flag = 1 if default is to participate in personal pensions / 0 to not participate
education:	highest education level achieved during the simulated lifetime (1 = lowest qualification, n = highest), in order of attainment (right columns come later – interpret with reference to <i>educndage</i> )
educndage:	ages at which education level changes
emp1/2:	employment status of benefit unit reference adult / spouse (0 indicates non-employment, and <i>n</i> indicates full-employment, where <i>n</i> = the total number of possible labour states, minus 1; intermediate numbers indicate intermediate employment states).
emig_age:	age emigrated out of simulated population
eqs:	equivalence scale
ful_dy:	fuel duty paid (£ per week)
hlthstate:	indicator for health / disability states – poorer states take higher values
hsgmd:	housing mortgage debt (£)
hsgmr:	housing mortgage interest (£ per week)
hsgrrt:	post-tax realised capital gain on housing wealth (£ per week)
hsguret:	unrealised capital gain on housing wealth (£ per week)
hsggw:	gross wealth held in housing (£)
humcap:	benefit unit human capital (wage potential) (£ per week)
ihr_dy:	insurance, higher rate duty paid (£ per week)
immig_age:	age immigrated into model population
immig_type:	immigrant region of origin (where accommodated)
inherit_age:	age at which inheritance received
inherit_val:	value of inheritance (£)
isa:	wealth held in Individual Savings Accounts (ISAs, £)
isa_cont:	contributions to ISAs (£ per week)
isr_dy:	insurance, standard rate duty paid (£ per week)
labinc:	labour income of benefit unit (£ per week)
leis:	proportion of time spent in leisure
na:	number of adults in benefit unit (1=singles 2=couples)
net:	benefit unit net (disposable) income (£ per week), excluding returns to housing
nic:	National Insurance Contributions of benefit unit (£ per week)
ninvinc:	net investment income on generic “other” wealth
nk:	aggregate number of dependent children
nk_allX:	number of children, in birth age X
nk_psnno:	psnno code of matured dependent children
nkd_allX:	indicator that one child from birth age X is disabled
obw:	own business wealth (£)
parttr1/2:	participation tax rates of reference person / spouse
peninc:	private pension (PP+OP) income received (£ per week)
ppc:	private pension contributions (£ p.w.)
PPcont:	aggregate contributions to private pension (including employer contribution) (£ p.w.)
PPcr:	type of private pension to which benefit unit may contribute (integer = 1,..., n where n = total number of private pension schemes considered; only reported if more than 1 scheme available).
PPpen:	aggregate accrued rights to private pension, defined as an annuity stream (£ p.w.)
PPpenb:	aggregate accrued rights to private pension, defined as a wealth equivalent (£)
prec:	age at which pension income first received
prett:	pre-tax and benefit benefit unit income (£ per week)

psnno:	unique person identifier
region:	internal geographic region
	1= North East;                      2=North West;                      3=Yorkshire and Humber;
	4=East Midlands;                      5=West Midlands;                      6=East;
	7=London;                      8=South East;                      9=South West;
	10=Wales;                      11=Scotland;                      12=Northern Ireland;
ret:	whether benefit unit defined as retired for pension purposes
ri:	proportion of wealth invested in risky assets
risky_r:	return to risky assets
semp:	self-employment flag (=1 implies self-employed, if working)
student:	student status (0 = non-student, 1= type 1 student, 2=type 2 student)
taxX:	benefit unit tax burden paid in tax band X (£ per week)
taxagg:	aggregate benefit unit tax burden (£ per week)
tbc_dy:	tobacco duty paid (£ per week)
train_decis:	NOT APPLICABLE
training:	NOT APPLICABLE
traintime:	NOT APPLICABLE
user_taxX:	user defined output X from tax routines
unempins:	NOT APPLICABLE
Val:	measure of expected lifetime utility
vat_rr:	reduced rate VAT paid (£ per week)
vat_sr:	standard rate VAT paid (£ per week)
w:	liquid wealth of benefit unit (£)
w2:	aggregate benefit unit net worth (£)
wage_offer:	flag = 1 if reference adult receives wage offer, 0 if they do not
wage_offer2:	flag = 1 if spouse receives wage offer, 0 if they do not
yrenter:	year entered simulation sample – sample ordered from earliest to latest year

The following relationship describes the evolution of liquid wealth in most periods:

$$w_{t+1} = w_t + net_t + hsgure_t + inherit_t - cons_t - comexcc_t - comexhs_t + \\ - comexot_t - comexhl_t - isa\_cont_t - sum(indirect\ taxes)_t \quad (1)$$

The exceptions are when relationship status changes, when a benefit unit first accesses private pension wealth, or when either the upper or lower bound on  $w$  is encountered. In the last of these cases,  $w$  is constrained to remain within the considered bounds.

$$prett_t = labinc_t + peninc_t + hsgrrret_t + ninvinc_t \quad (2)$$

$$net_t = prett_t + benagg_t + cpinc_t - taxagg_t - nic_t - ppc_t \quad (3)$$

The variable  $net$  represents the model's projection for disposable income before housing costs, as used in the DWP's HBAI publication. Disposable income after housing costs can be evaluated as:  $net - comexhs$ . Similarly, disposable income net of mortgage interest payments is obtained by:  $prett_t - hsgmr_t$ .

## Default summary statistics

### High-level summary statistics - hi\_level\_statistics.xls

The high level statistics that are reported by the model fall into two broad categories, which are each represented by a separate table. Simulated population averages for key benefit unit income, consumption, and balance sheet items are reported in one table, and statistics relating to the macro-economy are reported in the other. The population averages that are reported in the first table are reasonably self-explanatory. The statistics relating to the macro-economy, however, warrant further comment.

Economic analyses of the type for which LINDA has been devised can typically be distinguished in relation to their treatment of factor prices. On the one hand, *partial equilibrium* analyses assume that factor prices are fixed; this is also commonly referred to as the small open economy assumption. On the other hand, the alternative assumption is that factor prices adjust endogenously to reflect changes in demand and supply. In the case of LINDA, the analyst can choose between these two basic frameworks, as noted in relation to Form Z. Here, directing the model to generate results for the General Equilibrium in a closed economy results in the model adjusting interest rates and wage rates to reflect changes in the supply of capital and labour that are implied by the respective simulation.

The basic idea is that, if saving increases, then this raises the supply of capital in the economy. Increasing the supply of capital in the economy, all else held fixed, should reduce the rate of return paid to capital. This is simulated by LINDA on the assumption that aggregate production,  $Y$ , combines aggregate capital,  $K$ , and labour,  $L$ , in the form of a CES function:

$$Y = A(aK^{1-1/\varepsilon} + (1-a)L^{1-1/\varepsilon})^{\frac{1}{1-1/\varepsilon}}$$

Assuming that factor markets are perfectly competitive implies that capital and labour are paid their respective marginal products, so that the interest rate,  $r$ , and wage rate,  $w$ , are given by:

$$r + \delta = \frac{\partial Y}{\partial K} = AaK^{-1/\varepsilon} (aK^{1-1/\varepsilon} + (1-a)L^{1-1/\varepsilon})^{\frac{1/\varepsilon}{1-1/\varepsilon}}$$
$$w = \frac{\partial Y}{\partial L} = A(1-a)L^{-1/\varepsilon} (aK^{1-1/\varepsilon} + (1-a)L^{1-1/\varepsilon})^{\frac{1/\varepsilon}{1-1/\varepsilon}}$$

where  $\delta$  is the rate of depreciation of capital. The aggregate capital stock is set equal to aggregate benefit unit wealth less government debt. Similarly, aggregate labour supply is set equal to the aggregate wage bill, and these two (capital and labour) are combined to give aggregate production as described by the CES function referred to above. Investment is  $I = (\delta + g) \cdot K$ , where  $g$  is the assumed growth of the economy. Government consumption,  $G$ , is then calculated to equate aggregate income to expenditure:

$$G = Y - C - I$$

where  $C$  is aggregate benefit unit consumption. It should be noted that we do not consider the issue of the government budget balance because we do not cover all of the forms of taxation that are applied in practice (for example, LINDA currently omits taxation of firms).

When directed to generate results for the General Equilibrium in a closed economy, the model iteratively adjusts interest rates,  $r$ , and wage rates,  $w$ , until these are consistent with the associated aggregates generated for output, capital and labour supply. Note, however, there is no guarantee that the model will converge. The analyst is given a warning if the model has failed to find a solution after searching over 25 alternative parameter combinations, and can choose to continue with the analysis or cancel out in that case.

## Optional summary statistics

The model can be directed to report results from a set a pre-programmed analysis routines. These routines are designed to report data to dedicated Excel files, as described below.

*Please note that*, at the time of writing, a compiler error has been introduced with new versions of Windows that affects communications with Excel. Wherever this problem has been identified, we have addressed it by outputting the computed statistics in a CSV format. When the associated Excel files (described below) are first opened, they will display zeros wherever saved statistics should be. In this case, please press ALT+F8, and run the “data\_update” macro. We have brought this issue to the attention of Intel’s software engineers, and hope that it will be addressed in a more satisfactory manner shortly.

## High level analysis of population cross-sections and birth cohorts

The model can be directed to report age specific summary statistics for selected population cross-sections and birth cohorts. Where the model generates statistics for a cross-section, then it will save results into a file named “NNN YYYYcs.xls”, where NNN is replaced by the simulation name, and YYYY by the year of the relevant cross-section. Similarly, birth year statistics are saved into a file named “NNN YYYYby.xls”. This analysis routine delivers age and relationship specific moments for labour supply, employment income, disposable income, consumption, private pension participation, and wealth, each in a separate worksheet. Statistics are reported in both tabular, and graphical form.

## Poverty statistics

A workbook “poverty analysis.xls” is generated by the program and is placed in the sub-directory given by the simulation name. These statistics are specifically designed to consider the trade-off between the bearing of income support programs on the government budget and the incidence of poverty. A series of alternative metrics are used to generate poverty rates:

1. Distributional measures:
  - a. Disposable income before non-discretionary expenditure
  - b. Disposable income after non-discretionary expenditure
  - c. Consumption
    - i. Non-equivalised and equivalised (using the OECD scale)
2. Population subgroups:
  - a. Full population
  - b. Children under age 5
  - c. Single pensioners (over state pension age)
  - d. Couple pensioners (over state pension age)
3. Cross-section specific and over a five year time horizon.



### **Decile-level summary statistics for population cross-sections and birth cohorts**

A workbook analysis\_dec.xls is generated by the programme and is placed in the sub-directory given by the simulation name. Users are likely to be interested in both the absolute values and the differences from the base, which are each reported in separate worksheets.

The decile groups reported in the spreadsheet are each comprised of one tenth of the weighted sample population that survives to a given period, where lower deciles describe the circumstances of benefit units with lower lifetime income *as observed in the prevailing policy counterfactual*. Lifetime income is calculated as the present discounted value of the net (disposable) income stream, averaged over the period of survival. Survival probabilities in the model depend only on age and birth year. This means that, when considering evolving characteristics for a given birth cohort, then each benefit units will (approximately) contribute to the same lifetime income decile throughout its life-course.

The difference statistics hold all factors other than the assumed policy parameters constant between the base and counterfactual simulation populations. Hence, each benefit unit is subject to the same random draws in the two sets of simulations, and each “decile” reported in the spreadsheet is comprised of the same sample of benefit units at all points in time. This is crucially important to distinguishing the simulated responses to changes in the policy environment from other modelling considerations. A useful check that this aspect of the model is working as intended is to run a counterfactual simulation that holds all parameters fixed as the same parameters as for the simulation base. Difference statistics calculated between this test simulation and the base simulation should be very close to zero (subject to some rounding errors).

The statistics reported in the spreadsheet are defined in Table 1. As is implicit in the above discussion, the sheet shows arithmetic differences for all variables except the value function. Differences in expected lifetime utility between a given simulation and the associated simulation base are expressed either as compensating variations (£ of liquid wealth equivalents) or percentage differences, as little meaning can be given to absolute differences.

**Table 1 Data in Analysis\_Dec.xls and Differences\_Dec.xls**

<b>Variable</b>	<b>Notes and Definitions.</b>
number of benefit units contributing to statistic	Provides a measure of the un-weighted sample size contributing to the reported statistics – this provides an indication of the statistical reliability of the reported statistics (noting that each decile will be comprised of approximately 1/10 of the total population sample, and means based on fewer than 20 observations should be treated as approximate only).
number of adults	Describes number of adults in benefit unit
consumption	Consumption, including non-discretionary expenditure. (£ per week)
leisure	This is the proportion of the leisure available to someone who does not work. Someone who works full-time is defined as having leisure of 0.5. The ratio of the part-time working week to the full-time working week is user-determined in Form 1 as Part-time Ratio (1) for single people and the Lab Ratio variables for couples.
proportion employed	Proportion of population with any employment
gross labour income	Average income from employment (£ per week)
average contribution to private pension	Average employee and employer contributions to private pensions over decile (£ per week)
propn contributing to private pension	Proportion of decile making any contributions to private pensions
private income	private income = (gross labour income) + (investment income on non pension wealth) – (interest on debt) – (private pension contributions) (£ per week)
disposable income	disposable income = private income - taxes + benefits (£ per week)
unsecured debt	Average value of unsecured debts by population decile (£)
propn of population with unsecured debts	Proportion of decile with negative net liquid wealth (cash on hand)
net non-pension assets	Average value of net non-pension assets by population decile (£). Based only on data for benefit units without unsecured debt.
pension wealth	Average value of assets held in pensions (£)
total wealth	total wealth = (net non-pension assets) – (unsecured debt) + (pension wealth) (£)
value function	Remaining life-time welfare. Utility Units. Percentage rather than absolute differences should be considered.
upper threshold for decile	Threshold used to allocate benefit units to deciles as considered in relevant worksheet

## 7. Best Practice Methods of Use

This section provides a brief step-by-step guide concerning how the model should be used to explore the effects of policy alternatives. The guide has been written so that it will be applicable to a wide range of alternative subjects of interest, from studies concerned solely with the distributional implications of policy, to those that focus on behavioural responses to policy counterfactuals. Each step of a stylised analytical problem is described under a separate section heading, in approximate chronological order. At the end of each step we provide a practical example of the tasks involved with reference to the policy counterfactual in which 10 percentage points are added to the highest rate of income tax in the base policy specification assumed for the model.

*TIP: it is incredibly important that you allow ample time to conduct your analysis.*

### Step 1: specify policy parameters

There are two alternative ways to alter the policy environment in the model. The first is to alter the parameters of the existing model structure. New users of the model are encouraged to select policy parameters using the Excel front-end that is supplied with the file “Job File.xls”, as described in Section 3. Advanced users may find it easier to alter model parameters directly through the cells on the “input” sheet of “Job File.xls”. The second alternative is to alter the tax code directly; see Section 8 for details.

Having adjusted the model parameters, it is often advisable to check that the revised structure conforms to that which is desired. A number of tools are provided with the model to facilitate such checks.

### Checking differences with base simulation

The “check” tab in “Job File.xls” allows you to identify which parameters in the “input” sheet are different to those of the base simulation (stored in the “inputA” sheet). You can run this check after working through the front-end forms in “Job File.xls” in one of two ways. If you press the “LAUNCH MODEL” button on Form Z, then you can look at the “check” tab after the fortran program has started. Alternatively, you can choose the “EXIT” button on Form Z, saving “Job File.xls”, and then look at the “check” tab. In this second case, after you have confirmed that you are happy with the differences described between the prevailing model parameters (sheet “input”) and the model base (sheet “inputA”), you can launch the Fortran code manually by double-clicking on the program SIDD.exe.

### Validating the tax function

As noted in Section 3 (Form D4), there are two routines that are provided with the model that produce trial statistics for the simulated tax function. The terms of both test routines are defined by Excel files stored in the “MODEL\analysis\_files\” subdirectory. “tax\_test1.xls” allows you to generate test statistics for a range of alternative pre-tax incomes, for a given benefit unit type. “tax\_test2.xls” is similar to “tax\_test1.xls”, but allows you to vary both pre-tax income and benefit unit demographic characteristics.

These test routines can be run at any time after you have started running a given simulation.

- 1) Open the relevant excel file (“tax\_test1.xls” or “tax\_test2.xls”).
- 2) Define the alternative test cases that you would like to consider

- 3) Save the excel file.
- 4) Open “Job File.xls”
- 5) Run the SIDD macro
- 6) Enter the relevant simulation name in the text box adjacent to the button “ANALYSE TAX FUNCTION”
- 7) Press the “ANALYSE TAX FUNCTION” button.
- 8) Select the relevant analysis routine using the radial button.
- 9) Press the “ENTER and RUN” button.

A new simulation window will open, and will indicate when the analysis routine is complete. You can then re-open the relevant excel file (“tax\_test1.xls” or “tax\_test2.xls”) to check the results obtained.

### Example

We are interested in considering the effects of increasing the higher rate of income tax by 10 percentage points. Our example assumes that a model “base simulation” has already been run, as described in Section 2 of this manual. We alter the model parameters through the Excel front-end, as indicated in the following sequence of User Forms.

FORM 0: SIMULATION TASK

**NEW SIMULATION FOR UK**

location of existing job file to load model parameters from  
(e.g. c:\new\_base\job file.xls) leave blank by default

NEW SIMULATION FOR ITALY

RUN EXISTING JOB FILE

name to adopt for existing job file  
test

ANALYSE TAX FUNCTION

ANALYSE EXISTING SIMULATION

name of run to analyse

CONVERT RUN TO NEW BASE

name of run to adopt as new base

starting year for new base simulations  
2011

directory name for new base (e.g. base\_2006)  
?

location of existing job file to load parameters from  
(e.g. c:\new\_base\job file.xls)

LOAD EXISTING JOB FILE

UNDERTAKE SHORT RUN ANALYSIS

ADJUST NUMBER OF TAX OUTPUTS

UPDATE FERTILITY PROBABILITIES

1. PRESS THE “SET UP NEW SIMULATION” BUTTON

FORM 1: KEY PARAMETERS

simulation name

test

start year of simulation

2011

maximum population size

95000

?

end year of simulation

2040

maximum year of birth of any simulated cohort

2090

Tax function to simulate from

☐ 2016 tax and benefit structure

☒ 2011 tax and benefit structure

☐ 2010 tax Benefit Model Tables (DWP)

☐ 2006 tax Benefit Model Tables (DWP)

☐ user-defined tax structure

☒ allow for Universal Credit

tax function reference year

2011

number of additional outputs generated by tax function

0

reference number for user tax structure

3

price reference year for simulated output

2011

?

first year of Universal Credit

2017

?

Note that all financial terms are defined in prices for the tax function reference year

?

Reduced-form decisions

☐ project decisions using reduced form wherever possible

☐ project employment decisions using reduced-form

2006

2011

?

☐ project consumption decisions using reduced-form regression

Preference parameters

relative risk aversion (1/gamma)

1.55

utility price of leisure (alpha)

2.2

elasticity btw cons and leisure (epsilon)

0.6

discount Factor (delta)

0.97

short-run discount factor (beta)

1

number of grid slices

1

?

ENTER

RESET

BACK

- Enter a reference for the "Simulation Name", and then press the "ENTER" button.

76 | Page

FORM 2: USER DEFINED ANALYSIS ROUTINES

☐ generate long-file format data optimised for importing into Stata
☐ report simulated microdata as unformatted rather than csv output
☒ report individual specific consumption
☐ calculate supplementary income moments by age and year
☐ generate advisory statistics concerning the computational burden of simulation
☒ calculate supplementary statistics for analysing poverty
☐ count 18 year old students as dependents for evaluating poverty stats

first year 2011 last year 2040 poverty threshold 60 %

High-level analysis of population cross-sections

year 1 year 2 year 3  
year 4 year 5 year 6

High-level analysis of individual birth cohorts

birth year 1 birth year 2 birth year 3  
birth year 4 birth year 5 birth year 6

☒ tick if calculate statistics for equivalised income deciles

☐ analyse population cross-section min cross-section / birth year 1965
☒ analyse birth cohort max cross-section / birth year 1975

☒ tick if generate comparative statistics with population base
☐ tick if welfare comparisons defined as monetary equivalents (compensating variations)

ANALYSE TAXES ENTER ENTER and RUN BACK

- We are running an analysis of a policy counterfactual. It is likely to take some time for you to work out your preferred approach for this type of task. In our experience, we have found decile level statistics of differences with the base population for a younger birth cohorts to be particularly useful in gaining a high-level picture of how a given policy alternative

influences individual circumstances. Developing this type of narrative should be your first objective, as it will help you to interpret most statistics of interest. The model is directed to undertake this analysis by altering the front-end as indicated above.

WE SKIP FORMS 3 TO 5, WHICH DO NOT NEED TO BE ALTERED

FORM A1: INCOME TAX AND NATIONAL INSURANCE

×

### Income Tax Rates and Thresholds

Tax thresholds	Tax rates	NIC rates & UEL (LEL=Personal Allowance)
2nd tax threshold <input type="text" value="35000"/> £ p.a.	rate 1 <input type="text" value="20"/> %	rate 1 <input type="text" value="12"/> %
3rd tax threshold <input type="text" value="150000"/> £ p.a.	rate 2 <input type="text" value="60"/> %	rate 2 <input type="text" value="2"/> %
4th tax threshold <input type="text" value="200000"/> £ p.a.	rate 3 <input type="text" value="60"/> %	primary threshold <input type="text" value="139"/> £ p.w.
5th tax threshold <input type="text" value="250000"/> £ p.a.	rate 4 <input type="text" value="60"/> %	upper earnings limit <input type="text" value="817"/> £ p.w.
6th tax threshold <input type="text" value="300000"/> £ p.a.	rate 5 <input type="text" value="60"/> %	
	rate 6 <input type="text" value="60"/> %	

### Personal Allowances

Working lifetime	From state pension age	
personal allowance <input type="text" value="7475"/> £ p.a.	personal allowance <input type="text" value="10015"/> £ p.a.	
wdrwl threshold <input type="text" value="100000"/> £ p.a.	1: lower threshold <input type="text" value="24000"/> £ p.a.	2: lower threshold <input type="text" value="100000"/> £ p.a.
PA wdrwl rate <input type="text" value="50"/> %	1: upper threshold <input type="text" value="29080"/> £ p.a.	wdrwl rate2 <input type="text" value="50"/> %
	wdrwl rate1 <input type="text" value="50"/> %	

ENTER

ENTER and RUN

RESET

BACK

- Form Aa1 lists the policy parameters that we are interested in altering. Here, we add 10% to each of the terms highlighted above. As these are the only changes to the policy environment that we are interested in, we can then press the “ENTER and RUN” button as indicated.

FORM Z: RUN MODEL

☐ COARSE MODEL fast model that provides a course approximation of agent behaviour ?

☒ MEDIUM MODEL base specification - using this specification will aid comparisons

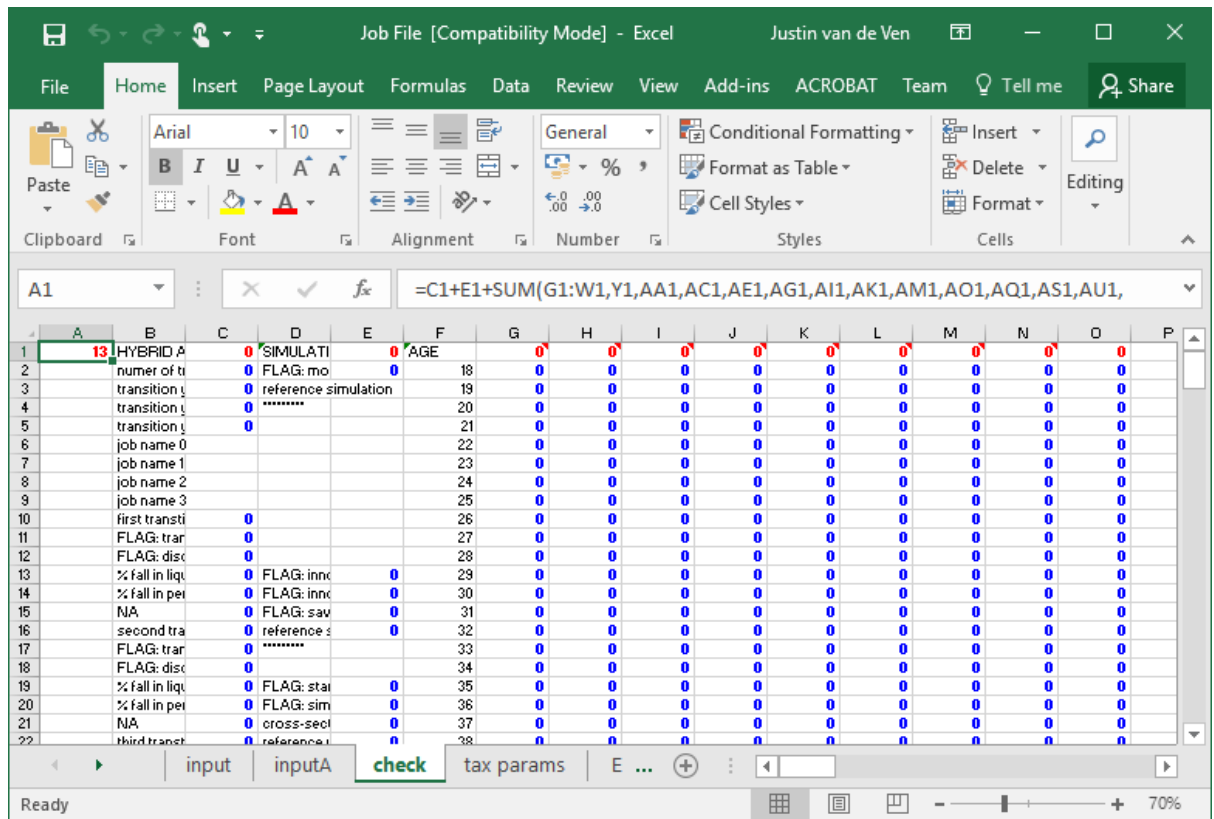
☐ FINE MODEL slow model that provides a fine approximation of agent behaviour

☐ Closed Economy GE adjust wages and interest rates to reflect labour and capital supply

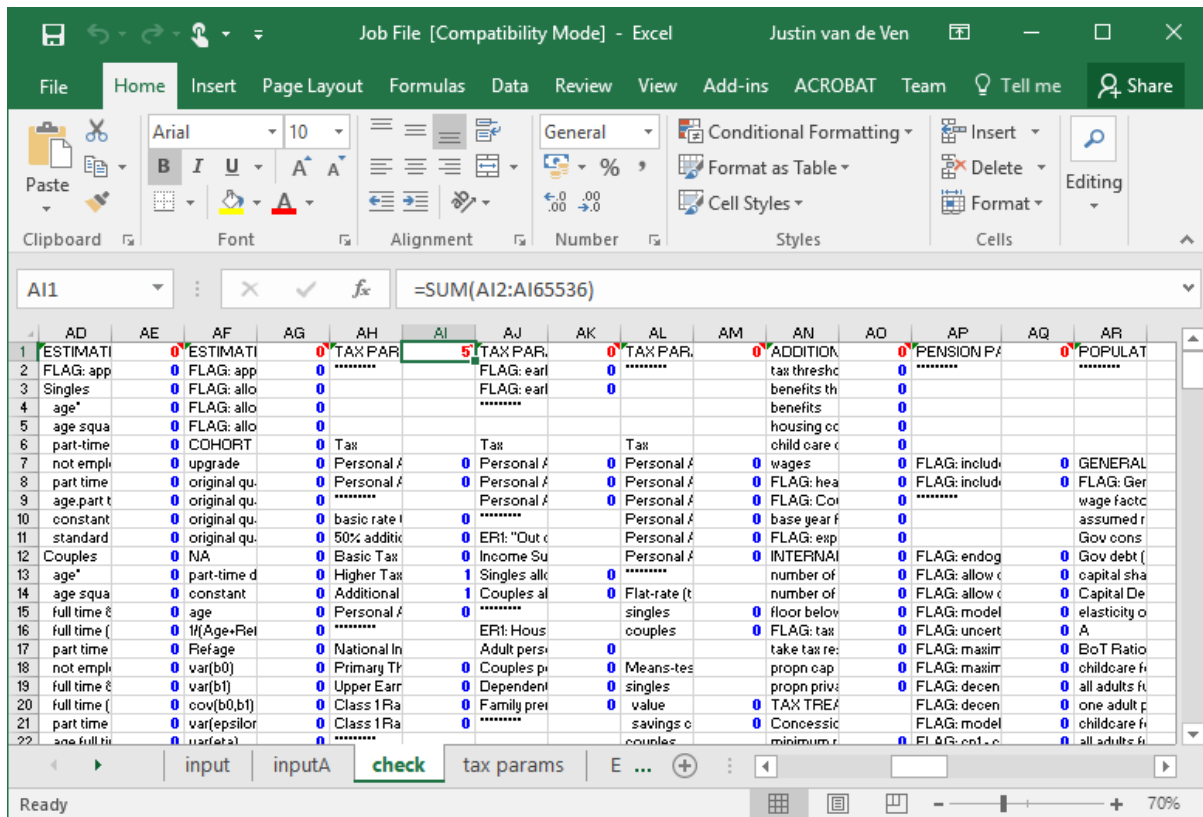
BACK LAUNCH MODEL TRANSLATE EXIT

5. It will usually be sensible to assume the “BASE Specification”, which has been carefully selected to balance accuracy against computation time. Here we then press the “EXIT” button, as we would like to check over the parameter changes that have been implemented by the model front-end.





6. Go to the “check sheet” of “Job File.xls”. The total number of parameter differences with the model’s base simulation are reported in cell A1 of this sheet (19). Looking across row 1 of the sheet will indicate which columns include altered parameters.



- Scrolling across row 1, we see that the first column that has been altered by the front-end is AJ. Cell AJ1 indicates that 5 parameters in this column have changed, and searching down the column indicate that values of rows 13, 14, 106, 107, and 108 have all altered. Checking the base parameters (in sheet inputA) against the model parameters described for the current simulation (sheet input) indicates that the front-end has increased the higher rates of tax as it was directed to do (step 4 above).

CONTINUING TO CHECK ACROSS THE “check” WORKSHEET INDICATES THAT THE ONLY OTHER MODEL PARAMETERS ALTERED FROM THOSE IN THE BASE SPECIFICATION CONCERN “ANALYSIS PARAMS”, WHICH INFLUENCE THE NATURE OF THE SIMULATION STATISTICS THAT WILL BE GENERATED INTERNALLY BY THE MODEL.

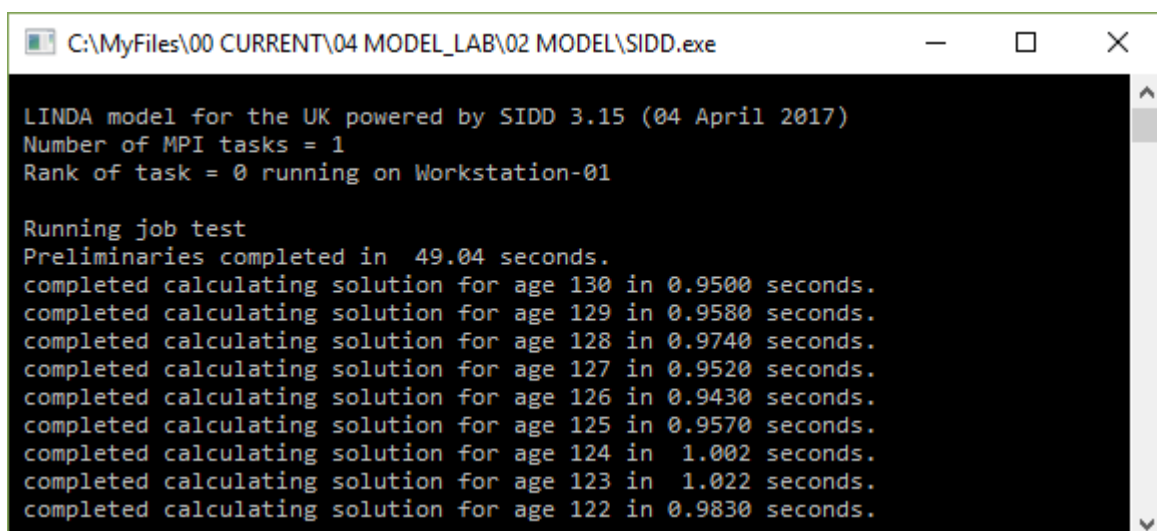
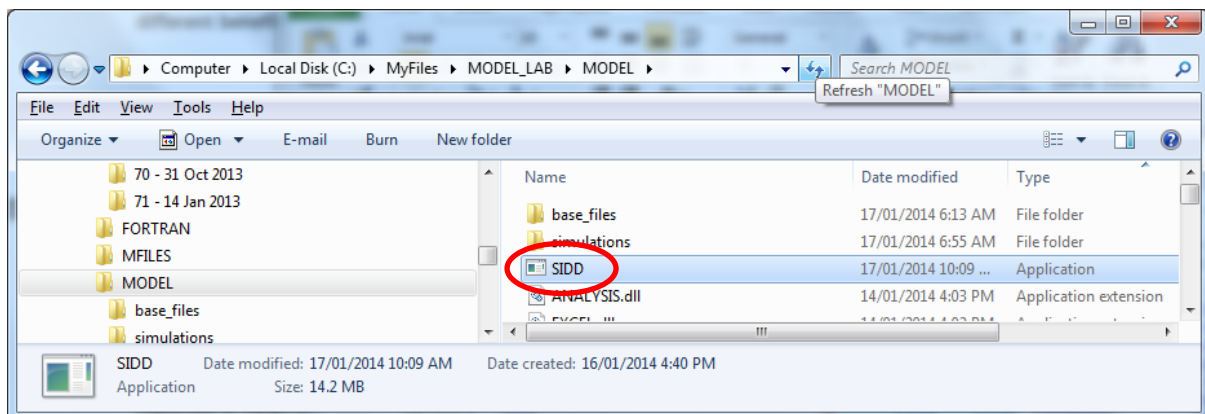
## Step 2: run model and generate output

As noted in Section 4, two types of output can be generated by the model. The model will solve simulated panel data for each benefit unit, in the form of \*.csv files (that can be opened by most statistical packages). In this case, each variable is saved in a separate file, each row represents a different benefit unit, and each column a different time period.

The model will generate a series of summary statistics for each simulation by default, which are reported in Excel files. The model can also be directed to generate a range of additional summary statistics; see Section 4 and “Form 2” in Section 3 for further details.

### Example

8. Having verified the model parameters for the new simulation correspond to those that we are interested in, we can launch the model program.
  - Save the file “Job File.xls”
  - Double click on the executable file “SIDD.exe”, to launch the model program, and wait for the model window to indicate that it is finished.



### Step 3: think about likely incentive effects

An important feature of the model is that savings and labour supply decisions are endogenous. This means that these decisions react to the incentives that are embodied by the assumed policy environment. Explaining the results that are reported by the model consequently depends in part on understanding the drivers underlying the simulated behaviour. It is useful to think about what behaviour you expect to see before the model completes its analysis, as this will help you to identify where to begin looking once the simulated results are in. It is easiest to think about incentives relative to the base simulation, as the model can be asked to generate comparisons with the base simulation by default.

#### Example

9. We have raised the marginal tax rate of all higher rate payers by 10 percentage points. This can be expected to have a large number of effects on the simulated population. Some of the most important are listed here in bullet point form:
  - Higher tax rates imply two key effects:
    - i. Affected benefit units will have lower lifetime income in the absence of any behavioural responses – this consideration will motivate responses that are sometimes referred to as a “wealth” or “income” effects.
    - ii. Affected benefit units will be subject to higher effective marginal tax rates on labour income, and on investment income that is not tax-shielded – this consideration will motivate responses that are sometimes referred to as “price” or “substitution” effects.
  - Likely wealth effects:
    - i. Lower consumption
    - ii. Increased employment
    - iii. Lower saving
  - Likely substitution effects:
    - i. Higher consumption, as effective post-tax returns to saving decrease
    - ii. Lower employment, as the marginal returns to labour supply have fallen
    - iii. Lower saving in assets that are subject to taxes
    - iv. Increased saving in assets that are tax shielded.

### Step 4: analyse model output

This stage of the analysis involves comparing the model output against the expectations that you formed in Stage 3 (described above). It is not uncommon to find that behaviour deviates from what you had initially expected, as the incentives embodied by policy can often be quite difficult to infer.

#### High level analysis

The model produces a large number of high-level summary statistics by default in the file DA1.xls. It can also be directed to report a series of age specific statistics for population cross-sections and individual birth cohorts (see Section 3). Through repeated use, you are likely to settle upon some subset of these results as an appropriate place to start your analysis.

#### Detailed statistical analysis

The model can be used to generate decile level statistics, and to produce associated comparisons with the base population. These statistics will often be sufficient to identify the key margins of

behavioural variation simulated under a given policy environment, and allow you to formulate a “story” underlying the results obtained.

### **What to do when results do not conform to expectations**

If the above statistics do not enable you to devise a compelling account of the results generated by the model, then it is often useful to focus upon the micro-data generated by for individual benefit units. Suppose, for example, that you cannot understand why labour supply falls under the policy environment of interest, relative to the base simulation. In this case, you could look for units that are simulated to reduce their labour supply substantively under the new policy environment. Bearing in mind that the model is designed so that the only differences between alternative simulations are due to the considered policy environments, this approach will hopefully provide clues as to the incentives that underlie the unanticipated behavioural responses. As a last resort, staff at the NIESR will attempt to provide technical support (subject to availability).

### **Example**

As noted under “Step 1” above, we often find it useful when interpreting responses to policy changes to begin with the difference statistics that can be reported for population deciles by the model (implemented by point 3 above). These statistics are reported in the excel file “analysis\_dec.xls” that should be saved in the \simulations\NAME subdirectory, where “NAME” here refers to the name you chose to give the simulation run (see point 2 above). The difference statistics with the base simulation are reported in the “differences with base” worksheet. Details of the statistics reported in this file are described in Section 6.

It is noted in Section 6 that the difference statistics generated by the model are designed so that the only variation between a policy counterfactual and the simulation base relates to the simulated policy conditions. If you have worked through the above example, then you should find that there are zeros for all statistics relating to the number of adults, and for all statistics reported to age 35. These results are obtained because (i) the same benefit units contribute to each decile group in the counterfactual and base simulations; (ii) the same random draws are used to project circumstances through time (implying the same number of adults for each benefit unit in each simulation); and (iii) our counterfactual simulation projects forward through time from 2011 and we are focussing here on birth cohorts born between 1965 and 1975, so that the youngest cohort affected by the analysis (cohort born in 1975) was aged 36 in the first year of the counterfactual (2011).

In columns to the left of the decile level statistics reported in the “differences with base” worksheet are age specific population averages for each of the variables reported in the spreadsheet. A selection of these statistics is reported in Figure 7.1 to Figure 7.4.

Figure 7.1 indicates that the policy counterfactual tends to increase leisure (reduce employment) to age 55, and increase employment thereafter. The model consequently suggests that substitution effects referred to under point 9 above dominate early in life, and wealth effects dominate later in life.

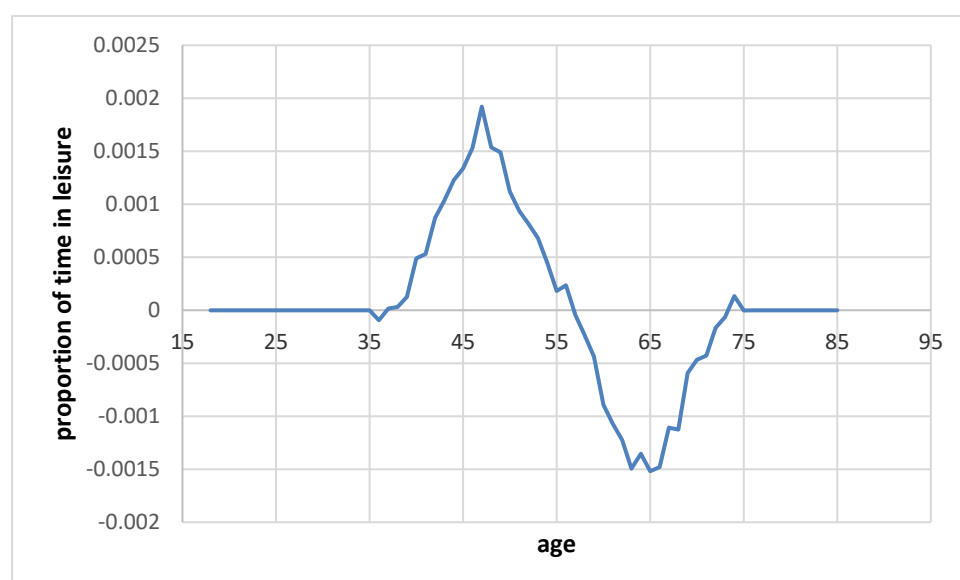
Figure 7.2 indicates that average private incomes fall under the policy counterfactual. This is consistent with the fall in labour supply early in the working life. Late in the working life, the higher labour incomes associated with increased labour supply are more than off-set by coincident reductions in investment income due to lower savings (see below). As a consequence of the fall in

private income and rise in tax rates, disposable income is also projected to fall. The lower lifetime income that is implied by a depressed disposable income stream shifts consumption down in all periods following the considered policy change.

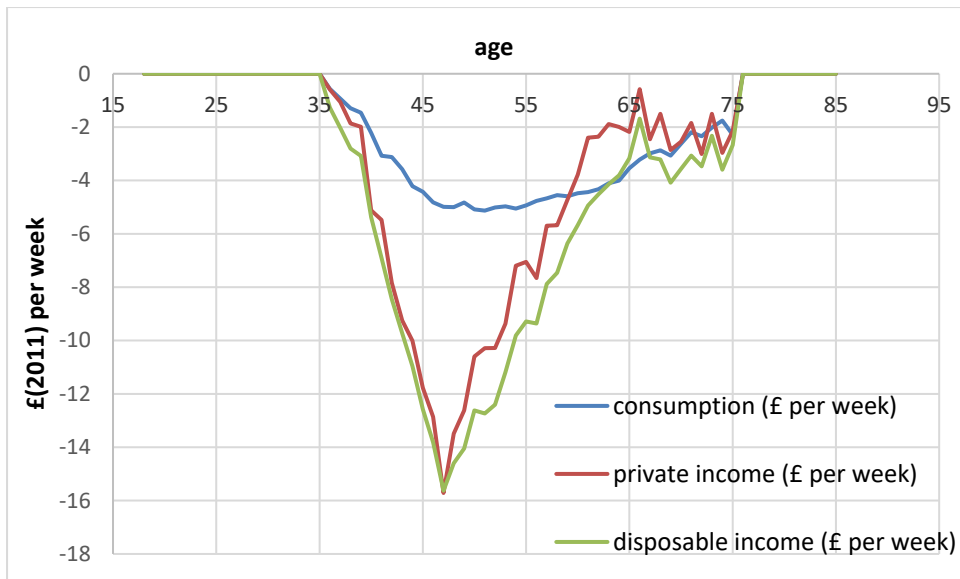
Figure 7.3 displays the influence of the policy counterfactual on savings. Consistent with the depressed disposable income stream under the policy counterfactual, all measures of wealth are projected to fall for much of the simulated time horizon. Note that the full recovery made by pension wealth late in the simulated lifetime is attributable to the enhanced incentives to save through pensions implied by higher income tax rates, which off-set the bearing that lower overall savings would otherwise have on pension wealth.

Figure 7.4 provides an indication of the dispersion of the population average effects discussed above. This figure indicates that high lifetime income people are disproportionately affected by the considered policy change, which is unsurprising given the nature of the policy change.

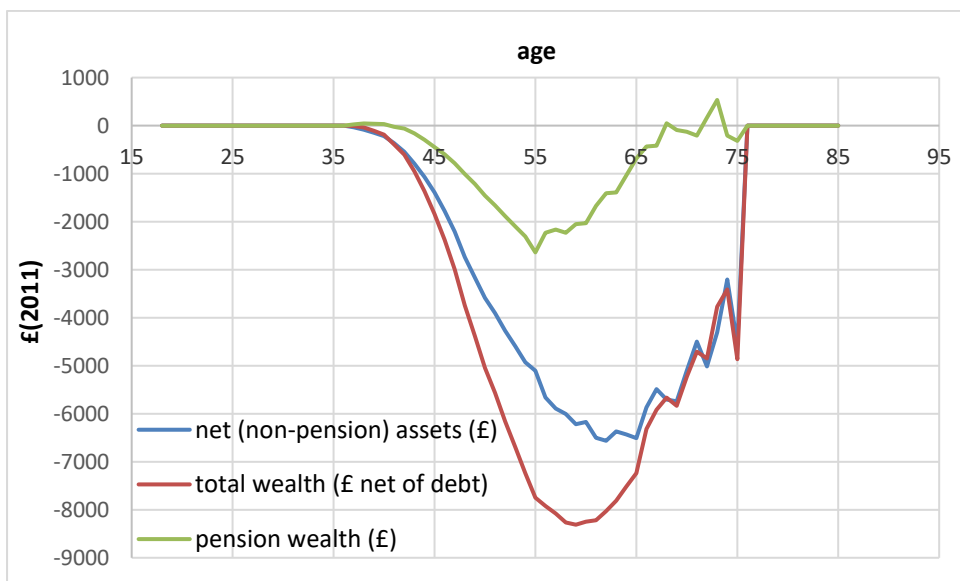
Note, however, that it is not uncommon to observe behavioural variation distributed quite widely by the model, even where a considered policy counterfactual is tightly targeted. This is because temporal variation of individual specific circumstances can see individual benefit units move into and out of contexts where they are affected by a targeted policy change. Furthermore, the uncertainty that characterises temporal variation of individual specific characteristics can motivate behavioural variation even amongst benefit units who are never directly affected by a considered policy reform. In the current example, it is therefore possible to identify benefit units who are never actually subject to the higher rate of tax (and are therefore not directly affected by the policy counterfactual), but who nevertheless alter their behaviour due to the possibility that they might be subject to the higher marginal rate of tax at some point in the simulated future.



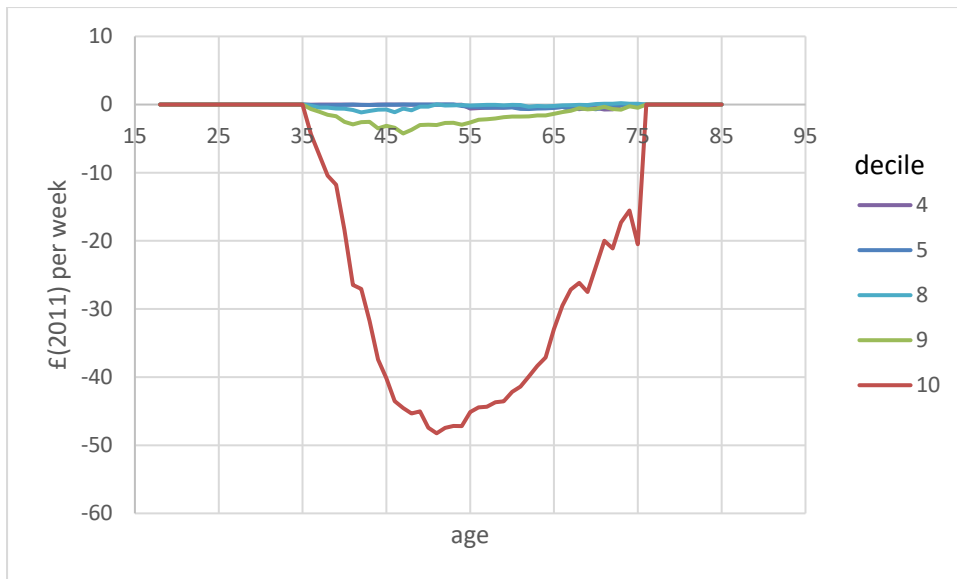
**Figure 7.1: Effects of increasing the higher rates of tax from 40 to 60 percentage points from 2011 on the proportion of family time spent in leisure – average effects for birth cohorts born between 1965 and 1975**



**Figure 7.2: Effects of increasing the higher rate of tax from 40 to 60 percentage points from 2011 on financial flows – averages for population birth cohorts born between 1965 and 1975**



**Figure 7.3: Average effects of increasing the higher rate of tax from 40 to 50 percentage points in 2006 on financial stocks of population birth cohort born in 1970**



**Figure 7.4: Effects on consumption of increasing the higher rate of tax from 40 to 60 percentage points from 2011 – decile averages for cohort born between 1965 and 1975**

### Step 5: package output

Having identified a behavioural “story” underlying simulated results, the packaging exercise is usually fairly straight-forward. As this exercise will vary, depending upon the subject of concern, we do not discuss it further here.



## 8. Adjusting the Program Code

The model is programmed in Intel Visual Fortran, and users have access to the routines that calculate taxes and benefits. The tax routines can be edited through Microsoft Visual Studio at the time of writing (the steps involved in setting-up this environment for use are provided in Section 2). In this section we describe some programming basics, before running through a practical example for simulated tax and benefits policy.

### Programming basics

#### Basic Code Structure

- The Fortran code that is provided with the model is organised into four broad structures, which can usefully be thought of as containers.
- The largest container is the “solution”, which is a set of files that comprise the basic building blocks that Fortran uses to generate program files
  - The “TAXES solution” can be opened by double-clicking on the file “TAXES.sln” in the “FORTRAN\TAXES\” subdirectory.
- The second largest container is the “source file”, into which code is written.
  - You can browse through the source files of a solution via the “Source Files” folder of the “Solution Explorer” (which can be seen by selecting “Solution Explorer” from the “View” menu of Visual Studio)
  - To add a new source file to a solution:
    - right click on the Source Files folder
      - select “add”, “new item”
      - select “Fortran Free-form File (.f90)”
      - make up a name for the file toward the bottom
      - and press the “Add” button
- Each source file can contain one, or a number, of MODULEs.
  - A MODULE is predominantly a container to organise a number of SUBROUTINES.
    - e.g. MODULE AA might contain SUBROUTINES AA1 and AA2; and MODULE BB might contain SUBROUTINES BB1 and BB2
    - a slight complication arises in relation to “global variables”, which is returned to below.
- Most MODULEs are organised as follows:
  - MODULE AA
    - This line denotes the start of the MODULE with the name AA
  - IMPLICIT NONE
    - This line is necessary to avoid easy programming errors – do a google search on it for further detail
  - CONTAINS
    - This line notes that the SUBROUTINES that follow are contained within the MODULE
  - \*\*\*\* SUBROUTINES then appear here \*\*\*\*
  - END MODULE AA
    - This line denotes the end of the module
- All of the program computations are undertaken by code that is organised within a series of SUBROUTINES.
  - e.g. SUBROUTINE AA1(x, y) takes a series of inputs x, performs a number of calculations, and then returns a series of outputs y.
    - We would execute this subroutine by entering the following code:  
call AA1(x,y)

- To use (call) SUBROUTINE XX from within SUBROUTINE YY, either:
  - the two SUBROUTINES must be organised within the same MODULE, or  
SUBROUTINE YY must be given access to the MODULE containing SUBROUTINE XX
    - e.g. in the above example SUBROUTINE AA1 could call AA2 by default, but would need to be given access to MODULE BB to call BB1 (or BB2)
- Each SUBROUTINE must be organised as follows (based on the above example):
  - SUBROUTINE AA1(x, y)
    - This line denotes the start of the subroutine, and the variables that are used as inputs and outputs – if the subroutine takes in no explicit inputs, and produces no explicit outputs, then we write “SUBROUTINE AA1()”
  - USE BB
    - This line gives SUBROUTINE AA1 access to the SUBROUTINES contained in MODULE BB
    - This line is only required if you want to access SUBROUTINES (or global variables) stored in MODULE BB
  - IMPLICIT NONE
    - This line is necessary to avoid easy programming errors – do a google search on it for further detail
  - real (8) :: x, y
    - This line of code refers to the “type definitions”, and usually covers a number of lines.
    - A “type definition” tells fortran the explicit nature of the data that each variable contains.
    - The variables that you will most commonly require will be limited to real(8) (a number with a decimal point) and integer(4) (a whole number without any decimals) types.
      - A variable cc is assigned a real type by; real(8) :: cc
      - A variable cc is assigned an integer type by; integer(4) :: cc
      - If cc is a matrix of real numbers with dimension (5,4) (5 rows and 4 columns), then it is assigned by; real(8) :: cc(5,4)
    - You must assign types to all of the variables that are included as inputs and outputs to a given subroutine (e.g. x and y in the example here)
    - You must also assign types to all of the variables that you use within the subroutine, and which are discarded after the subroutine is complete
      - Variables discarded after a subroutine is complete are commonly referred to as “local variables”.
  - \*\*\*\* You then add in programming code to undertake your desired calculations here \*\*\*\*
  - END SUBROUTINE AA1
    - This line denotes the end of your subroutine

The above covers just about everything you will need in relation to program structure. There is, however, one final complication. Fortran requires each variable that is used in any subroutine to be assigned a type (real / integer above). In most cases, the variables that you use will either be explicit inputs / outputs of a subroutine, or will be “local variables” that you don’t mind discarding after your desired computations within the subroutine are complete. Nevertheless, there are a number of variables that you might want to make common to a range of subroutines, without needing to repeatedly pass these variables as explicit inputs to each subroutine. Examples in relation to tax and benefits calculations include the number of adults and children in a benefit unit, the employment

status of adult benefit unit members, measures of gross income, and so on. This is achieved in the code using “global variables”.

- You will find in the set of source files included with the TAXES program, one called “2\_global.F90”.
- If you open this file, then you will see that it includes a module named “global\_tax”.
  - The MODULE global\_tax includes a series of variable type definitions, and no subroutines.
  - The variables defined within this module are referred to as “global variables”. This is because it is possible to share them between alternative subroutines without the need for explicit declarations.
- The global variables defined in MODULE global\_tax are assigned values within the SUBROUTINE initialise\_taxinputs (see Figure 1), found in the source file “1\_TaxTools.f90”
  - Note that SUBROUTINE initialise\_taxinputs is given access to the global variables by the “USE global\_tax” declaration at line 23
- Any SUBROUTINE that subsequently requires access to the global variables needs only to include the declaration “USE global\_tax” in its second line of code (as outlined above for SUBROUTINE structure)

### **Common programming steps**

It is beyond the scope of this manual to provide detailed advice concerning programming of new analysis procedures, which is best understood by obtaining hands-on experience. Here we provide a brief over-view of the steps involved in editing Fortran code, and some advice concerning use of the debugging environment.

The following steps are usually involved when editing the Fortran code:

- 1) Open a “program solution” (see the section on “Basic Code Structure” for a description of a “solution”).
- 2) Edit the program text
- 3) Save the revised text
- 4) “Re-build” the solution in a “debug configuration”
  - a. This essentially tells Fortran to use the new building blocks to create new program files
  - b. The debug configuration is designed to enable you to check that your revised program works as intended
- 5) Run some test analyses to make sure that the revised code works as intended
- 6) “Re-build” the solution in a “release configuration”
  - a. The release configuration is designed to omit the checks implemented in the debug configuration, and typically works much faster as a result
- 7) Run your desired analyses

The following will walk you through how to set-up the debugger, essentially addressing steps (1) and (4) listed above, with reference to the TAX routines provided with the model.

### *Opening a "Solution"*

- 1) Double click on the file "TAXES.sln" in the subdirectory "FORTRAN\taxes\
  - a. This should open up the Visual Studio (VS) programming environment
  - b. If you followed the steps set out in Section 2, this solution is now ready for editing (please ensure that this is the case).
- 2) In the "solution explorer" window, expand the "source files" folder
  - a. If the "solution explorer" window is not open, then you can open it by selecting the "View" menu at the top of VS, and then "Solution Explorer"
  - b. The following source files should be listed under the "source files" folder:
    - i. 0\_app\_taxes.f90
    - ii. 1\_TaxTools.f90
    - iii. 2\_gobal.f90
    - iv. AUS\_1.f90
    - v. IE\_1.f90
    - vi. IT\_1.f90
    - vii. UK\_1.f90
    - viii. UK\_2.f90
    - ix. UK\_3.f90
    - x. UK\_4.f90
- 3) Double click on the file "UK\_3.f90"
  - a. This should open a text file in the main window of Visual Studio
- 4) Press CNTRL+HOME
  - a. This should move the cursor to the top of the text file (if it wasn't already).
- 5) Toward the top of the text window, you should see a grey bar that is split into two parts. Click on the left part (which should have "UK\_params3" listed in it)
- 6) Select "UK\_tax3" (this text file has two "modules" in it)
- 7) Click on the right part of the grey bar, which lists all of the subroutines in the current module
- 8) Select "UK\_3" from the drop down menu
  - a. This will move the cursor to the beginning of the SUBROUTINE UK3

### *Re-build the Solution in a "Debug Configuration"*

1. Select the appropriate compile settings
  - a. In the "solution explorer", highlight the purple icon "TAXES"
  - b. Under the view menu of VS, select "Property Pages"
  - c. From the "Property Pages" window, press the "Configuration Manager" button
  - d. Under "Active solution configuration:", select "debug"
  - e. Under "Active solution platform:", selection "x64"
  - f. Press the "Close" button
  - g. Press the "OK" button
    - You can also do the above more easily by selecting the "Active solution configuration", and "Active solution platform" from the drop-down windows of VS, which may be visible as toolbars in the VS environment.
2. Build the solution
  - a. From the "Build" menu of VS, select "Clean Solution"
  - b. From the "Build" menu of VS, select "Build Solution"
    - You should see the following output:

```

1>----- Rebuild All started: Project: TAXES, Configuration: debug x64 -----
1>Deleting intermediate files and output files for project 'TAXES', configuration 'debug|x64'.
1>Compiling with Intel(R) Visual Fortran Compiler XE 15.0.0.108 [Intel(R) 64]...
1>2_global.F90
1>AUS_1.f90
...
1>IE_1.F90
1>0_app_taxes.f90
1>Compiling manifest to resources...
1>Microsoft (R) Windows (R) Resource Compiler Version 6.3.9600.17200
1>Copyright (C) Microsoft Corporation. All rights reserved.
1>Linking...
1>Creating library C:\MyFiles\MODEL_LAB\MODEL 02\TAXES.lib and object C:\MyFiles\MODEL_LAB\MODEL
02\TAXES.exp
1>Embedding manifest...
1>
1>Build log written to "file:///C:/MyFiles/MODEL_LAB/FORTRAN/TAXES/x64/debug/BuildLog.htm"
1>TAXES - 0 error(s), 0 warning(s)
===== Rebuild All: 1 succeeded, 0 failed, 0 skipped =====

```

- c. Check that the files have built to the correct location
  - Look in the “\MODEL 02\” subdirectory, and check that new files named “TAXES” have been generated by the compiler

We now turn to the steps involved in programming a new tax routine.

## Programming a new Tax and Benefits Regime

Taxes and benefits in the model can be altered, either by adjusting parameters for pre-programmed schemes (e.g. see Section 3), or by programming new transfer schemes from scratch. This section provides some guidance concerning the second of these two options. We begin by presenting a schematic for the organisation of the tax, and then provide a step-by-step guide to introducing new code into the model. We then finish up the section by describing how to alter the code so that it will generate a set of user defined outputs by default.

### Organisation of the Tax and Benefits Code

A stylised schematic of how the tax and benefit calculations are organised is provided in Figure 8.1. Arrows and numbers indicate approximate order of access, and associated inter-dependencies.

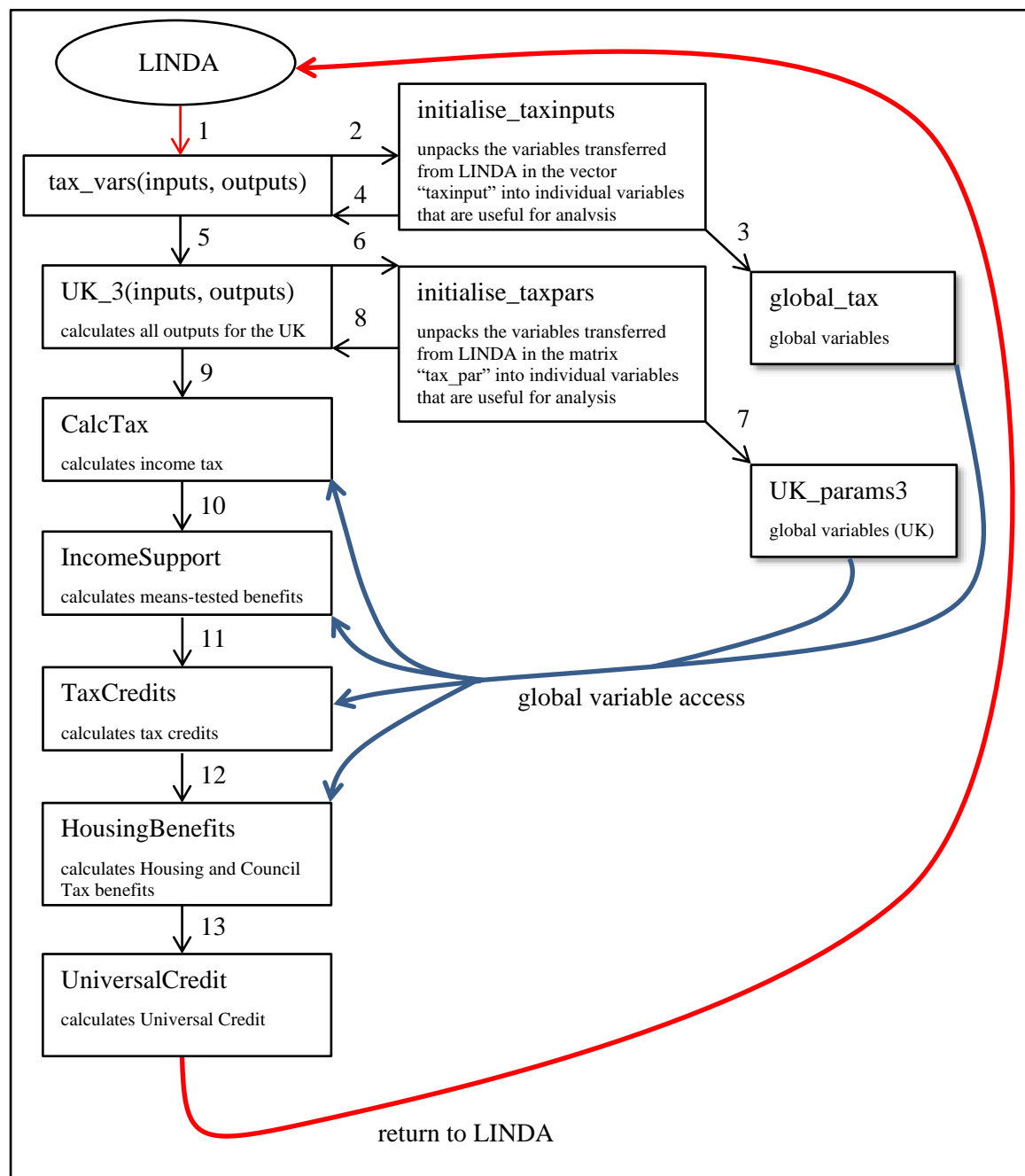


Figure 8.1: Stylised Schematic of the Calculation of Taxes and Benefits in LINDA

## Introducing user-defined tax schemes

An important feature of the LINDA model is that users can implement new tax and benefit schemes that extend beyond simple parameter adjustments of existing schemes. Suppose, for example, that you wanted to radically alter income support payable to working aged people from the scheme in place in 2010. The following provides a step-by-step guide to introducing a new user defined scheme.

- 1) Start by defining a test case
  - a. Open file “tax\_test1.xls” in the subdirectory MODEL\ANALYSIS\_FILES
  - b. Adjust the individual definition to reflect the circumstances of someone affected by the reform of interest. In our example, set:
    - i. age (cell B1) to 25
    - ii. year to 2010
    - iii. number of adults to 2
    - iv. number of children to 1
    - v. other values to those of potential interest
  - c. Save the file
  - d. Close “tax\_test1.xls”
  - e. Open “Job File.xls”
  - f. selected press ALT+F8
  - g. Run the SIDD macro
  - h. Press the “NEW SIMULATION FOR THE UK” button
  - i. Under “Simulation Name” type “test”
  - j. Select the “2010 tax benefit model tables” option
  - k. Under the “tax function reference year” type 2010
  - l. Press ENTER
  - m. In FORM 2, press the “ANALYSE TAXES” button
  - n. In FORM D4, select “Single individual type”
  - o. Press the “ENTER and RUN” button

*Step 1 will run a test simulation, and report the output to tax\_test1.xls – save a copy of this file under the name temp.xls for reference at a later stage*

- 2) Set the user-defined transfer system to replicate the pre-programmed transfer system for 2010
  - a. Add the user defined scheme to the Excel “job file”
    - i. Open “Job File.xls”
    - ii. Open the “tax params” worksheet
    - iii. Copy columns 9:14, and paste these into columns 2:7
    - iv. Save the excel file
    - v. With “Job File.xls” selected press ALT+F8
    - vi. Run the SIDD macro
    - vii. Press the “NEW SIMULATION FOR THE UK” button
    - viii. In FORM 1:
      1. Under “Simulation Name” type “test”
      2. Select the “user defined tax structure” option

3. Under the “tax function reference year” type 2010
4. Under the “reference number for user tax structure” type “3”
5. Press ENTER
- ix. In FORM 2:
  1. Press the “ANALYSE TAXES” button
- x. In FORM D4:
  1. Select “Single individual type”
  2. Press the “ENTER and EXIT” button

*Here we have altered “Job File.xls” so that it will direct LINDA to run a simulation based on a user defined tax structure. The user defined tax structure is denoted by the reference number 3 (step 2.a.viii.4 above). We have also set up “Job File.xls” to run a test of the assumed tax structure, which is important to ensuring that the revised model specification reflects that desired by the analyst. We return to this feature below.*

- b. Add the user defined tax structure to TAXES.sln
  - i. Double click on the TAXES.sln file
  - ii. Open file “0\_app\_taxes.f90”, by double-clicking on the file in the Solution Explorer
  - iii. Copy lines 113 to 116:

```
elseif ( tax_par4(15).lt.2.5 ) then
! UK 2006
```

```
call UK_2(age, year, n_taxp4, tax_par4, ndim_tax, tax_par, yy1, Rpstt, ...
```

- iv. Paste these lines at 117
- v. At line 117, replace 2.5 with 3.5
- vi. At line 118, replace “UK 2006” with “User defined 2010”
- vii. At line 120, replace UK\_2 with UK\_3

*This adds in a reference to the User Defined tax routine UK\_3 into the main TAXES program, using the reference value 3 defined in step 2.a.viii.4 above.*

- viii. In the Solution Explorer window, right-click on the “Source Files” folder, and select “Add”, and then “New Item”
- ix. Select “Fortran Free-form File”
- x. Under “Name”, enter “UK\_3.f90”
- xi. From the Solution Explorer window, double click on “UK\_1.f90”
- xii. Press CNTRL+A (to select all)
- xiii. Press CNTRL+C (to copy)
- xiv. From the Solution Explorer window, double click on “UK\_3.f90”
- xv. Press CNTRL+V (to paste)
- xvi. Press CNTRL+H (to do a search and replace)
- xvii. Search for the module name “UK\_params1” and replace with “UK\_params3”
  1. Ensure that the search and replace is limited to the “current document” – UK\_3.f90
- xviii. Search for the module name “UK\_tax1” and replace with “UK\_tax3”



1. Ensure that the search and replace is limited to the “current document” – UK\_3.f90
- xix. Search for the subroutine name “UK\_1” and replace with “UK\_3”
  1. Ensure that the search and replace is limited to the “current document” – UK\_3.f90

*This sets up the new User Defined code, copying over from the code that is provided with the model for 2010.*

- xx. From the Solution Explorer window, double click on “0\_app\_taxes.f90”
- xxi. At line 58, add “USE UK\_tax3”

*This permits the subroutine UK\_3 to be called from the code we added at step 2.b.vii above.*

- xxii. From the “File” menu, select “Save All”
- c. Rebuild TAXES in debug configuration
  - i. In the “solution explorer”, highlight the purple icon “TAXES”
  - ii. Under the view menu of VS, select “Property Pages”
  - iii. From the “Property Pages” window, press the “Configuration Manager” button
  - iv. Under “Active solution configuration:”, select “debug”
  - v. Under “Active solution platform:”, selection “x64”
  - vi. Press the “Close” button
  - vii. Press the “OK” button
    1. You can do the above more easily by selecting the “Active solution configuration”, and “Active solution platform” from the drop-down windows of VS, which may be visible as toolbars in the VS environment.
  - viii. From the “Build” menu of VS, select “Clean Solution”
  - ix. From the “Build” menu of VS, select “Build Solution”
    1. You should see the following output:

```
1>----- Build started: Project: TAXES, Configuration: debug x64 -----
1>Compiling with Intel(R) Visual Fortran Compiler XE 15.0.0.108 [Intel(R) 64]...
1>IT_1.f90
1>0_app_taxes.f90
1>Compiling manifest to resources...
1>Microsoft (R) Windows (R) Resource Compiler Version 6.3.9600.17200
1>Copyright (C) Microsoft Corporation. All rights reserved.
1>Linking...
1>Creating library C:\MyFiles\MODEL_LAB\MODEL 02\TAXES.lib and object C:\MyFiles\MODEL_LAB\MODEL 02\TAXES.exp
1>Embedding manifest...
1>
1>Build log written to "file:///C:/MyFiles/MODEL_LAB/FORTRAN/TAXES/x64/debug/BuildLog.htm"
1>TAXES - 0 error(s), 0 warning(s)
===== Build: 1 succeeded, 0 failed, 0 up-to-date, 0 skipped =====
```

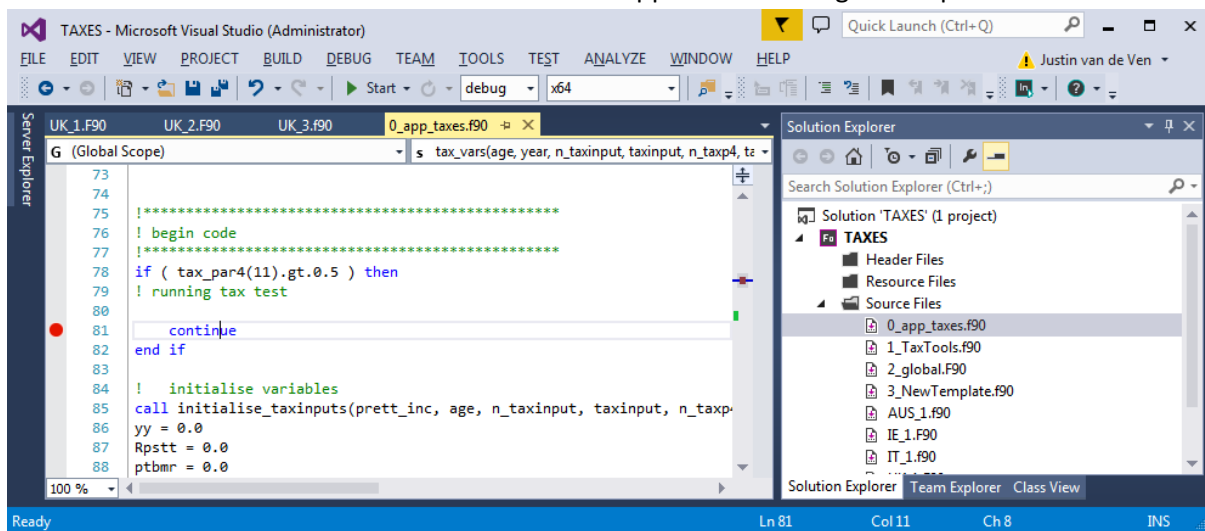
- x. Look in the MODEL subdirectory, and check that new files, all with the name TAXES.\*\*\* have been generated by the compiler

*Step 2 will have added new code into the TAXES routines, and set the model up to call this code.*

- 3) Run a first test case
  - a. In the MODEL subdirectory, double-click on SIDD.exe

*Steps 1 and 2 have been set up to allow you to check that the new code successfully replicates the 2010 code. Open up the temp.xls file created at the end of step 1, and compare this to the tax\_test1.xls file generated following step 3.a – the data in both files should be identical, with the exception that the tax\_test1.xls file should be more recent.*

- b. Ensure that the new code is being used
  - i. In VS, select open file 0\_app\_taxes.f90
  - ii. Clear all break-points, by selecting the “Debug” menu from VS, and select “Delete all breakpoints”
  - iii. Go to line 81
  - iv. Press F9 – a red dot should appear in the margin as depicted here



*As the comment indicates, this piece of code is designed to ensure that the breakpoint will only be encountered if the model is running a test simulation.*

- v. Press F5 to launch the debugger
  - vi. A yellow arrow should eventually appear at the red dot, indicating that the model has run to that point.
  - vii. Press F10 to step through the code, one line at a time and check that it does, in fact, calculate taxes via the UK\_3 subroutine that we introduced in step 2
- 4) Alter UK\_3.f90 code
  - a. In this stage, the tax and benefits code that we copied over from UK\_1.f90 to UK\_3.f90 can be altered to reflect the schemes of interest.
  - b. Our experience suggests that this process will involve the following stages:
    - i. Implement new code
    - ii. Attempt to compile code in debug configuration as described in step 2c above
      1. Correct any bugs identified by the compiler
    - iii. Run a test simulation with all break points deleted (see step 3.b.ii above)
      1. Correct any bugs identified by the debugger
    - iv. Check implied disposable income schedules, as reported in tax\_test1.xls, trialling alternative population combinations of interest

1. Where oddities are evident in the profiles, use the debugger to walk through the associated code to determine where remaining errors lie.
- v. Finalise code, and compile in “release configuration”

### Adjusting number of tax outputs

It is possible to alter the tax code of the model, so that it will generate additional summary statistics to those that are produced by default. This involves the following steps:

- 1) Define the number of additional statistics in the model parameters.
  - a. Add the number of additional tax statistics that you would like to generate with the model to the number currently defined in cell AO14 of sheets “input” and “inputA” in “Job File.xls”.
    - i. E.g. if the pre-existing value in cell AO14 is 17, and you would like to add an additional three outputs, then alter this cell to 20.
    - ii. This step can also be conducted through FORM 1 of the Excel front-end
  - b. Save “Job File.xls”.
- 2) Alter the Fortran code in the solution “TAXES.sln” to generate the statistics of interest
  - a. Note that these statistics need to be included as output variables in the subroutines that calculate taxes and benefits.  
e.g. you might alter the subroutine:
 

```
call UK_1(age, year, n_taxp4, tax_par4, ndim_tax, tax_par, yy1,
          cc_costs, hlth_costs, hs_costs, benefit_s, tax_s(1:8))
```

 so that it includes an additional output xx, by including xx at the end of the variable list as in:
 

```
call UK_1(age, year, n_taxp4, tax_par4, ndim_tax, tax_par, yy1,
          cc_costs, hlth_costs, hs_costs, benefit_s, tax_s(1:8), xx)
```
- 3) Alter the output vector to return the statistics to the model.
  - a. The additional statistics need to be sent to the subroutine pack\_taxoutputs, and then added to the end of the output vector as directed in that subroutine.  
e.g. in the above example, we would alter the code as indicated here:
 

```
call pack_taxoutputs(taxoutput, n_taxoutput, yy, cc_costs,
          hlth_costs, hs_costs, benefit_s, tax_s, xx)
```

 and then include xx in taxoutput, just after the line:
 

```
! user output add to the bottom here, altering the check imposed
          by the if statement as necessary
```
  - b. As the above comment suggests, it is also necessary to alter the check statement imposed by the if statement at the top of the pack\_taxoutputs subroutine to recognise the additional output:
 

```
if ( n_taxoutput.lt.20 ) then

elseif ( n_taxoutput.gt.20 ) then

end if
```
- 4) The model will then include the associated statistics in the panel data generated for each simulated population, under the name user\_toX, where X = 1, 2, 3, etc, for the first second and third output that has been added to the list of statistics reported by the tax function.

**TIP:** The analysis routines concerned with budgetary aggregates that are included with the model reference BenAgg and TaxAgg variables. If you would like the new scheme that you have programmed to feed into the budgetary statistics generated by these analysis routines, then it is necessary to include the value of any benefit as augmenting an element of the vector *benefit\_s* (in the case of benefits) or *tax\_s* (in the case of taxes).

## Appendix A: End User License

The computational engine upon which LINDA is based is referred to as the Simulator of Individual Dynamic Decisions, SIDD. LINDA is essentially a parameterisation and the policy environment that NIESR has implemented to permit SIDD to consider implications for the United Kingdom. The user license is for use of the SIDD engine. Model parameters assumed by LINDA are either high-level summary statistics that NIESR has calculated, and which are a matter of public record, or micro-data (i.e. the Wealth and Assets Survey) that must be accessed via third-party agreements not covered here.

### PLEASE READ CAREFULLY BEFORE INSTALLING

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This license agreement ("Licence") is a legal agreement between you (Licensee, or you) and the National Institute of Economic and Social Research, whose address is at 2 Dean Trench Street, Smith Square, London, SW1P 3HE, UK (Licensor, us or we) for the Simulator of Individual Dynamic Decisions Model software ("SIDD").

SIDD is a microsimulation model of tax and benefit systems, including the documentation (printed and electronic). For the avoidance of doubt, SIDD and this agreement does not include source input micro-data from surveys and administrative data sources.

We licence use of SIDD to you on the terms of this Licence Agreement. We do not sell the SIDD or accompanying documentation to you. We remain the owners of SIDD at all times.

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1.3. There are no implied Licences granted by this Licence

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6.2. Without prejudice to any other rights or remedy it may have hereunder, the Licensor may terminate this Licence immediately upon notice in writing to the Licensee in the event that the Licensee:

6.2.1. materially breaches this Licence and fails to remedy such breach (if capable of remedy) within thirty (30) working days from the date of receipt of written notice from the Licensor specifying the breach and requiring its remedy;

6.2.2. is declared insolvent by competent regulatory authority.

7. Liability: Nothing in this Licence is intended to exclude or limit the liability of either Party in respect of:

- (a) death or personal injury caused by its negligence;
- (b) fraudulent misrepresentation;
- (c) deliberate repudiatory breach of this Licence; or
- (d) any other liability which cannot be so excluded or limited under applicable law.

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8.1. This Licence contains the entire understanding between the Parties in relation to the subject matter of this Licence and supersedes all other agreements, negotiations, representations and undertakings, whether written or oral of prior date between the Parties.

8.2. If any provision of this Licence is held to be void or unenforceable by applicable law, it shall be severed therefrom and the remaining provisions of the Licence shall, to the extent possible, remain valid and fully enforceable.

8.3. Nothing in this Licence shall be construed as creating a joint venture, partnership, contract of employment or relationship of principal and agent between the Parties.

8.4. No third party shall have any right to enforce any term of this Licence.

## Appendix B: The Utility Function

This has two components to it. Within-period utility  $u$  is a function of total benefit unit consumption  $c_{i,t}$  adjusted for effective benefit unit size  $\theta_{i,t}$  and leisure time represented by  $l_{i,t}$ .

$\alpha$  represents the consumption-equivalent of leisure and  $\varepsilon$  the elasticity of substitution between consumption and leisure.

$$u\left(\frac{c_{i,j}}{\theta_{i,j}}, l_{i,t}\right) = \left( \left( \frac{c_{i,j}}{\theta_{i,j}} \right)^{(1-1/\varepsilon)} + \alpha^{1/\varepsilon} l_{i,t}^{(1-1/\varepsilon)} \right)^{\frac{1}{1-1/\varepsilon}} \quad (1)$$

Within-period utility enters into an intertemporal utility function in the manner represented below. Intertemporal discounting takes a quasi-hyperbolic form, where  $\delta$  is the long-run discount factor, and  $\beta$  is the excess short-run discount factor. When  $\beta = 1$ , preferences are time consistent, which implies that – for any given set of circumstances – the same decisions will maximise expected lifetime utility, regardless of when the decisions are made. That is, if an individual could commit to savings and employment decisions that take their evolving circumstances into account for any future age, then they will make the same decisions regardless of their current age. With  $0 < \beta < 1$ , intertemporal preferences exhibit myopia, which means that people would like to be more patient in the future than will actually be the case. The model assumes that people are ‘sophisticatedly’ myopic, in the sense that they are aware of their own self-control problems and react to them. This can result, for example, in a preference to lock savings away in a pension rather than a bank account, to avoid the temptation of spending the savings prematurely.

$\gamma$  is relative risk aversion, and  $\phi_{j-t,t}$  is the probability of surviving  $j$  years, given survival to age  $t$ .  $\zeta_a$  and  $\zeta_b$  represent the warm glow utility derived from leaving a positive bequest  $w^+_{i,t+1}$ .

$$U_{i,t} = \left[ u\left(\frac{c_{i,t}}{\theta_{i,t}}, l_{i,t}\right)^{1-\gamma} + \beta E_t \left\{ \sum_{j=t+1}^T \delta^{j-t} \left( \phi_{j-t,t} u\left(\frac{c_{i,j}}{\theta_{i,j}}, l_{i,j}\right)^{1-\gamma} + (1 - \phi_{j-t,t}) (\zeta_a + \zeta_b w^+_{i,t+1})^{1-1/\gamma} \right) \right\} \right]^{\frac{1}{1-\gamma}} \quad (2)$$

## Appendix C: Pre-programmed tax and transfer systems for the UK

### Appendix C.1: Transfer system applicable in April 2011

#### Appendix C.1.1 Taxes<sup>11</sup>

- *Income taxes*

Income taxes are calculated separately for each simulated adult. The 'taxable income' of an adult is evaluated by aggregating their income from employment (both employee and self-employed), retirement pensions, and investment returns on assets held outside of pensions and Individual Savings Accounts, and deducting their respective personal allowance. In contrast to practice, this definition of taxable income omits jobseeker's allowance, a stylisation that is likely to have a negligible bearing on simulations as individual employment circumstances are assumed to be stable within each year (so that individuals in receipt of Jobseekers Allowance do not typically pay income tax).

The personal allowance for individuals under state pension age is set equal to £7475 per year in 2011, and is withdrawn by 50p for each £1 of income in excess of £100,000 per year. The personal allowance for individuals in excess of state pension age is set equal to £10,015 per year<sup>12</sup>, and is withdrawn in stages, at the rate of 50p for each £1 of private income between £24,000 and £29,080 per year, and then again at the rate of 50p for each £1 of private income in excess of £100,000 per year.

Income taxes are paid at the rate of 20% on taxable income up to the basic rate limit of £35,000 per year, at the rate of 40% on income between £35,001 and the higher rate limit of £150,000, and at the additional rate of 50% on all taxable income in excess of £150,000 per year. All thresholds and personal allowances are assumed to grow in line with wages under both the principal and negative calibrations.

- *National insurance contributions*

Class 1 (employee) National Insurance contributions are calculated on the earnings of each adult under state pension age. Contributions are paid at the rate of 12% on earnings in excess of the Primary Threshold (worth £139 per week in 2011) and under the Upper Earnings Limit (£817 per week), and at the rate of 2% on earnings in excess of the Upper Earnings Limit. Furthermore, individuals who are identified as having contracted out of the State Second Pension, receive a contracted out rebate worth 1.6% on all earnings in excess of the Primary Threshold. All thresholds are assumed to grow in line with wages under both the principal and negative calibrations.

- *Taxes on consumption*

Simulating taxes on consumption for the UK is complicated by the different rates of Value Added Tax and excise duties that are payable on different goods and services, which contrasts with the aggregate measure of non-durable consumption projected by LINDA. To accommodate this variation, we have estimated a series of reduced form regressions that describe the fraction of total non-durable expenditure on each of six consumption categories: goods liable to the full rate of VAT,

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<sup>11</sup> See Pope and Roantree (2014) for a concise review of the UK tax system.

<sup>12</sup> This personal allowance is mid-way between the personal allowances provided to individuals aged 65-74 and those aged 75+ in 2011-12.

goods liable to the reduced rate of VAT, alcohol, tobacco, fuel, and insurance premia distinguishing those liable to the standard and higher rates of tax. These reduced form models are used to approximate benefit unit consumption of each of the six expenditure categories during each year, and the associated tax burden is evaluated by multiplying by the relevant tax or duty rate.

In the case of VAT and taxes on insurance premia, the relevant rates are unambiguously defined: the full-rate of VAT in 2011 was 20% and the reduced rate was 5%; the standard rate of tax applied to insurance premia was 6% and the higher rate was 20%. In contrast, the duties levied on alcohol, tobacco and fuel vary substantially across individual products. Averages were consequently calculated for the rates applied to individual products within these three broad consumption categories, weighting by expenditure share (data supplied by HM Treasury). These calculations yielded indirect tax rates (inclusive of VAT) of 50% for alcohol, 66% for fuel, and 80% for tobacco.

The reduced form models for consumption shares were calculated using data drawn from the Living Cost and Food Survey, pooled over the years 2001 to 2010 (115,827 observations). Each of the six categories of consumption were evaluated following coding used for the IGOTM effective as at 31 August 2012. After testing a number of alternatives, we selected a linear regression specification for all six consumption categories, defining the respective consumption share as a function of age, relationship status, numbers of children, education status, disposable income, and consumption.

- *Council Tax*

Council tax is assumed to depend on relationship status, and the number and age of dependent children. It is modelled based on imputed bedrooms, consistent with the definition of the “bedroom entitlement” applied for housing benefit (see Section 5.2). One bedroom is imputed for each single adult / cohabitating couple, another for each child aged 13 or over, and another for every 2 children aged under 13 years, subject to a maximum of four bedrooms. Furthermore, higher rates of council tax are assumed to apply to couples than to singles. The rates assumed for 2011 are: £14.17 per week for single adults and £19.23 for couples in a one bedroom house; £16.19 for singles and £22.26 for couples in a two bedroom house; £18.22 for singles and £27.32 for couples in a three bedroom house, and £20.24 for singles and £32.38 for couples in a four bedroom house. These rates are all indexed to wage growth.

### **Appendix C.1.2 Benefits<sup>13</sup>**

All benefits values and thresholds, unless otherwise stated, are assumed to be frozen (in nominal terms) from 2016 to 2020, and to be indexed to prices thereafter.

- *Income support prior to state pension age*

Support to benefit units with low incomes who are not affected by a health condition (see employment and support allowance below), and do not satisfy the age requirements of the pension credit (see below) is modelled on income support. The maximum benefit payable under income support is comprised of a number of components. Single adults are eligible for income support worth £71 per week in 2011, and couples for £111.45 per week. Benefit units with dependent children under age 6 are assumed to be eligible for healthy start vouchers worth £6.20 per week for

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<sup>13</sup> See Hood and Oakley (2014) for a concise review of the benefits system in Great Britain.



new-borns, decreasing to £3.10 per week for children aged 1 to 5. Free school meals are also included, worth £5.52 for each child aged 5 to 10.

Furthermore, benefit units that are identified as home owners with a mortgage are eligible for assistance with mortgage interest payments, worth up to 3.85% per annum (nominal, 1.85% real) on a mortgage of up to £200,000.

The benefits referred to here are means-tested, withdrawn at the rate of £1 for each £1 of private income, and at the rate of £1 per week for every £250 of non-housing capital in excess of a £6,000 disregard for those on income support.

- *Employment and Support Allowance*

Employment and Support Allowance (ESA) is designed to support working-aged individuals with a 'limited capability for work'. Claimants must be aged between 16 and state pension age, and must satisfy a related health test. The model abstracts from the contributory benefit and (13 week) assessment phase, focussing on income related ESA 'main phase' payments. The benefit tops-up income to the relevant applicable amount, equal to the sum of personal allowances and premia.

Employment and support allowance is modelled in two alternative ways, depending upon whether disability is described explicitly within the prevailing model specification.

ESA payments are simulated based on a set of personal allowances and premia. When disability is implicit in the model, then eligible rates are based on imputed population averages. When disability is explicit in the model, then rates vary by individual specific circumstances.

The simulated personal allowance is worth £67.50 per week (in 2011) for single and sole parents, and £105.95 per week for a couple. Furthermore, the model simulates premia per week equal to:

- £26.75 for work related activity recipients
- £32.35 for support recipients
- £31.00 for carers
- If eligible for the enhanced rate living component of the PIP (see below):
  - £14.05 for single adults
  - £20.25 for couples
- If eligible for the living component of PIP, and:<sup>14</sup>
  - single, without anyone receiving Carer's Allowance in respect of household, or
  - couple, both receiving living component of PIP and only one receiving subsidised care under Carer's Allowance:
    - £55.30 per week (doubled if couple and no CA received)

Only the premium for 'support recipients' is reflected in the version of the model that omits health. Furthermore, benefit units that are identified as home owners with a mortgage are eligible for

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<sup>14</sup> The model assumes that single adults do not receive this benefit, but couples who both receive the living component do receive a single share of the allowance. These assumptions are based on the premise that the carer allowance is always claimed, although only one share of the carer's allowance is claimed for couples.

assistance with mortgage interest payments, worth up to 3.85% per annum (nominal, 1.85% real) on a mortgage of up to £200,000.

The applicable amount, equal to the sum of personal allowances and premia, is withdrawn at the rate of £1 for each £1 of private income, and £1 per week of benefit for every £500 of non-pension non-housing wealth over a £10,000 threshold.

- *Disability Living Allowance (DLA) and Personal Independence Payment (PIP)*

DLA and PIP are designed to help benefit units with disabled members who are under state pension age meet the costs associated with their conditions. Attendance Allowance, which is described in the following subsection, plays the same role as DLA/PIP for claimants in excess of state pension age. The PIP replaced DLA for new claimants from April 2013, and is scheduled to be open to all existing claimants by late 2017. The two schemes share many similarities and are consequently simulated together. The most important differences between the two schemes are that the PIP includes two rates of care payments, relative to three payable under the DLA. The reduction in the number of care (daily living) payments under PIP aligns the benefit with the Attendance Allowance.

Furthermore, the health assessment for the PIP focusses on the ability of an individual to 'participate in society', in contrast to the DLA's reference to specific health conditions. The following discussion focusses upon the PIP, as this is the most relevant benefit for forward projections.

PIP has two components, and a claimant can receive either one or both of these depending upon their circumstances. The daily living component is designed to subsidise the costs of care required by a disabled individual. The rate of payment depends on an official assessment of care needs, with a standard rate equal to £49.30 per week, and an enhanced rate of £73.60 per week. The mobility component of PIP pays a benefit to subsidise outdoor journeys by individuals aged 5 years and above, and is payable at a standard rate of £19.55 per week, and an enhanced rate of £51.40 per week. The PIP is non-taxable, non-means tested, and non-contributory.

Receipt of PIP passports individuals to premia under a range of alternative programmes:

- The Child Tax Credit increases by £2,800 for a disabled child (disabled child addition).
  - The Working Tax Credit increases by £2,650 in 2011.
  - The Working Tax Credit increases by a further £1,130 if the enhanced rate living component is payable.
  - The labour condition required to receive the WTC is relaxed to part-time for one adult.
  - Disability premia under ESA (see Section 15.1)
  - Exempts the benefit unit from the benefits cap.
- *Attendance allowance (AA)*

AA is payable to individuals from state pension age, and provides similar support to the daily living component of the PIP for working aged people. Like the PIP's daily living component, AA is payable at two rates; the lower rate is equivalent to the standard rate of PIP (£49.30 per week in 2011), and is payable if an individual requires care during the day or night (but not both). The higher rate corresponds to the enhanced rate of PIP (£73.60 per week), and is payable if an individual requires care during both the day and night. Like PIP, AA is non-taxable, non-means tested, and non-contributory.

Although initial claims to the PIP are limited to individuals who are under state pension age, on-going claims to PIP are not discontinued from state pension age. This has the advantage that mobility payments, which are not payable under the AA, can continue to be received into older age.<sup>15</sup>

Eligibility for AA increases the pension credit guarantee credit by £55.30 per week for each qualifying adult, in respect of foregone Carer's Allowance (see conditions defined for ESA).

- *Carer's allowance (CA)*

CA provides support to individuals who are 16 or over, and who provide regular and substantial care to a person receiving AA or the living component of PIP. The benefit pays a standard rate of £55.55 per week, and cannot be claimed by an individual in full-time education or earning more than £102 per week (in 2014). The benefit is taxable and non-contributory. CA increases the eligible benefit payable under IS, PC, or ESA by £31.00 per week. CA also exempts the spouse from the 16 hour working condition to receive the WTC.

Some individuals may be eligible to Carer's Allowance at the same time as they are eligible to either Income Support or Employment and Support Allowance. The model is designed to select the benefit option that maximises each individual's disposable income. It does this by first considering eligibility for a CA payment, and any associated IS/ESA premia. The eligible IS payment is then evaluated, taking into account any relevant CA premium. ESA eligible payments are then evaluated in the same way, and the maximum payment selected between IS and ESA. This maximum is compared against the relevant CA payment to determine which benefit the individual should take-up.

- *Pension credit*

The pension credit is comprised of two elements, both of which are modelled explicitly. The guarantee credit is payable from age 60 in all years prior to 2010, rising to age 61 in 2010, 62 in 2012, 63 in 2014, 64 in 2016, and from simulated state pension age thereafter. Simulated state pension age is projected to remain at 65 years until 2018, increasing to 66 in 2019, to 67 in 2026, and to 68 in 2034.

The age of eligibility for the guarantee credit is defined with respect to planned variation of state pension age for women, taking into consideration the division of time into discrete annual intervals that is a feature of the model. Specifically, state pension age for women increased to 60 years and 1 month in May 2010, 61 years and 1 month in May 2012, 62 years and 1 month in May 2014, and is projected to rise to 63 years and 3 months by July 2016, 64 years and 1 month by November 2017, and 65 years by November 2018 at which time the state pension age of men and women will be equalised. Thereafter, existing legislation that will see state pension age of both men and women increase to 65 years and 1 month by January 2019, 66 years and 1 month by May 2026, and the government has announced its intention to increase state pension in line with longevity thereafter.<sup>16</sup>

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<sup>15</sup> The same issue applies to DLA, with the added advantage in relation to that scheme that the third (lower) rate of care payment – not available under either PIP or AA – also remains payable into older age.

<sup>16</sup> The 2012-based projected mortality data reported by the ONS indicate that the period life expectancy at birth in the UK was 79 for men, rising to 84.1 years in 2037. This implies an increase in life expectancy of 0.2 years for each year that birth is delayed. The Chancellor as part of the 2013 Autumn statement that people

The guarantee credit provides a maximum benefit worth £137.35 per week to a single adult in 2011, and £209.70 to a couple. Furthermore, benefit units that are identified as home owners with a mortgage are eligible for assistance with mortgage interest payments, worth up to 3.85% per annum on a mortgage of up to £200,000. These payments are subject to a means-test on total benefit unit private income and non-housing capital, with benefits reduced £1 for every £1 of private income, and by £1 for every £500 of non-housing wealth in excess of a £10,000 disregard.

The savings credit provides additional income to benefit units that have private income in excess of a minimum threshold and are above state pension age. Savings credit increases at the rate of 60p for every £1 of private income in excess of £103.15 per week for singles in 2011, and £164.55 per week for couples, up to a maximum benefit worth £20.52 per week for singles in 2011 and £27.09 per week for couples. Any private income earned beyond the sum required to obtain the maximum savings credit benefit, reduces the benefit at the rate of 40p in the £1.

The maximum benefits payable under the guarantee credit are assumed to increase with real wages. In contrast, the maximum value of the savings credit is assumed to be indexed to prices. This implies that the savings credit threshold grows faster than earnings.

- *Working tax credit*

Working tax credit is payable to any benefit unit over age 24, with at least one adult in full-time employment, or with at least one adult in some employment and with a dependent child.<sup>17</sup> The maximum benefit payable is comprised of a basic element worth £1920 per year in 2011, plus an additional element worth £1950 per year for single-parents and couples, plus an element worth £790 per year for benefit units with at least one adult working at least 30 hours per week. Furthermore, benefit units in which all adult members work at least 16 hours per week are eligible to subsidised childcare for children aged 14 and under, equal to 70% of qualifying childcare costs up to a maximum of £175 per week for a single child, and £300 per week for two or more children.

The benefits payable under the working tax credit are means-tested in conjunction with benefits payable under the child tax credit described below.

- *Child tax credit*

The child tax credit is payable to benefit units with dependent children under 20 years of age. The maximum benefit payable is comprised of a family element worth £545 per year in 2011, and a child element worth £2,555 per year for each qualifying child.

Eligible benefits under the child tax credit are aggregated with those of the working tax credit and subject to a common means test. Any benefit unit income in excess of a minimum threshold reduces the total tax credits payable, at the rate of 41p per £1. The minimum threshold is £6,420

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should expect to spend one third of their lives in retirement. Combining these two details suggests that each year that birth is delayed should increase state pension age by 0.133 years, suggesting that state pension age should increase by 1 year in every 7.5 years.

<sup>17</sup> These conditions are designed to approximate the rules concerning employment applied by the WTC, which require most claimants to work at least 30 hours per week. Disabled individuals, lone-parents, and individuals aged 60 and over can work 16 hours per week, and couples with dependent children must work a combined total of at least 24 hours per week.

per year in 2011 for benefit units eligible to both the working tax credit and the child tax credit, and £15,860 per year for those eligible to only the child tax credit.<sup>18</sup>

- *Child benefit*

Benefit units with dependent children receive Child Benefit. The benefit is worth £20.30 per week in 2011 for the first child and £13.40 per week for each subsequent child. Child benefits are not means-tested.

- *Housing benefit*

Housing benefit is paid in respect of simulated rent payments to benefit units that have sufficiently low incomes. The maximum benefit payable under housing benefit is equal to rent expenditure capped at the respective local housing allowance. The local housing allowance is determined by rates graded by the bedroom entitlement of the benefit unit. The bedroom entitlement allows one bedroom for each single adult / cohabitating couple, another for each child aged 13 or over, and another for every 2 children aged under 13 years, subject to a maximum of four bedrooms. The local housing allowance is £162.50 per week in 2011 for one bedroom, £188.50 per week for two bedrooms, £221 per week for three bedrooms, and £260 per week for four bedrooms.<sup>19</sup>

Housing benefit is means-tested with respect to a broad measure of income that is net of child care costs eligible to subsidies via the working tax credit (see above), and most taxes and benefits (excluding the disability living allowance). The measure of income also includes imputed returns on non-housing wealth, calculated as £1 per week for every £250 of wealth in excess of a £6,000 disregard for individuals under the age of eligibility for Employment and Support Allowance (see above), and £1 per week for every £500 of non-housing wealth in excess of a £10,000 disregard otherwise. This measure of income is then reduced by an earnings disregard, worth £5 per week for single people, £10 per week for couples, and £25 per week for lone-parents, with an additional £17.10 disregard applied for benefit units with at least one adult working full-time, or at least one adult working and with dependent children.

Any excess of this measure of income above the benefit unit's relevant applicable amount reduces housing benefit at the rate of 65p in every £1. The applicable amount is equal to £67.50 per week for single adults, £72.30 for lone-parents, and £105.95 for couples, increasing by £62.33 for each dependent child (aged 18 and under). Couples and lone-parents are also eligible to an additional family premium worth 17.40 per week.

- *Council tax benefit*

Council tax benefit is provided to subsidise the costs to households of council taxes (see Section 4.6.1). Although council tax benefit was available in 2011, it has been amended to a localised benefit from 2013/14. Nevertheless, council tax benefit is modelled by default in the form that it took prior to localisation of the benefit. This structure assumes that council tax benefit is subject to the same means-testing rates and thresholds as housing benefit described above, with the exception

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<sup>18</sup> This means test ignores the second threshold used to means test child tax credits in 2011/12 as this feature was withdrawn from 2012/13.

<sup>19</sup> In practice, the bedroom entitlement distinguishes dependent children by sex of dependent children, which is omitted in the model assumptions defined here. The assumed local housing allowances are set equal to 65% of the relative caps imposed in April 2011, an assumption that is broadly based on the (now discontinued) DWP Tax Benefit Model Tables.

that the benefit is withdrawn the rate of 20p in every £1. As council tax benefit and housing benefit are withdrawn simultaneously, this implies 85p of aggregate (council tax and housing) benefit is withdrawn for every £1 of income above the benefit unit's relevant applicable amount so long as both benefits are received.

- *Allowance for imperfect benefits take-up*

Take-up of benefits by a benefit unit in any year is modelled as a random event. Each benefit unit in each year is assigned a number drawn from a uniform [0,1] distribution. This number is compared against the "take-up rate" associated with the benefit unit's circumstances in the respective year. If the number is less than the take-up rate, then the benefit unit is assumed to take-up their benefits; otherwise they do not.

Take-up rates distinguish between benefit units, based on labour supply, family demographics, and age, as described by the following table:

no adult employed			
working lifetime		from state pension age	
without children	with children	singles	couples
57%	62%	64%	56%
at least one adult employed			
without children		with children	
income to £10,000 p.a.	income £10,000+ p.a.	income to £10,000 p.a.	income £10,000+ p.a.
47%	28%	97%	69%

The take-up rates for benefit units without any employment were set equal to figures reported for 2013/14 in DWP (2015). Benefit units under state pension age are subject to take-up rates reported for (income based) Job Seekers Allowance (table 4.3.1), and those in excess of state pension age are subject to rates reported for the Pension Credit (table 2.3.4). The take-up rates and income thresholds assumed for analysis are drawn from Tables 4 (with children) and 11 (without children) of HMRC (2015). These tables report take-up rates for Child Benefit, Child Tax Credit and Working Tax Credit estimated for 2013-14 (updated in February 2016).<sup>20</sup>

- *Tax residuals*

Tax residuals are model parameters that can vary by birth year and age. The influence that these residuals have on disposable income is determined within the tax function, and so is otherwise unconstrained. These residuals have been suppressed in the current calibration for the model by setting them to zero.

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<sup>20</sup> A common rule is assumed for disability related benefits (DLA, AA, and CA), as for other non-housing benefits, due to the unique difficulties associated with identification of disability benefit take-up rates (on which, see Kasparova *et al.*, 2007, for DLA and AA, and Berthoud, 2010, for CA).

## Appendix C.2: Transfer system applicable in April 2016

The transfer system pre-programmed for 2016, is broadly similar to that described for 2011, with the most differences limited to associated rates and thresholds. This section describes the differences between the two transfer systems.

### Appendix C.2.1 Taxes

- *Income taxes*

The 2016 income tax code introduces the Personal Savings Allowance (PSA), relative to the 2011 code. The PSA increases an individual's personal allowance, relative to two thresholds on total taxable income. Below the threshold of £43,000 per year, investment income is subject to an allowance of £1000 (in 2016). Below the threshold of £150,000 per year, investment income is subject to an allowance of £500, otherwise the PSA is set to 0.

The personal allowance for all individuals is set equal to £11000 per year in 2016, and is withdrawn by 50p for each £1 of income in excess of £100,000 per year.

Income taxes are paid at the rate of 20% on taxable income up to the basic rate limit of £43,000 per year, at the rate of 40% on income between £43,001 and the higher rate limit of £150,000, and at the additional rate of 50% on all taxable income in excess of £150,000 per year.

- *National insurance contributions*

Contributions are paid at the rate of 12% on earnings in excess of the Primary Threshold (worth £155 per week in 2016) and under the Upper Earnings Limit (£827 per week), and at the rate of 2% on earnings in excess of the Upper Earnings Limit.

- *Taxes on consumption*

The only change in consumption taxes implemented between 2011 and 2016 is the standard rate assumed for insurance premia, which increased from 6% to 10%.

- *Council Tax*

Council tax parameters were unaltered between 2011 and 2016.

### Appendix C.1.2 Benefits<sup>21</sup>

All benefits values and thresholds, unless otherwise stated, are assumed to be frozen (in nominal terms) from 2016 to 2020, and to be indexed to prices thereafter.

- *Income support prior to state pension age*

Single adults are eligible for income support worth £73.10 per week in 2016, and couples for £114.85 per week. Benefit units with dependent children under age 6 are assumed to be eligible for healthy start vouchers worth £6.20 per week for new-borns, decreasing to £3.10 per week for children aged 1 to 5. Free school meals are also included, worth £5.52 for each child aged 5 to 10.

Furthermore, benefit units that are identified as home owners with a mortgage are eligible for assistance with mortgage interest payments, worth up to 3.85% per annum (nominal, 1.85% real) on a mortgage of up to £200,000.

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<sup>21</sup> See Hood and Oakley (2014) for a concise review of the benefits system in Great Britain.

The benefits referred to here are means-tested, withdrawn at the rate of £1 for each £1 of private income, and at the rate of £1 per week for every £250 of non-housing capital in excess of a £6,000 disregard for those on income support.

- *Employment and Support Allowance*

The simulated personal allowance is worth £73.10 per week (in 2016) for single and sole parents, and £114.85 per week for a couple. Furthermore, the model simulates premia per week equal to:

- £0 for work related activity recipients
- £36.20 for support recipients
- £34.60 for carers
- If eligible for the enhanced rate living component of the PIP (see below):
  - £15.75 for single adults
  - £22.60 for couples
- If eligible for the living component of PIP, and:<sup>22</sup>
  - single, without anyone receiving Carer's Allowance in respect of household, or
  - couple, both receiving living component of PIP and only one receiving subsidised care under Carer's Allowance:
    - £61.85 per week (doubled if couple and no CA received)

Only the premium for 'support recipients' is reflected in the version of the model that omits health. Furthermore, benefit units that are identified as home owners with a mortgage are eligible for assistance with mortgage interest payments, worth up to 3.85% per annum (nominal, 1.85% real) on a mortgage of up to £200,000.

The applicable amount, equal to the sum of personal allowances and premia, is withdrawn at the rate of £1 for each £1 of private income, and £1 per week of benefit for every £500 of non-pension non-housing wealth over a £10,000 threshold.

- *Disability Living Allowance (DLA) and Personal Independence Payment (PIP)*

The standard rate of the daily living component equals to £55.10 per week, and the enhanced rate equals £82.30 per week (in 2016). The mobility component of PIP pays a standard rate of £21.80 per week, and an enhanced rate of £57.45 per week.

Passports to alternative programmes:

- The Child Tax Credit increases by £3,140 for a disabled child (disabled child addition).
- The Working Tax Credit increases by £2,970 in 2016.
- The Working Tax Credit increases by a further £1,275 if the enhanced rate living component is payable.
- The labour condition required to receive the WTC is relaxed to part-time for one adult.
- Disability premia under ESA
- Exempts the benefit unit from the benefits cap.

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<sup>22</sup> The model assumes that single adults do not receive this benefit, but couples who both receive the living component do receive a single share of the allowance. These assumptions are based on the premise that the carer allowance is always claimed, although only one share of the carer's allowance is claimed for couples.



- *Attendance allowance (AA)*

The AA's daily living component the lower rate is £55.10 per week in 2016, and the higher rate is £82.30 per week. Eligibility for AA increases the pension credit guarantee credit by £61.85 per week for each qualifying adult.

- *Carer's allowance (CA)*

The CA standard rate is £62.10 per week, and cannot be claimed by an individual in full-time education or earning more than £110 per week (in 2016). CA increases the eligible benefit payable under IS, PC, or ESA by £34.60 per week. CA also exempts the spouse from the 16 hour working condition to receive the WTC.

- *Pension credit*

The guarantee credit is payable from age 64 in 2016, and from simulated state pension age thereafter. Simulated state pension age is projected to remain at 65 years until 2018, increasing to 66 in 2019, to 67 in 2026, and to 68 in 2034.

The guarantee credit provides a maximum benefit worth £151.20 per week to a single adult in 2016, and £230.85 to a couple. Furthermore, benefit units that are identified as home owners with a mortgage are eligible for assistance with mortgage interest payments, worth up to 3.85% per annum on a mortgage of up to £200,000. These payments are subject to a means-test on total benefit unit private income and non-housing capital, with benefits reduced £1 for every £1 of private income, and by £1 for every £500 of non-housing wealth in excess of a £10,000 disregard.

Savings credit increases at the rate of 60p for every £1 of private income in excess of £126.50 per week for singles in 2016, and £201.80 per week for couples, up to a maximum benefit worth £14.82 per week for singles in 2016 and £17.43 per week for couples. Any private income earned beyond the sum required to obtain the maximum savings credit benefit, reduces the benefit at the rate of 40p in the £1.

- *Working tax credit*

The basic element of the WTC is worth £1960 per year in 2016, plus an additional element worth £2010 per year for single-parents and couples, plus an element worth £1960 per year for benefit units with at least one adult working at least 30 hours per week. WTC provides a subsidy of 85% of qualifying childcare costs, up to a maximum of £645.35 per month for a single child, and £1108.04 per month for two or more children.

- *Child tax credit*

The CTC family element is worth £0 per year in 2016, and the child element is worth £2,780 per year for each qualifying child.

The income threshold above which tax credits are withdrawn is £6,420 per year in 2016 for benefit units eligible to both the working tax credit and the child tax credit, and £16,105 per year for those eligible to only the child tax credit.<sup>23</sup>

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<sup>23</sup> This means test ignores the second threshold used to means test child tax credits in 2011/12 as this feature was withdrawn from 2012/13.

- *Child benefit*

The benefit is worth £20.70 per week in 2016 for the first child and £13.70 per week for each subsequent child.

- *Housing benefit*

The local housing allowance is £162.50 per week in 2016 for one bedroom, £188.50 per week for two bedrooms, £221 per week for three bedrooms, and £260 per week for four bedrooms.<sup>24</sup>

Means-tested income includes imputed returns on non-housing wealth, calculated as £1 per week for every £250 of wealth in excess of a £6,000 disregard for individuals under the age of eligibility for Employment and Support Allowance (see above), and £1 per week for every £500 of non-housing wealth in excess of a £10,000 disregard otherwise. This measure of income is then reduced by an earnings disregard, worth £5 per week for single people, £10 per week for couples, and £25 per week for lone-parents, with an additional £17.10 disregard applied for benefit units with at least one adult working full-time, or at least one adult working and with dependent children.

Any excess of this measure of income above the benefit unit's relevant applicable amount reduces housing benefit at the rate of 65p in every £1. The applicable amount is equal to £73.10 per week for single adults, and £114.85 for couples, increasing by £66.90 for each dependent child (aged 18 and under).

- *Council tax benefit*

Council tax benefit is provided to subsidise the costs to households of council taxes (see Section 4.6.1). Although council tax benefit was available in 2011, it has been amended to a localised benefit from 2013/14. Nevertheless, council tax benefit is modelled by default in the form that it took prior to localisation of the benefit. This structure assumes that council tax benefit is subject to the same means-testing rates and thresholds as housing benefit described above, with the exception that the benefit is withdrawn the rate of 20p in every £1. As council tax benefit and housing benefit are withdrawn simultaneously, this implies 85p of aggregate (council tax and housing) benefit is withdrawn for every £1 of income above the benefit unit's relevant applicable amount so long as both benefits are received.

- *Benefits Cap*

Non-carer households are subject to a maximum value for all welfare benefits received, equal to £20,000 per year in 2016.

## **Appendix C.3: Universal credit**

Universal credit is designed to replace income support (including income based jobseeker's and employment and support allowances), housing benefit, the working tax credit, and child tax credit. Universal credit has been in planning since the conservative party annual conference in 2010, and has been rolled-out progressively since April 2013, and is scheduled to have replaced the existing benefit schemes by 2017/18. This policy shift is consequently built into the model.

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<sup>24</sup> In practice, the bedroom entitlement distinguishes dependent children by sex of dependent children, which is omitted in the model assumptions defined here. The assumed local housing allowances are set equal to 65% of the relative caps imposed in April 2011, an assumption that is broadly based on the (now discontinued) DWP Tax Benefit Model Tables.

The maximum payment under universal credit is simulated by aggregating the maximum sums payable under income support, child tax credit, and housing benefit, and then adding the maximum childcare component payable under the working tax credit. This maximum benefit is then withdrawn at the rate of 65p for each £1 of earned income net of taxes and national insurance contributions earned above the benefit unit's relevant "work allowance". Furthermore, any pension income received is deducted from the universal credit payable, and each £250 of non-housing wealth in excess of a £6,000 disregard reduces the universal credit by £1 per week (in 2011 prices).

The work allowance depends upon whether housing related support would have been received through either income support (off-setting mortgage interest) or housing benefit (off-setting rent). If so, then so-called "lower work allowances" apply, worth £25.21 per week to single adults in 2011, £59.72 to lone parents, £25.21 to couples, and £50.41 to couples with children. Otherwise, "higher work allowances apply, which are identical to the lower allowances for benefit units without children, but are worth £166.67 per week to lone parents, and £121.71 to couples with children.