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The evolution of the UK tax base.

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In this brief the Sheffield Political Economy Research Institute (SPERI) considers the changing tax base of the UK state. Taxation takes many different forms, encompassing progressive taxes such as income tax, regressive taxes such as VAT, and taxes targeted on private enterprises such as corporation tax. The economic downturn significantly affected tax revenues, and the coalition government since 2010 has sought to cut some taxes, to boost economic recovery, but at the same time raise others, in support of deficit reduction. It is necessary to consider, therefore, what impact these changes have had on the nature of the UK tax base.

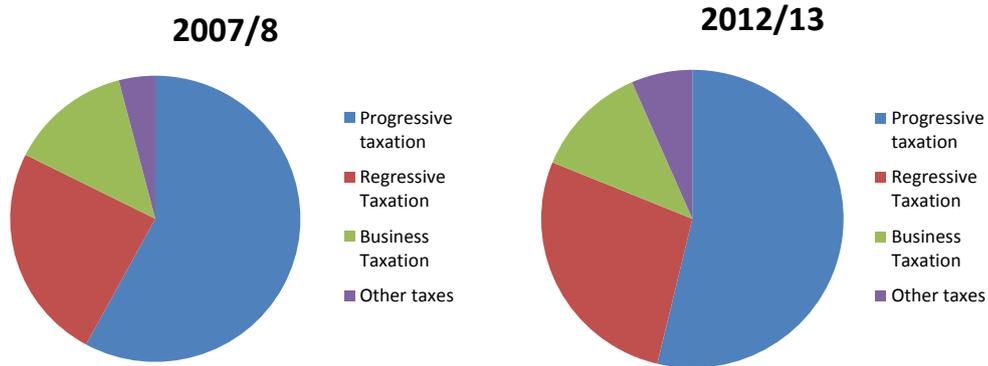
Background

- There are today a range of different forms of taxation. Some are widely considered to be 'regressive', such as Value Added Tax, in that they are levied on individuals at the same rate, irrespective of income or wealth.
- Other taxes are considered to 'progressive', such as income tax, in that the rates at which they are levied are variable, with more affluent individuals generally contributing a greater proportion of their income or wealth in tax.
- There are also a large range of taxes targeted at private enterprises rather than individuals, generally targeting company profits.
- Progressive taxation is a constitutive element of redistributive politics. That higher earners should pay proportionately more towards social goods that are either universally available, or targeted at the poor, has become a cornerstone of post-war welfare settlements.
- The UK has become a more unequal society in recent decades, meaning that we would, ostensibly, expect to see affluent groups contributing greater amounts through taxation.
- However, increasing inequality may in fact be explained by the withdrawal or softening of redistributive fiscal mechanisms.
- The Coalition Government have designed a number of tax changes in order to either restore growth or support deficit reduction. Each category of taxation has been significantly affected.
- For instance, the top-rate of income tax has been lowered to 45 per cent, the main rate of corporation tax has been incrementally lowered (it will be 20 per cent by April 2015), and VAT has been increased to 20 per cent.

Evidence

- This analysis defines as 'progressive' forms of taxation which either are levied variably according to income, or targeted on significant wealth transfers, namely income tax, National Insurance (which is paid by employers as well as employees), council tax, capital gains tax, stamp duty and inheritance tax.
- In 2012/13, progressive taxes contributed 54 per cent of total tax revenues. This is down from 58 per cent five years ago, just before the financial crisis.
- This analysis defines as 'regressive' taxes levied on individuals at the same rate, irrespective of income or wealth, namely VAT and the various additional or alternative duties levied on specific consumer goods.
- In 2012/13, regressive taxes contributed 28 per cent of total tax revenues, an increase from 25 per cent five years ago, just before the financial crisis.
- Taxes on businesses, namely corporation tax, business rates, and petroleum revenue tax, now contribute 12 per cent of tax revenues, down from 14 per cent five years ago.

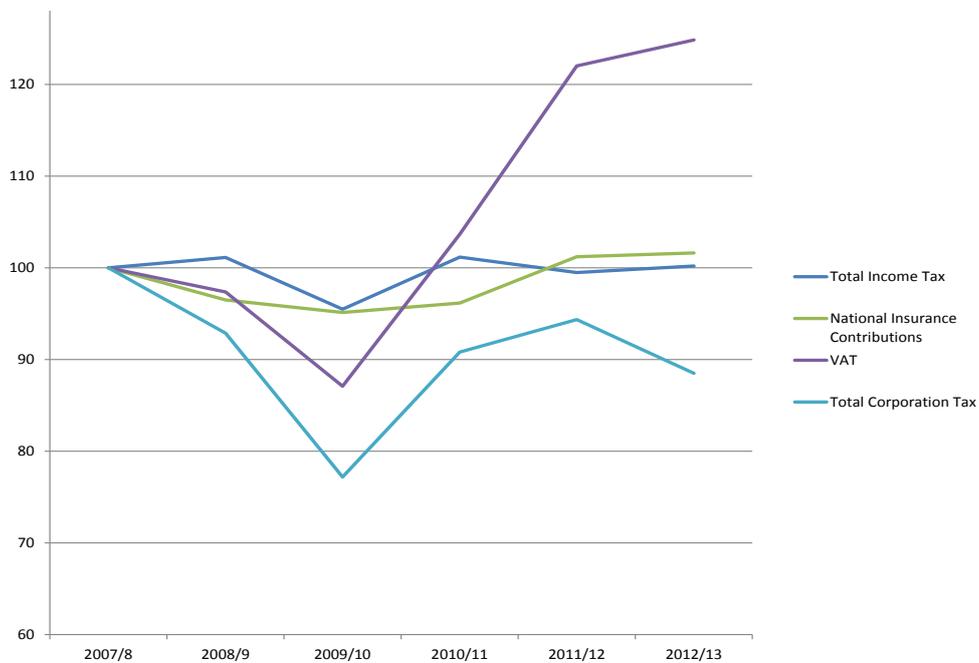
Charts 1a and 1b: UK tax base by type of taxation



Sources: see annex

- Of all the major forms of taxation (those accruing over £40 billion in the 2012/13 financial year), VAT has taken on an increasingly prominent role relative to 2007/8, not least due to a rise in the rate to 20 per cent, and the greater volume of goods it is levied upon. VAT revenue has risen from £80.6 billion (16 per cent of tax income) to £100.7 billion (18 per cent of tax income).
- The revenues from corporation tax, in contrast, have continued to contract. This is at least partly due to the incremental reduction in the main corporation tax rate, which will be 20 per cent by April 2015. The graph below indexes the revenue from these major taxes against its 2007/08 value to demonstrate this change.

Chart 2: Change in revenue from major taxes relative since financial crisis



Source: HMRC (2014)

It should be noted, however, that according to Office for Budget Responsibility (OBR), by 2017/18 the tax base will to some extent have reverted back to its pre-crisis progressive/regressive balance, albeit not entirely.

- However, this forecast is based on projections of strong earnings growth – previous OBR projections of earnings growth have proven overly optimistic.
- Furthermore, this reversion is not evident in relation to business taxation, which will continue to decline as a proportion of the UK tax base.

Table 3: UK tax base by type of taxation, including projection (summary) (%)

	2007/08	2012/13	2017/18 (projections)
Progressive Taxation	57.9	53.8	56.6
Regressive Taxation	25.4	28.4	26.7
Business Taxation	13.6	12.3	10.8
<i>Sources: see annex</i>			

Analysis

- It is clear that the UK tax base has become more regressive since the financial crisis.
- This transformation is forecast to reverse, to some extent, over the next few years. Yet even if this transpires, the evidence presented here demonstrates one of the main characteristics of how the UK state, especially under the stewardship of the coalition government, has sought to achieve deficit reduction in recent years.
- Indeed, the decline in the portion of revenue arising from business taxes in the UK tax base is set to continue, demonstrating one of the main features of the coalition's attempt to bring about economic recovery.
- Progressive taxation are making a smaller contribution to UK tax revenues than might otherwise be the case precisely because progressive taxes, principally income tax, have been made less progressive. It is also worth noting that the progressive nature of some ostensibly progressive taxes, such as council tax, is questionable.
- Similarly, business taxation is making a smaller contribution precisely because the main example of such taxes has been significantly cut.

Conclusion

The UK tax base has, to some extent, been transformed by the economic downturn and its aftermath, and reforms undertaken by the coalition government. Regressive taxes make up a higher proportion of tax revenues, and both progressive individual taxes and taxation targeted on private enterprises make up a lower proportion. Furthermore, revenue from business taxes is set to contract even further, even as economic growth returns, as proposed cuts are fully implemented. The shift towards regressive taxation is set to be reversed, to some extent, over the next few years. Yet even if this reversal is realised in practice, which is far from certain, this brief helps to demonstrate one of the main characteristics of how the UK state, and especially the coalition government, has sought to achieve deficit reduction since the financial crisis.

References

- HMRC (2014) HMRC Tax and NIC Receipts: January 2014, available at <http://www.hmrc.gov.uk/statistics/receipts/info-analysis.pdf>
- HM Treasury (2009) Budget 2009: Building Britain's Future, available at http://downloads.bbc.co.uk/news/nol/shared/bsp/hi/pdfs/22_04_09bud09_completereport_2591.pdf
- OBR (2014) Economic and Fiscal Outlook: March 2014, available at <http://cdn.budgetresponsibility.org.uk/37839-OBR-Cm-8820-accessible-web-v2.pdf>

Annex

Table A1: UK tax base by form and type of taxation, including projection

	2007/08		2012/13		2017/18 (Projection)	
	£bn	%	£bn	%	£bn	%
Progressive Taxation						
Income Tax	151.8	29.4	152.3	27.4	201.3	28.7
National Insurance	100.4	19.5	104.5	18.8	132.0	18.8
Stamp Duty	14.1	2.7	9.1	1.6	20.1	2.9
Council Tax	23.3	4.5	26.3	4.7	29.8	4.2
Capital Gains Tax	5.3	1.0	3.9	0.7	8.2	1.2
Inheritance Tax	3.9	0.8	3.1	0.6	5.4	0.8
Regressive Taxation						
VAT	80.6	15.6	100.7	18.1	123.3	17.6
Fuel Duties	24.9	4.8	26.6	4.8	29.1	4.1
Tobacco Duties	8.1	1.6	9.6	1.7	10.6	1.5
Spirits Duties	2.4	0.5	3.0	0.5	3.5	0.5
Wine Duties	2.6	0.5	3.5	0.6	5.0	0.7
Beer and Cider	3.3	0.6	3.6	0.6	3.7	0.5
Duties Air Passenger	2.0	0.4	2.8	0.5	3.6	0.5
Duties Vehicle Excise	5.4	1.0	6.0	1.1	5.6	0.8
Duties Insurance Premium Tax	2.3	0.4	3.0	0.5	3.4	0.5
Business Taxation						
Corporation Tax	46.9	9.1	40.4	7.3	44.5	6.3
Business Rate	21.4	4.2	26.3	4.7	30.8	4.4
Petroleum Revenue Tax	1.7	0.3	1.7	0.3	1.0	0.1
Other Taxes*	15.5	3.0	30.4	5.5	41.5	5.9
TOTAL	515.9		556.8		702.4	

*Includes income tax and corporation tax credits (which reduce income tax and corporation tax revenue)

Sources: HMT (2009); OBR (2014)



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