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Taking control: Which taxes could be devolved to English local government?

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Taking control: which taxes could be devolved to English local government?

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Preface

This report has been written as part of a major programme of research and analysis supported by IFS's Local Government Finance and Devolution Consortium. Consortium members include Capita, the Chartered Institute of Public Finance and Accountancy (CIPFA), PwC and the Economic and Social Research Council (ESRC). Support provided by the Municipal Journal, and a range of councils across England, including those represented by the Society of County Treasurers, is also gratefully acknowledged.

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Executive summary

In recent years, there has been renewed interest in the question of whether additional taxes should be devolved to English local government:

- The past decade has seen a number of changes to how local government is funded, including the introduction of business rates retention. Broadly, these changes have focused on giving councils more control over their funding and providing stronger financial incentives to councils to drive local growth and development. Devolution of additional tax revenues and powers could be seen as a natural extension of this agenda.
- After years of cuts, councils in England face serious short-term funding pressures. In the longer term the costs of funding social care are likely to increase faster than the revenues councils receive from council tax and business rates. While these issues could be addressed by using national taxation to increase the grant-funding given to councils, devolution of additional tax revenues and powers could also play a role.

This report: looks at the taxes currently devolved to local government in England and in other countries; sets out criteria which can be used to assess whether different taxes and tax powers are in fact suitable for devolution; applies these to a range of taxes; and looks at how much could be raised in different parts of England from different options.

Key policy messages

- **Of the large taxes we look at, income tax seems the most promising candidate for partial devolution.** Concerns about tax competition between councils and about volatility and inequality in revenues could be mitigated by restricting councils' powers to a flat-rate local income tax: a 3p tax on all income bands, for example, would raise £19bn. However, a local income tax would still involve some additional administration and compliance costs, and mean tackling a number of tricky technical issues.
- **Giving councils substantial new powers over council tax – such as the ability to revalue properties in their area – could pose problems for the redistribution of funding between councils.** In particular, it would make assessing the revenue raising capacity of different councils – a vital step in this process – much more difficult. **It is likely to be better to revalue and reform council tax at a national level:** this is overdue and could make the tax fairer and, if desired, raise more revenues.
- **There is currently significant interest in tourist taxes.** While such taxes would be administratively feasible and would raise useful amounts in a few well-visited areas, **they would raise little money in many more places.** The economic case for such a new tax is also far from clear cut.
- While tax devolution could give councils more options and discretion over how to raise funding, it is **not a panacea for their funding issues.** Ultimately, what's needed is either tax increases (whether at a local or national level) or lower expectations of what councils can provide.

1. Introduction

Local government finance in England is in the midst of a period of significant change. Alongside substantial cuts to the overall amount of funding available to English councils, there has been a move to make councils' funding more dependent on their own choices and local economic activity. Primarily, this is aimed at generating stronger financial incentives for councils to grow their tax bases and reduce local spending needs, although this also means increasing the risks of short-term volatility in funding and of longer-term divergences between funding and spending needs opening up.

100% retention of business rates was intended as the centrepiece of this shift – councils would be allowed to retain all real-terms growth in their business rates revenues, but would have to bear the cost of any real-terms falls (subject to a safety net to prevent excessive falls in funding). However, the legislation required to take forward key parts of this plan was not resurrected following the June 2017 general election and the government now intends to move the sector only to 75% retention (from April 2020).¹

Thus, in this report, we explore an alternative route by which the government could create greater financial incentives for councils – an expansion of the range of taxes from which councils are directly funded. For example, if councils kept a portion of the income tax revenue raised in their respective areas, there would clearly be an incentive for councils to promote growth in their income tax base. In this report, we discuss the pros and cons of expanding the range of taxes from which councils are directly funded, as well as examining the relative merits (and viability) of specific taxes as sources of local revenues.

In fact, the devolution of additional taxes is something that has been proposed numerous times in numerous ways by a sector that is keen to have more control over its own revenues. In November 2017, England's seven regional Mayors jointly called for greater control 'over existing taxes and the revenues they create',² whilst a number of cities have discussed the possibility of levying a 'tourism tax' on overnight stays in their areas,³ and Nottingham has even implemented a levy on employers who provide workplace parking.⁴ Furthermore, in many countries, a much wider suite of taxes is available to sub-national governments than in England, as is discussed further in Section 2.

Discussion of the merits of local taxation in general, and of possible candidate taxes in particular, forms the main body of this report but it is worth noting one possible political advantage of increased tax devolution. In a time of growing spending pressures for councils in England (adult social care costs, for example, are projected to grow

¹ This was announced in the Ministry of Housing, Communities and Local Government's Local Government Finance Settlement 2018-19: <https://www.gov.uk/government/speeches/provisional-local-government-finance-settlement-2018-to-2019-statement> (accessed at 1/2/2019).

² See press release at <https://www.london.gov.uk/press-releases/mayoral/mayors-unite-to-call-for-major-devolution-to-cities> (accessed at 1/2/2019).

³ For example, Bath and North East Somerset Council: <https://www.theguardian.com/uk-news/2018/jan/10/bath-revives-plan-to-impose-tourist-tax>; the Greater London Authority: <https://www.london.gov.uk/sites/default/files/tourism-levy-for-london-wp83.pdf>; Birmingham City Council: <https://www.birminghammail.co.uk/news/midlands-news/how-birmingham-pay-commonwealth-games-14003899>.

⁴ Nottingham City Council, Workplace Parking Levy: <http://www.nottinghamcity.gov.uk/transport-parking-and-streets/parking-and-permits/workplace-parking-levy/> (accessed at 1/2/2019).

considerably faster than councils' revenues from council tax and business rates), tax devolution might make increases in the overall national tax burden less politically painful – some tax rises would be the responsibility of councils rather than central government.

We further discuss the pros and cons of tax devolution in Section 3, where we also use this discussion to inform our choice of criteria for assessing the various taxes that could be used as a source of local revenues. In Section 4, we then assess possible options for extending councils' powers over council tax. In Section 5, we assess the stamp duty land tax as a candidate for devolution and we look at how the tax base varies around the country; in Sections 6, 7 and 8, we do so for corporation tax, VAT and income tax, respectively. We conclude in Section 9. In Appendix A, we discuss the possibility of a locally controlled tourism tax on overnight stays. Appendix B provides some additional empirical analysis of different taxes.

2. English and international contexts

Before examining possible taxes that could be devolved to English councils, in this section we describe the current suite of taxes over which councils have control. We then compare this to systems of local tax in a number of other advanced economies, many of which make use of a wider range of taxes for sub-national taxes than England.

2.1 Local tax devolution in England

Unlike Northern Ireland, Scotland and Wales, no taxes are devolved specifically to England. However, some tax powers are devolved by the UK government to English local government, mostly in relation to council tax and business rates. Revenues from council tax and a proportion of business rates are used alongside grant funding from central government and income from sales, fees and charges to fund local government services and investments.

Council tax

It is important to note that the amount of grant funding given to each local authority (or council) takes into account the revenues they can raise themselves from council tax.⁵ So councils with lots of expensive houses in high tax bands do not benefit in full from this (their grant funding is lower) while those with lots of cheap houses in low council tax bands are compensated for this (their grant funding is higher).

Councils do retain the additional revenue they collect if they increase their council tax rates, and bear the costs if they reduce their council tax rates. This allows for some discretion over their overall budgets. There are, however, two limits placed on councils' rate-setting powers:

- Council tax is charged according to which of eight valuation bands (A to H) a property is assessed to be in. Whilst councils set the overall level of council tax charged, the ratios between the charges applied to different bands is centrally fixed: for example, the charge on a property in Band H must be twice that on a property in Band D and three times that on a property in Band A. The allocation of properties to bands (i.e. the valuation of properties) is also determined by central government (and, remarkably, is still based on estimates of property values as of 1991).
- The government has at times used capping powers to prevent councils from increasing their council tax rates by more than a certain percentage. Since 2012–13, councils have had to hold a referendum if they wish to increase council tax by more than a set percentage: for example, more than 3% for councils without adult social care responsibilities, and more than 6% for councils with adult social care responsibilities in 2018–19. In 2019–20 these limits will be set at 3% and 5% respectively.

⁵ Historically, this was done by estimating how much council tax each council would raise if it set its council tax rate at some centrally determined rate. Since 2016–17, it has been done based on how much council tax each council raised given its actual council tax rate in 2015–16.

Central government has also mandated several discounts and exemptions that councils must grant to taxpayers, including a 25% discount for households containing only a single adult eligible to pay for council tax and an exemption for households containing only students. These act to reduce the size of councils' tax bases and hence council tax revenues and they benefit defined groups of households that might differ from the groups that councils would themselves choose to help.

Councils do have some powers over tax rules and the tax base. For example, they are able to give furnished second homes or holiday homes a discount of up to 50%, and are also able to give a discount to empty properties at their own discretion. Since 2013–14, councils in England have also been responsible for designing their own Council Tax Reduction Schemes for working-age households with low incomes. Councils can thus affect the size of their tax base by adjusting the generosity of their reduction scheme.

Business rates

Since 2013–14 and the introduction of the business rates retention scheme (BRRS), councils' funding has also depended partly on the business rates revenues raised in their areas. The scheme is calibrated such that councils' own business rates revenues only affect their funding to the extent that they experience real-terms change in those revenues. Those that do so retain up to 50% of the real-terms change, although all councils are protected against excessive falls in funding resulting from real-terms falls in their business rates revenues (a 'safety net').⁶ The aim of this approach is to provide incentives to councils to support economic growth (and particularly development of new commercial property): they see their budgets increase if their business revenues increase. At the same time, the scheme continues to redistribute the existing stock of business rates revenues according to the needs of different councils, thus supporting poorer parts of England.

Separately from the BRRS, councils have some control over business rates policy and revenues in their areas:

- They may grant discretionary reliefs to narrow or broad groups of ratepayers, reducing their business rates bills by up to 100%. As with all tax policies, they must comply with European Union (EU) state aid rules (which, for example, means that reliefs targeted at particular firms are not allowed). In practice, this power has been used relatively little: discretionary reliefs amounted to just 0.4% of the gross business rates yield in 2017–18, compared with 9.3% for mandatory reliefs.
- They may levy a 'business rate supplement' of up to 2p in the £1 of rateable value, which must be approved by a majority of ratepayers.⁷ Any revenue raised must be spent on economic development. In practice, this power has only been used once – to help fund the development of Crossrail in London.
- Similarly, mayors of combined authorities (mostly covering major urban areas such as Greater Manchester, Merseyside and the West Midlands, but also Cambridgeshire and Peterborough) have the ability to levy a 2p supplement to

⁶ The government plans to increase retention from 50% to 75% from 2020–21 (and in some areas has already piloted 100% retention).

⁷ Defined both in numerical and rateable value terms.

fund new infrastructure projects, subject to agreement from the business representatives of Local Enterprise Partnerships.

The government also mandates a number of business rates reliefs that must be granted, including reductions in bills for properties occupied by registered charities, small businesses, and also retailers, restaurants/cafes and pubs where the properties have a rateable value of less than £51,000.

2.2 Locally raised revenues as a share of spending

Although this system clearly implies fairly limited local discretion to vary tax bases and rates, it is worth also considering how revenues from local taxation compare to local government's expenditure responsibilities.

At first glance, it appears that a large proportion of local government's overall expenditure is financed by grants from central government, rather than from local taxes. All-in-all, the Office for Budget Responsibility (OBR) estimates that local government spending in England amounted to around £131 billion in 2017–18. By comparison, council tax revenues totalled around £28 billion, or 21% of that total, whilst retained business rates totalled around £15 billion, or 11% of that total.⁸

However, much of the £131 billion of expenditure referenced above is not under the direct control of councils. This includes: housing benefit, which councils administer but for which councils have no control over policy; policing responsibilities, which are carried out by separate local and regional police authorities; and fire services, which are provided by separate fire authorities in many areas. Furthermore, councils' schools expenditure is directly funded by the Dedicated Schools Grant, which is ring-fenced for schools. Grants to pay for public health services are likewise ring-fenced.

If these ring-fenced funding-streams are stripped out, council tax revenues amount to not 21% of councils' expenditure, but 52%.⁹ When retained business rates revenue is also taken into account, the proportion of spending under significant local control that is funded by local tax revenues amounts to 84%.

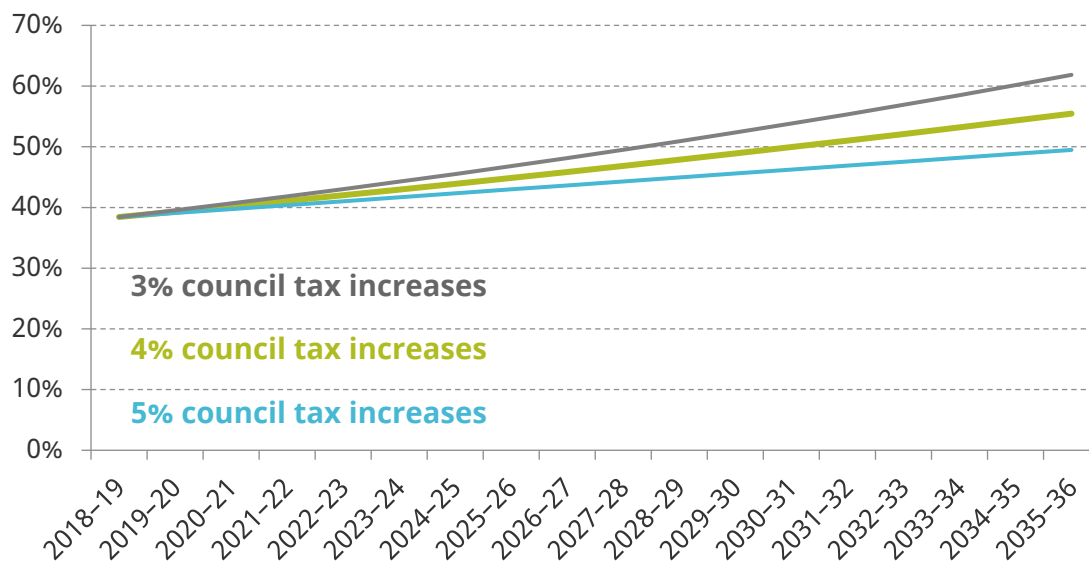
On this measure, councils are thus responsible for raising a clear majority of their 'core spending power'. However, revenues from council tax and business rates are unlikely to keep pace with rising costs and demands for services in the future. Figure 2.1 shows projections of the percentage of councils' revenues from council tax and 75% of business

⁸ Figures taken from Office for Budget Responsibility (2018), 'October 2018 Economic and Fiscal Outlook – supplementary fiscal tables: expenditure', available at <https://obr.uk/efo/economic-fiscal-outlook-october-2018/>.

⁹ Authors' calculations using Ministry of Housing, Communities and Local Government (2018), 'Local authority revenue expenditure and financing England: 2017 to 2018 final outturn', available at <https://www.gov.uk/government/statistics/local-authority-revenue-expenditure-and-financing-england-2017-to-2018-final-outturn>.

rates¹⁰ that would have to be spent on adult social care services alone to meet future cost pressures, under various scenarios for council tax increases.

Figure 2.1. Projections of the percentage of council tax and business rates revenues needed to meet rising demands and costs of adult social care



Source: Authors' projections using estimated council tax and retained business rates revenues from the local authority revenue account budgets (2018-19), and projections for social care spending pressures reported in Johnson et al. (2018).

For example, even if council tax bills are increased by 4% a year, every year, adult social care spending could increase from 38% to 45% of these revenues by the mid-2020s and 55% by the mid-2030s. This would imply that the real-terms local tax revenues available to other important services – such as public health, children's social services and housing – would not increase at all during the 2020s and would be *falling* in the 2030s.

It therefore seems highly likely that either funding from central government grants will have to be increased (at a time when central government will also face rising costs, such as for healthcare and pensions), or new sources of locally raised revenues will have to be found, such as devolved taxes.

2.3 Devolved taxes in other countries

Furthermore, the current tax base of councils, limited as it is to property, is relatively narrow. This is especially apparent in comparison with the taxes devolved to local and regional governments (such as regional or state governments) in other countries.

In some cases, taxes are devolved such that sub-national governments have direct ability to affect the revenues they receive – through changing tax rates or the tax base. In other cases, sub-national governments are instead assigned a portion of the revenues raised in

¹⁰ The figure shows 75% of business rates revenues because the government plans to introduce 75% retention from 2020-21. Regardless, the focus of this graph is the *change* in the percentage over time, rather than the actual level.

their area from a given tax. Although they are not able to affect these revenues directly, this may still provide sub-national governments with an incentive to pursue policies that will cause revenues to increase. For example, being assigned a share of corporation tax raised in their area could encourage sub-national governments to pursue policies that will boost business profitability, or attract more businesses to their area. With this in mind, we discuss below some of the taxes that are commonly devolved to sub-national governments in other countries.

Property taxes

Of course, as in England, in most countries property taxes come under the purview of sub-national governments – they collect the revenues, and also tend to set the rates. In countries with two tiers of sub-national governments, property taxes are mostly devolved to the lowest level of government, although in Germany and Belgium regional tiers also have the right to tax properties.

As described above, there are limits to English councils' ability to set council tax rates, and this is not unusual among other countries. For example, in a number of countries, such as Denmark and Finland, property tax rates must fall between centrally mandated minimums and maximums. It is also common to find that, as in England, although local government sets the rates for property taxes, it does not have primary control over the property tax base (such is the case in France).

Income taxes

Local income taxes are less common. As will be discussed later, this is perhaps unsurprising given their pro-cyclicality and the mobility of high-income taxpayers (which could lead to tax competition and a race to the bottom).

Where local income taxes do exist, they tend to take the form of a flat-rate tax – progressive taxation is carried out at a national level. For example, in Sweden, Finland and Denmark, sub-national income taxes, levied at a flat rate, constitute a substantial proportion of total income tax revenues, but progressive taxation is only part of the national income taxes.¹¹ There are also countries where sub-national levels of government levy discretionary surcharges to the national income tax that make up a relatively small proportion of total income tax revenues, such as Italy and Belgium.¹²

There are very few countries where sub-national income taxes are themselves progressive, and these tend to be countries with a federal structure (e.g. Switzerland, Canada and the United States). Spain, which is, strictly speaking, not a federation, has allowed its regions to employ progressive taxes on 50% of their tax bases since 2011.

However, both of the above categories are in the minority – in few countries are sub-national governments given power over income tax. What is more common is the sharing of income tax revenues with sub-national levels of government. In a large number of European countries, sub-national governments are allowed to retain a proportion of

¹¹ In Sweden, all three tiers of local government are able to levy their own local income taxes, with the largest share of those revenues going to the lowest tier of government. In Denmark, local income taxes are levied at the lowest level of government (i.e. the municipalities), and not by the regions. Finland has only one sub-national tier of government, which is municipal.

income tax revenues raised in their areas whilst having no control over the tax rates or tax bases. One example of this is Germany, where both the Lander and municipalities are assigned a portion of income tax revenues.

Sales tax/value added tax

In the United States, states, counties, cities and various other local authorities (such as school boards) are able to levy and retain revenues from sales taxes, whilst in Canada the provinces are able to charge a discretionary surcharge on the national value added tax (VAT), which can be in the form of a sales tax or an additional VAT.

In Europe, EU rules prevent variation in VAT rates within a country. Instead, many European countries provide for the sharing of VAT revenues between national and sub-national governments. This means that sub-national governments retain a portion of VAT revenues raised in their area, but cannot directly change either the tax rate or the definition of the tax base. This is the case, for example, in Italy, Portugal and Spain.¹³

Corporation tax

Sub-national discretion over corporation tax or business taxes is not as rare in Europe as discretion over VAT. For example, municipalities in Germany set the rate and receive the revenues from the 'trade tax', which is charged on business profits. It is of a similar size to the national corporation tax, although the tax base is slightly different. Italian regions levy a tax 'on productive activities' (IRAP), although there are fairly restrictive limits placed on how high or low this tax can be, and it is small relative to the national corporation tax. Elsewhere, Canadian provinces are also able to levy substantial corporation tax rates that are almost as large as the federal rate.

As with other taxes, there are a number of countries where corporation tax revenues are shared with sub-national governments, but sub-national governments do not have any control over the tax rate or the scope of the tax base. In Denmark, municipalities receive a fraction of the corporate income tax paid by companies in their jurisdiction, and similar systems are in place in, for example, Finland and Portugal.¹⁴

Other small taxes

In many countries, sub-national governments levy tourism taxes – particularly in certain cities. For example, in Rome there is a small city tax levied per person per night, German cities are able to charge up to 5% of the room rate, and Dutch municipalities can charge up to 6% of the room rate. In fact, the UK is one of only nine countries from the EU-28 that does not charge a tourist accommodation tax as of 2018.

Inheritance tax is also employed as a source of local revenues in some countries. In Belgium, regions have control over inheritance tax, both in terms of the rates and the base, and they collect and retain the revenues from it. The lowest tier of local government in Poland is also able to levy its own inheritance tax, as are regions in Spain, although their control over the tax base is more limited. Assignment of inheritance tax is also a feature of

¹³ In Italy, VAT revenues are assigned to regions, the highest level of sub-national government. VAT in Portugal is assigned to the single level of sub-national government, which is made up of municipalities and two autonomous regions covering the islands of Azores and Madeira. In Spain, VAT is assigned to the CCAA (the highest, regional level of sub-national government).

¹⁴ Both Finland and Portugal have only one tier of sub-national government.

some systems – for example, in Germany the Lander receive the revenues from a nationally defined inheritance tax.

Various taxes on vehicles are also a feature of sub-national government taxation in a number of countries, including Belgium (at the regional level), Germany (where they are apportioned to sub-national governments) and Spain (the highest tier of sub-national government has some control over the tax rate on the registration of vehicles) to name but a few. However, it is worth noting that all three of these taxes, although relatively prevalent in systems of local finance, tend to represent relatively small shares of total local government finance.

Table 2.1 summarises the above examples.

Table 2.1. Examples of local taxation in other countries

	Devolved	Assigned
Income tax	Sweden (regional and local), Finland (local), Denmark (local). Progressive taxes levied in Canada (regional), United States (regional and local), Spain (regional)	Germany (regional and local)
Sales tax/VAT	United States (regional and local – sales taxes); Canada (regional – VAT)	Belgium (regional), Italy (regional), Portugal (regional), Spain (regional), Germany (regional and local)
Corporation tax	Germany (local – ‘trade tax’), Canada (regional), Italy (regions)	Denmark (local), Finland (local), Portugal (local)
Tourism tax	Italy (local), Germany (local), Netherlands (local)	
Inheritance tax	Poland (local), Spain (regional)	Germany (regional)
Vehicle taxes	Belgium (regional), Spain (regional)	Germany (regional)

Notes: This table provides examples of where different taxes are devolved or assigned to sub-national government but it is not exhaustive in its coverage. The terms regional and local are used here to differentiate between upper and lower tiers of sub-national government – with reference to Canada and the United States, for example, regional refers to provinces/territories and states, and local refers to counties, cities and other local authorities. Not all US states charge income tax, and not all of those that do charge it progressively. Finland and Portugal only have one-tier of elected sub-national government.

Sources: European Commission (2012), Nicol (2014), COSLA (2018) and PWC (2019).

3. The advantages, disadvantages and criteria for tax devolution

In this section, we discuss the criteria by which the appropriateness of different taxes for devolution can be assessed. First though, we discuss some of the commonly cited arguments for and against tax devolution put forward by economists and political scientists.

3.1 Advantages and disadvantages of tax devolution

Advantages

The so-called ‘fiscal federalism’ literature has identified a range of potential benefits of tax devolution, although these often involve trade-offs against other objectives:

- **Provision of incentives for local government.** Allowing local government to retain local tax revenues can create positive financial incentives for councils: they directly benefit from growing the devolved tax base, and in many cases, though not all, such growth is likely to go hand in hand with broader economic growth. Although it is difficult to conclusively identify this effect in practice, a series of analyses by the OECD has found empirical evidence to suggest that, for example, countries where sub-national governments rely more on grants (and less on own-tax revenues) have lower GDP per capita, lower human capital and lower public sector investment spending.¹⁵ In addition, a literature review and meta-study by Baskaran, Feld and Schnellenbach (2016) finds that, in general, tax devolution is associated with faster economic growth, although estimates are sensitive to the way the degree of tax devolution is measured and to the study methodology.

However, **the flipside of stronger incentives for local government is that tax devolution can also expose councils to greater funding risk.** A reliance on tax revenues for funding means that volatility and variation in those revenues will directly affect councils’ ability to provide the services for which they are responsible: areas with small tax bases or areas that have seen big falls in their tax bases may struggle to fund the range and quality of services provided by rich and/or growing areas.

- Both the strength of financial incentives and the degree of risk for short-term volatility and long-term divergences in revenues will depend on what, if any, revenue equalisation arrangements are put in place. Systems that redistribute more to compensate for differences in revenues – and, more particularly, differences in *changes* in revenues – will provide greater insurance against risk, but will also weaken incentives for councils to grow local tax bases.¹⁶
- **More efficient expression of local preferences and greater local accountability.** Tax devolution can allow local and regional governments more

¹⁵ In particular, see Blöchliger (2013), Blöchliger and Égert (2013) and Fredriksen (2013).

¹⁶ This issue is discussed more in Amin-Smith, Phillips and Simpson (2018) and in Ministry of Housing, Communities and Local Government (2018a).

control over the particular balance between taxation and spending in their area. Thus, differences in preferences between the populations of different areas can be expressed through varying levels and distributions of taxation (and hence also spending). It can also mean that where councils have better information about the appropriate level of taxation and spending in their area than the central government, they have the means to put this information to use.

- It has also been argued by some economists that for local governments to have meaningful fiscal control, they in fact need only to be able to significantly affect their revenues at the margin.¹⁷ The key word here is ‘significantly’. As previous IFS research has noted (Ridge and Smith, 1991), if local taxes cover only a small proportion of the costs of local spending overall, there will be a ‘gearing’ effect. In such a scenario, although local taxes may be required to cover all of the costs of increasing local expenditure at the margin, a given percentage increase in local expenditure will require a much higher percentage increase in local tax revenue. This may have negative implications for accountability – it could make it harder for local voters to use comparisons between areas as a way of judging if their local council is making good use of the tax. If local taxes cover only a small proportion of the costs of local spending overall, this would also increase the importance of central grant funding to local governments, potentially exacerbating lobbying pressures and the politicisation of the grant allocation process.

Disadvantages

The literature has also identified a range of potential drawbacks to tax devolution:

- **Economic distortions and the potential downwards and upwards pressure on tax rates.** While the incentives to promote tax base growth provided by tax devolution can be beneficial, they can also be distortionary. In particular, councils may not take account of the impact of their policies (including tax policies) on the tax bases of other councils. This is important because part of any increase in a council’s tax base following a policy that makes the area more attractive to taxpayers may reflect a movement in activity away from other council areas – thus implying a corresponding reduction in the tax bases of those other areas. Councils may, to some extent, be able to increase their tax bases only at the expense of tax bases in other areas.

Such fiscal externalities are likely to be greater for taxes that have mobile tax bases; that is, where taxpayers can relatively easily change their location or activities to shift tax bases between different areas to take advantage of differences in tax and other policies. It can lead to downward pressure on tax rates and revenues as local policymakers compete for mobile tax bases by cutting tax rates.¹⁸

As with the more beneficial incentives discussed above, the strength of the incentive to compete over tax bases will depend on fiscal equalisation arrangements. In particular, councils will have more incentive to engage in tax competition when systems are less redistributive: less of any increase in local tax

¹⁷ McClure (1999).

¹⁸ See, for example, Ter-Minassian (1997).

bases following competitive tax rate reductions will be offset by reductions in equalisation grants or transfers.¹⁹

It is also worth noting that the partial devolution of taxes to local government could increase the likelihood of tax increases. This can happen when local areas keep all mechanical increases of revenues as a result of a tax rate increase, but do not bear all of the behavioural costs associated with a reduction in the size of the tax base if that tax base is shared with the national government.

On a more practical level, the fact that tax devolution would allow the political pain of increasing tax rates to be shared between local and national politicians (rather than falling on national politicians only) might be seen as beneficial in the context of the rising spending pressures discussed in Section 2.2.

- **Administrative challenges.** In many cases, there are likely to be economies of scale in centralised tax administration that devolution to a local level would mean foregoing – in other words, it may be more costly overall to administer such taxes locally than centrally.²⁰ Even where administration would continue to be carried out centrally, variation in tax rates and rules across areas would increase administration and compliance costs to some extent. Moreover, there are some taxes for which it would be conceptually and technically difficult to apportion tax bases and revenues between areas. This is particularly true for taxes where taxpayers' operations span multiple local areas, and their tax liabilities are not necessarily linked to specific geographic areas.
- **Transparency and complexity.** A tax system where a range of taxes are devolved and where different levels of government share the same tax bases can mean less transparency in the system overall. This could limit voters' ability to understand the structure of government and how they can exert control over it.²¹

3.2 Criteria for assessing candidates for devolution

The advantages and disadvantages of tax devolution naturally suggest criteria by which the appropriateness of different taxes for devolution can be assessed. The following criteria provide the framework by which we evaluate the various candidate taxes in the rest of this report.

- **Would devolution be administratively sensible?** The administrative feasibility of apportioning tax bases between local areas differs significantly between taxes and can be a first-order issue in deciding whether to devolve a tax.
- **What incentives would the tax create for local government?** Whilst the provision of positive incentives can be a consequence of local tax devolution, the exact incentives that are created will differ according to the tax being considered.

¹⁹ Thus, decisions over equalisation systems involve balancing the provision of beneficial incentives on the one hand, and the limiting of fiscal externalities, volatility and divergences on the other.

²⁰ For example, there are likely to be substantial economies of scale in collection and enforcement for certain taxes. See Vehorn and Ahmad (1997).

²¹ Further discussion is available in Darby, Muscatelli and Roy (2002).

Devolution of some taxes may even lead to undesirable incentives – for example, the incentive to engage in policies (including cuts to tax rates) that primarily shift tax bases from other councils, rather than increase overall tax bases.

- **How economically efficient would devolution be?** Economic efficiency is always a consideration in evaluating a given form of taxation, but there are two specific concerns that arise in the case of local taxes.
- The first reflects the argument laid out above that local tax devolution can allow for the fuller expression of local preferences and increase democratic accountability. In order for this to be true, **local taxes should be paid by those who can vote in a local area**, and vice versa. Consider, for example, a situation where a substantial proportion of the incidence of a given tax falls on non-residents, and therefore non-voters, in a particular local authority. This could lead to excessive levels of taxation, as the voters in that area would be able to choose higher spending whilst only bearing a proportion of the additional cost. Such an issue is more likely to be a problem with some taxes than with others.
- The second efficiency consideration that arises in the case of local taxation is that local taxes may distort behaviour in the context of mobility of the tax base – **so that taxes with less mobile tax bases are likely to be more suitable candidates for devolution**. Differences in tax rates between areas could affect households' decisions about where to live and firms' decisions about where to locate their business. If councils are given discretion over the rates of taxes on mobile tax bases, this mobility could limit councils' power to affect their own revenues. For example, a council wishing to raise more revenues might increase the rate of a certain tax, and see part of the relevant tax base (e.g. high-income households) move to a neighbouring area with lower rates. This would reduce the size of the council's tax base, and could even negate the effect on revenues of the initial rate hike. Relatedly, a council faced with a mobile tax base may cut tax rates in order to attract households and businesses, and this could lead to tax competition – one of the dangers of further tax devolution described above.
- **How evenly distributed is the tax base?** Devolving a tax with an unevenly distributed tax base could mean areas having different amounts of funding available, and thus being able to provide different levels of service or having to charge different tax rates to avoid this. Of course, as discussed above, revenue equalisation arrangements can be used to redistribute tax revenues from those areas with large tax bases to those with small tax bases. However, such arrangements would affect councils' incentives to grow local tax bases. Also, complex equalisation arrangements could make the system as a whole less transparent and accountable and could increase the prevalence of political lobbying. **Thus taxes where tax bases are more evenly distributed will tend to be better candidates for devolution, all else equal.**
- **How stable are revenues?** The risks to councils' funding implied by greater tax devolution will depend on how stable the revenues that individual authorities receive from a given tax are – revenue streams that are very volatile would make it difficult to ensure consistent levels of service provision. However, the requirement that local tax bases should be relatively stable has a tendency to come into conflict

with another potentially desirable feature – that revenues respond to local economic conditions. If the revenues from a given tax do not respond to local conditions, devolution of that tax will provide less strong incentives for councils to grow their local economies. Furthermore, the revenues from such a tax may, over time, decrease in size relative to the economy. This could become a particularly problematic feature in England, where social care pressures are likely to place increasing strain on council budgets over the coming decades. **Stability therefore has to be traded off against buoyancy.**

4. Further council tax and business rates powers

As discussed in Section 2, council tax and business rates are the only significant taxes over which local government in England currently has a degree of control. However, that control is limited, with important constraints on local powers over tax rates and bases. Therefore, one option for tax devolution would be to expand local powers over council tax and business rates.

In this section, first we describe how these two sources of revenues are distributed across the country, before looking at the advantages and disadvantages of various expansions to councils' powers over these taxes.

4.1 How are council tax and business rates revenues distributed?

The £28 billion of council tax and £15 billion of business rates revenues that are retained by councils are not raised equally around England. To some extent, this reflects differences in the council tax rates set by different councils, and different arrangements for the share of business rates retained locally in different parts of the country.²² However, it also reflects differences in the size of local tax bases – or, in other words, the amount that would be raised if the same tax rates and arrangements were applied in every part of the country.

Figure 4.1 shows the council tax base per person of each upper-tier council area,²³ based on the revenues they would obtain if they each set their council tax rate at the national average. Variation mainly reflects differences in the proportion of properties in each tax band in different councils, but it also reflects different impacts of mandatory discounts or exemptions (such as for single adults or students).

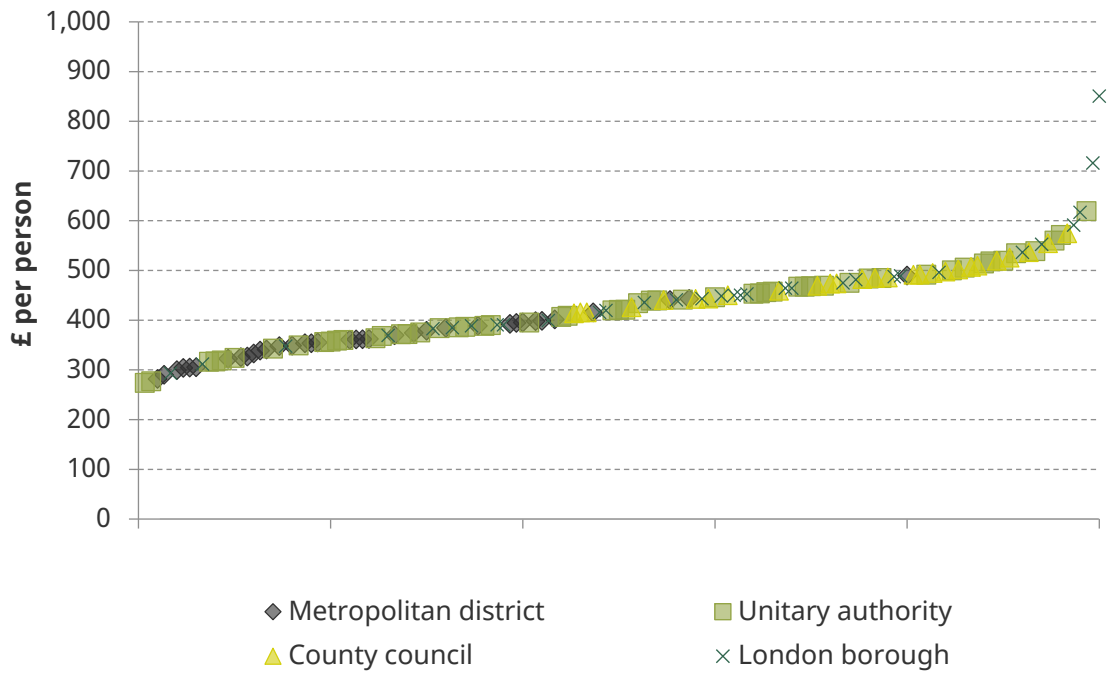
In 2018–19, the area with the largest council tax base per person, Kensington and Chelsea, had a base more than three times larger than the area with the smallest council tax base, Nottingham. 10% of councils would have raised more than £520 per person if they had charged the average rate in 2018–19, whilst the 10% of councils with the smallest tax bases per person would all have raised less than £325 per person.

Figure 4.2 shows that business rates tax bases are even more unevenly distributed than council tax bases. The tax base per person for Westminster (which is so high that the scale in the figure does not allow it to be shown) was 46 times greater than that of the council with the lowest tax base per person, Redbridge. More generally, 10% of councils had a tax base per person of more than £590 per person, whilst in the 10% of councils with the smallest tax bases, it amounted to less than £250 per person.

²² Amin-Smith, Phillips and Simpson (2018) provide further information on this.

²³ By upper-tier councils we mean counties, unitary authorities, metropolitan districts and London boroughs.

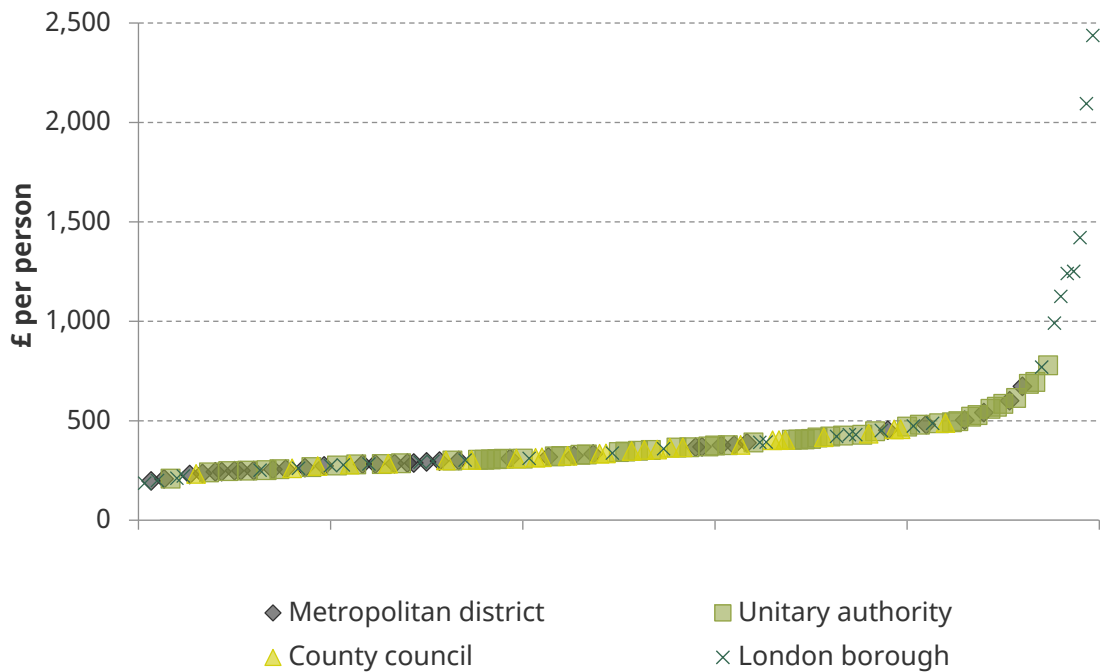
Figure 4.1. Council tax base per person at average rates, 2018-19, by council and council type



Notes: The average council tax rate used for this calculation excludes council tax levied by the Greater London Authority and other Combined Authorities, Police Authorities and Fire Authorities.

Source: Authors' calculations using Chartered Institute of Public Finance and Accountancy (2018) and ONS (2018a).

Figure 4.2. Business rates revenues per person, 2018-19, by council and council type



Notes: Westminster and the City of London are excluded for scaling purposes.

Source: Authors' calculations using Department for Communities and Local Government (2018) and ONS (2018a).

As discussed in Section 2.1, to address the large disparities in local tax bases, the local government finance system includes equalisation grants and transfers between councils (tariffs and top-ups). The future calculation and frequency of updating of these equalisation measures is a key part of ongoing policy reviews by the Ministry of Housing Communities and Local Government. While final decisions on this will not be made until the autumn of 2019, it seems likely that reforms will increase the extent to which councils gain or lose as local tax bases change (particularly in the longer term).²⁴

4.2 Would further powers over council tax and business rates be suitable for devolution?

Looking beyond the finance system changes being examined in existing policy reviews, there are a number of potential ways to extend councils' powers over council tax and business rates.

- (i) **Additional powers over headline tax rates.** As discussed in Section 2.1, local referendums are required if councils wish to increase council tax by more than centrally determined limits, and business rates increases are capped at inflation. The main rationale for these limits relates to the accountability of councils to taxpayers.

The council tax referendum requirement means that direct authorisation from local residents (most of whom will be council taxpayers) is required for large council tax increases. In that way, it does increase accountability over tax decisions. But such an approach is unusual: decisions over tax rates by the UK government (or devolved and local governments elsewhere in the UK) are not subject to referendum. Instead, accountability to residents operates through elections where candidates set out manifestos or plans, and voters decide how to vote on a range of issues including tax. The governments elected may not always stick to their stated plans, but this could be punished at the next election if voters so choose. It is not clear why council tax is considered a special case where accountability via regular elections is deemed insufficient.

Business rates are somewhat different. Unlike council tax, where those on whom the tax is formally incident can all vote in local elections, the owners or occupiers of properties subject to business rates often will not be able to: they may live in a different area. This means reliance on regular local elections could be seen to provide insufficient accountability to taxpayers. Indeed, this was one of the arguments for moving to a system of centrally determined business rates in 1990: ²⁵ a large majority of owners and occupiers would be living somewhere in the country (rather than overseas) and could vote in national elections.

As highlighted in Section 2.1, councils do have powers to levy small increases in business rates to fund increases in expenditure on economic development,

²⁴ Ministry of Housing, Communities and Local Government (2018a, 2018b).

²⁵ See Ridge and Smith (1990) for a discussion of this rationale. The rationale for capping increases in the business rates tax rate (called the 'multiplier') at inflation is less clear.

subject to referendums of business rates taxpayers. One option to increase local flexibility while retaining accountability would be to loosen or remove the cap on these increases, and give councils more flexibility on how resulting revenues are spent.

- (ii) **Additional powers over reliefs, discounts and exemptions.** While councils have broad powers to offer discretionary reliefs for business rates, they have less power to do this for council tax. Furthermore, a number of reliefs, discounts and exemptions are mandated by central government.

Giving councils more control over reliefs, discounts and exemptions would involve some additional administration and compliance costs, but would be administratively feasible, given councils currently administer both taxes. It would allow for greater realisation of local preferences and also allow councils to use taxes to target specific policy goals more closely. This could involve reforming or removing existing mandatory policies (e.g. if it were felt that the benefits did not exceed the revenue foregone) and the introduction of new discounts.

However, if councils were given such powers, it would be important to ensure that the equalisation system was based on assessments of local tax bases stripping out the effect of individual council's decisions. If they did not, then councils would have a strong incentive to offer extensive reliefs, safe in the knowledge that any subsequent reduction in their tax bases would be largely compensated for by equalisation arrangements. Instead, central government would need to decide on reference tax system – which may or may not include any reliefs, discounts and exemptions – on which equalisation would be based.

- (iii) **Power to change council tax relativities.** This would enable the council tax structures of councils to more closely reflect local preferences for redistribution, and would provide an additional way in which overall revenues could be increased or decreased other than by changing the headline tax rate. For example, a council could choose to make their local system more progressive by increasing the ratio between tax payments for high-band and low-band properties (the current maximum ratio is 3:1). The Scottish Government, for instance, increased tax rates on Band E to H properties in Scotland such that the maximum ratio increased to approximately 3.65:1 in April 2017.²⁶ We estimate that such a reform, if carried out in England, would have raised around £1.0 billion in additional revenues for English councils in 2018–19.

As with reliefs, discounts and exemptions, it would be important that the equalisation system was based on a fixed 'reference' set of relativities rather than each council's actual relativities. The decision on what the fixed relativities were would have big implications for the funding received by different councils, given significant differences in the proportions of properties in different bands across England.

²⁶ This increased band relativities on Bands E to H from 122%, 144%, 167%, and 200% of the Band D tax rate to 131%, 163%, 196%, and 245%, respectively.

For example, the use of existing relativities would mean that if councils used the powers to increase progressivity and revenues, most of those revenues would remain in areas with lots of high-band properties. However, using a more progressive reference set of relativities would redistribute such revenue increases towards areas with lots of low-band properties, compensating for the limited additional revenues they could raise themselves.

- (iv) **Powers to revalue properties in their area.** As it stands, property revaluation is the responsibility of central government – which, for council tax, it has failed to exercise in over 25 years. It has been suggested that devolving powers over revaluation could make it more likely to happen – which would mean council tax reflected up-to-date relative property values, rather than property values in 1991.²⁷

However, local revaluation would pose significant problems for equalisation arrangements between councils. Comparison of tax bases between councils that had and had not revalued (or had revalued at different times) would become a much more complex task.

For example, if one wanted to use the updated values to calculate the tax base for those areas that had revalued, one would have to decide what tax rate to use in such calculations. Would the tax rate that would be revenue neutral at a national level be used? In that case, a national revaluation would need to underlie every local revaluation, which would add significantly to costs. Moreover, such an approach would mean perverse incentives. Those councils where values had increased by more than the average would see their taxpayers pay more, on average, yet would receive no additional funding after accounting for equalisation (or alternatively could set lower tax rates to stop average bills increasing, but have lower funding than before revaluation). Revaluation would therefore be unattractive. In contrast, those councils where values had increased by less than the average could see average bills fall or funding rise as a result of revaluation, making it a very attractive proposition.

To avoid such distortions, one would have to keep using the tax base as measured according to the last national revaluation – in 1991. This would mean that new properties built in areas that had carried out revaluations would have to be valued twice: once according to the updated valuations for taxation purposes; and a second time according to 1991 values for equalisation purposes. This would add to administration costs and complexities, especially if different councils revalued at different times.

Moreover, equalisation arrangements would be based on a tax base measure that increasingly deviated from councils' actual capacity to raise council tax revenues. This would mean relatively more funding would flow to areas seeing increases in relative house prices, and less to areas seeing falls in relative house prices, which could contribute to geographical inequalities.

²⁷ See, for example, Independent Commission on Local Government Finance (2015).

Summary

Therefore, while there may be scope for increasing councils' discretion over tax rates, reliefs, discounts and exemptions, more radical suggestions – such as devolving powers to carry out revaluations – look much more difficult to implement, without a fundamental reassessment of the local government finance system.

5. Stamp duty land tax

Stamp duty land tax (SDLT) is a tax levied on land and property transactions, with the amount due based on the value of the transaction. In recent years, there have been calls for its devolution, not least by the Greater London Authority's London Finance Commission. Thus after first illustrating the geographical distribution and volatility of SDLT revenues, this section discusses the case for devolving this tax to local government.

5.1 The distribution and volatility of stamp duty

Nearly £12.8 billion was raised from SDLT in England in 2017–18 in today's prices.²⁸ These revenues were highly unevenly distributed around the country though, as illustrated in Figure 5.1. SDLT revenues ranged from just £33 per person in Hartlepool to £3,489 per person in Westminster.²⁹ In one-fifth of council areas, SDLT revenues were less than £71 per person, while in another fifth they were more than £294, around four times higher.

Figure B.1 in Appendix B shows how these revenues were distributed by type of authority. On average, the revenue collected per person in London boroughs was 239% of the national average, while in metropolitan districts (which include the West Midlands) revenues per person were just 38% of the national average.

This wide variation reflects three factors:

- Differences in the volume of property transactions, particularly in relation to the construction and sale of new properties.
- Differences in property prices. Property prices are much higher in some parts of the country (e.g. London and parts of the South East) than in others (e.g. large parts of the North and parts of the West Midlands). This is illustrated in Figure B.2 in Appendix B.
- The highly progressive rate structure, which means that high-valued properties, especially residential ones, are subject to much higher tax rates than lower-valued properties.

Changes in transaction volumes and property prices over time also mean that SDLT revenues are very volatile. This is illustrated in Figures 5.2 and 5.3.

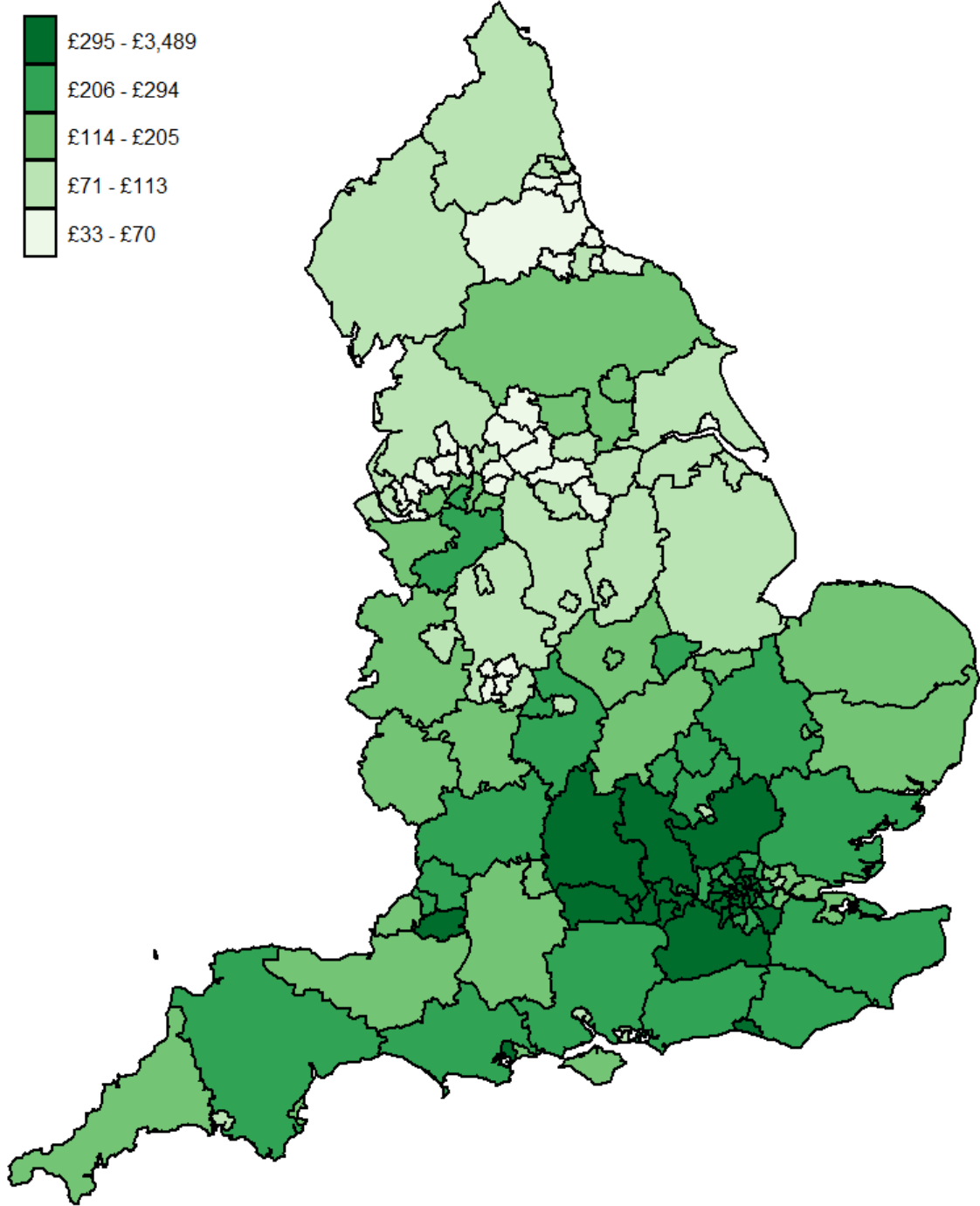
Figure 5.2 shows how stamp duty revenues per person changed between 2006–07 and 2017–18 in selected English regions. The most notable change was the large fall in SDLT revenues between 2007–08 and 2008–09, which was largely driven by a big fall in property transactions in the late 2000s recession, although falls in property prices (as well as some temporary tax cuts) also contributed. The fall was of a similar magnitude in percentage terms in all areas (around 50–55%) but was very different in cash terms given the large

²⁸ 2017–18 revenues have been updated to 2018–19 levels using the GDP deflator measure of inflation.

²⁹ In fact, the City of London shows revenues of more than £18,000 per person, but is excluded from the figure as an extreme outlier.

differences in revenues per person: the fall in revenues was equivalent to £52 per person in the North East of England but £252 per person in London.

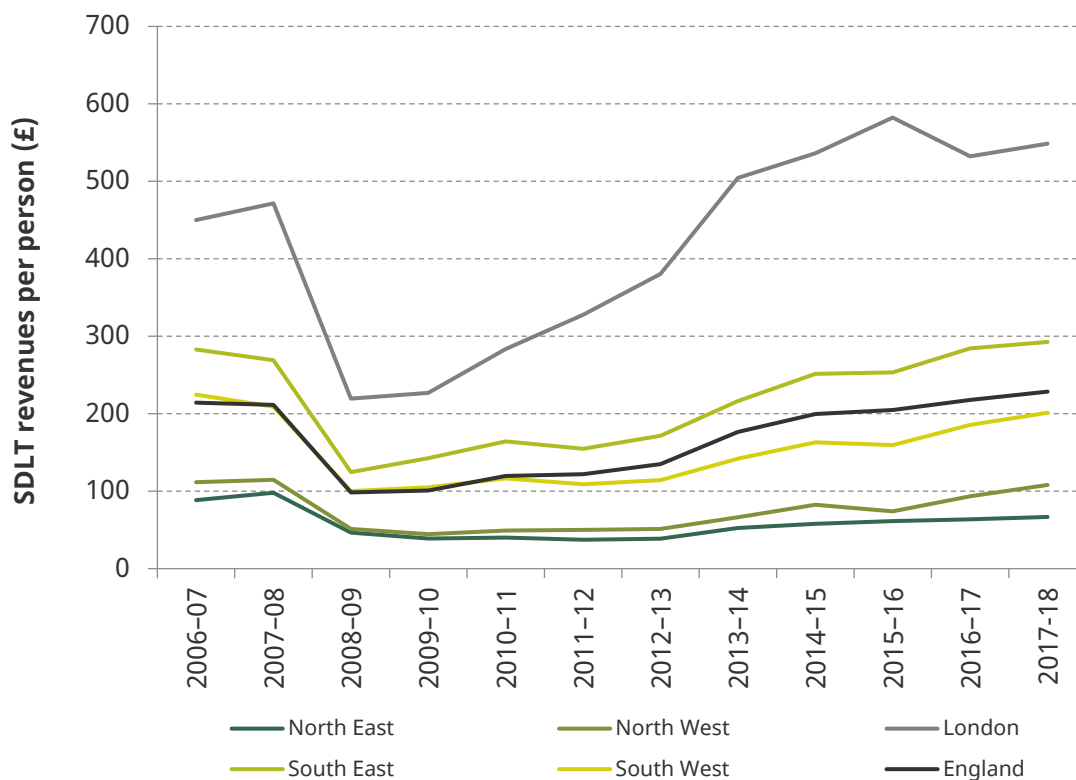
Figure 5.1. SDLT revenues per person (2018-19 prices), by upper-tier council, 2017-18



Note: Isles of Scilly excluded due to lack of data.

Source: Authors' calculations based on data from HMRC (2018) and ONS (2019a).

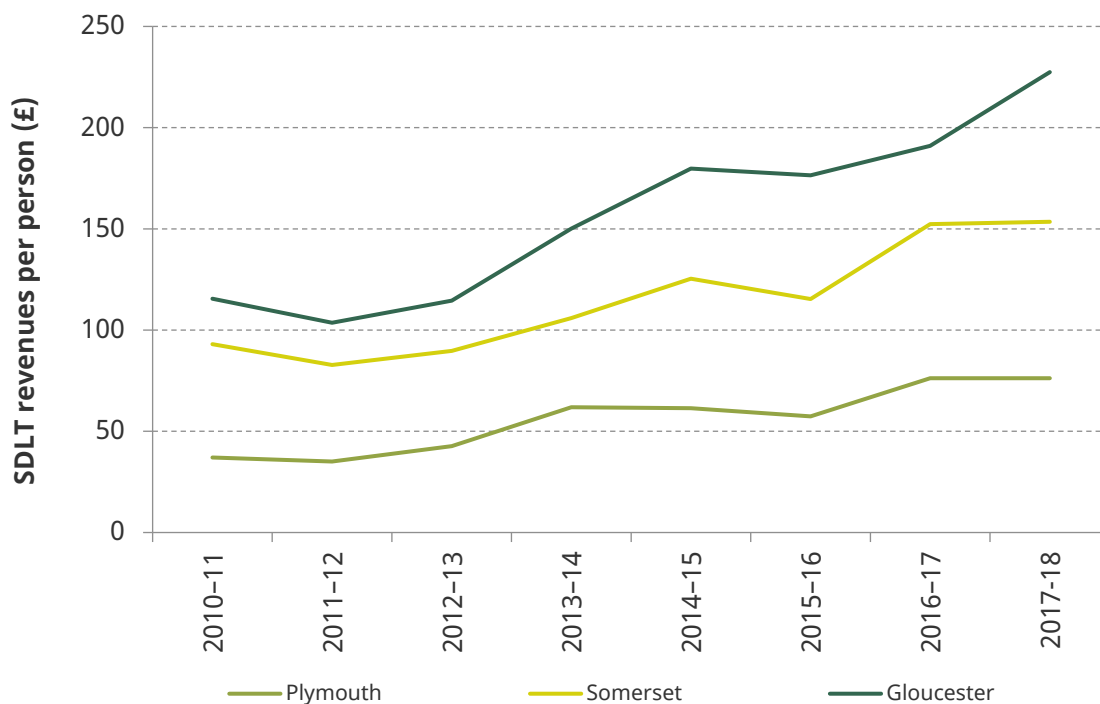
Figure 5.2. SDLT revenues per person (£2018-19 prices) for selected regions



Note: Isles of Scilly excluded due to lack of data.

Source: Authors' calculations based on data from HMRC (2018) and ONS (2019a).

Figure 5.3. SDLT revenues per person (2018-19 prices) for selected council areas



Source: Authors' calculations based on data from HMRC (2017) and ONS (2019a).

Figure 5.2 also shows that since 2009–10, revenues have recovered across England, but at different rates in different regions. In the North East, for instance, revenues per person in 2017–18 were still 32% below their 2007–08 levels, while in London they were 16% above them. This partly reflects changes in tax rates and bands – SDLT was made more progressive over this period. But to a large extent it reflects the fact that property prices recovered from the recession much more strongly in London than the North East.

If these changes had been borne at a local level, these divergences would have meant funding for council services in the North East falling relative to funding for council services in London, for example.

Figure 5.3 shows revenues from 2010 onwards for three council areas in the South West – Plymouth, Somerset and Gloucester – as an example of the volatility and divergence between areas that can be exhibited by SDLT revenues. Revenues per person in Gloucester in 2010 were 24% higher than in Somerset, but by 2016–17 revenues per person in Gloucester were nearly 50% higher. Somerset also illustrates that revenues can be volatile from year to year: revenues fell by 11% between 2010–11 and 2011–12 and they saw another temporary decrease of 8% in 2015–16. Such volatility is generally driven by volatility in transactions – associated with large non-residential transactions, new-build homes and macroeconomic trends.

5.2 Would stamp duty be suitable for devolution?

On one hand, property taxes in general are seen as relatively good candidates for devolution. They are levied on a relatively immobile tax base, since the stock of property is, by its nature, of fixed location, and it is administratively straightforward to assign property locations between areas. The first of these is clearly less true for stamp duty, since the tax base is property transactions (which may be mobile) rather than actual properties, but the second argument holds. However, there are some specific features of SDLT that make it a less attractive option for devolution:

- As shown above, **the tax base is very unequally distributed across England**. While this could be addressed by large-scale redistribution of SDLT revenues between councils, such a scheme could be complicated to administer (especially as local reforms lead to different councils' thresholds and tax rates diverging: differences in revenues driven by such policy variation would need to be stripped out before working out how revenues should be redistributed). Such large-scale redistribution could also lead to a 'gearing' issue similar to that mentioned in Section 3: changes in tax rates could lead to much larger changes in the amount of SDLT retained by councils paying into the redistributive system, while leading to much smaller changes for councils that instead rely on revenues redistributed from other councils. Areas with high tax bases may therefore have a tendency to put up taxes (because they would gain significant amounts of revenue) and those with low tax bases may have a tendency to reduce taxes (because it wouldn't cost them much).
- Moreover, **SDLT revenues are highly volatile, with trends diverging significantly between different areas**. High volatility could pose a significant risk to councils' budgets, especially as they are not currently able to borrow to pay for

day-to-day spending. The divergence in trends in SDLT revenues would mean that councils would see very different changes in their revenues over time, which may not accord with how their spending needs are changing. Again, this volatility and divergence could be addressed by providing top-up funding to councils seeing large falls in their revenues and by updating the redistribution system frequently. But frequently redistributing revenues could stymie the incentives local areas have to take action to boost the local tax base (e.g. by increasing approvals for new homes and commercial properties).

- **SDLT is one of the most economically undesirable taxes we currently have.** By taxing people only when they buy a property or land, it disincentivises mutually beneficial land and property transactions. As a result, people are less likely to trade up or trade down and so they end up in less suitable houses. They are also less likely to move to take advantage of job opportunities or to be closer to (or further away from!) friends and family. While these drawbacks exist whether SDLT is devolved or not, it seems less likely that the tax would be reduced or abolished – as would be desirable – if it were devolved to councils which came to rely on it for a substantial proportion of their revenues (a much bigger proportion than for central government), especially given that they are facing rising spending pressures.³⁰

For these reasons SDLT does not appear to be a good candidate for devolution.

³⁰ Note that current constraints on councils' powers over council tax also make it less likely that they would abolish or substantially reduce a devolved SDLT.

6. Corporation tax

Corporation tax is a tax on the profits of incorporated businesses and unincorporated associations.³¹ Profits are calculated as:

- income from trading (e.g. sales of goods and services), investments (e.g. interest or dividends received) and capital gains (i.e. increases in the value of investments and assets);
- *minus* wage and materials costs, debt interest and capital depreciation allowances (which generally allow firms to offset their spending on capital goods over a number of years).

The corporation tax rate has been 19% since 2017–18, and is due to fall to 18% in 2020–21. Revenues were £57.1 billion in 2017–18, of which £56.6 billion relates to onshore activities (offshore oil and gas activities in the North Sea are subject to a specific corporation tax regime). Focusing on England in particular, HM Revenue and Customs (2018) estimates that £49.6 billion was raised from onshore corporation tax in 2017–18.

Devolving or assigning a portion of corporation tax revenues could therefore provide a significant revenue source for local government. We calculate that a 3% local corporation tax rate would provide councils with revenues of £7.8 billion. But how would such revenues be distributed across England? And how good a candidate for devolution is corporation tax? Sections 6.1 and 6.2 address these questions in turn.

6.1 How are corporation tax revenues distributed?

Because corporation tax payers generally need to provide a tax return that covers all their operations in the UK, and many corporations operate in multiple parts of the country, actual revenue figures by local area do not exist, unlike for the property taxes discussed in Section 5. However, the Office for National Statistics (2018) has produced estimates of the tax take by region, making use of information on where each corporation's registered office is, and the distribution of each corporation's employees across regions.³²

The latest year for which figures are available is 2016–17. Table 6.1 shows estimated revenues and revenues per person for each English region in that year (as well as the revenues a decade earlier, in 2006–07). Revenues are estimated to be substantially higher in London than in the rest of England, although this gap has narrowed over time, likely driven by the decline in profitability of the financial services sector (which is particularly concentrated in London).

³¹ Unincorporated associations are organisations set up through an agreement between a group of people who come together for a reason other than to make a profit (e.g. a voluntary group or a sports club). However, if their activities do generate a profit, these profits are subject to corporation tax under UK tax law.

³² Specifically, corporation tax due on overseas income, interest income, income from land and property, and capital gains is allocated to the region containing the registered office. Corporation tax due on trading profit – which makes up the majority of corporation tax revenues – is allocated to regions according to employment distributions.

Table 6.1. Corporation tax revenue (2016–17 £), by region, 2006–07 and 2016–17

Region	Total corporation tax raised in 2006–07 (£ million)	Total corporation tax raised in 2016–17 (£ million)	Corporation tax raised per person in 2006–07 (£)	Corporation tax raised per person in 2016–17 (£)
North East	1,058	1,323	419	507
North West	3,956	4,661	579	655
Yorkshire and the Humber	3,309	3,459	651	645
East Midlands	2,170	2,916	501	626
West Midlands	2,952	3,717	550	648
East	3,427	4,482	617	738
London	18,410	17,052	2,429	1,932
South East	6,401	8,475	783	951
South West	3,121	3,748	618	690

Source: Authors' calculations based on data from ONS (2018) and ONS (2019a).

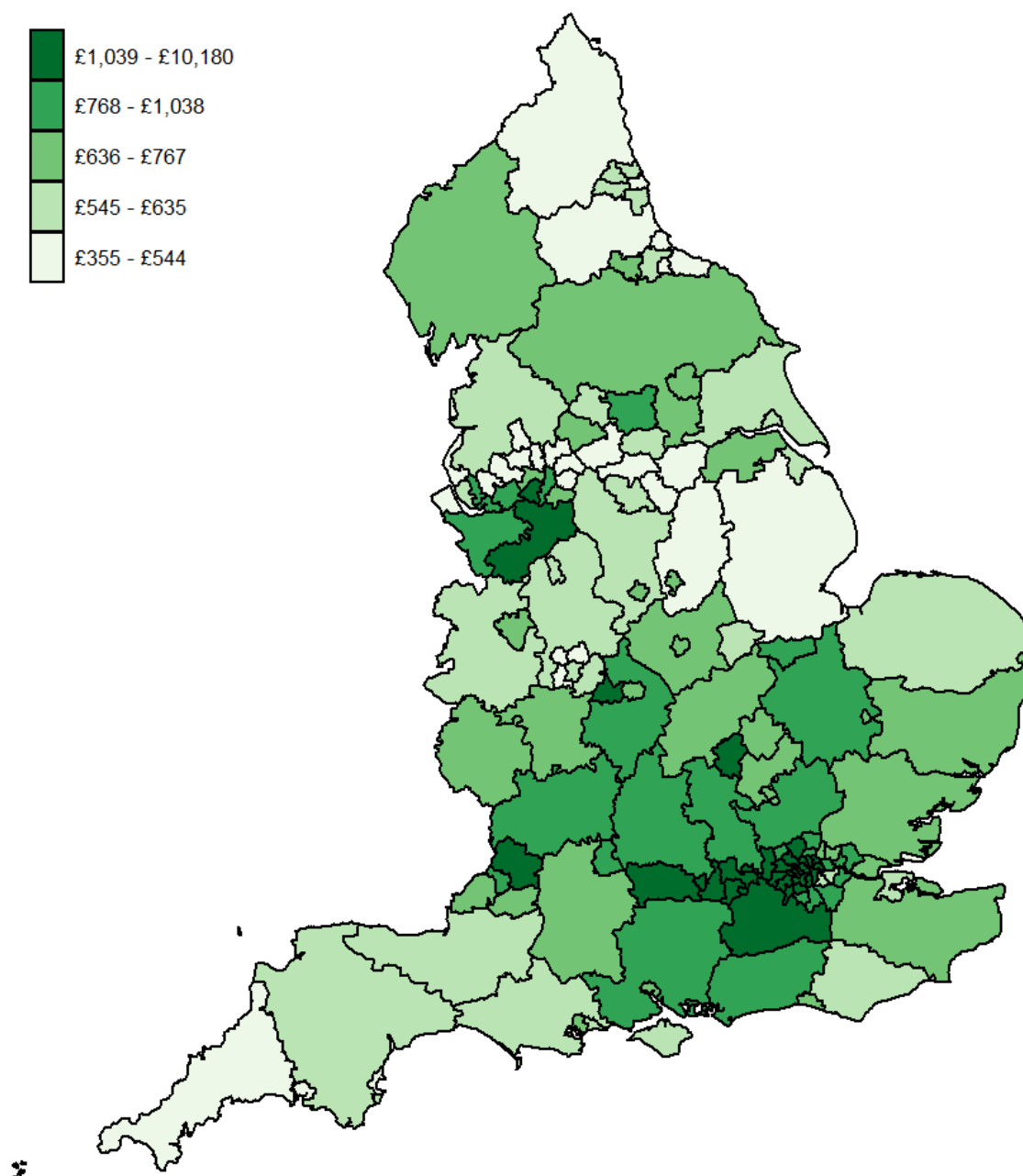
Official estimates at the local authority level are not available. Building on an approach developed by the Centre for Cities (McGough and Piazza, 2016), we produce our own estimates based on ONS estimates of gross value added (GVA) by local authority. In particular, the corporation tax of a region is apportioned to local authorities on the basis of their share of that region's GVA *excluding the education, health and public administration sectors* (which are excluded because they are largely operated by the government and therefore not subject to corporation tax).³³ These estimates should be treated with a degree of caution: the corporation tax base differs from GVA in several ways, not least by excluding the wages of employees. However, given a strong correlation between GVA per person and official estimates of revenues per person at a regional level (a correlation coefficient of 0.96), such estimates should provide a broad indication of how corporation tax revenues vary across local authorities.

Figure 6.1 shows further that corporation tax revenues per person were quite unevenly distributed around the country: ranging from just £355 per person in South Tyneside to £10,180 per person in Westminster.³⁴ In one-fifth of council areas, corporation tax revenues were less than £545 per person, while in another fifth of councils they were more than £1,038 per person, nearly twice as much. While this suggests less relative variation than is evident for stamp duty revenues, it still implies significant inequalities across councils.

³³ This differs from the Centre for Cities work, which uses overall GVA for their apportionment.

³⁴ In fact, the City of London shows revenues of more than £309,000 per person using this method, but is excluded from the figure as an extreme outlier.

Figure 6.1. Corporation tax revenues per person (£), by upper-tier council, 2016–17



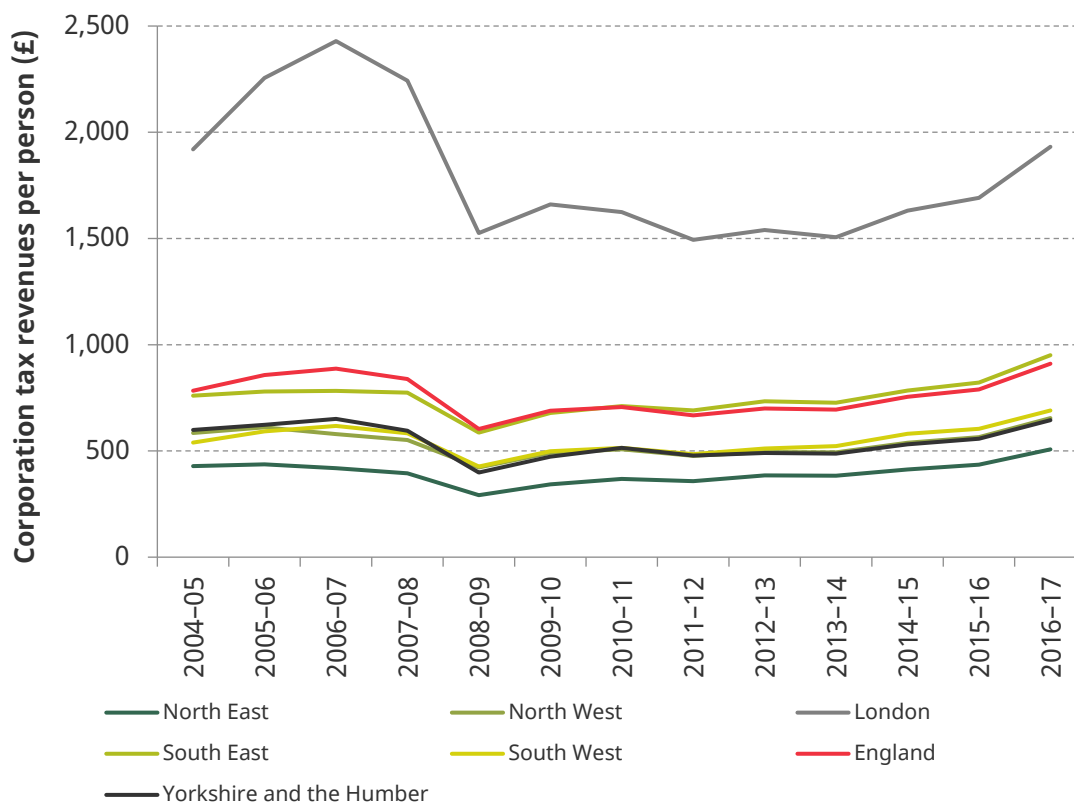
Note: City of London excluded as an extreme outlier – with revenues of more than £320,000 per person.

Source: Authors' calculations based on data from ONS (2017,2018b, 2019a).

There is also significant volatility in corporation tax revenues over time – largely due to changes in corporate profits. This is illustrated in Figure 6.2, which shows how corporation tax revenues per person for selected regions changed between 2004–05 and 2016–17. It shows that revenues per person fell substantially during the financial crisis, dropping by approximately 32% across England as a whole between 2006–07 and 2008–09, but have since recovered.

There also appears to be notable variation in relative revenue volatility (and revenue growth) across regions. For instance, during the financial crisis, corporation tax revenues declined by only 23% in the East Midlands but by 27% in the North West, 31% in the South West and nearly 40% in Yorkshire and the Humber (as well as by 37% in London). And while England as a whole has seen consistent growth in corporation tax revenues per person since 2011–12, this has not played out in all regions. So, while the South West has experienced steady year-to-year increases, other regions (such as the North East, North West, East Midlands, and Yorkshire and the Humber) have not. As a result, the South West now has higher revenues per person than regions such as the North West and Yorkshire and the Humber (which had higher revenues per person in 2004–05).

Figure 6.2. Corporation tax revenues per person (2018–19 £) for selected regions



Source: Authors’ calculations based on data from ONS (2018b, 2019a).

6.2 Would corporation tax be suitable for devolution?

Probably the main rationale for devolving part of corporation tax to councils in England would be to provide them with **financial incentives to grow the tax base** – i.e. corporate profits – recorded as deriving from their area. This could include both increasing the profitability of existing incorporated businesses in their area and attracting profitable new incorporated businesses to their area.

Powers to vary the rate would also allow councils to use corporation tax as a policy lever to promote local economic development, **and better match local preferences over tax levels and mix**. The corporate tax rate could be increased to raise additional revenue to

increase spending or cut other tax rates, or could be reduced if councils wanted to shift the tax burden to other tax bases, or were willing to reduce spending.

Corporation tax has also tended to be buoyant, automatically increasing as corporate profits grow as a result of inflation and economic growth.

However, assessment of corporation tax against the criteria set out in Section 3 suggests it is not a good candidate for devolution:

- **Apportioning the corporation tax base between different areas is conceptually and administratively difficult.** The profits of incorporated businesses typically result from multi-stage and multi-input processes. For example, the profits of a retailer will reflect the activities of its warehouses, stores, website and support operations (marketing, human resources, corporate strategy teams, etc.), which may take place in different locations. How can profits be split between these different activities and locations given there are no formal transactions (and prices) involved? Conceptually, is such a question even valid given that profits may be generated by such activities taking place in conjunction?³⁵

In practice, two broad approaches are used to apportion taxable profits between different areas:

- Internationally, the ‘arm’s-length’ principle is generally used. This means transactions between subsidiaries of corporations operating in different countries must be valued according to the prices that would be paid if the subsidiaries were in fact unrelated businesses. It requires accurate records of such transactions to be kept, and prices to be decided and in some cases agreed with the tax authorities. The latter can be difficult, especially when the transactions relate to highly specialised goods, services or intellectual property that are not traded between other parties. Ambiguity over appropriate prices means that corporations operating in multiple countries have scope to manipulate the prices they use in order to maximise their taxable profits in low-tax countries and minimise them in high-tax countries. Similarly, they have an incentive to borrow in high-tax countries and shift money around internally to fund investment in low-tax countries. To guard against these risks, countries employ various ‘transfer-pricing’, ‘thin capitalisation’ and ‘interest allocation’ rules. But these are both complex to design and implement, resulting in high administration and compliance costs, and somewhat arbitrary in their effects, leading to numerous legal disputes (Mirrlees et al., 2011). For this reason, devolving corporation tax on such a basis to English local government would seem unattractive.³⁶

³⁵ For example, without stores, the retailer’s marketing activities would not generate profits; while without marketing, the retailer’s stores could suffer from a lack of custom.

³⁶ It is worth noting that while such an approach is proposed for devolution of the corporation tax rate to Northern Ireland, it will only apply to large businesses: small businesses will be treated as either fully subject to the Northern Ireland or main Great Britain rates, depending on whether more than 75% of working time and wage costs are in Northern Ireland. This cut-off point, while simpler to implement than the arm’s-length

- A second approach is known as formula apportionment, which is used to apportion business income tax revenues between US states, Canadian provinces, Italian regions and German municipalities, among others. This involves apportioning taxable profits across areas according to a formula including factors such as the location of sales, property and wage bills. The aim is to *proxy* where profits are generated, while avoiding the administration and compliance costs and difficulties associated with attempts to apply the arm's-length principle. However, there are still costs associated with reporting and verifying information on the factors included in the formula used. And the growth of e-commerce may also pose a problem for such an approach: allocation to where warehouses/facilities are located is likely to mean greater scope for tax-induced distortions in economic activity; but allocation to where customers are located is likely to impose much higher administration and compliance costs. Thus, while more practical than the arm's-length approach, formula apportionment still comes with significant issues.
- **The corporation tax base is relatively mobile across areas.** This means that there is significant scope for variations in tax rates across local areas to lead to distortions to taxpayer behaviour, with resulting revenue and broader economic costs. This is likely to be particularly true for the arm's-length approach – where despite transfer-pricing and other rules, scope for profit-shifting can still be significant.³⁷ Corporations can also decide where to locate their investments and their employees to take advantage of lower tax rates – effects that can be exacerbated under formula apportionment.³⁸

Depending on the equalisation regime put in place, there may be either downwards or upwards pressure on local corporation tax rates:

- If the tax base is highly responsive to changes in tax rates, increases in the tax base could offset a significant part of the cost of reducing the local corporation tax rate. This can be true at a national level too, but if a large part of such an increase in the local tax base reflects shifts from other parts of the country, increases in the local tax base would be at least partially offset by reductions in the tax base elsewhere.³⁹ This could mean that devolution could lead to corporation tax being lower than it would otherwise be because local governments are unlikely to take account of such spill-over effects in the same way national government would.
- On the other hand, because corporation tax is formally levied on business owners who may not be resident in a particular area and hence eligible to

approach, could however distort decisions for businesses based in Northern Ireland to take on employees in Great Britain.

³⁷ See Heckemeyer and Overesch (2013) for an overview.

³⁸ See Reidel (2010) for a case study using Germany's wage-bill-based apportionment formula.

³⁹ Recent evidence suggests at least half of the changes in employment that result from changes in state-level corporation taxes in the United States reflect shifts in employment to/from other states (Giraud and Rauh, forthcoming).

vote in a particular area, this could lead to upwards pressure on local corporation tax rates and a lack of democratic accountability.

The greater the degree of fiscal equalisation, the more likely it is that the latter factor would outweigh the former. This is because increased (decreased) fiscal transfers would offset more of the decrease (increase) in the local corporation tax base when tax rates are increased (decreased).

- **The corporation tax base is unequally distributed and highly volatile**, as shown in Section 6.1. Potentially complex redistribution and insurance mechanisms would therefore need to be put in place if the government wanted to avoid significantly increasing the scope for funding divergences between different local areas.

Assignment

Assignment of a proportion of corporation tax to local government would avoid issues associated with rate variation – distortions to business activity and tax competition – but still provide local incentives to boost the tax base (the strength of which would depend on the degree of revenue equalisation).

However, there would still be administration and compliance costs associated with apportioning tax revenues to different local governments via transfer-pricing or formula apportionment arrangements. And while taxpayers would not have an incentive to manipulate their reported figures to reduce their tax liability (as the tax rate would be the same everywhere), that does not mean that they would always be accurate, especially under a transfer-pricing-type regime. For example, there could be opportunities for councils where a corporation's headquarters is located to offer non-tax benefits (e.g. custom or improved services or infrastructure) if the corporation apportions more of its profit to the headquarters. Given the concentration of headquarters in London, especially for the largest corporations, such collusive misreporting could result in shifts in assigned revenues to London.

Potentially complex arrangements to equalise revenues and ameliorate revenue volatility would also still be needed if the government wanted to avoid significantly increased funding divergences between areas.

Summary

Overall then, corporation tax does not appear a particularly attractive candidate for devolution or assignment.

7. VAT or a local sales tax

Value added tax (VAT) is a proportional tax paid on the value added by businesses with turnovers of £85,000 a year or more:⁴⁰ it is charged on sales, but businesses deduct any VAT they paid in their input purchases from other businesses. It is paid by both incorporated and unincorporated businesses. Unlike corporation tax, it does not allow for the deduction of a business's own labour costs (the wages and other benefits paid to their employees are part of the value the business has generated).

The standard rate of VAT is 20%. However, 0% and 5% rates apply to a range of goods and services including all exports, most food, construction of new houses, public transport, children's clothing and domestic fuel and power. A number of goods and services, including rent, education, health and financial services, are exempt from VAT, meaning that no VAT is charged in their sale, and businesses producing them cannot reclaim VAT paid on their inputs.

Revenues were £127.5 billion in 2017–18, of which HMRC estimates that £108.4 billion was raised in England.^{41 42} Devolution of a portion of VAT revenues could therefore provide a significant revenue source for English councils. For example, we calculate that allowing councils to retain revenues from a 3p local VAT on the standard rate eligible tax base (and 0.75p on the 5% rate tax base) could provide £16.8 billion of revenues. However, as with corporation tax, such a policy would pose significant difficulties.

7.1 How are VAT revenues distributed?

Because VAT-registered businesses generally need to provide a tax return that covers all their operations in the UK, actual revenue figures by local area do not exist. However, as with corporation tax, the Office for National Statistics (ONS) have produced estimates of the tax take by region,⁴³ based on a combination of data from household expenditure surveys, GVA for sectors exempted from VAT, and government public service spending.

The latest year for which figures are available is 2016–17. Table 7.1 shows estimated revenues and revenues per person for each English region in that year (as well as the revenues a decade earlier, in 2006–07). At this level, VAT revenues per person are more evenly distributed than revenues from SDLT and corporation tax: ranging from £1,751 per person in the North East to just over £2,135 in the South East (only 1.2 times higher). While we do see VAT revenue growth across all regions over the past decade, this has been fairly similar for different regions – meaning that there has been very little change in relative inequalities (in VAT revenues per person) between regions over the period.

⁴⁰ Firms with turnovers over £85,000 are required to register for VAT; those with turnovers below £85,000 can voluntarily register if they wish.

⁴¹ HMRC (2018).

⁴² All revenues reported in 2018–19 £s – uprated using GDP deflators.

⁴³ Office for National Statistics (2018).

Table 7.1. VAT revenue (2018–19 £), by region, 2006–07 and 2016–17

Region	Total VAT raised in 2006–07 (million £)	Total VAT raised in 2016–17 (million £)	VAT raised per person in 2006–07 (£)	VAT raised per person in 2016–17 (£)
North East	3,798	4,565	1,504	1,751
North West	10,475	13,305	1,533	1,869
Yorkshire and the Humber	7,975	10,071	1,568	1,878
East Midlands	6,487	8,694	1,499	1,867
West Midlands	7,971	9,870	1,484	1,721
East	9,282	11,965	1,670	1,969
London	13,593	18,776	1,794	2,127
South East	13,927	19,033	1,703	2,135
South West	8,439	10,659	1,670	1,963

Source: Authors' calculations based on data from ONS (2018b, 2019a).

Official estimates at the local authority level are not available. To obtain such estimates, we use an approach developed by the Centre for Cities (McGough and Piazza, 2016), which breaks the VAT tax base into a range of categories and apportions VAT using different methods for each category, such as employment in relevant sectors, GVA and population. As with our estimates of local corporation tax bases, these estimates should be considered as indicative only.

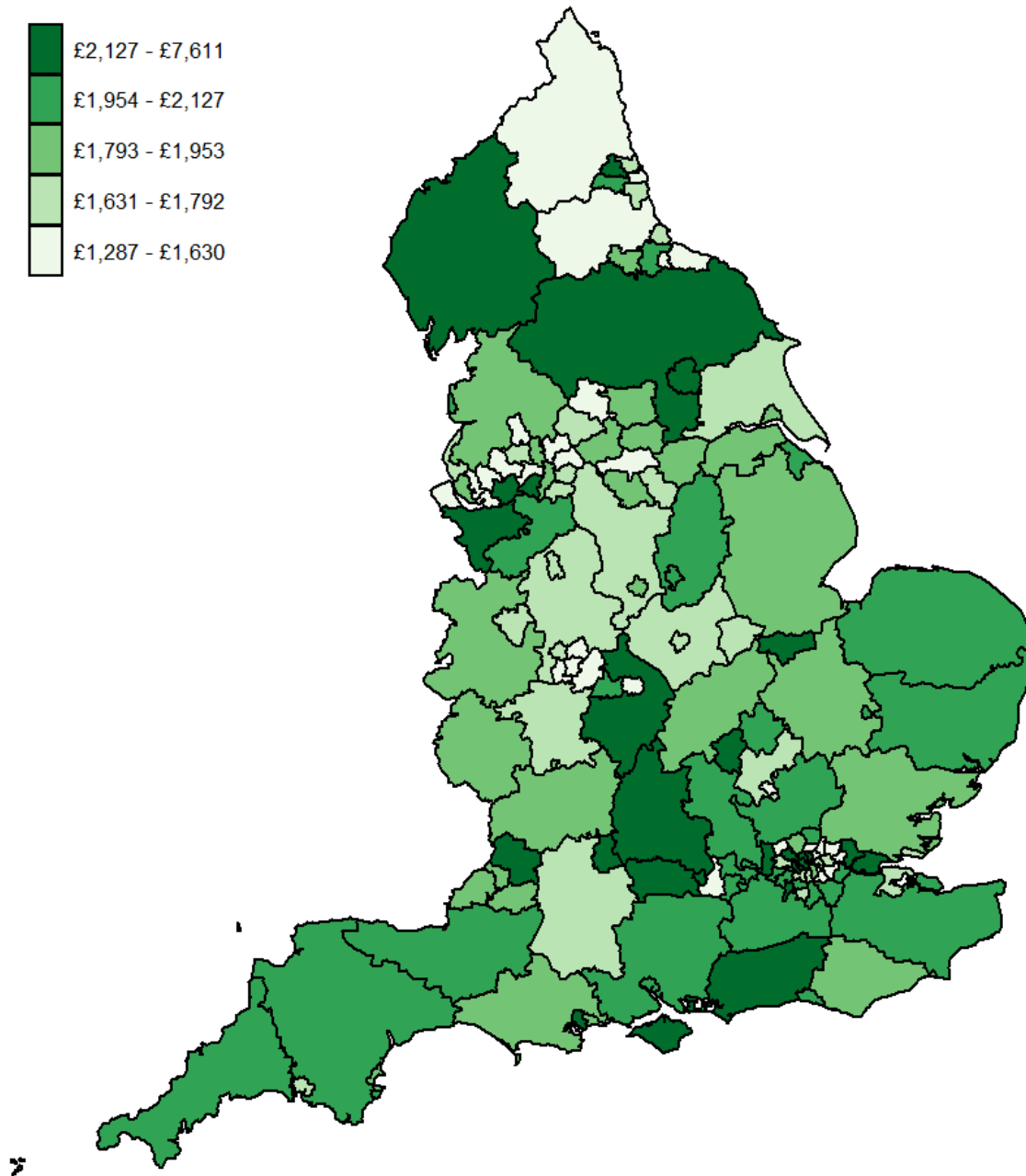
Figure 7.1 shows that there was notable variation in VAT revenues per person across councils. However, these were more evenly distributed around the country than SDLT or corporation tax revenues: ranging from £1,287 per person in Knowsley, to £7,611 per person in Westminster (a ratio of 6.0, compared to a ratio of 28.7 for corporation tax). In one-fifth of council areas, VAT revenues were less than £1,631 per person, while in another fifth of councils they were more than £2,127 (i.e. only 30% higher).

Turning to trends over time, Figure 7.2 shows a significant fall in VAT revenues at the time of the late 2000s recession (15% between 2006–07 and 2009–10) and an even strong rebound following this (27% between 2009–10 and 2011–12). However, to a large extent this reflects the effects of a temporary reduction in the standard rate of VAT (from 17.5% to 15% in 2009, and a permanent increase to 20% in 2011). Stripping out the mechanical effects of these rate changes, revenues fell (5% between 2006–07 and 2008–09) and subsequently rebounded only modestly (1% between 2008–09 and 2011–12). This is unsurprising as general household spending varies less with the ups and downs of the economy than both property purchases (and prices) and corporate profits.

However, the figure also shows that trends can differ between different parts of the country (all of which faced the same tax rate changes). For example, between 2006–07 and 2009–10, VAT revenues are estimated to have fallen by just 10% in the North East of England but 23% in the South East. They subsequently rose by an estimated 23% and 43% between 2009–10 and 2011–12. And in the period between 2011–12 and 2016–17 revenue growth has varied between 5% in the North East and 13.5% in the South East. If borne locally via a devolved VAT, councils in the South East would therefore have seen more

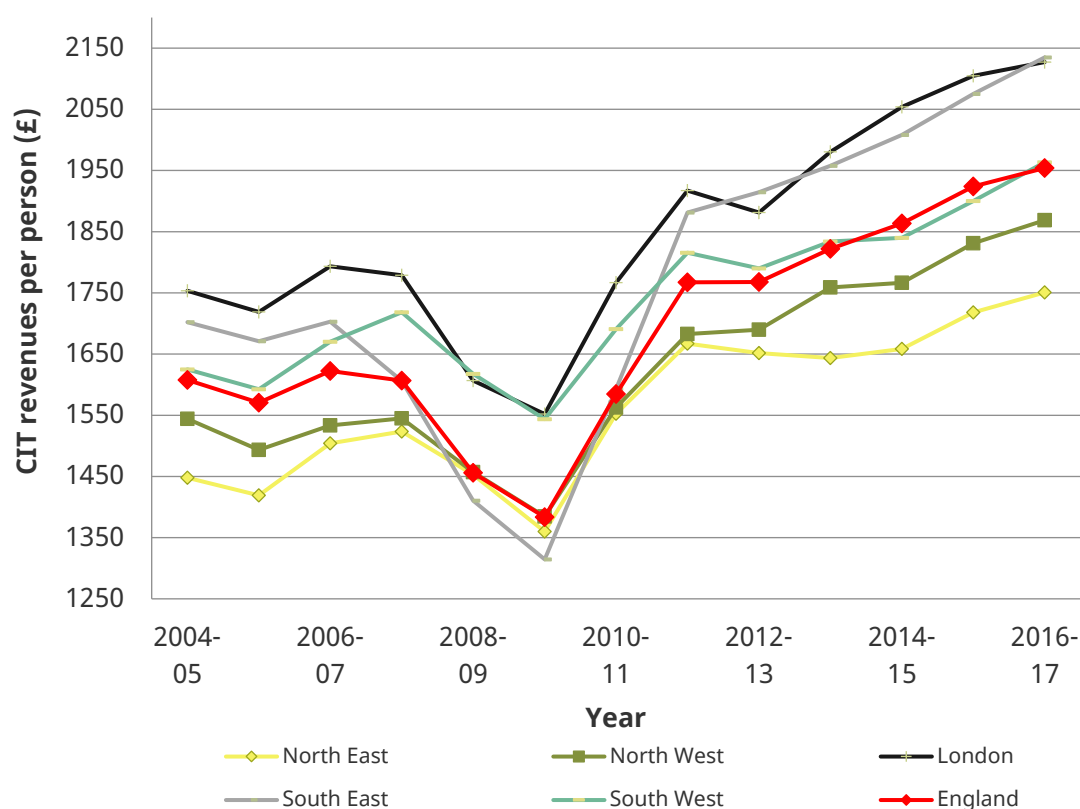
volatile revenues during the recession than those in the North East, but stronger growth in the years after the recession.

Figure 7.1. VAT per person (2018-19 £), by council area, 2016-17



Note: City of London excluded as an extreme outlier – with revenues of more than £40,747 per person.

Source: Authors' calculations based on data from ONS (2017a,2018b,2019a,2019b) and DfBEIS (2018).

Figure 7.2. VAT revenues per person (2018–19 £), by region, 2004–05 to 2016–17

Source: Authors' calculations based on data from ONS (2018b, 2019a).

7.2 Would VAT be suitable for devolution?

As with corporation tax, one of the main rationales for devolving part of VAT to councils in England would be to provide them with **financial incentives to grow the tax base** – value added recorded as deriving from their area. This could include both increasing the value added by existing businesses in their area and attracting new businesses to their area. These incentives would be broader than for corporation tax as VAT applies to businesses' labour costs as well as profits – thus incentivising councils to take action to promote employment and earnings too.

Powers to vary the rate would also allow councils to use VAT as a policy lever to promote local economic development, and **better match local preferences over tax levels and mix**. The VAT could be increased to raise additional revenue to increase spending or cut other tax rates, or could be reduced if councils wanted to shift the tax burden to other tax bases, or were willing to reduce spending.

VAT is also generally a buoyant tax, with revenues automatically increasing as value added increases as a result of inflation and economic growth.

However, like corporation tax, VAT has properties that make it a relatively poor candidate for devolution to local government.

- **Apportioning VAT revenues to different local areas is conceptually and administratively difficult.** Similar to corporation tax, this partly relates to difficulties in apportioning value added between different stages and activities conducted by a single business, such as warehouse, store, website and support operations.
 - However, it also reflects the way VAT works: it is charged on sales, but businesses can deduct the VAT they have paid on their inputs. Devolved VAT could mean businesses not only having to charge different VAT rates in different areas, but also having to record where their input purchases came from, as different amounts of VAT would be deductible based on this. This would involve high administration and compliance costs. Alternatively, borders between local government areas could work like international borders for the purposes of VAT: businesses ‘exporting’ to another local government area would charge a 0% rate on their ‘exports’. But this would require businesses to record where their business customers were located and to charge VAT accordingly, which would again be a costly process.
 - Giving local government the power to set a local sales tax as opposed to a VAT would avoid these problems. A sales tax differs from a VAT in that the tax is only levied on sales to final consumers or unregistered businesses. Because no tax is charged on sales to registered businesses, there is no need for a system of deduction of sales tax paid on business inputs. This makes devolution easier and, as discussed in Section 2, the United States has a system of sales taxes varying by state, county and city.
 - However, sales taxes come with their own issues. Businesses need to distinguish whether a sale is to a registered business or not, and to charge tax accordingly. In order to reduce prices for final consumers and registered businesses, they have an incentive to misclassify such sales as business sales, which is hard for the tax authorities to check and prevent. Partly as a result, sales taxes are seen as more prone to tax evasion than VATs.⁴⁴
- **The VAT base is relatively mobile across areas.** Consumers are able to change where they buy goods in services in response to differences in VAT or sales taxes, and this in turn may affect where businesses choose to locate. This is particularly true when people live close to ‘borders’ between different tax rates, and when the transaction value is high, as the monetary and time costs involved in travelling to the low-tax area are then relatively low. Evidence for such cross-border shopping is found in numerous studies, covering numerous goods including tobacco, alcohol, petrol and food.⁴⁵ Impacts can also be significant: a study on petrol suggested Chicago’s tax base was 40% lower as a result of cross-border purchases from the neighbouring areas of Illinois and Indiana with lower taxes, for instance (Manuszak and Moul, 2009).

⁴⁴ See Zodrow (1999).

⁴⁵ Leal, Lopez-Laborde and Rodrigo (2010) provide an overview,

- The growth of internet shopping is likely to have exacerbated this issue, except in the case where internet retailers are required to charge taxes based on where people live rather than where the retailer or its warehouses were based. Evidence from the United States – where this approach is not allowed, and many online sales have traditionally avoided sales tax altogether – suggest such effects can be big. For example, a 4% cut in New York’s sales tax was accompanied by an average 15% fall in internet and catalogue sales as people switched back to physical stores (Hu and Tang, 2014). Significant effects of sales taxes on physical and internet sales on Ebay and for cigarettes across the United States have also been found (Einav et al, 2014; Goolsbee, Lovenheim and Slemrod, 2010).
- The evidence therefore suggests that variation in local VAT or sales tax could cause significant distortions to where expenditures take place.
- As with corporation tax, depending on the equalisation rules in place, tax competition between local areas, or the political attractiveness of increasing a tax that may fall to a significant extent on people living elsewhere, could also lead to downward or upward pressure on VAT rates.

Assignment

While preventing tax competition and economic distortion associated with variation in tax rates, assignment of part of VAT revenues would still involve the tricky issue of apportioning revenues between local areas.

However, a number of EU countries, including Italy, Spain and Portugal, assign part of revenues to sub-national government; and in the UK, half of estimated VAT revenues for Scotland are set to be assigned to the Scottish Government (in lieu of grant funding from the UK Treasury). The method used for Scotland is unlikely to be suitable for assignment to local government though – it relies to a large extent on surveys of household spending, for which sample sizes for councils would be too small to be reliable (HM Treasury, 2018). Estimated tax takes for different councils could vary significantly from year to year, based on the particular sample of households in the survey that year, and such statistical ‘noise’ could swamp the ‘signal’ due to genuine changes in business activity and VAT revenue.

Potentially complex arrangements to equalise revenues and ameliorate revenue volatility would also still be needed if the government wanted to avoid significantly increased funding divergences between areas.

Summary

Overall then, VAT or sales tax do not appear particularly attractive options for devolution or assignment.

8. Income taxes

Income tax is a tax paid by individuals on their earnings (from employment and self-employment) and other income (such as dividends, pensions, rent receipts, etc.). A progressive system of marginal tax rates is applied: in the current financial year, 2018–19, the first £11,850 of income is untaxed; the next £34,500 is taxed at a rate of 20%; the next £103,650 is subject to a tax rate of 40%; and income above £150,000 is subject to a 45% tax rate.⁴⁶

The Scottish Government has the power to vary tax rates and thresholds for income from sources other than interest and dividends, and the Welsh Government has the power to vary rates (but not thresholds) levied on income from sources other than interest and dividends. While presently all decisions on income tax in England are taken by the UK government, a local income tax has been mentioned at various points over the past decade by both the Labour Party and the Liberal Democrats. So would it be a good candidate for devolution?

8.1 How are income tax revenues distributed?

In 2017–18, income tax revenues amounted to £163 billion across England, making it the country's 'biggest' tax.⁴⁷ Like SDLT (and unlike corporation tax and VAT), HMRC produces its own estimates of income tax revenues by council area, based on tax administrative data. Estimates for the most recent year available, 2015–16, are shown in Figure 8.1.

It shows that estimated income tax revenues per person raised from different council areas vary significantly. For example, in one-in-five council areas, income tax revenues per person were estimated to amount to less than £1,580, while in another one-in-five areas they were estimated to be more than £3,674 per person, around 2.3 times as much. In general, the amount of income tax raised per person is relatively low in urban areas of the North and Midlands and relatively high in West London and the Home Counties. And at the very top of the distribution, residents of Kensington and Chelsea paid an average of £30,270 in income tax.

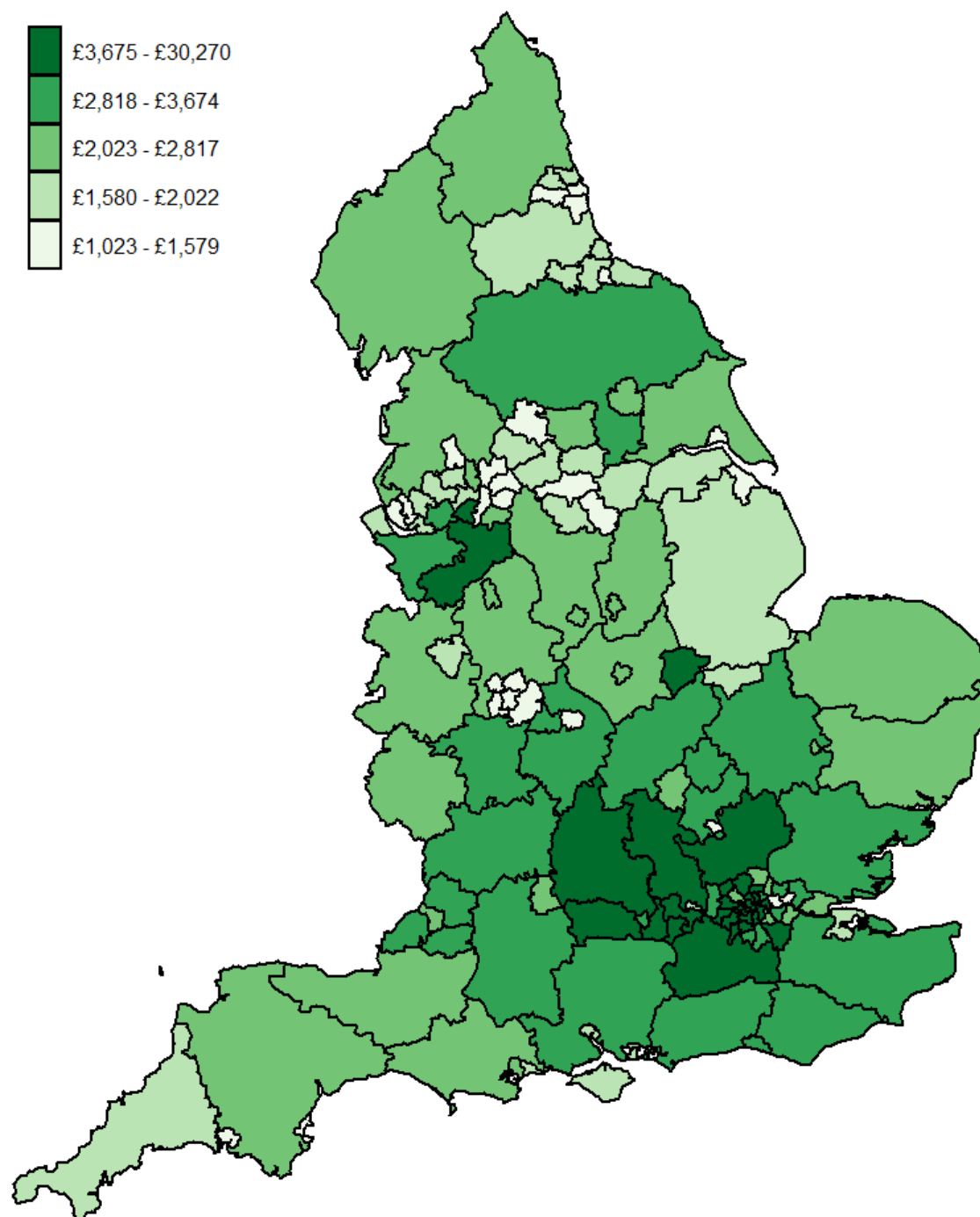
This unequal distribution reflects the following.

- There are variations in average levels of taxable incomes between different council areas (see Figure B.3 in the Appendix).
- The income tax system has a progressive structure, with progressively higher marginal (and hence average) tax rates applied as income increases. This means revenues vary even more than average incomes between areas.

⁴⁶ Note that the tax-free personal allowance of £11,850 is progressively withdrawn once income reaches £100,000. This means that the effective marginal income tax rate for incomes between £100,000 and £123,700 is 60%, despite the headline rate being 40%.

⁴⁷ All revenues reported in 2018–19 £s – uprated using GDP deflators.

Figure 8.1. Income tax revenues per person (2018–19 £), by council area, 2015–16



Note: Isles of Scilly and City of London excluded due to small sample sizes and imprecision of data.

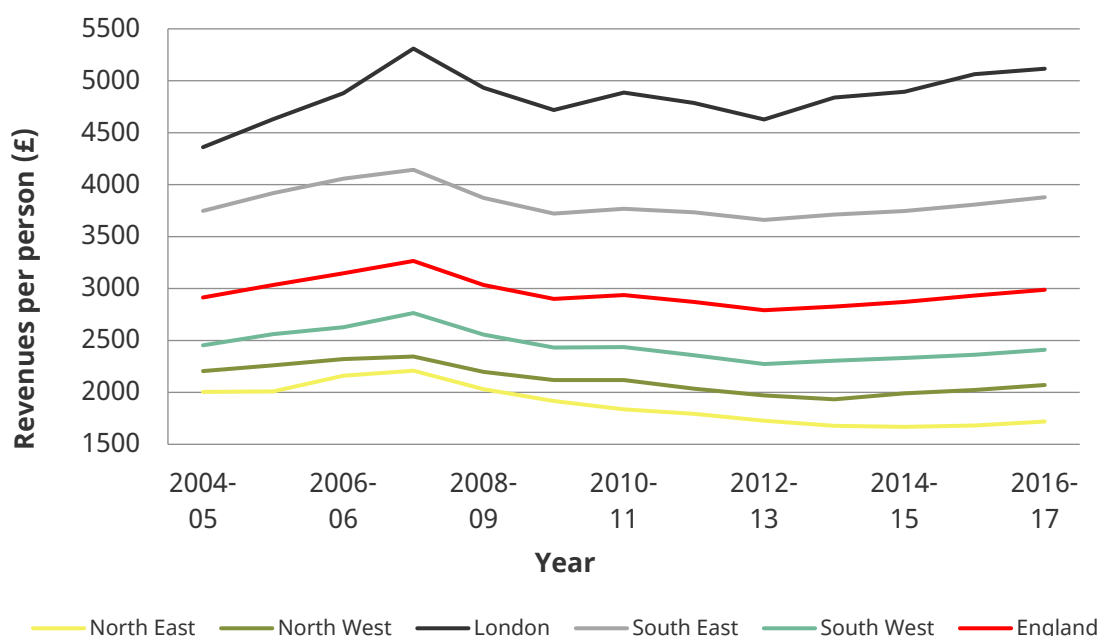
Source: Authors' calculations based on data from HMRC (2018b) and ONS (2019a).

Revenues can also change over time, as incomes and rate structures change. This is illustrated in Figure 8.2, which shows how income tax revenues per person for selected regions changed between 2004–05 and 2016–17.

The figure shows that revenues fell in the years following the financial crisis: down by 10–14% between 2007–08 and 2009–10, for instance. The figure also shows that, since then, revenues have rebounded somewhat in London (up 8%) but have continued to fall in the North East (down 10%) and the North West (down 2%).

This divergence in large part reflects reforms to the income tax system that have made it more progressive: the personal allowance has been increased substantially, reducing the tax paid by lower earners and taking millions out of paying income tax entirely, while policies at the top (including the 45% additional rate, the tapering of the personal allowance and restrictions on pension contributions relief) have increased average tax rates. This greater progressivity has increased average tax bills in areas with relatively high incomes (such as London) and decreased average tax bills in areas with relatively low incomes (such as the North East and North West).

Figure 8.2. Income tax revenues per person (2018–19 £), for selected regions, 2004–05 to 2016–17



Source: Authors’ calculations based on data from ONS (2018b,2019a).

8.2 Would income tax be a suitable for devolution?

As with corporation tax and VAT, one rationale for devolving part of income tax to local government is that doing so would **provide councils with the financial incentives** to grow the tax base – taxable personal income – deriving from residents of their area. This could include both increasing the incomes of existing residents and attracting new residents with high incomes to their areas. And because councils would gain wherever their residents worked, councils would have an incentive to facilitate residents’ access to (high-earning) jobs in neighbouring areas by, for example, investing in local transport infrastructure, as well as an incentive to increase the number and earnings of jobs in the local area.

Powers to vary the rate would also allow councils to use income tax as a policy lever to promote local economic development **and better match local preferences over tax levels and mix**. The income tax rate could be increased to raise additional revenue to increase spending or cut other tax rates, or could be reduced if councils wanted to shift the tax burden on to other tax bases, or were willing to reduce spending.

Income tax is also a buoyant tax, with revenues automatically growing as incomes increase as a result of inflation and economic growth.

A number of other features of income tax also make it a better candidate for devolution than corporation tax and VAT, in particular:

- **Apportionment of income taxpayers and revenue between areas is more straightforward.** Those organisations responsible for the administration and remittance of income tax – such as HMRC, employers, pension providers, etc. – should have the residential addresses of taxpayers, meaning allocating taxpayers different council areas and calculating, remitting and allocating tax payments accordingly should be possible. In fact, income tax is already partially devolved to Scotland (and from April 2019, Wales), which has required HMRC to identify which country taxpayers have their primary residence in, and ensure taxes are levied and allocated accordingly.

This is not without its challenges though. First, addresses for some taxpayers may be missing or out of date – there is no statutory requirement on taxpayers (or their employers) to tell HMRC about any changes of address. Second, a number of taxpayers have multiple properties, and HMRC may find it difficult to determine which one is their main residence. In this context, variation in tax rates across councils could incentivise taxpayers to claim that their main residence is the one where the council sets the lowest tax rate.

And even if feasible, administration and compliance costs would increase at least to some extent. Tax administration and payroll systems would need to be adapted to allow for identification of where different people live, and potentially application of different tax rates. Experience in Scotland highlights particular issues with relief for charitable contributions ('Gift Aid') and the tax treatment of employee contributions to certain kinds of pension funds – which to date have been addressed by continuing to apply rest-of-the-UK rules in the first instance, and asking taxpayers to contact HMRC for an adjustment if this makes them worse off.⁴⁸

- **Local income taxpayers would be able to vote in local elections.** On the one hand, this means they could hold local politicians to account for their decisions on income tax rates, which would often not be the case for payers of a local VAT or corporation tax (or business rates).

⁴⁸ HM Revenue and Customs (2018). Further information available at <https://www.gov.uk/government/publications/pension-schemes-relief-at-source-for-scottish-income-tax-newsletter-february-2018/pension-schemes-relief-at-source-for-scottish-income-tax-newsletter-february-2018>.

On the other hand, there are also a significant number of eligible voters who do not pay income tax – in any given year, for instance, almost half of adults have income too low to pay income tax⁴⁹ – or who pay very little income tax. Those not expecting to pay (much) income tax in the foreseeable future could have an incentive to choose higher levels of tax and spending, knowing that they would not bear (much of) the associated costs.

However, this is a feature of income tax irrespective of whether it is devolved or not. Furthermore it affects virtually all taxes to some extent; and some taxes such as SDLT – which is paid only when purchasing a property above the exemption threshold – significantly more than income tax.

- **People are less mobile than sales and corporate profits.** It is more costly for people to move house than it is to change where they shop, or for corporations to shift where they attribute their profits to.

However, mobility of high-income taxpayers in particular could have significant revenue effects, and empirical evidence suggests such individuals are relatively responsive to differences in tax rates between jurisdictions – and we would expect those responses to be larger for differences between councils than between countries.⁵⁰ Councils could try to take advantage of that mobility by selectively reducing tax rates on those with high incomes, which could result in tax competition between councils. This could lead to an erosion of revenues from high-income taxpayers and a decline in the progressivity of the tax system.

8.3 A flat-rate local income tax?

Devolving powers for a small supplemental local income tax on top of national income tax rates would limit the extent of this mobility issue. This is because while a council would bear the full ‘mechanical’ effect on revenues of a lower tax rate, it would only gain part of the ‘behavioural’ effect on revenues of more high-income taxpayers moving to the area: the bulk of the revenues from these extra high-income taxpayers would flow to the national government via the national income tax rates.

Indeed, such effects could provide an incentive to councils to increase tax rates on those with the highest incomes: they would gain the full mechanical revenue effect of the higher tax rate, but bear only part of the behavioural revenue effect of the smaller tax base.

However, both downwards and upwards pressure on tax rates for those with the highest incomes could be addressed by restricting the powers devolved to application of a flat-rate income tax rate. Councils could then only cut or increase tax rates for those with the highest incomes if they cut or decreased them for everyone. This is how local income taxes work in much of Scandinavia (see Section 2), and was how Scotland’s income tax powers worked up until 2017–18. Such an approach limits local discretion over the progressivity of the income tax in order to reduce the risk of

⁴⁹ Pope and Waters (2016) reports that 56.3% of adults would pay income tax in 2016–17.

⁵⁰ See Esteller et al. (2016).

competition-induced reductions in top tax rates and tax-base-sharing-induced increases in top tax rates.

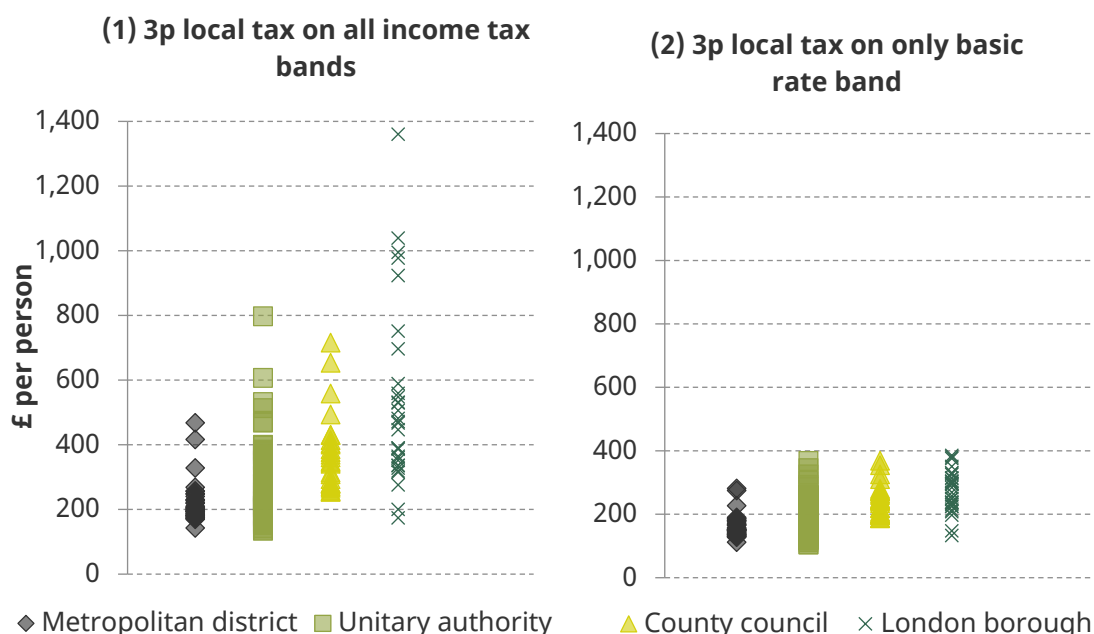
Such an approach has further benefits.

Revenues from a flat-rate income tax would generally be less volatile than overall income tax revenues because they would depend less on the amount paid by those with the very highest incomes – which tends to be particularly pro-cyclical, and subject to change as people migrate.

Revenues from such a flat-rate local income tax would be significantly less unequally distributed than under the progressive national income tax system. This is because the impact of the concentration of high earners and low earners in different parts of the country would not be magnified by the application of tax rates that increase with income.

However, the revenues raised from a flat-rate local income tax would still vary significantly between council areas because of differences in income levels. This is illustrated in Figures 8.3, 8.4 and 8.5, which show estimates of how much would be raised in different council areas from a flat 3p income tax applied to either all tax bands, or applied to only the basic rate tax band. The former would raise £19 billion, the latter around £12 billion, across England as a whole, based on income tax and earnings distribution data from 2015–16 that has been updated to 2018–19 levels using national tax revenue outturns and forecasts.

Figure 8.3. Revenues per person from a 3p local income tax, by council and council type, 2018–19 terms



Note: Isles of Scilly and City of London excluded due to small sample sizes and imprecision of data. Kensington and Chelsea – with simulated revenues of £2,379 per person – is excluded in the left hand graph (for simulation (1)) for ease of presentation.

Source: Authors' calculations based on data from HMRC (2018b) and ONS (2017b, 2019a). Further information on methodology available from the authors on request.

Figure 8.3 makes clear that revenues from a flat-rate local income tax levied on all bands of income would be significantly more unevenly distributed around the country than from one charged only on the basic rate of income tax. This is particularly true for London, reflecting the concentration of people with very high incomes in places such as Kensington and Chelsea (which, with estimated revenues of £2,379 per person under the flat-rate tax applying to all bands, is in fact off the scale) and Westminster, and their sparseness in places such as Barking and Dagenham, and Newham. Such people still matter a lot for revenues under a flat-rate local income tax applying to all bands, but matter much less for a flat-rate local income tax applying to only the basic rate band (as their income in higher bands would not be subject to this tax).

More generally, under a flat-rate local income tax applying to all bands, the tenth of councils with the highest revenues per person would have revenues around three times as high (£549) as the tenth of councils with lowest revenues per person (£179). But under one applying to the basic rate band only, the tenth of councils with the highest revenues per person would have revenues only around 2.3 times as high (£311) as the tenth of councils with the lowest revenues per person (£135).

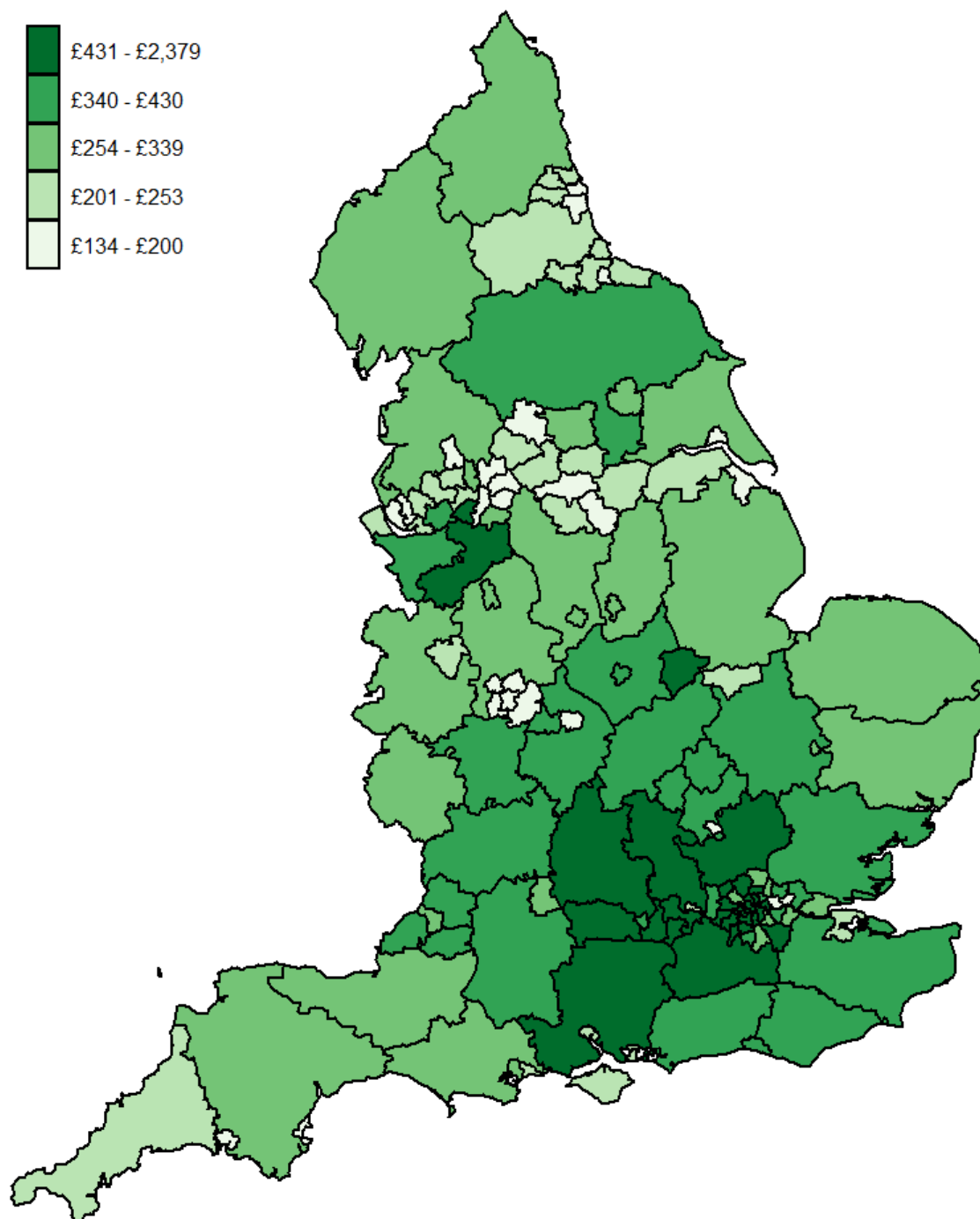
Figures 8.4 and 8.5 show that despite differences in the degree of inequality in revenues, the parts of the country with relatively high and relatively low revenues per person look similar for both variants of the flat-rate income tax. In both cases, for instance, revenues would tend to be higher in west London and the Home Counties (as well as a few affluent parts of the north such as Cheshire), and lower in urban areas in the West Midlands, North West, North East, and Yorkshire and the Humber.

The precise rankings of different areas would change though. For example, rather than having the highest revenues per person, Kensington and Chelsea would have only the ninth highest revenues per person, behind places such as Richmond-upon-Thames, Surrey, and Windsor and Maidenhead. Again, this reflects the fact that the very highest incomes would matter much less for a flat-rate local income tax that applied only to the basic rate band – having a generally affluent population matters more (and Kensington and Chelsea, in fact, has relatively more pockets of severe deprivation and low income than the places that take its place at the top of the revenue chart).

Despite differences in scale, in both instances variation in revenues is significant enough that large-scale redistribution of local income tax revenues between council areas would be required if the government wanted to avoid such a tax leading to large differences in funding and hence service provision. This redistributive system would have more work to do under a flat-rate local income tax that applied to all bands though. And as discussed in Section 3, the government would face a trade-off between the amount of redistribution it undertook and the strength of financial incentives councils would have to grow their local tax bases.

The nature of those financial incentives would differ somewhat depending on whether the local income tax applied to all tax bands or just the basic rate band. Councils would gain revenue from all increases in income under a local income tax applying to all tax bands; but would only gain from increases in income up to the higher rate threshold for a tax applying to the basic rate band only. This could mean more focus on increasing the employment and earnings of low and medium skilled people, and less focus on boosting the earnings of those with high earnings already.

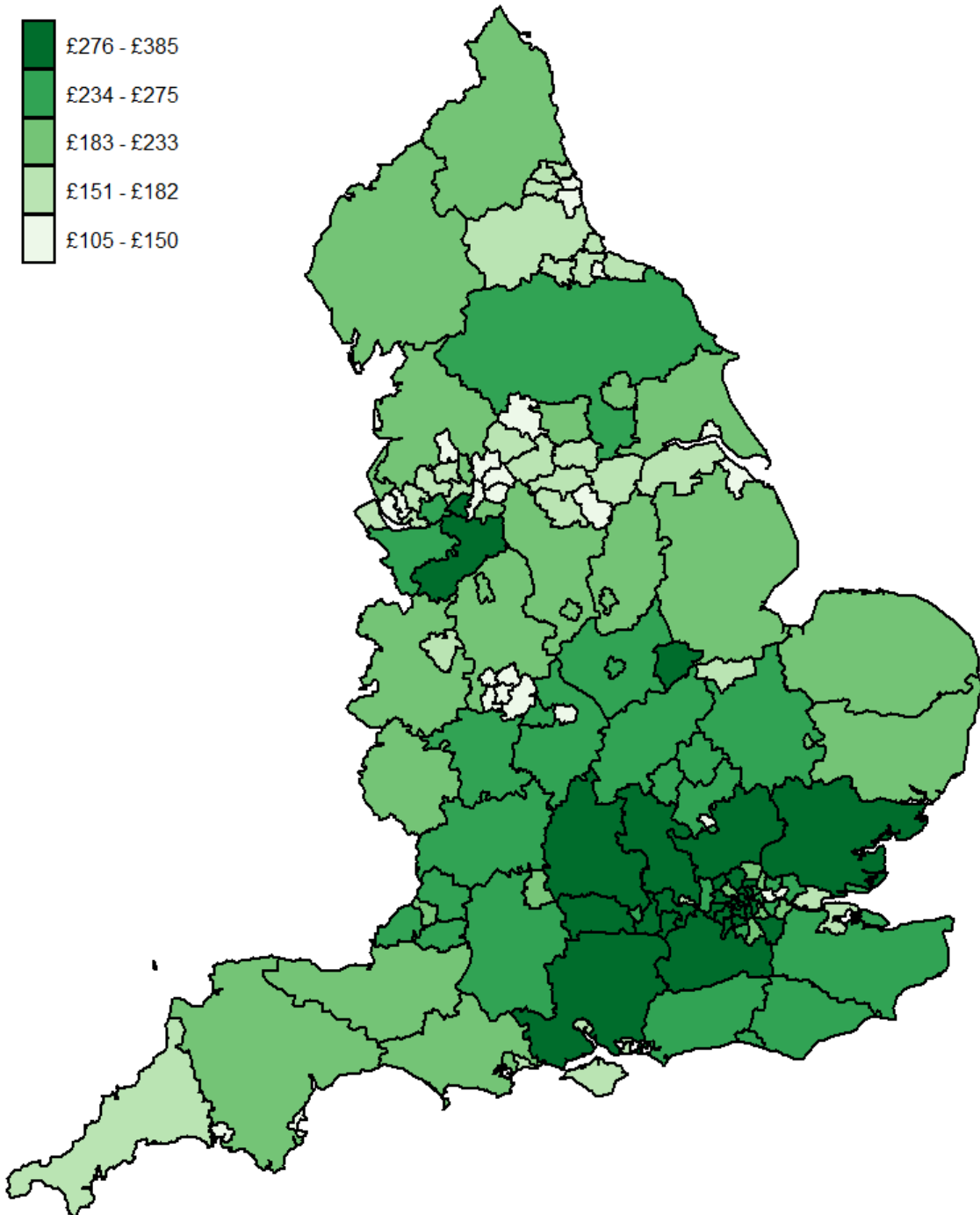
Figure 8.4. Revenues per person from a 3p local income tax on all bands, by upper-tier council area, 2018–19 terms



Note: Isles of Scilly and City of London excluded due to small sample sizes and imprecision of data.

Source: Authors' calculations based on data from HMRC (2018b) and ONS (2017b, 2019a). Further information on methodology available from the authors on request.

Figure 8.5. Revenues per person from a 3p local income tax on the basic rate band, by upper-tier council area, 2018-19 terms



Note: Isles of Scilly and City of London excluded due to small sample sizes and imprecision of data.

Source: Authors' calculations based on data from HMRC (2018b) and ONS (2017b, 2019a). Further information on methodology available from the authors on request.

Overall though, devolving a flat rate of income tax could bring many of the benefits of tax devolution (including local discretion on funding levels and financial incentives to expand the local tax base), while limiting the degree of revenue volatility and inequality, and tackling concerns about downward or upward pressure on the tax rates applied to those with the highest incomes.

9. Discussion and conclusions

So, is the time ripe for devolution of a wider range of tax powers and revenues to English local government?

Such devolution could bring a range of benefits, including:

- Giving local government control over additional sources of revenues could provide stronger financial incentives to councils to grow their local economies.
- Allowing for greater expression of local preferences, as voters in different areas would be more able to choose the particular balance between taxation and spending in their areas.

There is also the possibility tax devolution taxes could make it more politically feasible to raise taxes to meet rising public service demands and costs, because the political pain of doing so could be shared between local and national governments. If this is the case though, it touches on one of the unavoidable issues underlying discussion of tax devolution – if local government sees this as a way of increasing their funding, any tax devolution would have to mean either an overall increase in the national tax burden or a reduction in revenues for central government. This simple truth must not be lost in discussion.

There are also some clear downsides to further tax devolution. For one thing, it could, if badly implemented, create negative rather than positive incentives for councils. In particular, devolution of certain taxes could result in tax competition between areas and a ‘race to the bottom’, which would result in revenue erosion for all councils. Such a situation would also mean that councils would have little real control over their local tax rate, and thus compromise any ability that tax devolution might otherwise give them to better express local preferences over tax and spending.

It is also the case that tax devolution can create additional complexity in the tax system, both for the taxpayer and for the administrator, which for some taxes could mean devolution coming at a substantial cost. Furthermore, additional tax devolution would have to be accompanied either by increasingly complex equalisation arrangements between areas – redistributing revenues from those areas where newly devolved taxes raise a lot to those where they raise little – or by the possibility of wider funding gaps between different areas.

Of course, not all taxes are born equally – they have different effects on economic efficiency and equity, and vary in their ease-of-collection (both for taxpayers and tax authorities). In much the same way, not all taxes are equally suitable for devolution – the above considerations apply differently to different taxes. Much of this report has therefore focused on assessing the case for devolving a series of different taxes – and our findings are summarised in the table overleaf.

What is our assessment of different options?

	Benefits	Drawbacks
Council tax and business rates – more powers	Administratively straight-forward to increase power over rates, discounts, reliefs and exemptions.	<ul style="list-style-type: none"> • Councils' incentives would remain focused on property development rather than wider economic growth. • Giving councils powers over tax bands and revaluation would pose problems for revenue equalisation.
Stamp Duty Land Tax	Apportionment to councils administratively straight-forward.	<ul style="list-style-type: none"> • Revenues highly unequally distributed and very volatile. • An economically damaging tax that should be abolished, which is less likely if devolved.
Corporation Tax	Broaden the financial incentive of councils to include boosting profitability of local businesses.	<ul style="list-style-type: none"> • Difficult to apportion tax base (profits) between areas. • Relatively mobile tax base. • Business owners may not be local voters – accountability problem. • Unequally distributed and highly volatile.
VAT or sales tax	Broaden the financial incentive of councils to include boosting value-added of local businesses.	<ul style="list-style-type: none"> • Difficult to apportion tax base (value-added) between areas. • Relatively mobile tax base. • Shoppers may not be local voters – accountability problem.
Income tax	<ul style="list-style-type: none"> • Should be possible to apportion tax base (incomes) between areas – although not without admin and compliance costs. • Broaden the financial incentive of councils to include boosting income and employment of local residents. • Income taxpayers are local voters – helps accountability. 	<ul style="list-style-type: none"> • High income taxpayers may be relatively mobile. • High income taxpayers are unevenly distributed and have volatile incomes. • But both of these issues could be mitigated by only allowing councils to levy a flat rate, especially if restricted to the basic rate band.
Tourist accommodation tax	<ul style="list-style-type: none"> • Should be possible to apportion tax base (accommodation stays) between areas. • A financial incentive to support tourism industry. 	<ul style="list-style-type: none"> • Tourists unlikely to be local voters – accountability problem. • Would not raise much, and what would be raised would be very unequally distributed.

The amounts different taxes could raise would also vary significantly. Our estimates suggest:

- A flat-rate 3% local income tax could raise around £19.3 billion;

- A 3% local VAT on standard rated products and 0.75% local VAT on products subject to the reduced rate, £16.8 billion;
- All of stamp duty land tax, around £12 billion;
- A £5 per night tax overnight stays in tourist accommodation around £2.1 billion;
- Increases in Bands E–H council tax that match recent increases in Scotland, around £1 billion.

Taking all of this together, our view is that if the government wanted to devolve significant new tax revenues to local government in England, income tax would be the best option. Unlike a tourist tax or modest tinkering to council tax, a local income tax could provide significant sums – albeit only if either tax rates went up, or central government made do with less revenue itself following devolution.

A local income tax would also provide clear and broad incentives to local governments to grow their economies – in particular, to increase employment and earnings among their residents, whether that be via working in the local area or commuting to better paid jobs. Concerns regarding tax competition and the volatility and inequality of revenues could be partially addressed by devolving powers over only a flat-rate local income tax.

But there would still be significant challenges.

- Despite being less unequally distributed than the progressive national income tax, a flat-rate local income tax would raise significantly more in some areas than others. We estimate that revenues per person from a flat-rate tax across all tax bands would be more than six times higher in many richer parts of west London than in areas such as Hull and Blackpool. A system to redistribute revenues between councils would be required in order to avoid this translating into huge disparities in funding for local services.
- Income tax rates that varied across areas would be more complex for employers, taxpayers, and HMRC to deal with. Up-to-date records on where taxpayers live – which, at present, employers and HMRC do not always have – would be needed. Experience in Scotland also suggests particular issues around the Gift Aid scheme for charitable contributions, and certain types of pension contributions.

Ultimately there is a trade-off between the stronger financial incentives and greater local control and accountability that devolving income tax powers and revenues could bring, and the risk of bigger divergences in funding and public services and higher administration and compliance costs that such devolution would also entail.

Decisions would also have to be taken about which tier of local government (e.g. Combined Authorities, counties or districts) would have control over local income tax rates and revenues. On the one hand, devolution to lower tiers would allow for the greatest degree of local control. On the other hand, devolution to higher tiers would mean less volatile and unequal revenues, a smaller increase in administration and compliance costs, and potentially less scope for migration-induced distortions (it is easier to move small distances than it is larger distances because, e.g., one can keep the same job). Robust debate over how business rates revenues should be shared between upper-tier counties and lower-tier districts suggest that answering this question could be politically tricky.

Finally, it is worth returning to a point made right at the beginning of this report. Councils in England currently fund around 84% of spending over which they have significant control out of their existing council tax and business rates. And they are set to retain more of the business rates they collect, increasing this share further from April 2020.

In the short term then, there might be a practical challenge with devolving significant new tax revenues to local government.

Would that be simply transferring additional revenues from national to local government with no additional responsibilities? Local government would certainly like that, but it would mean less revenue for services funded by the national government such as healthcare and schools (or higher borrowing or increases in other taxes by the national government).

Would the government instead devolve tax revenues and powers but try to claw back some funding by imposing 'tariffs' on councils higher tax revenues? These tariffs could be based on tax rates and estimates of the tax base at the point of devolution – so if councils subsequently increase (or decrease) tax rates or see their tax base grow (or fall) they get to benefit (or lose) in terms of revenues. But such an approach would mean councils would be exposed to all the ups and downs of local tax revenues, while having to pay a fixed amount over to central government. This could be particularly financially risky.

Rather than taking either of these two approaches, two others seem more sensible.

First, the government could devolve additional spending responsibilities alongside the additional tax revenues. What these would be would have to be carefully considered – for instance, would they be suitable services to be managed and funded at a local level, and would expected demands and costs in future align with the expected growth in revenues available to councils. And the government would have a choice over whether the new spending responsibilities devolved matched the additional revenues, or whether it used devolution as a way of providing at least some additional funding to councils (or indeed, as a way of further reducing funding levels after accounting for the additional responsibilities).

Second, a more incremental approach to tax devolution could be adopted. Section 2 also highlighted that looking to the future, councils' revenues from council tax and business rates look highly unlikely to keep pace with the demand and cost for services such as adult social care. In particular, as the population ages, the gap between costs/demands and revenues is likely to grow over time. The government could therefore progressively devolve tax powers and revenues to councils over time, to help them meet those rising costs and demands. This could mean starting with a modest local income tax (e.g. between 0.5% and 1%), giving councils progressively more freedom to increase rates over time.

And of course, government could meet those rising costs and demands from increasing taxes at the national level – and transferring this to councils in the form of grants. Or it could hold down taxes locally and nationally but have to accept that the services councils could provide would degrade over time as costs and demands rise. Because ultimately tax devolution per se is not the answer to funding shortfalls – more funding is.

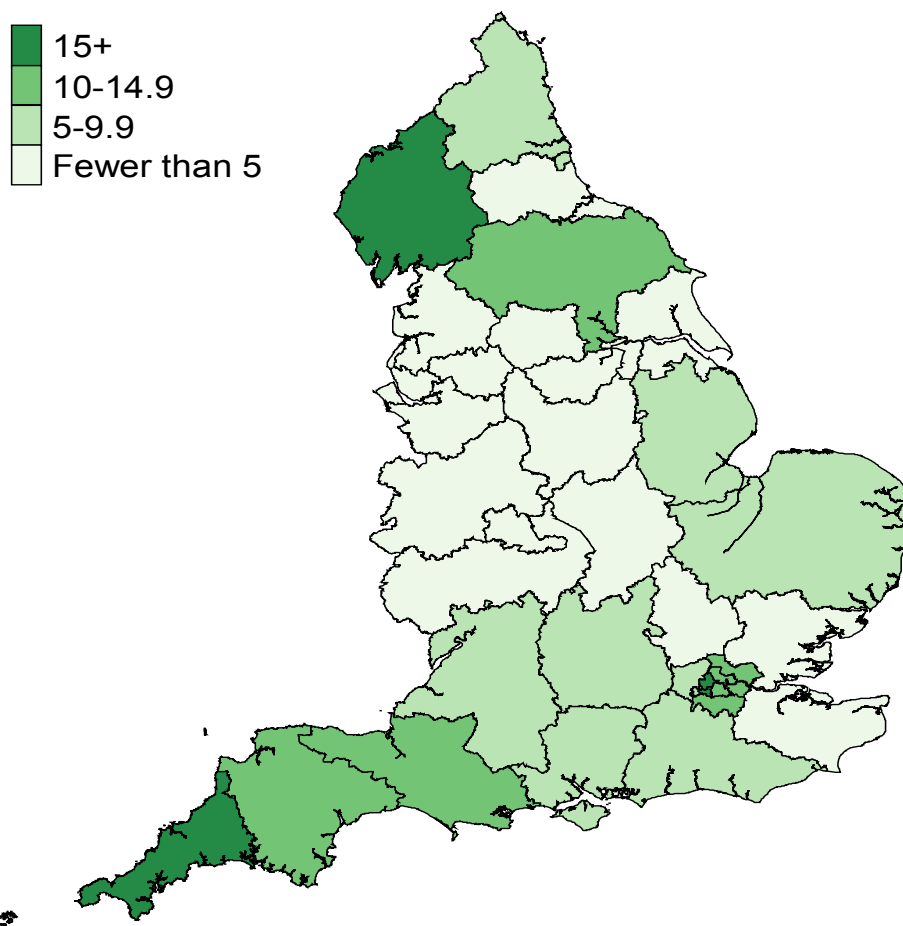
Appendix A: Tourism tax

As mentioned in the introduction to this report, a number of councils, especially those in cities, have discussed the idea of being able to levy a tax on overnight stays in tourist accommodation. Section 2 touched on the fact that such taxes are common in other countries – many major European cities levy some form of occupancy tax.

A.1. How are overnight stays distributed across the country?

Figure A.1 shows that the distribution of overnight stays in tourist accommodation (measured on a per resident basis) is fairly unequal across England – inner London, Cumbria and Cornwall have considerably higher levels (15+ nights per resident per year) in places such as the Midlands and more urban areas of the North West such as Merseyside and Greater Manchester (<5 nights per resident per year).

Figure A.1. Overnight stays per resident in 2016, by region



Sources: Overnight stays from Eurostat (2018a). Population data from Eurostat (2018b).

The data used here are at the regional level⁵¹ and it is likely that this masks even greater disparities between areas. For example, it is likely that overnight stays in Greater

⁵¹ In particular, it is at the level of NUTS 2 regions.

Manchester, which in 2016 had an average of four overnight stays for every resident, would be heavily weighted towards Manchester City council. The surrounding metropolitan boroughs are likely to have had considerably fewer overnight stays.

A.2. Assessing the case for a (local) tourism tax

In assessing the case for a tourism tax, we must consider both the merits of introducing such a tax at all, as well as whether it would make sense for it to be devolved to councils.

The case for a tourism tax

The argument often made to advocate for a tourism tax is that tourism imposes what economists call a negative externality – essentially a spill-over cost – on local areas (and on other tourists) through such channels as the need for increased street cleaning and maintenance, the extra congestion created, and the regulation of entertainment venues and popular attractions. This cost is one that is not priced into the cost to tourists of engaging in these activities. For example, tourists incur very little cost by littering. The most economically efficient solution to these problems might be to tax the costly activities directly, but this is clearly infeasible. Taxing overnight stays could thus be seen as an indirect way of doing so, if not the optimal way.

It is worth noting that from an economic efficiency perspective, introducing a tax to account for a negative externality does not actually imply that the revenues from such a tax should be retained locally. This is because the purpose of the tax would be to ensure that tourists faced the *full* cost of their visit (i.e. including any spill-over costs imposed on the local area) rather than to raise money to cover those costs.

One argument that could be made against the imposition of a tourism tax is that it might reduce the volume of tourism. Tourists are, at the margin, sensitive to prices and if a tax were to push up the price of visiting somewhere, this could reduce the numbers doing so. The exact magnitude of this effect is difficult to predict. Various studies have tried to estimate the elasticity, or responsiveness, of tourism to a country to the price of holidaying in that country, but this would clearly differ by area.⁵² Areas with unique attractions, such as London, might expect that the volume of tourism would be less sensitive to a small tourism tax than other areas, as tourists might see London as having fewer close substitutes.

A tourism tax would also throw up certain questions of administration and compliance. For example, on the one hand, if a way were not found to levy it on the more informal sector, such as AirBnB and other short-term lettings, this could create a distortion of demand away from the formal sector. On the other hand, finding a way to ensure compliance across the whole sector could be costly, which would be of particular concern when weighed against the relatively small amount of revenues likely to be raised by this tax, as shown below. Of course, there are ways in which this could be addressed – some cities, such as Amsterdam, have made agreements with AirBnB such that AirBnB collects and pays the tourism tax on behalf of its hosts. Nevertheless, other informal lettings may still pose a problem.

⁵² For example, Blake and Cortes-Jimenez (2007) found a price elasticity of demand of -0.61 , implying that a 1% increase in the cost of holidaying in the UK results in a 0.61% fall in demand.

Would it make sense as a local tax?

Clearly, unlike some of the taxes considered in this report, **a tourism tax would be relatively straightforward to apportion locally**. Also, the externalities caused by tourism are likely to differ between areas, and thus it may in fact make more sense for a tax targeted at these externalities to be set locally. Councils may have better information about the impact of tourism in their areas and it could be politically difficult for there to be substantial variation across areas if the tax were set centrally. Furthermore, as mentioned above, the sensitivity of tourism demand to changes in price is likely to differ between areas, and this might affect the rates councils in different areas would prefer to set.

However, **the revenues likely to be raised from a tourism tax would be far from evenly distributed across areas**, as shown in Figure A.1. London, for example, accounts for around 30% of all overnight stays in England. Councils with higher levels of tourism might argue that the higher levels of revenue they could raise would reflect the costs tourism imposes on them. However, as discussed above, revenues from a tax aimed at ‘correcting’ for a negative externality do not have to be spent on the specific associated costs for an economically efficient outcome to be reached. Allowing councils to retain the proceeds from a tourism tax would either necessitate some form of equalisation or would mean accepting that it would imply different levels of funding for different areas.

Whilst not an argument against the introduction of a tourism tax per se, it is worth noting that if councils see a tourism tax as a way of raising substantial amounts of revenues, they will be disappointed. Table A.1 shows how much the tax would raise when set at different levels, assuming it did not deter any tourists from visiting. If, for example, it was levied at £5 per overnight stay everywhere in England, it would raise just over £2bn nationally, or £38 per person. This is many times smaller than the £19bn that would be raised from a 3p income tax on all bands, or the £12bn that would be raised from a 3p tax on the basic rate. In fact, a £5 tax would be high relative to most European cities. In practice, it is likely that revenues would tend to be lower than this – Bath council last year discussed the possibility of a £1 tax. Such a tax would raise only £420m nationally, which, for example, would include less than £16m for all five upper-tier areas in the Gloucestershire, Wiltshire and Bristol/Bath area, or £6 per resident. A £1 ‘tourism tax’ would thus raise 28 times less than a 3p surcharge on the basic rate of income tax. Nevertheless, at the margin, councils might still see revenues from a tourism tax as a useful source of extra funds.

Table A.1. Revenues from a tax on overnight stays

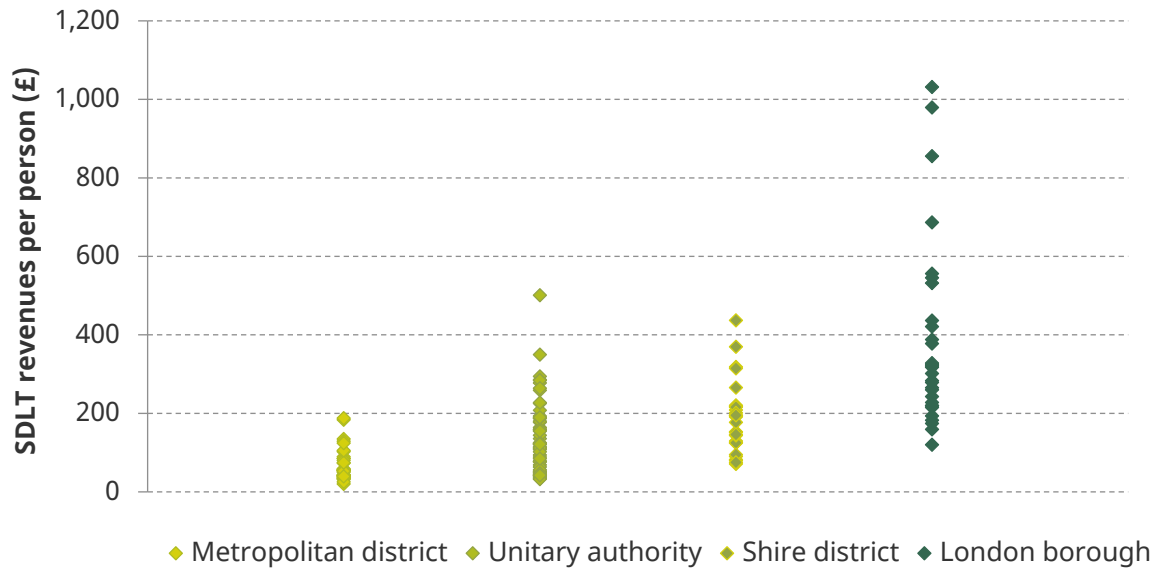
Tax level	Total revenues raised	Total revenues raised per capita
£1	£420m	£8
£2	£840m	£15
£3	£1,250m	£23
£4	£1,670m	£30
£5	£2,090m	£38

Notes: These figures use tourism data for 2016, but revenue estimates have been updated by nominal GDP growth since then.

Source: As Figure A.1, and nominal GDP from OBR (2019b).

Appendix B: Additional figures

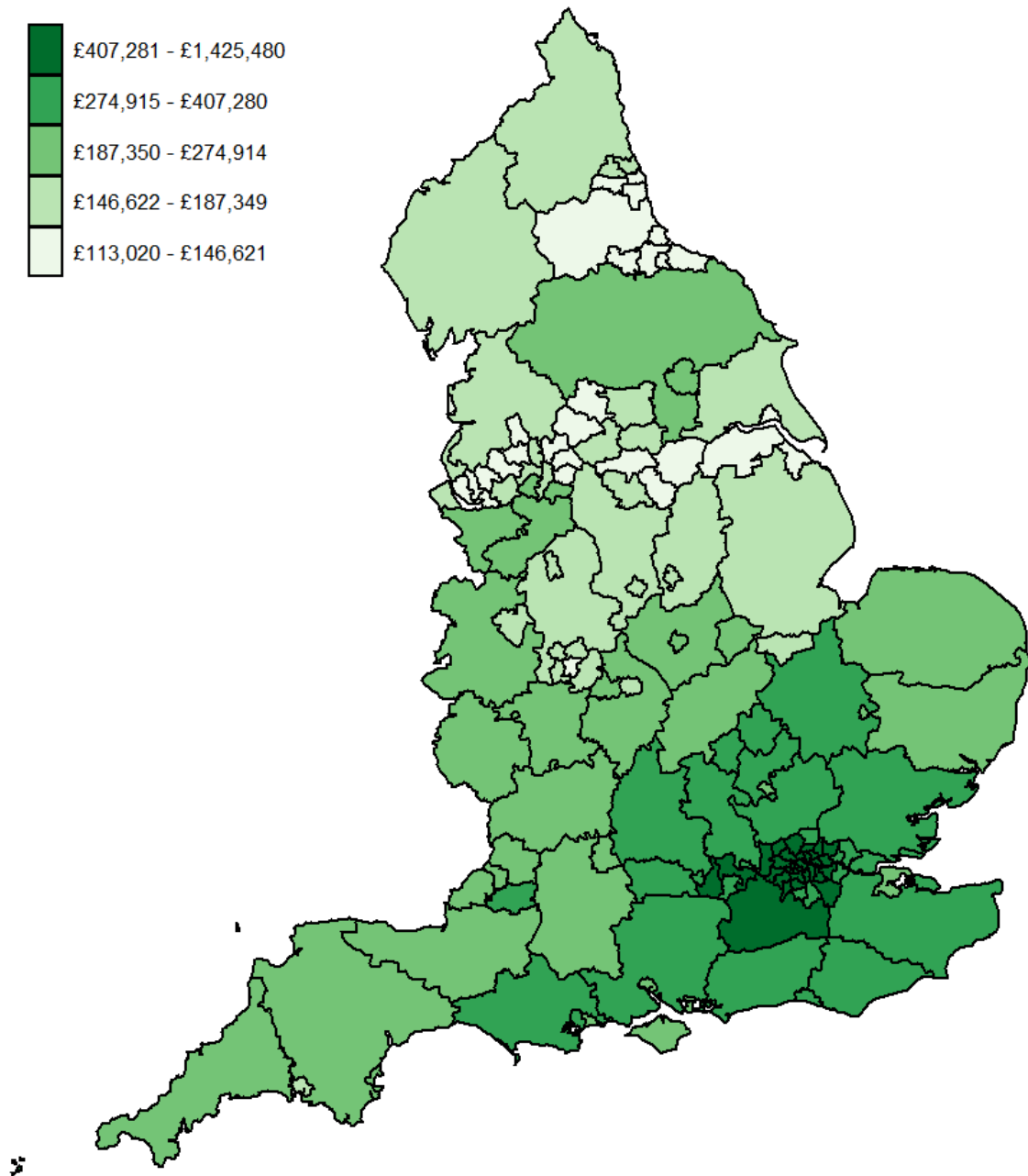
Figure B.1. SDLT revenues per person (2018–19 £), by upper-tier council area, 2017–18



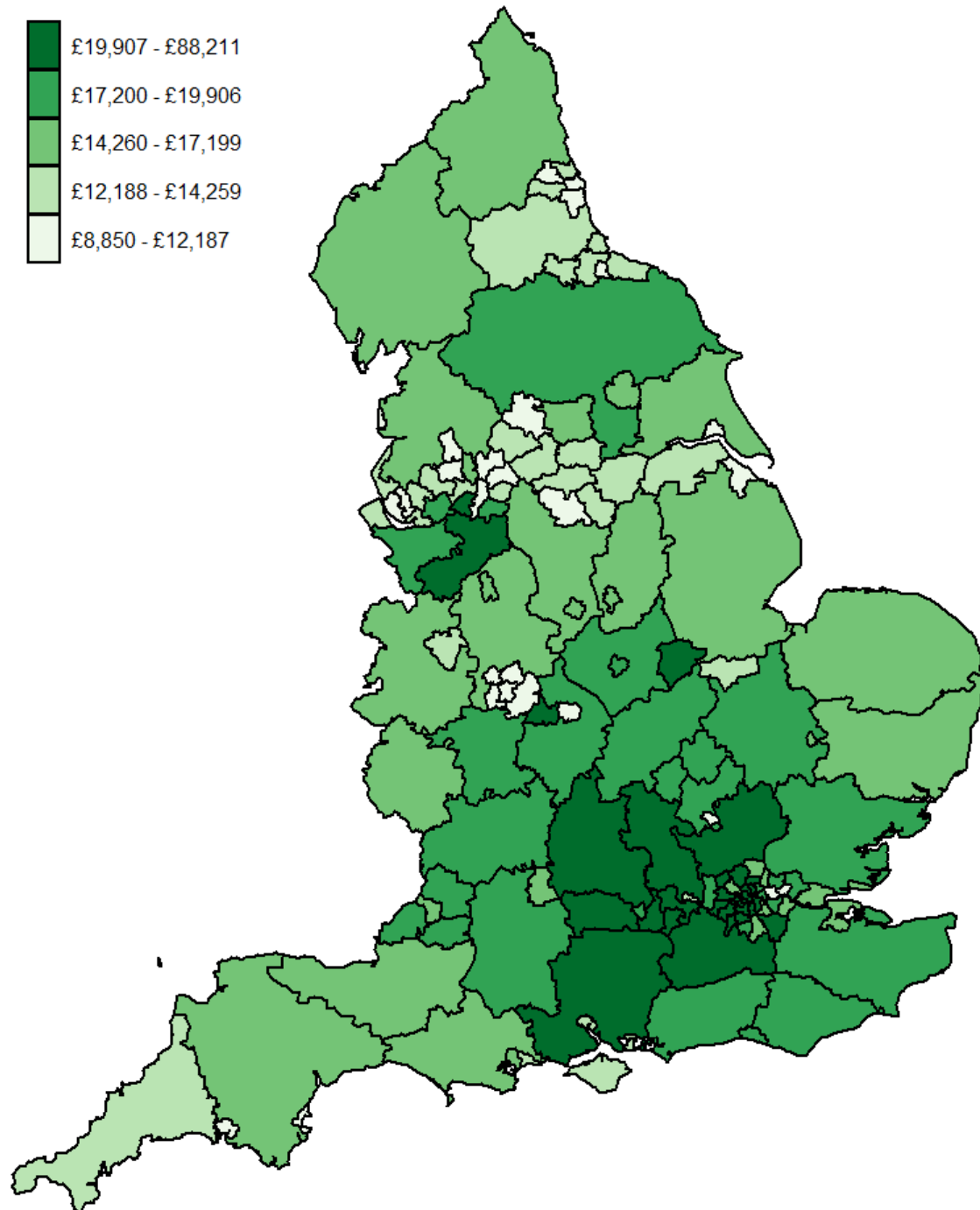
Note: Isles of Scilly excluded due to lack of data. Westminster, Kensington and Chelsea, and the City of London are excluded for scaling purposes.

Source: Authors' calculations based on data from HMRC (2018) and ONS (2019).

Figure B.2. Median price paid on residential property transactions (2018–19 £), by upper-tier council area, 2017–18



Source: Authors' calculations based on data from ONS (2018c).

Figure B.3. Taxable income per person (2018–19 £), by upper-tier council area, 2015–16

Note: Isles of Scilly and City of London excluded due to small sample sizes and imprecision of data.

Source: Authors' calculations based on data from HMRC (2018b) and ONS (2019a).

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