

BRIEFING

TAX, SPEND AND NORTHERN PRODUCTIVITY

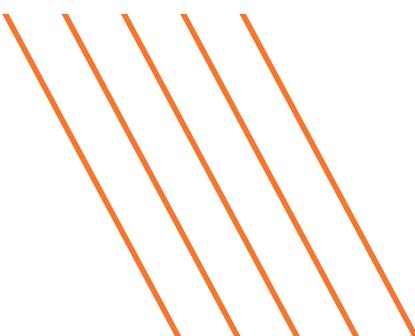
A REGIONAL ANALYSIS OF HOUSEHOLD
INCOME, TAXATION AND PUBLIC SPENDING

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IPPR North specialises in regional economics, localism and community policy. Our approach is collaborative and we benefit from extensive sub-national networks, regional associates, and a strong track record of engaging with policymakers at regional, sub-regional and local levels.

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IDEAS to
CHANGE POLICY

1. INTRODUCTION AND CONTEXT

This briefing paper explores recently published figures on income, taxes and benefits, and the important differences between households across the country (ONS 2015a). It places this analysis in the context of the spatial imbalance in economic growth and transport infrastructure investment in the UK.

Public expenditure, taxation and productivity are closely related, and they interact not just with households, businesses and nations, but regions' economies too. In the best of circumstances, public investment – in human capital or in transport infrastructure – can underpin long-term local economic growth, higher incomes, and higher tax revenue to support vital public services and social security spending. In less ideal circumstances, public expenditure *reacts* to low growth and low incomes, and a region draws on more public spending than it generates in taxation.

Given that we are currently facing the dual challenge of deficit reduction and poor productivity, it is therefore crucial that the north of England's productive capacity is fully realised. The UK's economic imbalances are far more complex than just a North–South divide, but there is a stark economic disparity between London and the rest of the country. To make a few of many possible comparisons: compared to the national average, London is 29.2 per cent more productive, annual wages are 29.0 per cent higher, and house prices are 85.3 per cent higher (ONS 2015b, 2014a, 2015c). That said, while the North as a whole is generally less prosperous, it contains within it many flourishing local economies, and with the right investments could go some way towards meeting its significant potential (IPPR North and NEFC 2012).

London's economic dominance has inevitable consequences for taxation and for expenditure on public services. A (broadly) progressive tax system by definition means that people with higher incomes will tend to pay more tax. So because London is more productive, and Londoners are better paid than the rest of the country, an average household in London will tend to contribute more to the national pot than those in other regions. This was confirmed by recent figures which showed that the average household in London contributed 23.8 per cent more in taxation than the national average (ONS 2015a).

The UK is clearly somewhat reliant on London to drive national economic growth and contribute proportionally more taxation. However, policy perpetuates and even exacerbates this reliance by awarding London yet more public spending, while other parts of the country, and the north of England in particular, have experienced many years of underinvestment.

However, this is only part of the story. To give a full illustration of the important relationship between public expenditure, taxation and productivity, this briefing draws comparisons between London, the North and the country as a whole, and demonstrates the following points.

- First, while this tax and spend pattern is a natural consequence of a progressive tax system in an imbalanced economy, the imbalance itself is not entirely natural. Rather, it is in part a result of policy choices. Looking historically at transport infrastructure investment in the capital, for example, shows how policy can underpin ever-higher productivity,

but also how it reinforces the economic imbalance and, therefore, gaps in wages and taxation.

- Second, looking at the data in detail reveals that beneath the headline figures there are also big regional differences in the types of taxes paid, and in the different cash benefits and public services that households benefit from.

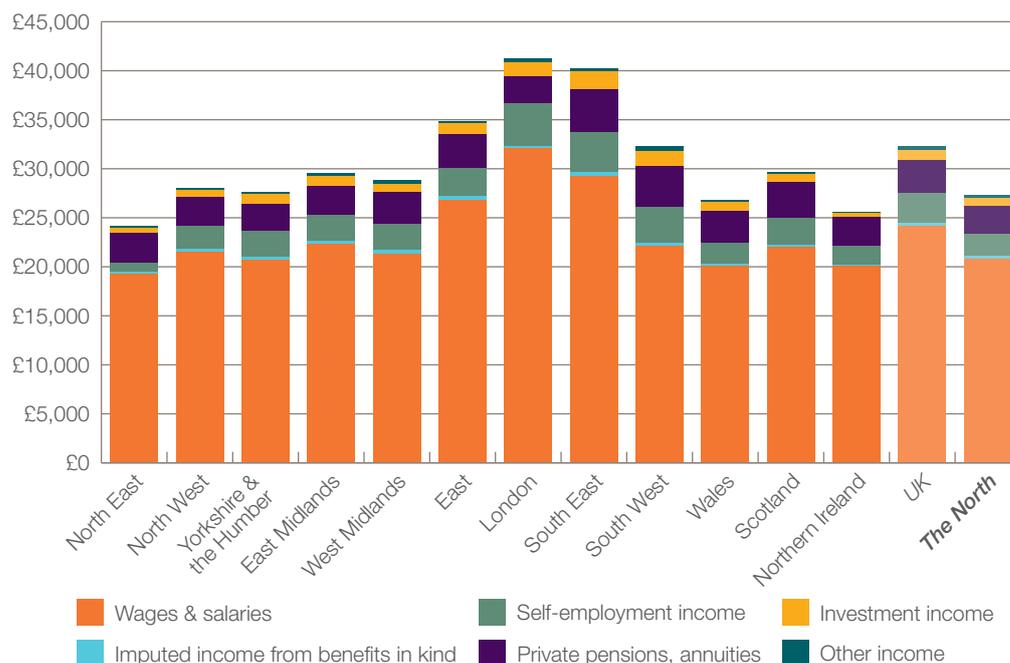
2. ANALYSIS

Income from wages and investments

Original income (which includes wages and salaries as well as pensions and other source of income) is far higher in London (ONS 2015a).¹ In the capital, the average household receives £41,000 in original income – that’s £9,000 more than the national average, £14,000 more than in the North as a whole, and £17,000 more than the average in the North East (where original income is lowest in the country). The main reason for this is that wages – which make up 75.0 per cent of original income – are £8,000 higher in London than they are nationally, although income from self-employment and investment are also higher there. Only income from private pensions and annuities is lower in the capital.

Figure 1.1

Average annual original income per household, by region, 2011/12–2013/14



Source: ONS 2015a

Taxes

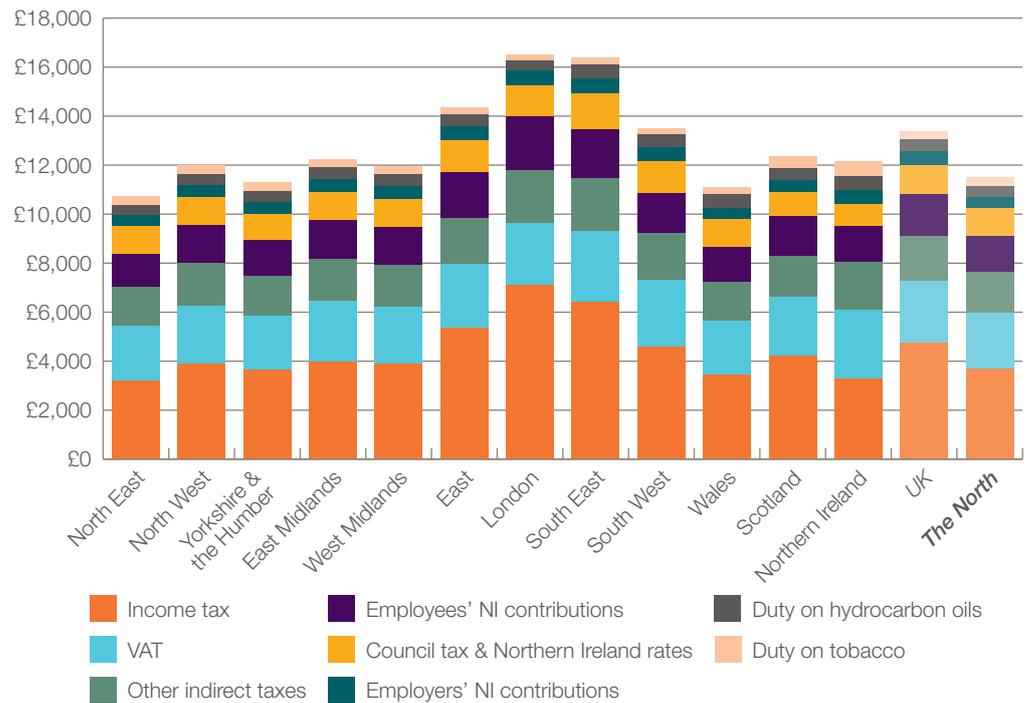
The concentration of high-income households in London means that average income tax and national insurance contributions levels are higher there too. The average London household will pay £2,400 more in income tax than the national average, and £3,400 more than a household in the North. Similarly, the average London household will pay £460 more in national insurance contributions than the national average, and £680 more than in the North.

¹ All data in this chapter is taken from ONS 2015a, unless stated otherwise.

The pattern with respect to indirect taxes is more complex. Households in the South East, South West and Northern Ireland tend to contribute more, due largely to higher contributions in VAT. In contrast, London households tend to pay more in stamp duty, while paying significantly less in taxes on hydrocarbon oils (that is, fuel duty).

Figure 1.2

Average direct and indirect taxes per household by region 2011/12–2013/14



Source: ONS 2015a

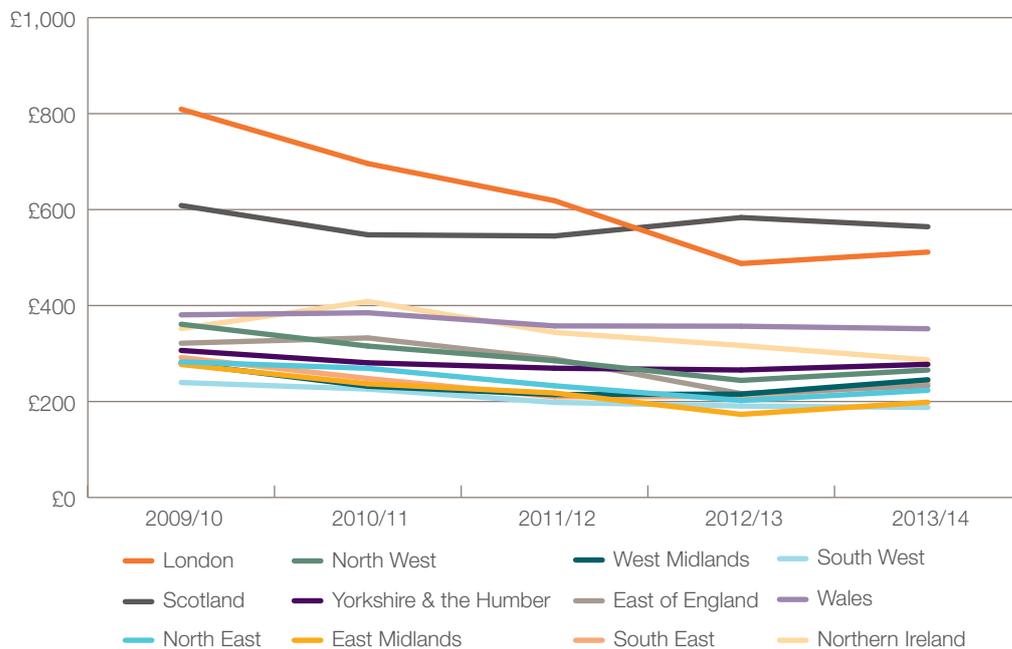
Transport infrastructure and the economy

The north of England has attracted disproportionately low levels of government investment in transport infrastructure, both in relation to London (as set out in figure 1.4 below) and, more importantly, relative to comparator regions in continental Europe. This disparity looks set to continue: planned government expenditure on transport from 2014/15 onwards remains heavily skewed towards London, as figure 1.4 illustrates.

Also, as figure 1.5 shows, London and the devolved nations spend proportionally more on supporting their economies through public spending. Wales, Scotland, Northern Ireland and London all spend more on economic affairs and skills; this includes expenditure on transport, tertiary education, agriculture, forestry and fishing.

Figure 1.3

Government expenditure on transport per capita by English region, 2009/10–2013/14, in real terms (2013/14 prices)



Source: Cox and Raikes 2015: 6

Figure 1.4

Total planned spend per resident on transport infrastructure from 2014/15 onwards, in real terms (2013/14 prices)*

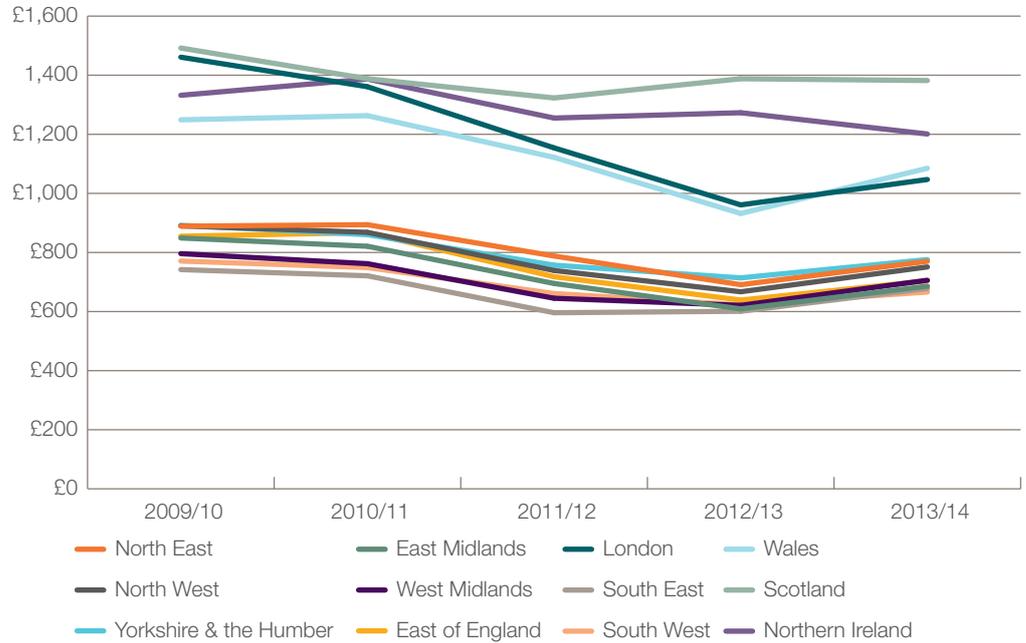


Cox and Raikes 2015: 7

*Note: figures only include projects in which public money is involved (public-private or public only).

Figure 1.5

Government expenditure on economic affairs and skills per capita by English region, 2009/10–2013/14, in real terms (2013/14 prices)



Source: author's calculations using HMT 2014a and ONS 2014b

*Note: The definition of 'economic affairs and skills' is discussed further in Cox E, Henderson G and Raikes L (2014) *Rebalancing the books: How to make the 2015 spending review work for all of Britain*, IPPR North. <http://www.ippr.org/publications/rebalancing-the-books-how-to-make-the-2015-spending-review-work-for-all-of-britain>

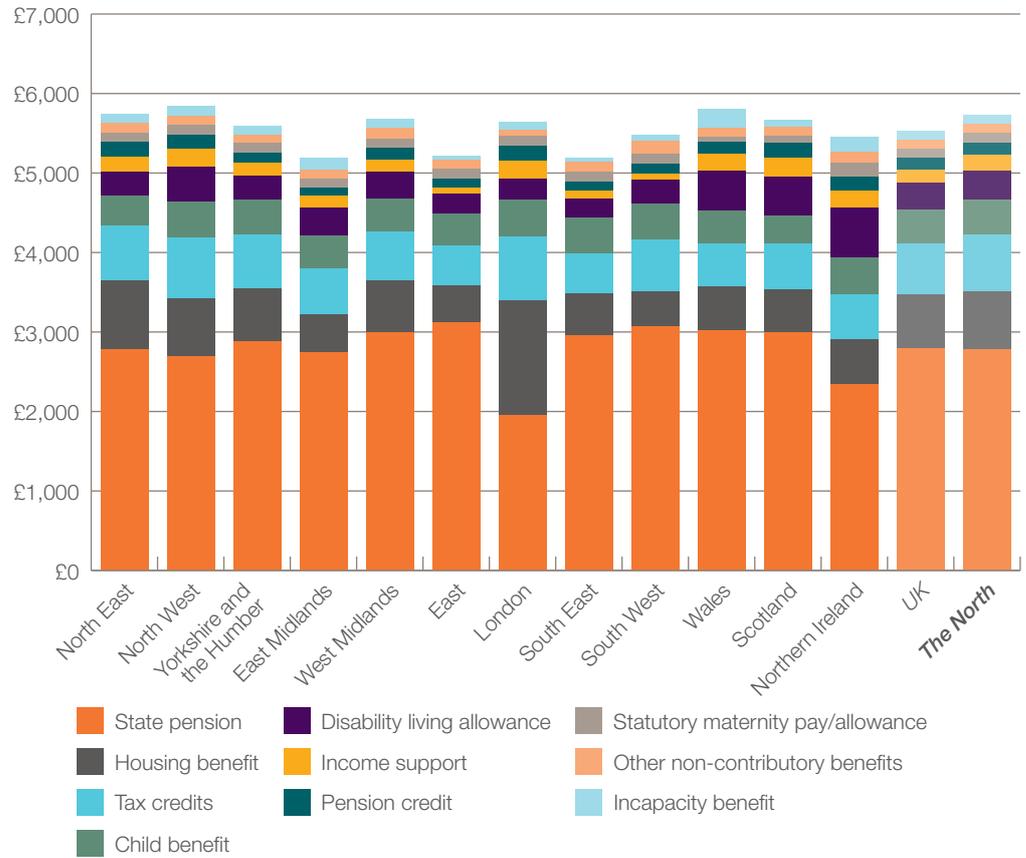
Cash benefits

Much of the disparity in the cash benefit income of households in different parts of the country is caused by housing benefit and the state pension. On average, London households receive £840 less from the state pension than the national average, and £830 less than the average in the North (London has a smaller proportion of over-65s than any other region). However, housing benefit expenditure is £760 more in London than the national average, and £720 more than in the North.

If the state pension is removed from the equation, London is significantly *more* dependent on cash benefits than the UK average. Much of this is due to housing benefit income, but London households also receive more in child benefit and tax credits than those in any other region. It might be expected that differing unemployment rates across the country would be *the* major factor in determining total cash benefits expenditure – but, while on average households in London received less in jobseeker's allowance than those in the North, they nevertheless received more than the UK average (despite the strength of the capital's economy).

Figure 1.6

Average cash benefit income per household, by region, 2011/12–2013/14



Source: ONS 2015a

Public services

In addition to spending on transport infrastructure, housing benefit, tax credits and child benefit, the average London household receives more ‘benefits in kind’ (that is, public services), particularly in the form of education, and subsidies for bus and rail travel. Compared to the country as a whole, London households receive £668 more value from public services:

- £590 more on education²
- £90 more on bus travel subsidy
- £50 more on rail travel subsidy
- £30 more on housing subsidy³
- £20 more on school meals and Healthy Start vouchers
- £100 less on the NHS.

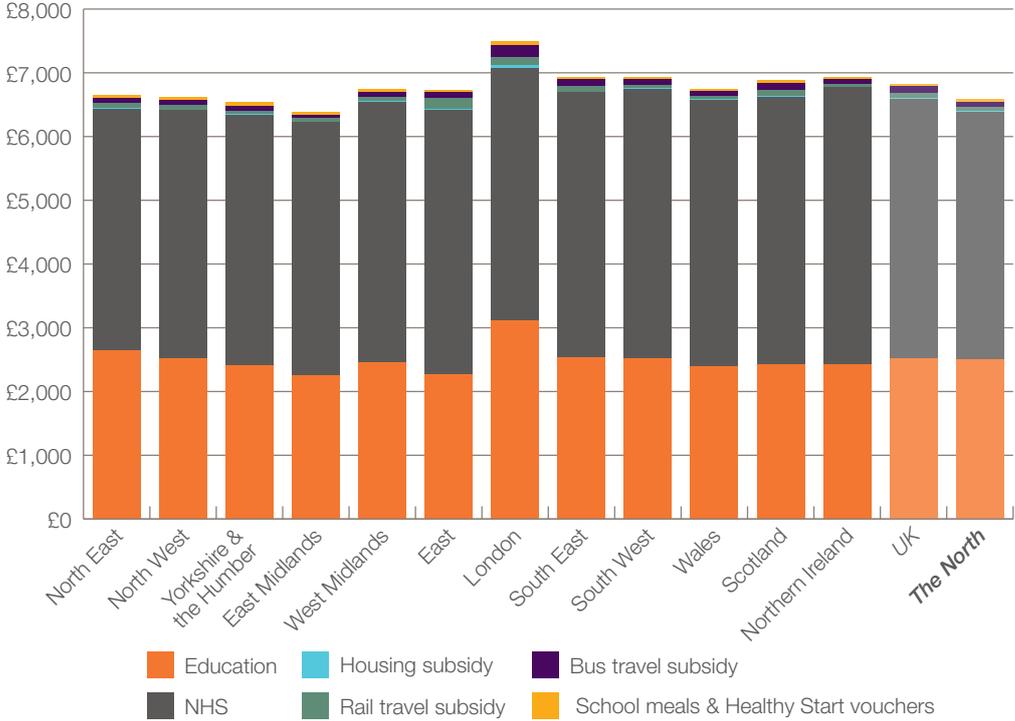
² The school funding formula is complex, but this disparity may be due to the London weighting in teachers’ salaries, and/or the additional funding that more deprived pupils attract.

³ This includes ‘the contribution from central Government to the housing revenue accounts of local authorities and grants paid to Scottish Homes, the NIHE, housing associations and registered social landlords’. Source: http://www.ons.gov.uk/ons/dcp171766_407902.pdf

In total, the average London household gets £899 more value from services than the average household in the North:

- £610 more on education
- £110 more on bus travel subsidy
- £70 more on rail travel subsidy
- £40 more on housing subsidy
- £60 more on school meals and Healthy Start vouchers
- £80 more on the NHS.

Figure 1.7
Average 'benefits in kind' per household, by region, 2011/12–2013/14



Source: ONS 2015a

3. COMMENT

The regional tax and spend patterns in the UK are predictable. As in any country with a progressive tax system, areas in the UK with more high-income households tend to contribute more in taxation than those with more lower-income households. However, the UK is unlike most other developed countries in that our economy is so imbalanced – an imbalance exacerbated by our centralised political system.

While it is both natural and broadly desirable for an area of high income and high productivity to contribute proportionally more in tax, what is less natural is for that area to also attract a disproportionate amount of transport infrastructure expenditure.

Taking all households' income, taxes, benefits and benefits-in-kind into account, a household in the north of England is on average £9,639 poorer than one in London. By far the biggest factor in this disparity is that higher income households are concentrated in London; the capital therefore contributes more in direct taxes.

While the higher income of households in London, and their resultant higher tax contribution, is largely due to the role that London plays both nationally and globally, it is also underpinned by transport infrastructure investment, which has been disproportionately concentrated on the capital. While income from cash benefits is on average lower in London than in the North, it is still above the national average, and the picture is far more complex than one of a dependent North propped up by a productive capital. The primary reason for the disparity in cash benefits is higher household income from the state pension outside of London. However, households in the capital tend to receive more income from tax credits and housing benefit than those elsewhere, and Londoners also benefit from public services to a greater degree than the rest of the country.

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