What is dynamic tax modelling?

TaxPayers'
Alliance

What is a tax model?

When tax changes are proposed and put through an economic model to assess their impact.

What is a static model?

A static model tends to only focus on changes to tax revenue for the Treasury, without considering the impact on the wider economy. A static model usually finds that a tax cut will result in reduced tax revenues.

What is a dynamic model?

A dynamic model takes into consideration how tax changes may affect behaviour and incentives. For instance, a tax cut might mean that a family decides to buy a new car. Or it might mean that a business decides to invest in new machinery, making it more efficient. This means more tax-generating activity, which can nullify some – or all – of the revenue loss from a tax cut.
A dynamic model might find that a tax cut could stimulate growth and therefore generate tax revenue elsewhere.

Dynamic tax modelling works for the individual, for business and the nation's finances

Our objective

To produce a dynamic model of the UK tax system to inform the public about the impact of tax changes.

In the coming months, we will create a new dynamic tax model that challenges the Treasury's conventional wisdom that lower taxes mean reduced revenues.

This will lead to a healthier tax debate, looking not just at government revenues but the wider economic repercussions. We can help parliamentarians, policy makers, journalists and taxpayers better understand tax proposals and how they affect the UK economy.

Our major new project will be divided into four phases:

Phase 1: Developing the pilot model

A pilot model will be created to show the effects of tax changes on the medium-term growth rate of GDP, investment and wages. This phase will include:

- a review of background research
- identifying and collecting data on key parameters
- development of the model

Phase 2: Finalising the core model

This crucial next step would seek to stress test the work in phase 1 and ensure this model is ready to be used for a wider purpose. It includes:

- checking for user-friendliness and accuracy
- publishing the finished model for both internal and external use

Phase 3: Putting the core model to use

We will use the core model in our day-to-day work, including to:

- analyse major fiscal events like the Budget and other proposed changes to tax rates
- strengthen our own research programme
- enhance our reactive commentary
- support live events and broadcast appearances
- share our findings across the country through our digital and ground campaigns

Our dynamic model won't just be for the TPA. We will encourage others to use the model as well. Other organisations – including government departments – will be able to use it to see the benefits of a dynamic, rather than static, approach to assessing tax changes.

Our dynamic model can be presented and demonstrated to politicians during fiscal debates, or explained to commentators looking to understand the impact of Budget announcements.
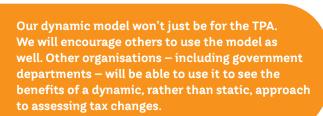
Phase 4: Extensions to the core model

Later extensions to our core model can add varying levels of analysis, both to take on more economic variables and to keep the model up to date. This could include building extensions to:

- distinguish between taxation and benefits
- analyse how Budget policy affects unemployment
- consider how Budget decisions affect inflation

> *Mapping out potential tax changes using dynamic scoring gives us a much clearer and more accurate picture of how policy impacts families and businesses in the real world. In the US, sophisticated models like those proposed by the TPA helped us to make more informed decisions and deliver better bang for the taxpayers' buck. It's important that those who believe in a free and open economy back projects like this which will help politicians go for growth.*

**Tyler Goodspeed,
former Chairman of the
Council of Economic Advisers to the
President of the United States of America**

It's time to invest

The Chancellor's delay on corporation tax hikes to 2023 offers the TaxPayers' Alliance a unique opportunity to challenge the prevailing narrative that taxes must go up. With over £5,000 borrowed for every person in the country during the pandemic, we must protect the next generation and make a positive case for growth. Investing today in our dynamic tax model will ensure this.

> *Dynamic tax scoring is an area that commands real interest in parliament, and has the potential to deliver real utility for the Treasury. It deserves serious consideration.*
>
> **Rt Hon Sajid Javid MP,**
> **former Chancellor of the Exchequer**

> *Fiscal policy matters – for businesses, for jobs, for ordinary people. This is a valuable piece of work for the TPA to take on and dynamic modelling will, I hope, become a normal part of Westminster policymaking in the years to come.*
>
> **Andy Silvester,**
> **Editor, *City A.M.***

> *The response to the pandemic has blown a crater in the public finances. As ever, the response from too many politicians and commentators is that taxes must go up to fill the coffers. But good economists know the damage that can be caused by higher taxes. We must go for growth – and a new economic model that shows the real life response to tax changes will help determine the best fiscal policies to do that.*
>
> **Allister Heath,**
> **Editor, *The Sunday Telegraph***

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