

The TaxPayers' Alliance was launched by Matthew Elliott and Andrew Allum in early 2004 to speak for ordinary taxpayers fed up with government waste, increasing taxation, and a lack of transparency in all levels of government.

No party was standing up for taxpayers and nearly all politicians were committed to bigger government, higher spending and secretive deals behind closed doors.

The TaxPayers' Alliance sought to challenge this status quo. The United States, Germany and Italy all had groups dedicated to defending taxpayers. The TaxPayers' Alliance was set up to ensure that British taxpayers were no longer ignored by politicians.

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Executive summary

- The UK economy has performed reasonably well in recent years after a period of sluggish growth following the great recession. Unemployment is at its lowest point since early 1975. However, wage growth has remained slow, and many households are struggling to cope with the cost of living.
- In response to this, a consensus has emerged among the major political parties that the government should intervene more to help those on modest incomes.
- However, the evidence reveals that far from ameliorating the financial burden placed on households, government policies are currently compounding it.
- The common agriculture policy of the European Union has resulted in food prices being higher for consumers in the UK due to tariffs, subsidies, and overly restrictive regulations.
- Stamp duty and planning regulations mean that buying a home is now unaffordable for many people, while expensive rents are taking up a significant proportion of take-home pay.
- Increases to the minimum wage have led to higher prices for consumers in restaurants and hotels and decreased the employment opportunities of low skilled workers.
- Despite being subsidised by taxpayers, childcare costs in the UK are very high compared to other major economies due to regulations.
- Energy bills are high in the UK due to 'green' taxes to pay for renewable energy subsidies.
- Transport is expensive in the UK due to fuel duty and government intervention in the railways.
- The UK has one of the highest rates of air passenger duty making holidays more expensive.
- Pigouvian taxes on tobacco and alcohol consumption increases their price and impacts those on low incomes the most. The revenue raised from taxes on alcohol and tobacco far exceed their externalities.
- Income tax, national insurance contributions, and council tax all take a sizeable amount of money away from households.
- VAT increases the price of goods significantly which results in further pressure being placed on household budgets.

Headline figures

Housing

The average monthly rental price in the UK is £350 a month more than the European average.

Childcare

If regulations were relaxed and followed a model similar to that in Sweden, the average UK household which uses childcare could save up to £7,732.20 each year on childcare costs.

Energy

9 per cent of the average household's annual bill is a result of 'green' taxes. This amounts to £105 each year.

Transport

As a result of duties on fuel, motorists in the UK would be paying 77.08 pence more per litre for petrol and 77.20 pence more per litre for diesel.

Holidays

For flights from the UK, air passenger duty (APD) is levied. For short haul flights this is £13 which is 43 per cent higher than the next highest equivalent tax in Greece (£9). APD is nearly twice as high as the rate applicable in Italy (£6.80), more than two times the rate in Germany (£5.70), and more than three times the rate in France (£4.20).

For long haul flights, UK APD is £75. This is more than twice the level of the next highest tax for long haul journeys, which is levied by Germany (£32). It is more than five times the rate levied by France (£14.50), and more than ten times that levied by Italy (£6.80).

Smoking

Tobacco duty results in cigarettes being much more expensive. For example, a duty is levied at 16.5 per cent of the retail price plus £207.99 per 1,000 cigarettes. Therefore, for a packet of 20 cigarettes that amounts to £4.15 plus the 16.5 per cent.

Alcohol

Alcohol duty means that a pint of beer is 52 pence more expensive and a pint of cider is 22 pence more expensive. As for wine, a 750 millilitre bottle is £2.08 more expensive and a bottle of sparkling wine is £2.67 more expensive. A 70 centilitre bottle of whisky is £7.74 more expensive due to alcohol duty. The average household spends 1 per cent of their disposable income on alcohol duty, which is equivalent to £263 each year.

Direct taxation

In the financial year ending 2016, households paid on average £7,800 per year in direct taxes, equivalent to 18.7 per cent of their gross income.

VAT

The average household spends 8.4 per cent of their disposable income on VAT. This amounts to £2,209.20 on VAT each year.

Introduction

An examination of the socio-economic history of the United Kingdom reveals an upward trend in terms of standard of living over the centuries.¹ However, despite this increase in living standards, many people, especially those on low and middle incomes, either find themselves struggling to make ends meet.

In light of this, the main political parties have proposed policies of greater government intervention to ease the burden on low and middle earners.

For example, when Theresa May became prime minister in July 2016, she pledged that under her, the government would help those who were 'just about managing'.² Moreover, 'the good that government can do' was the repeated refrain of her Conservative conference speech in September 2016.³ This was followed by a general election manifesto in June 2017 which contained a raft of policies which involved the government intervening to help improve the lives of those on modest incomes.⁴

The Liberal Democrats and Labour also had a plethora of policies advocating for greater action by the government in order to improve the lives of those on low and middle incomes.^{5 6} There is now political consensus: the government should intervene in order to improve the standard of living of low and middle earners.

This paper aims to challenge this consensus. It will first take a general survey of the standard of living in the UK before focussing on ten specific areas which have a significant impact on household budgets and the role that government intervention plays.

The paper will argue that rather than ameliorating conditions for those on low and middle incomes, government intervention frequently exacerbates the hardships that they are facing.

¹ Floud, R., & Johnson, P., eds. *The Cambridge Economic History of Modern Britain* (Cambridge: CUP, 2004).

² May, T., *Statement from the new Prime Minister Theresa May*, 13 July 2016, <https://www.gov.uk/government/speeches/statement-from-the-new-prime-minister-theresa-may>.

³ May, T., *Prime Minister: the good that Government can do*, 5 October 2016, <http://press.conservatives.com/post/151378268295/prime-minister-the-good-that-government-can-do>.

⁴ *The Conservative Party General Election Manifesto 2017*, 18 May 2017, <https://www.conservatives.com/manifesto>.

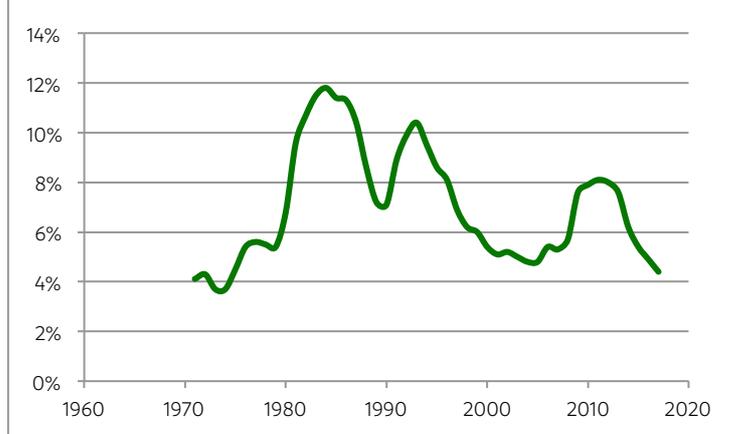
⁵ *The Liberal Democrats General Election Manifesto 2017*, 17 May 2017, <https://www.libdems.org.uk/manifesto>.

⁶ *The Labour Party General Election Manifesto 2017*, 16 May 2017, <http://www.labour.org.uk/index.php/manifesto2017>.

The overall picture

In recent years the UK economy has performed reasonably well. This comes after a sustained period of slow growth following the great recession. For example, the unemployment rate for the period of April to June 2017 was 4.4 per cent, which is the lowest it has been since early 1975.⁷

Chart 1: UK unemployment rate 1971-2017 (aged 16 & over, seasonally adjusted)

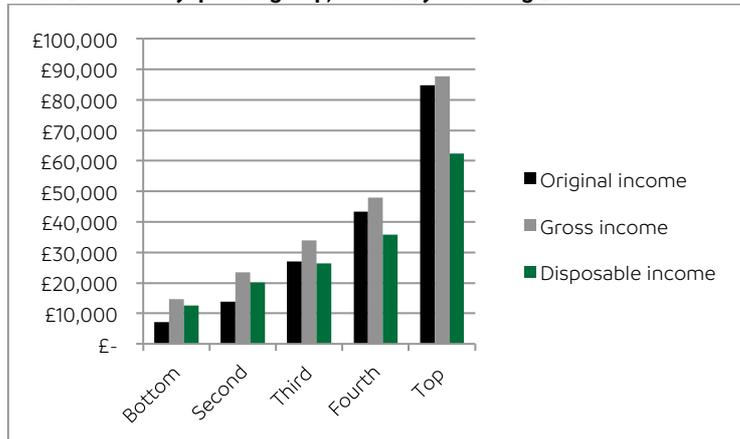


Source: ONS

However, wage growth has remained sluggish.⁸ As a result, even though the rate of employment in the UK is very high, many households are facing increased pressures on their disposable incomes and are struggling with the cost of living.

The cost of living is a real concern for many people in the United Kingdom, and this is particularly true for those on modest incomes. A 2015 YouGov poll found that the cost of living was the biggest policy concern for households on low and medium incomes. This poll revealed that the cost of living is a more pressing concern for these households than issues such as the NHS, education, immigration, affordable housing, and terrorism.⁹

Chart 2: Income by quintile group, financial year ending 2016



Source: ONS

Furthermore, a recently published survey by Nielsen found that 45 per cent of people living in the UK believe that the UK economy is in recession.¹⁰ The research from Nielsen revealed that British consumers are now the ninth most confident in Europe, down from

⁷ ONS, *UK Labour Market: August 2017*, 16 August 2017.

⁸ ONS, *Analysis of real earnings: August 2017*, 16 August 2017.

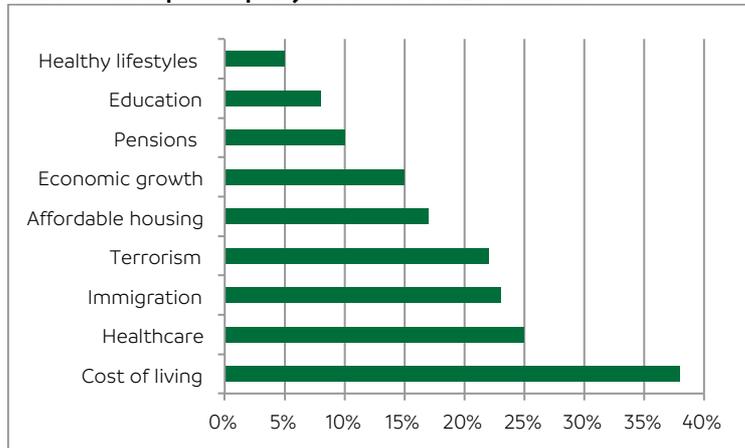
⁹ YouGov, 2015.

¹⁰ Nielsen, *Q2 2017 Consumer Confidence Report*, 17 August 2017.

second at the end of 2016.¹¹ The study also showed that the Nielsen Index is also down from 106 in 2016 to 99, which is below the 100 score that indicates overall optimism.¹²

In the financial year ending 2016 total average household expenditure remained level at £528.90 per week when compared with the same period the year before, where figures are adjusted for inflation.¹³ In recent years spending has increased from its 2012 nadir of £507.20.¹⁴ However, average spending has not returned to the pre-economic downturn levels seen before 2007.¹⁵

Chart 3: Most important policy issues for C1 & C2 households

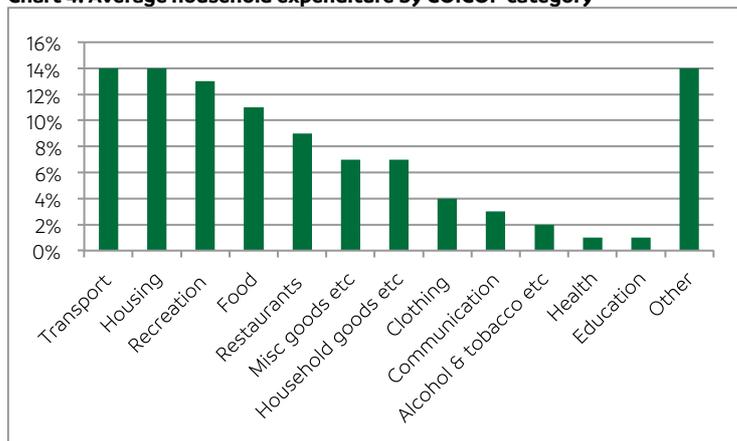


Source: YouGov

Transport and housing (excluding mortgage interest payments, and council tax for households in Great Britain and domestic rates for households in Northern Ireland), fuel and power were the highest expenditure classification of individual consumption by purpose (COICOP) categories.¹⁶

The average weekly amount spent on transport in the financial year ending 2016 was £72.20.¹⁷ The largest contributing factor to this being petrol and diesel.

Chart 4: Average household expenditure by COICOP category



Source: ONS

As for how the different regions of the UK compare, London had the highest average household expenditure of £652.40, whilst the North East's average weekly spending was

¹¹ *Ibid.*

¹² *Ibid.*

¹³ ONS, *Family spending in the UK: financial year ending March 2016*, 16 February 2017.

¹⁴ *Ibid.*

¹⁵ *Ibid.*

¹⁶ *Ibid.*

¹⁷ *Ibid.*

more than £200 lower at £423.50.¹⁸ The main contributor to this disparity is the cost of housing.¹⁹

Transport and housing were the highest expenditure categories for the majority of UK regions.²⁰ The exceptions to this were the North East, the North West, and Yorkshire and the Humber; households in these regions spent the most amount of money on recreation and culture.²¹

The main reason for this dissimilarity was that these regions had a higher proportion of expenditure on package holidays.²²

Chart 5: Average weekly household expenditure by region



Source: ONS

¹⁸ *Ibid.*

¹⁹ *Ibid.*

²⁰ *Ibid.*

²¹ *Ibid.*

²² *Ibid.*

Food

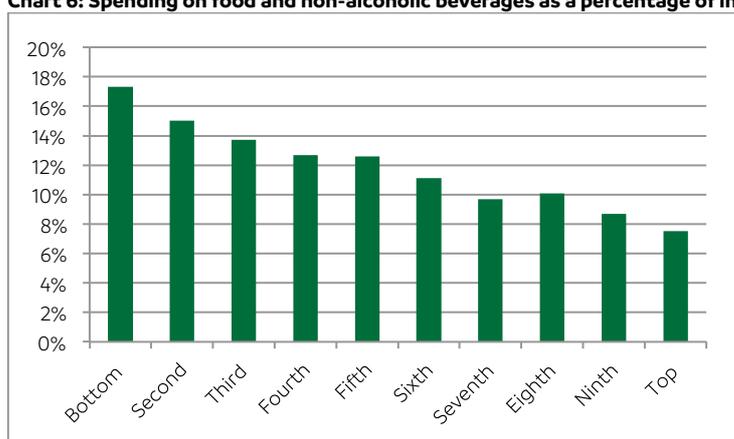
Spending on food and non-alcoholic beverages has fallen from approximately 40 per cent of total household spending to approximately 11 per cent.²³ However, spending on food and non-alcoholic beverages still account for a significant proportion of household expenditure. The UK average weekly household spending on food and non-alcoholic drinks consumed at home was £56.80.²⁴

The data reveals that lower income households spend a higher proportion of their total expenditure on food and non-alcoholic drinks; this is similar to patterns seen in previous years.²⁵ In the financial year ending 2016, households with the lowest incomes spent 17.3 per cent of total expenditure on food and non-alcoholic drinks.²⁶ In comparison, households with the highest incomes spent 7.5 per cent of total expenditure on this category.²⁷

Food and non-alcoholic beverages are obviously essential, but unfortunately there has been an increase in reports of cases where people have been finding it difficult to adequately feed themselves and their families.²⁸ In response to this, there have been calls from the media and campaign groups for the government to do more to address the situation.²⁹

However, more government action is not the correct solution. Rather, the reason why food is at its current price is a result of government policies, principally at the European level.

Chart 6: Spending on food and non-alcoholic beverages as a percentage of income by decile group



Source: ONS

In the context of this paper, the cost of food and non-alcoholic beverages is unique. This is because the prices are unnaturally high not as a result of the policies of the government of the United Kingdom, but rather due to the common agricultural policy (CAP) of the European Union.³⁰ The common agricultural policy has the impact of increasing food prices for consumers in three ways.

The first way in which the CAP leads to higher food prices for consumers is through tariffs on products which are imported into the European Union. Agriculture tariffs under the CAP are more than three times higher than the average EU tariff and stand at 8.5 per

²³ ONS, *Family spending in the UK: financial year ending March 2016*, 16 February 2017.

²⁴ *Ibid.*

²⁵ *Ibid.*

²⁶ *Ibid.*

²⁷ *Ibid.*

²⁸ The Trussell Trust, *Early Warnings: Universal Credit and Foodbanks*, 25 April 2017.

²⁹ Kerridge, K., 'There's a food poverty crisis in the UK. And the government is starved of ideas.' *The Guardian*, 31 March 2017.

³⁰ Vaidya, A., *Globalization: Encyclopedia of Trade, Labour, and Politics* (California: ABC-CLIO, 2006).

cent.³¹ However, for some product groups, tariffs can be much higher than this. For example, 37.4 per cent for dairy, 24.6 per cent on sugar, and 16.2 per cent on animal products.³²

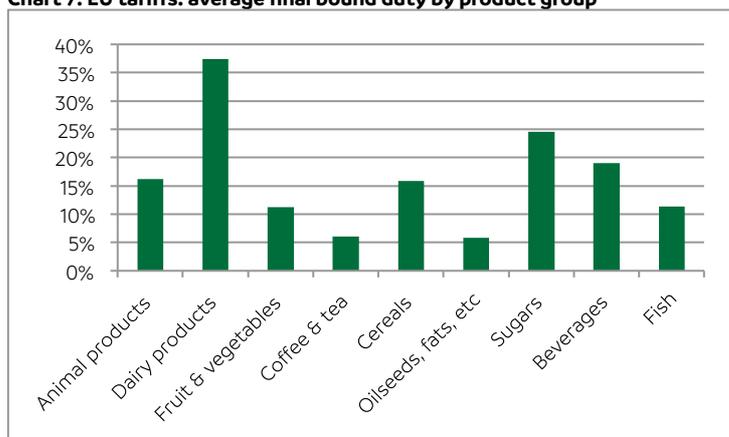
Tariffs can be even higher for individual products. For example, calculations by the Agriculture and Horticulture Development Board have revealed that the tariff on processed chicken is 88 per cent.³³

Furthermore, the CAP means that tariffs are also placed on farming machinery and equipment such as tractors that are imported from outside of the EU.³⁴ This raises the price of these products which places increased pressure on farmers. This increases the cost associated with production which is then passed onto consumers. The result is higher food prices and increased pressure on household budgets.

Therefore, it is clear that imposing agricultural tariffs results in increased food prices for consumers. This is supported by Halligan & Lyons who calculated that food in the UK is approximately 17 per cent more expensive as a result of the common external tariff.³⁵ Moreover, this was not an unforeseen consequence of the CAP, as the white paper which set out the UK government's case for joining the European Economic Community in 1971 estimated that: "membership will affect food prices gradually over a period of 6 years, with an increase of about 2.5 per cent each year in retail prices".³⁶

The second way in which the Common Agricultural Policy of the European Union results in higher food prices for consumers is due to taxpayers subsidising EU farmers.³⁷ Not only are these subsidies a burden on taxpayers, they also increase food prices for consumers.

Chart 7: EU tariffs: average final bound duty by product group



Source: WTO

Subsidies are used to prop up producers. This means that they are shielded from the true impact of the market. This results in the agricultural sector being inefficient and unproductive. As a consequence, it costs farmers more money to create their produce. The end result is higher food prices for consumers.

A review of the academic literature supports this point and illuminates further the pernicious effect of farming subsidies. For example, Spittler *et al*, have argued that

³¹ WTO, *Tariff Profiles: European Union*, http://stat.wto.org/TariffProfiles/E28_e.htm.

³² *Ibid.*

³³ Agriculture and Horticulture Development Board, *What Might Brexit Mean for UK Trade in Agricultural Products?* 12 October 2016, https://ahdb.org.uk/documents/Horizon_Brexit_Analysis_Report-Oct2016.pdf.

³⁴ Ward, M., *Statistics on UK-EU Trade*, House of Commons Library, Briefing Paper, No. 7851, 17 August 2017.

³⁵ Halligan, L., & Lyons, G., *Clean Brexit*, Policy Exchange, January 2017.

³⁶ HM Government, *The United Kingdom and the European Communities*, 07 July 1971, <http://archives.eui.eu/en/fonds/194159?item=UWK/NS.B-4-546>.

³⁷ European Union, *Council Regulation (EC) No. 73/2009*, 19 January 2009, <http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=LEGISSUM:ag0003>.

agricultural subsidies have resulted in inefficiencies in the food market.³⁸ Furthermore, a report by the OECD highlighted the negative impact of agricultural subsidies on food prices.³⁹

Switzerland provides a useful example. Swiss farmers receive the world's second highest subsidies to the extent that subsidy payments account for approximately 50 per cent of gross farm receipts.⁴⁰ However, many Swiss farmers still live in poverty and the price of their produce, especially meat, is incredibly high by international standards.⁴¹

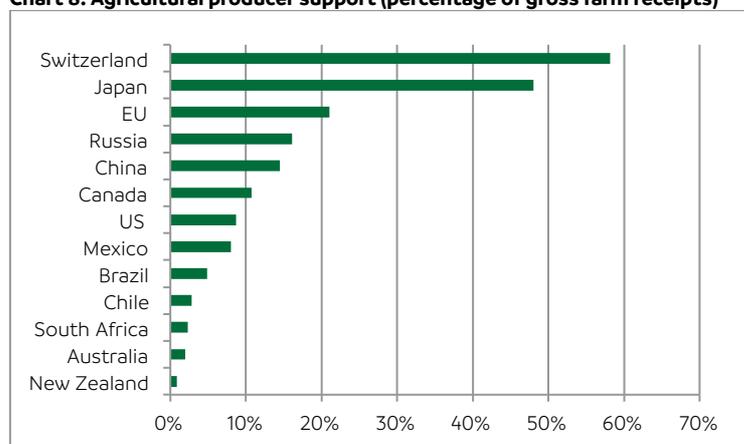
A report by the OECD concluded that subsidies are the reason why the Swiss farming sector is so inefficient and unproductive and thus why their produce is so expensive.⁴²

In New Zealand on the other hand, prior to 1984, New Zealand farmers received incredibly generous subsidies from the taxpayer. This period was characterised by low productivity and high levels of inefficiency. For example, farmers reared 70 million sheep and 50 million lambs, many of which were rendered into a fertiliser as supply far exceeded demand.⁴³

Moreover, the farming sector had a productivity increase of only one per cent a year during this period.⁴⁴ However, in 1984 the subsidies were abolished. The farmers were now exposed to market forces. The farmers responded to this by meeting the preferences of the consumer; the result was increased productivity, larger profits for farmers, and lower prices for the consumer.⁴⁵

Therefore, the evidence would appear to suggest that one of the reasons why food prices in the UK are unnaturally high is due to subsidies being paid to farmers. Not only is this a further burden on the taxpayer, but it also results in the farming sector being inefficient and unproductive which leads to higher food prices.

Chart 8: Agricultural producer support (percentage of gross farm receipts)



Source: OECD

The final way in which the common agricultural policy results in higher food prices for consumers is regulations relating to food standards.

³⁸ Spittler, J., Ross, R., & Block, W., 'The Economic Impact of Agricultural Subsidies in the United States', *The Journal of Social, Political, and Economic Studies*, Vol. 36, No.3, 2011.

³⁹ OECD, *Agricultural Policies in OECD Countries: At a Glance* (Paris: OECD Publishing, 2006), p. 69, Table 2.12.

⁴⁰ OECD, *Switzerland- Agricultural Policy Monitoring & Evaluation*, 2011.

⁴¹ Eurostat, *Comparative price levels for food, beverages, and tobacco*, June 2017.

⁴² OECD, *Switzerland should enact reforms that allow the competitive parts of the farming sector to flourish*, 27 March 2015.

⁴³ Stringleman, H., & Peden, R., 'Story: Sheep farming', *Te Ara: The Encyclopedia of New Zealand*, 24 November 2008

⁴⁴ Chamberlin, B., *Farming and Subsidies: Debunking the Myths*, (New York: Cornell, 1996).

⁴⁵ *Ibid.*

Under the CAP, food which has been treated in various ways and which comply with the health and safety standards of countries outside of the EU and EEA are not allowed to be sold within the UK. An example of this is chlorine washed chicken.

In the United States it is common to wash chicken carcasses in chlorine water at the end of the production process in order to kill harmful bacteria such as salmonella. This differs from the EU's more expensive strategy which aims to control hygiene at all stages of production. The CAP means that chlorine washed chicken cannot be sold in the EU on health and safety grounds.⁴⁶

Despite a report by Spence for the Adam Smith Institute demonstrating that eating chlorine washed chicken is as harmful as drinking a glass of water,⁴⁷ the idea that it might be sold in UK stores generated a flurry of febrile reporting calling on the government to maintain the current health and safety standards after the UK leaves the European Union.⁴⁸

The European Union has adopted a similar stance in regard to hormone treated beef. Since 1989, hormone treated beef has been debarred from being sold within the EU.⁴⁹ As with the chlorine washed chicken, the EU's concerns about health and safety would appear to be unfounded; the World Trade Organisation has stated that the EU's stance is not based on scientific evidence.⁵⁰

Furthermore, the EU has banned the production and sale of genetically modified and genetically edited food (with the exception of only a few products).⁵¹ As with chlorine washed chicken and hormone treated beef, the EU's health and safety concerns are not based upon a solid scientific foundation. For example, the chief scientific advisor to the European Commission has stated that GM food is safe.⁵² In addition to the chief scientific advisor, the French Supreme Court,⁵³ The American Association for the Advancement of Science,⁵⁴ The US National Academy of Sciences,⁵⁵ and the Royal Medical Association⁵⁶ have all concluded that genetically modified organisms do not pose a health risk to humans.

The EU's stance on health and safety has resulted in food prices being higher for consumers. US methods produce fresh chicken at 79 per cent of the price of equivalent birds on UK supermarket shelves.⁵⁷

Moreover, beef is much cheaper to produce in the US when compared to the UK which results in lower prices for US consumers,⁵⁸ whereas UK consumers are prevented from accessing the cheaper US products.

⁴⁶ Josling, T., & Tangermann, S., 'TTIP and Agriculture: Another Transatlantic Chicken War?' *Choices*, Agriculture and Applied Economics Association, 2nd Quarter 2016, 31(2).

⁴⁷ Spence, P., *Chlorinated Chicken: Why you shouldn't give a cluck*, Adam Smith Institute, July 24 2017.

⁴⁸ Monbiot, G., 'Chlorinated chicken? Yes, we really can have too much trade', *The Guardian*, 25 July 2017 (Monbiot subsequently retracted his claims).

⁴⁹ Josling, T., & Tangermann, S., 'TTIP and Agriculture: Another Transatlantic Chicken War?' *Choices*, Agriculture and Applied Economics Association, 2nd Quarter 2016, 31(2).

⁵⁰ Johnson, R., 'The US-EU Beef Hormone Dispute', *Federation of American Scientists*, Congressional Research Service, (January 2017).

⁵¹ Josling, T., & Tangermann, S., 'TTIP and Agriculture: Another Transatlantic Chicken War?' *Choices*, Agriculture and Applied Economics Association, 2nd Quarter 2016, 31(2).

⁵² Fleming, J., *No risk with GMO food, says EU chief scientific advisor*, *Euractiv*, 24 July 2012.

⁵³ de La Hamaide, S., 'French court annuls ban on growing Monsanto GMO maize', *Reuters*, 28 November 2011.

⁵⁴ American Association for the Advancement of Sciences, *Statement by the AAAS Board of Directors on Labelling of Genetically Modified Foods* 20 October 2012.

⁵⁵ The US National Academy of Sciences, *Safety of Genetically Engineered Foods: Approaches to Assessing Unintended Health Effects*, 2011.

⁵⁶ Key, S., Ma, J., & Drake, P., 'Genetically modified plants and human health', *Journal of the Royal Society of Medicine*, Vol. 101, Issue 6, 2008.

⁵⁷ Agriculture & Horticulture Development Board, *Poultry Pocketbook*, May 2016.

⁵⁸ United States Department of Agriculture, *Retail prices for beef, pork, poultry cuts, eggs, and dairy products*, 2017.

Furthermore, the use of genetically modified organisms allows farmers to produce higher yields in a less expensive and more efficient way. They pass on the savings to the consumer which results in lower prices.⁵⁹

As discussed, all but a few genetically modified organisms are debarred from being produced or sold in the UK by the European Union. As with chlorine washed chicken and hormone treated beef, UK consumers are prevented from accessing these products. This explains why food prices in the UK are higher than in, for example, the United States.

The price of fish

Fishing in UK waters is regulated by the common fisheries policy (CFP) of the EU.

Under the CFP, fishermen from other EU member states have the right to catch fish in UK waters.⁶⁰ This, coupled with quotas placed on the number of fish caught, has resulted in fish stocks in UK waters being depleted and thus the number of fish caught by UK fishermen has decreased.⁶¹

When one examines historical trends in fishing, the data reveals that three events have corresponded with a drastic decrease in the number of fish landed by UK fishermen. These three events have been the first world war, the second world war, and the UK's accession to the European Economic Community (EEC).⁶²

The data strongly suggests that the CFP has resulted in a dramatic decline in the number of fish landed by UK fishermen. For example, in 1970, before the UK's accession to the EEC, UK fishermen landed 948,000 tonnes of fish.⁶³ In post-accession 1975, this figure had decreased to 842,000 tonnes.⁶⁴ The number of fish landed by UK fishermen has continued to decrease over the years and the figure stood at 415,000 tonnes in 2015.⁶⁵

The impact of the CFP on the amount of fish landed by UK fishermen is illuminated further when one considers the international situation. Although UK vessels land a large number of fish compared to other EU countries, they land far fewer than vessels from countries which are not bound by the CFP such as Norway and Iceland.⁶⁶

Chart 9: Landings of fish in UK by home fishing fleet (thousand tonnes), 1890-2015



Source: House of Commons Library

⁵⁹ Brookes, G., & Barfoot, P., 'GM crops: global socio-economic and environmental impacts 1996-2014', *PG Economics Ltd*, 2016.

⁶⁰ Khalilian, S., Froese, R., Proelss, A., & Requate, T., 'Design for Failure: A Critique of the Common Fisheries Policy of the European Union', *Marine Policy*, Volume 34, Issue 6, November 2010.

⁶¹ *Ibid.*

⁶² Dempsey, N., Rutherford, T., & Allen, G., *UK Sea Fisheries Statistics*, House of Commons Library, Briefing Paper, No. 2788, 30 November 2016.

⁶³ *Ibid.*

⁶⁴ *Ibid.*

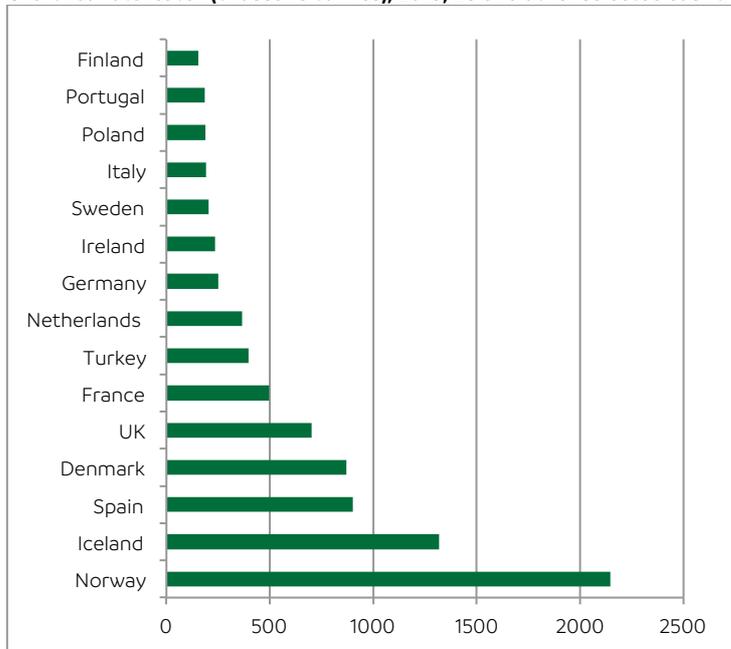
⁶⁵ *Ibid.*

⁶⁶ Eurostat, *Fisheries Statistics in Detail*, October 2016.

The amount of fish being landed by UK vessels has decreased under the CFP, but consumption of fish in the UK has increased.⁶⁷ As demand for fish has been outstripping supply, we would expect to see upward pressure on prices. This is supported by the data, which reveals that the price of fish has increased quickly compared to other food products since the UK became subject to the CFP.⁶⁸

Therefore, it is clear that the common fisheries policy of the EU has had an impact on the stock of fish in UK waters and the number of fish landed by UK vessels. This, coupled with increased demand, has resulted in increased prices for consumers.

Chart 10: Total catch (thousand tonnes), 2015, EU and other selected countries



Source: Eurostat

In this section we have seen that various EU policies have resulted in higher food prices for consumers. For example, tariffs on food imported into the EU increases their price.

Moreover, subsidies paid to EU farmers results in the agricultural sector becoming uncompetitive which results in higher prices for consumers.

Furthermore, regulations concerning food production and innovation have prevented UK consumers from accessing cheaper alternatives.

Finally, the common fisheries policy has led to the depletion of UK fishing stocks and a decrease in the number of fish being landed by UK vessels.

⁶⁷ The statistics are convoluted when making a comparison with pre-accession figures due to different measurements of staples. However, see the *Sea Fish Statistics* from various years since the 1970s.

⁶⁸ ONS, *Economic Trends*, 2016

Housing

Housing costs are one of the largest expenses facing households in the United Kingdom.⁶⁹ House prices in the UK have increased by an average of 300 per cent since 1995⁷⁰ and in some areas of London by 1,000 per cent.⁷¹

By international standards, housing costs in the UK are incredibly high with the UK having the highest average monthly rent prices in the European Economic Area.⁷²

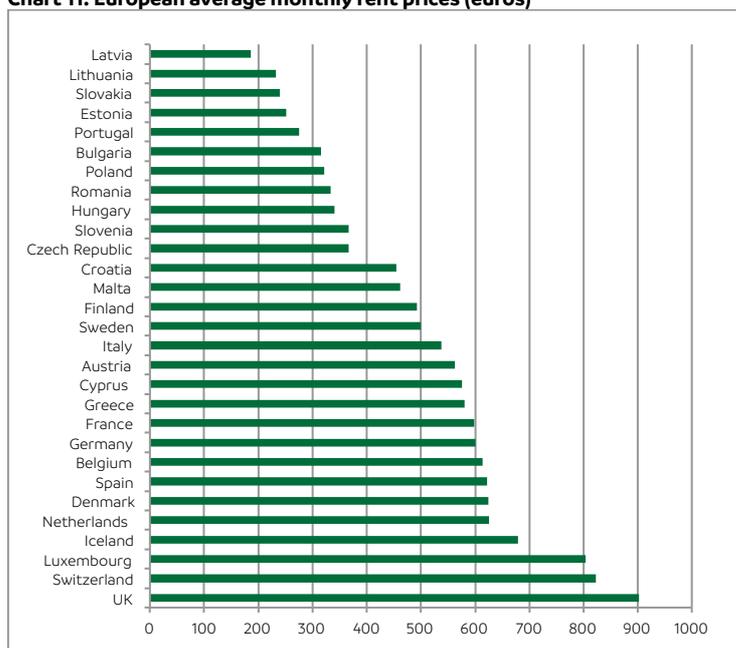
For example, the average UK rent price is £350 a month higher than the European average.⁷³ Further evidence of this is provided by academic research.

For example, Cheshire *et al* found that: “In the Netherlands the price [of housing] per square metre was 45 per cent less than the UK”.⁷⁴

Moreover, they stated that in Germany: “the real price of houses fell in both decades of the 1980’s and 1990’s and was completely stable over the whole period 1991 to 2002, compared to an annual percentage rate of increase in the UK of 3.6, which is the highest for any OECD country”.⁷⁵

Very high rents can have a negative impact on the quality of life of households.⁷⁶ As a result, there are frequent calls from the media and anti-poverty campaigners for the government to do more to address the problem. Such calls were answered by Labour who promised to implement a raft of measures such as rent caps in their 2015 and 2017 General Election manifestos.⁷⁷

Chart 11: European average monthly rent prices (euros)



Source: Eurostat

⁶⁹ ONS, *Family spending in the UK: financial year ending March 2016*, 16 February 2017.

⁷⁰ Cook, L., *Savills*, 15 January 2016.

⁷¹ *Ibid.*

⁷² Koessler, J., *UK Rental Prices*, National Housing Federation

⁷³ *Ibid.*

⁷⁴ Cheshire, P., Nathan, M. & Overman, H. *Urban Economics & Urban Policy: Challenging Conventional Policy Wisdom*. (Massachusetts: Edward Elgar Publishing, 2014).

⁷⁵ *Ibid.*

⁷⁶ Tuffrey, B., *The human cost: How the lack of affordable housing impacts on all aspects of life*, Shelter, March 2010.

⁷⁷ *The Labour Party General Election Manifesto 2017*, 16 May 2017, <http://www.labour.org.uk/index.php/manifesto2017>.

A discussion of the folly of rent controls goes beyond the scope of this paper.⁷⁸ Instead we will limit our analysis to an examination of the ways in which current government policies contribute to the very high housing costs in the UK.

The reason why housing costs are so high is due to a shortage of supply. For example, in London alone, 50,000 new homes a year need to be built in order to address the current housing shortage and to accommodate London's burgeoning population.⁷⁹ However, London's new housing supply is only at approximately 30,960 a year.⁸⁰

It is a fundamental principle of economics that when demand outstrips supply, then upward pressure will be placed on prices. This is why renting is so expensive in the UK, and especially in London. There are simply not enough homes for all the people who need one.

Chart 12: Expenditure on rent per week, by country and region



Source: ONS

However, we must consider why supply is not keeping pace with demand. Given that housing is essential for the safety and wellbeing of people, why is it so scarce and expensive in the UK? The answer is government action. Government policies have exacerbated the housing crisis by restricting supply and thus increasing prices.

In her 2017 conference speech, Theresa May recognised the burden placed on households by high housing costs.⁸¹

However, the policies proposed will not help the vast majority of people to own their own home nor will it relieve the burden placed on households by high rental prices.

For example, her plans to fund the building of 25,000 homes for social rent by 2021 equates to 5,000 a year. This will be ineffective given that, as discussed above, London alone needs an extra 50,000 homes built each year in order to address its housing crisis. As a result, 5,000 homes for the country as a whole will have a negligible impact on increasing housing affordability.

Moreover, her proposal to extend help to buy will actually exacerbate the housing crisis because the housing crisis is a supply side problem. Increasing demand by giving money to the small proportion of the population that qualify for help to buy will place further upward pressure on prices for those who do not qualify.

⁷⁸ For an introduction see, Niemietz, K., *The Key to Affordable Housing*, Institute of Economic Affairs, September 2016.

⁷⁹ *London Strategic Housing Market Assessment* (2013) and *Mayor of London's Housing Strategy* (2014).

⁸⁰ DCLG, *Net Additional Dwellings by Local Authority District, 2004/5 to 2013/14*.

⁸¹ May, T., *Theresa May's speech to Conservative Party Conference 2017*, 4 October 2017, <https://www.conservatives.com/sharethefacts/2017/10/theresa-mays-conference-speech>.

The first way in which the government contributes to the UK's housing affordability problem is by the planning system. By international standards, the UK has an incredibly complex planning system.

The UK has a plethora of rules and regulations relating to home building. For example, there are rules which restrict the height of buildings. There have been numerous academic studies into the impact of planning regulations on housing supply and affordability.

For example, research conducted by Hilber & Vermeulen, concluded that the largest impact on house prices was caused by the regulatory constraints imposed by the planning system on development. Their study found that the planning system was responsible for 35 per cent of UK house prices.⁸²

Further support comes from a report published by the European Commission (hardly a stranger to excessive rules and regulations), which argued that the UK planning system is "complex and costly" and is exacerbating the housing crisis in the UK.⁸³

A review of the academic literature reveals that this is also the case outside of the UK. For example, Chang-Tai Hsueh & Enrico Moretti of the University of Chicago found that housing supply constraints in the United States has a drastic impact on living standards.⁸⁴ They concluded that if even modest steps were taken towards liberalising the planning system, then wages and living standards could improve by approximately one tenth.⁸⁵

The conclusion arrived at by the University of Chicago study is supported by numerous other academic studies on the impact of planning regulations on housing affordability. For example, Malpezzi concluded that: "Our results suggest that housing regulation raises housing rents and values".⁸⁶

Moreover, a study conducted by Dawkins & Nelson found that: "The most significant policy implication to be gleaned from this research is that local planning plays a significant role in determining the severity of housing price inflation attributable to urban containment policies".⁸⁷

Furthermore, research conducted by Saks found that: "raising the degree of housing supply regulation by one standard deviation results in 17 per cent less residential construction and twice as large growth in housing prices".⁸⁸

Moreover, a study conducted by Chi-Man Hui & Sze-mun Ho found that, in Hong Kong: "The analysis demonstrates that most of the planning variables affect housing prices statistically".⁸⁹

In addition, research by Caldera & Johansson which focused on OECD countries revealed that local land-use regulation has become a constraint in the supply of new housing units in many countries, including the UK.⁹⁰

⁸² Hilber, C., & Vermeulen, W., 'The Impacts of Restricting Housing Supply on House Prices and Affordability', *DCLG*, 2010.

⁸³ European Commission, *Country Report United Kingdom 2017*, 22 February 2017.

⁸⁴ Hsieh, C., & Moretti, E., 'Housing Constraints and Spatial Misallocation', *NBER*, Working Paper No. 21154, May 2014.

⁸⁵ *Ibid.*

⁸⁶ Malpezzi, S., 'Housing Prices, Externalities, and Regulation in US Metropolitan Areas', *Journal of Housing Research*, Vol. 7, Issue 2, 1996.

⁸⁷ Dawkins, C., & Nelson, A., 'Urban Containment Policies and Housing Prices: an International Comparison with Implications for Future Research', *Land Use Policy*, Vol. 19, Issue 1, January 2002.

⁸⁸ Saks, R., 'Job Creation and Housing Construction: Constraints on Metropolitan Area Employment Growth', *Finance and Economics Discussion Series*, Divisions of Research and Stability and Monetary Affairs, 2005.

⁸⁹ Chi-man Hui, E., & Sze-mun Ho, V., 'Does the Planning System Affect Housing Prices? Theory and Evidence from Hong Kong', *Department of Building and Real Estate, The Hong Kong Polytechnic University*, 2002.

⁹⁰ Caldera, A., & Johansson, A., 'The Price Responsiveness of Housing Supply in OECD Countries', *Journal of Housing Economics*, Vol. 22, Issue 2, September 2013.

Planning regulations not only relate to the types of homes which can be built, but also where they can be built. For example, the government limits the supply and thus decreases the affordability of housing through its green belt policy, restricting building in areas surrounding major UK cities.

Such restrictions reduce the supply of developable land around cities which then reduces housing supply and consequently lowers housing affordability. This is supported by Papworth, whose study revealed that 90 per cent of land in England remains undeveloped and that only 0.5 per cent would need to be developed to fulfil this decade's housing need.⁹¹

Furthermore, his research found that simply removing restrictions on land within a 10 minutes' walk of a railway station would allow the development of 1 million more homes within the green belt surrounding London alone.⁹² His research concluded that building restrictions on the green belts have a detrimental impact on living standards as they reduce housing supply and lower housing affordability.⁹³

This point is augmented by Cheshire & Sheppard. Their paper concluded that regulations relating to green belts are a factor as to why housing affordability in the UK compares unfavourably with other developed countries.⁹⁴

Green belts further exacerbate the housing crisis by constraining supply and thus decreasing housing affordability.

The final way in which government policy contributes to low housing affordability that we shall now consider is stamp duty. The government levies a tax on the purchase of properties in the UK.⁹⁵

The evidence would appear to suggest that this further exacerbates the problem as it would discourage people from downsizing their houses which would increase supply and thus reduce prices.

For example, there are approximately 16.1 million households in the UK which are under-occupied.⁹⁶

In a joint report, the LSE and the Berkeley Group highlighted the negative impact of stamp duty.⁹⁷

Moreover, research from the Institute of Public Care at Oxford Brookes University revealed that stamp duty provides a disincentive for elderly people to move to a smaller home and so its abolition would incentivise older people to move and thus free up the housing market.

Further support for this point is provided by a recently released research paper from the LSE and the VATT Institution for Economic Research. The paper found that the rate of home moving would be 27 per cent higher if stamp duty on properties was abolished.⁹⁸

⁹¹ Papworth, T., *The Green Noose: An Analysis of Green Belts and Proposals for Reform*, Adam Smith Institute, 14 January 2015.

⁹² *Ibid.*

⁹³ *Ibid.*

⁹⁴ Cheshire, P., & Sheppard, S., 'The Introduction of Price Signals into Land Use Planning Decision Making: a Proposal', *Urban Studies*, 42 (4). 647 -663, 2005.

⁹⁵ HM Government, *Stamp Duty Land Tax*, 2017, <https://www.gov.uk/stamp-duty-land-tax/residential-property-rates>.

⁹⁶ ONS, *Overcrowding and Under-Occupation in England and Wales*, 17 April 2014,

http://webarchive.nationalarchives.gov.uk/20160107121343/http://www.ons.gov.uk/ons/dcp171776_360082.pdf.

⁹⁷ Whitehead, C., Travers, T., Scanlon, K., & Fernandez, M., *Creating the Conditions for Growth*, LSE, October 2013.

⁹⁸ Hilber, C., & Lyytikäinen, T., 'Transfer Taxes and Household Mobility: Distortion on the Housing or Labor Market?', *Journal of Urban Economics*, Vol. 101, 57-73, 2017.

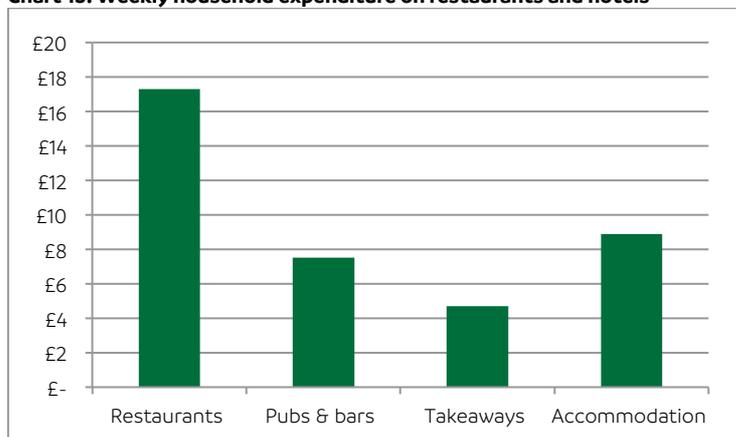
We have therefore seen the ways in which the government contributes to low housing affordability in the UK. Government action reduces housing affordability by imposing a restrictive planning system and levying stamp duty.

Restaurants and Hotels

Money spent by households on restaurants and hotels is not essential and can rightly be categorised under discretionary spending. It does however make up 9 per cent of total household expenditure.⁹⁹

In the financial year ending 2016, UK households spent an average of £45.10 per week on restaurants and hotels.¹⁰⁰ This is an increase of £1.80 when compared with the previous year, where figures have been adjusted for inflation.¹⁰¹

Chart 13: Weekly household expenditure on restaurants and hotels



Source: ONS

This is of interest to us due to minimum wage legislation. In the 1990s, the Labour government introduced the National Minimum Wage Act 1998 which required employers to pay all employees a minimum wage, regardless of their skills, experience, or qualifications. This was seen as a positive step by anti-poverty campaigners and was followed in 2015 by legislation introduced by the Conservative government to increase the minimum wage yet further.

There are calls by pressure groups to introduce the minimum wage even further, and Labour pledged to raise it to £10 per hour in their 2017 general election manifesto.¹⁰²

However, the evidence strongly suggests that minimum wage legislation has an impact on the cost of living, especially in relation to household spending on restaurants and hotels.

First, it is important to note that out of all industries, restaurants and hotels have the highest proportion of workers on the minimum wage in the UK.

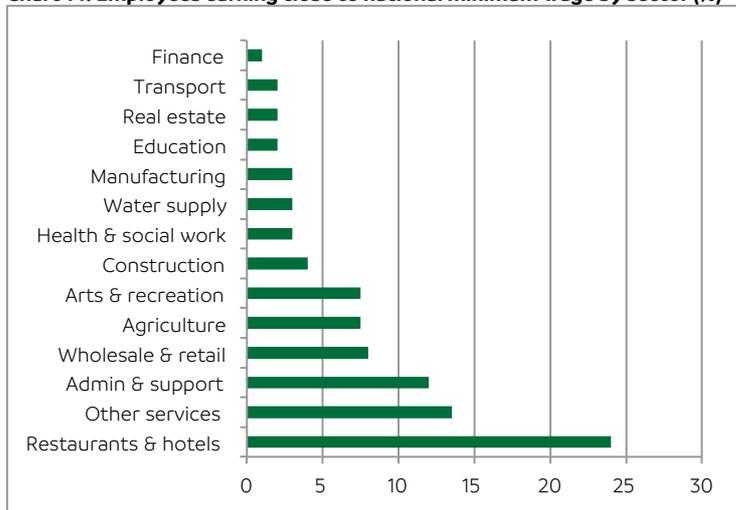
⁹⁹ ONS, *Family spending in the UK: financial year ending March 2016*, 16 February 2017.

¹⁰⁰ *Ibid.*

¹⁰¹ *Ibid.*

¹⁰² *The Labour Party General Election Manifesto 2017*, 16 May 2017, <http://www.labour.org.uk/index.php/manifesto2017>.

Chart 14: Employees earning close to national minimum wage by sector (%)



Source: Labour Force Survey

Second, a review of the academic literature reveals that increasing the minimum wage can result in higher prices for consumers.

For example, Wadsworth found that in a UK context, prices in several minimum wage sectors, notably takeaway food, canteen meals, hotel services and domestic services, do appear to have risen significantly faster than prices in non-minimum wage sectors.

These effects were particularly significant in the four years immediately after the introduction of the minimum wage.¹⁰³ This is supported by Draca *et al*, who found that in sectors such as restaurants and hotels, companies pass on the higher wage costs in the form of higher prices to consumers.¹⁰⁴

This is also the case in other countries. For example, a study by Aaronson *et al*, found that a 10 per cent increase in the minimum wage could lead to approximately a 0.7 per cent increase in prices at US restaurants.¹⁰⁵

A similar conclusion was reached by Basker & Khan, who examined the impact of the minimum wage on fast food prices in US restaurants. They found that increasing the minimum wage had a significant impact on the prices of pizza and burgers.¹⁰⁶

Moreover, a study by Fougere *et al*, found a positive and significant impact of the minimum wage on restaurant prices in France.¹⁰⁷

The impact of the national minimum wage on employment opportunities

As an important aside, the impact of increasing the national minimum wage on employment opportunities will now be examined.

With the cost of living in the UK being so high and with many households on low incomes struggling to make ends meet, increasing the minimum wage in 2015 was seen as a progressive step and was welcomed by the main political parties. This is understandable. The cost of living is very high, and it is only right that those who work hard, as opposed to being dependent upon the welfare state, earn enough money to live comfortably.

¹⁰³ Wadsworth, J., 'Did the National Minimum Wage Affect UK Prices?', IZA, Discussion Paper No. 4433, September 2009.

¹⁰⁴ Draca, M., Machin, S., & Van Reenen, J., 'Minimum Wages and Firm Profitability', *American Economic Journal: Applied Economics*, 129-151, January 2011.

¹⁰⁵ Aaronson, D., French, E., & MacDonald, J., 'The Minimum Wage, Restaurant Prices, and Labour Market Structure', *The Journal of Human Resources*, Vol. 43, No.3, 2008.

¹⁰⁶ Basker, E., & Khan, M., *Does the Minimum Wage Bite into Fast-Food Prices?*, University of Missouri, September 2013.

¹⁰⁷ Fougere, D., Gautier, E., & Le Bihan, H., 'Restaurant Prices and the Minimum Wage', *Journal of Money, Credit, and Banking*, Vol. 42, Issue 7, October 2010.

However, the evidence suggests that increasing the minimum wage can result in an increase in unemployment, especially for those in low skilled jobs.

For example, Clemens & Wither examined the impact of increasing the minimum wage in the US during the great recession. Their study found that minimum wage increases reduced the national employment-to-population ratio.¹⁰⁸

This is supported by a plethora of other academic studies. For example, Meer & West found that increases to the minimum wage in the US resulted in firms being far less likely to hire new staff.¹⁰⁹

Moreover, Neumark & Wascher found that increases to the minimum wage results in fewer employment opportunities, especially for low skilled workers.¹¹⁰

Work remains the best route out of poverty. The OECD,¹¹¹ the Joseph Rowntree Foundation,¹¹² and the Centre for Social Justice¹¹³ have all pointed out that, while not a panacea, work provides the best route out of poverty for households and allows them to increase their standard of living. Furthermore, unemployment can have a devastating psychological impact on individuals, and also places an increased burden on public services due to the decrease in tax receipts for HM Treasury.

It is still too early to assess the impact of the latest increase to the national minimum wage in the UK. However, the evidence strongly suggests that it will result in an increase in unemployment.

Low skilled workers are the most likely to be adversely affected by an increase in the minimum wage as they will have far fewer employment opportunities. As a result, many households may find themselves facing unemployment, which will mean that their route out of poverty is taken away, along with any opportunity to increase their standard of living.

Therefore, the evidence would appear to strongly suggest that minimum wage legislation has increased prices in restaurants and hotels, and thus has had a detrimental impact on the cost of living for UK households.

It is still too early to analyse the impact of the legislation introduced by the Conservative government to increase the minimum wage. However, the likely outcome of this will be higher prices for UK consumers which will have a negative impact on household budgets.

Moreover, further increases to the national minimum wage are likely to result in fewer employment opportunities, especially for low skilled workers.

In this section we have seen that government action has increased prices for consumers using restaurants and hotels. The government has done this by the introduction of, and increases to, the minimum wage. Furthermore, the minimum wage has had a negative impact upon the employment opportunities of low skilled workers.

108 Clemens, C. & Wither, M., *The Minimum Wage and the Great Recession: Evidence of Effects on the Employment and Income Trajectory of Low-Skilled Workers*, University of California at San Diego, September 2016.

109 Meer, J., & West, J., *Effects of the Minimum Wage on Employment Dynamics*, Massachusetts Institute of Technology, August 2015.

110 Neumark, D., & Wascher, W., 'Minimum Wages & Employment: A Review of Evidence from the New Minimum Wage Research', *NBER*, November 2006.

111 OECD, 'Is Work the Best Antidote to Poverty?', *OECD Employment Outlook*, 2009.

112 Kemp, P., Bradshaw, J., Dornan, P., Finch, N., & Mayhew, E., *Routes out of Poverty*, Joseph Rowntree Foundation, 2004.

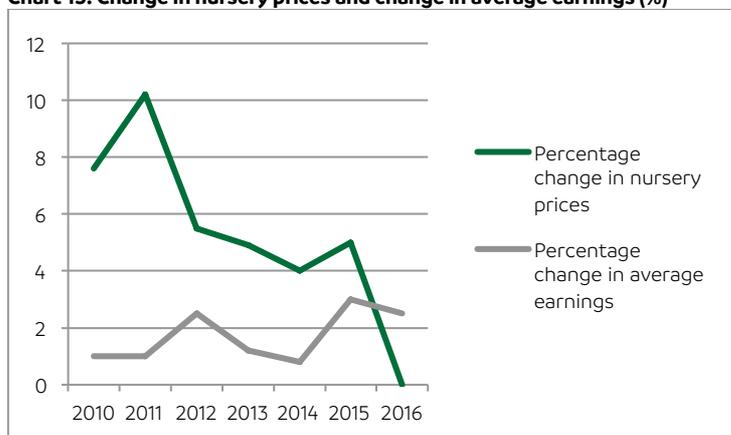
113 The Centre for Social Justice, *Signed On, Written Off: An Inquiry into Welfare Dependency in Britain*, 2013.

Childcare

Although not essential in the same way as food or housing, childcare is of great importance to families. It ensures that children are kept safe and that parents can return to work and thus contribute to the economy and increase their household income.

The cost of childcare has risen dramatically over the past few years. Prices have increased at a much higher pace than inflation and wages since 2009.¹¹⁴

Chart 15: Change in nursery prices and change in average earnings (%)

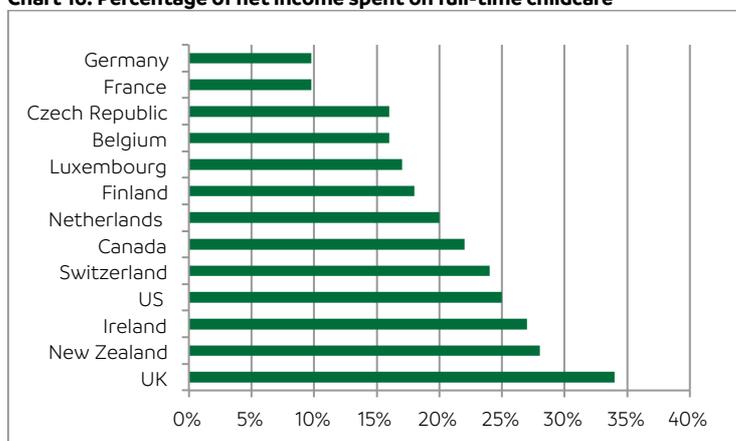


Source: Family and Childcare Trust and ONS

Moreover, UK childcare is expensive by international standards.

For example, households in the UK are spending a higher proportion of their net income on full-time childcare than in other advanced economies including Australia, Canada, and the United States.¹¹⁵

Chart 16: Percentage of net income spent on full-time childcare



Source: OECD

The median household disposable income for the financial year ending 2016 was £26,300.¹¹⁶ As the average household which uses childcare spends 33.8 per cent of their income on it,¹¹⁷ this amounts to £8,889 each year. If costs were brought down to the OECD average of 13 per cent,¹¹⁸ then this would be reduced to £3,419.

¹¹⁴ Rutter, J., *Childcare Survey 2016*, Family and Childcare Trust, 2016.

¹¹⁵ Richardson, L., *Cost of Childcare Across OECD Countries*, Directorate for Employment, Labour and Social Affairs, Social Policy Division.

¹¹⁶ ONS, *Household Disposable Income and Inequality in the UK: Financial Year Ending 2016*, 10 January 2017.

¹¹⁷ OECD, 'Society at a Glance 2016', *OECD Social Indicators*, 05 October 2016.

¹¹⁸ *Ibid.*

In Germany, the average household which uses childcare spends 9.7 per cent of their income on it.¹¹⁹ Therefore, if the UK adopted a similar system to that of Germany, then the average household could spend as little as £2,551 each year on childcare, whereas if the system was more like Spain, where households which use childcare spend 5.6 per cent of their income on it,¹²⁰ then average childcare costs could cost as little as £1,472.80 each year.

If the UK was to follow a system similar to that of Sweden, where the average household which uses childcare spends 4.4 per cent of their income on it,¹²¹ then average childcare costs could be reduced to £1,157 each year. Therefore, if the rules relating to childcare in the UK were similar to those in Sweden, then the average UK household which uses childcare could save up to £7,732 each year on childcare costs.

The high cost of childcare also has an impact on the employment prospect of parents. For example, a British Chambers of Commerce survey found that 9 per cent of business leaders have had an employee leave their job due to childcare costs.¹²²

The survey also found that 28 per cent of business leaders have had employees reduce their working hours as a result of the high cost of childcare.¹²³ This not only impacts the ability of households to earn extra money and so improve their living standards, but it also has a negative impact on the economy.

As with food and housing, there are calls from pressure groups and the media for the government to do more in order to ease the pressure on household budgets. However, the government is already heavily involved in the funding and provision of childcare.

Taxpayers in the UK now spend approximately £7 billion on childcare each year.¹²⁴ Furthermore, the government heavily regulates the childcare sector. We will now consider one way in which government action contributes to the relatively high price of childcare in the UK.

One way in which government action contributes to the high cost of childcare is the regulations concerning staff to child ratios and the qualifications of staff. By international standards, the UK imposes very restrictive staff to child ratios. For example, in the UK there can only be three children aged under one per staff member. This is the same as for the Republic of Ireland, but is very high by western European standards.¹²⁵

Furthermore, when one considers the provision of childcare for children aged one, the UK has a higher ratio than the Republic of Ireland. Again, the ratio is very high by international standards.¹²⁶ Although not represented in the graphs, it is also useful to indicate that there are no mandated ratios for childcare in Denmark, Spain, and Sweden.¹²⁷

¹¹⁹ *Ibid.*

¹²⁰ *Ibid.*

¹²¹ *Ibid.*

¹²² British Chambers of Commerce, *Time for Action on High Cost of Childcare*, 2016.

¹²³ *Ibid.*

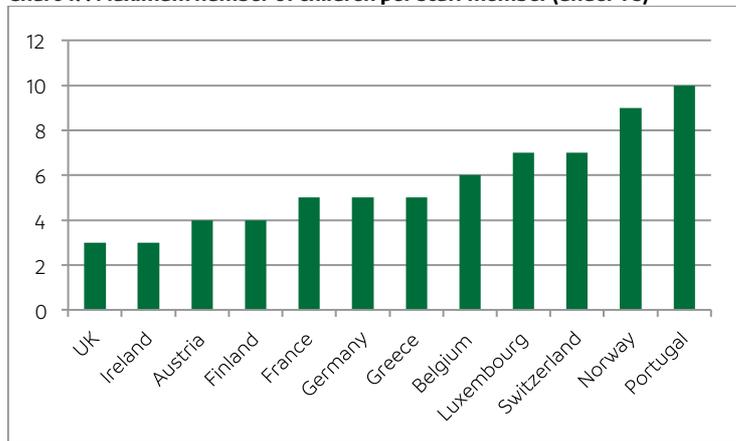
¹²⁴ Rutter, J., *Childcare Survey 2016*, Family and Childcare Trust, 2016.

¹²⁵ Pascal, C. Bertram, T., Delaney, S., & Nelson, C., *A Comparison of International Childcare Systems*, Centre for Research in Early Childhood, July 2013.

¹²⁶ *Ibid.*

¹²⁷ *Ibid.*

Chart 17: Maximum number of children per staff member (under 1's)



Source: Centre for Research in Early Childhood

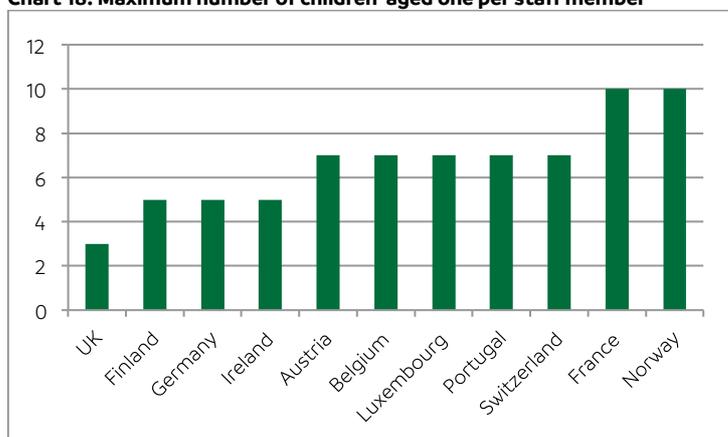
During the coalition government of 2010-2015, there was talk of relaxing the child to staff ratios in order to help save parents money.

For example, in her role as parliamentary undersecretary of state for education and childcare, Liz Truss highlighted the fact that restrictive child to staff ratios were contributing to high childcare costs. As a result, she proposed relaxing the ratios.¹²⁸

However, her plans were blocked by the then deputy prime minister Nick Clegg, who erroneously stated that such reforms would not lower costs for parents.¹²⁹

There are also regulations about the level of training and qualifications which staff must possess. Again, the UK has very high standards by international standards. For example, in the UK, staff in formal childcare settings require an NVQ Level 2, as do registered childminders. Supervisors require a higher level NVQ. Many other advanced economies allow a far greater degree of latitude in this regard.¹³⁰

Chart 18: Maximum number of children aged one per staff member



Source: Centre for Research in Early Childhood

Academic research would appear to suggest that regulations relating to qualification requirements and staff to child ratios have an impact on the price of childcare.

For example, Thomas & Gorry examined childcare in a US context, and concluded that increasing the staff to child ratio by one child across all age groups can reduce fees by between nine and 20 per cent.¹³¹ Moreover, their research revealed that requiring

¹²⁸ Truss, E., *More Great Childcare: Raising Quality and Giving Parents More Choice* Department for Education, January 2013.

¹²⁹ Watt, N., 'Nursery Ratios: Clegg Blocks Tory Attempts to Relax Childcare Standards', *The Guardian*, 6 June 2013.

¹³⁰ *Ibid.*

¹³¹ Thomas, D. & Gorry, D. *Regulation and the Cost of Child Care*, George Mason University, Mercatus Working Paper, August 2015.

teachers to have a high school diploma results in an increase in childcare costs of between 22 and 46 per cent.¹³²

The evidence reveals that the UK childcare sector is highly regulated by the government with rules relating to the ratio of staff members to children and also the level of training required for members of staff. Moreover, the childcare sector in the UK is heavily regulated compared to many other developed economies. The research suggests that this high level of regulation contributes to the high costs associated with childcare in the UK.

¹³² *Ibid.*

Energy

As with food and housing, energy is essential for households.

Energy prices have continued to rise over the past few years and so households are spending a significant proportion of their incomes on paying their energy bills. As a result, 'fuel poverty' is a reality for many people and so those on low incomes often face a stark choice between spending their income on food or on heating.

Total bills have risen around 28 per cent in real terms since 2004.¹³³ Bills rose rapidly from 2004 to 2008, since then they have fluctuated around the current level.¹³⁴ This has been against a backdrop of generally increasing prices and large reductions in energy consumption.¹³⁵

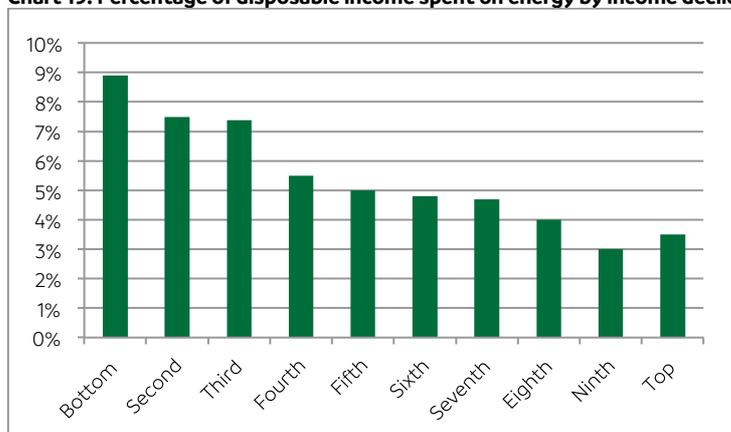
Price rises have been driven by higher wholesale energy prices, and the cost of low-carbon, policies have also increased by £90 since 2004.¹³⁶

Gas consumption for a typical dual-fuel household fell 37 per cent between 2004 and 2015, while electricity consumption fell 18 per cent.¹³⁷ If households consumed the same amount of gas and electricity as they did in 2004, average bills in 2016 would be £490 higher due to price rises.¹³⁸

Energy bills rose as a share of household total expenditure between 2004 and 2009, increasing from 3.4 per cent to 5.5 per cent. They have since fluctuated around that level.¹³⁹

Those in the lowest income groups spend a greater part of their total expenditure on their energy bills. The data reveals that those in the lowest income group spent 9 per cent of their total expenditure on their energy bills.¹⁴⁰ In comparison, expenditure on energy bills for those with the highest incomes made up only 3 per cent of total expenditure.¹⁴¹

Chart 19: Percentage of disposable income spent on energy by income decile



Source: ONS

Fuel poverty is a devolved matter and England uses a slightly different definition than the one used in Scotland, Wales, and Northern Ireland. Using the latest available data, we

¹³³ Committee on Climate Change, *Energy Prices and Bills- Impacts of Meeting Carbon Budgets*, March 2017.

¹³⁴ *Ibid.*

¹³⁵ *Ibid.*

¹³⁶ *Ibid.*

¹³⁷ *Ibid.*

¹³⁸ *Ibid.*

¹³⁹ *Ibid.*

¹⁴⁰ ONS, *Family spending in the UK: financial year ending March 2016*, 16 February 2017.

¹⁴¹ *Ibid.*

learn that 2,379,000 households in the UK are defined as 'fuel poor'. This amounts to 10.6 per cent of households.¹⁴²

In Scotland, the number of fuel poor households stands at 748,000 which amounts to 31 per cent.¹⁴³ In Wales the figure is 291,000 or 23 per cent of households.¹⁴⁴ The most recently available data for Northern Ireland reveals that the number of fuel poor households stood at 294,000 which is 42 per cent of households.¹⁴⁵

Looking to the future, electricity prices are projected to rise a further 33 per cent between 2016 and 2030.¹⁴⁶ This is due to expected further rises in wholesale and retail costs and climate policy costs. As for gas, prices are projected to rise a further 30 per cent within the same time period.¹⁴⁷

Given that rising energy prices are plunging many on low incomes into penury, energy prices have now become a hot topic for politicians. Consequently, the 2015 Labour manifesto contained a pledge to cap energy prices (a move which was condemned by the Conservative government as 'Marxist'). Then, during Theresa May's ill-fated bid to increase her majority in the House of Commons by appealing to the 'just about managing', the Conservative manifesto in the 2017 general election contained a very similar commitment.¹⁴⁸

The desire of politicians to ease the burden on low earners caused by very high energy prices is understandable. However, government intervention is not the answer. In fact, as with the other areas already discussed in this paper, government intervention is a contributing factor to spiraling energy costs.

A significant proportion of energy prices are the result of the various schemes that force energy companies to include minimum shares of energy from renewable sources in their portfolios. Those schemes represent a subsidy to the renewable energy sector which are paid through energy bills. Together with related green measures, they represent a significant proportion of the retail gas price and retail electricity price.

For example, the annual bill for a typical dual-fuel household in 2016 was around £1,160, of which £615 was for gas use and £545 was for electricity.¹⁴⁹ Approximately £105 (9 per cent) of the bill is the result of low-carbon policies.¹⁵⁰

Passing on the cost for subsidies to consumers clearly places a burden on households. This is supported by a report by Jenkins which found that environmental policies: "drive up energy prices directly through the environmental charges in the bill but also indirectly, and significantly, through the impact on generation and network investment costs".¹⁵¹

Furthermore, the total cost of renewable energy subsidies is also felt in other ways. For example, renewable energy subsidies also raise the cost of production in energy-intensive sectors which, in various ways, will also be passed on to consumers.

The main contributor to energy bills is the wholesale price of gas and electricity. However, it is clear that government intervention in the form of 'green' taxes and subsidies for renewable energy are an important factor in why energy bills are so

¹⁴² National Energy Action, *UK Fuel Poverty Monitor, 2016-2017*, 2017.

¹⁴³ *Ibid.*

¹⁴⁴ *Ibid.*

¹⁴⁵ *Ibid.*

¹⁴⁶ Committee on Climate Change, *Energy Prices and Bills- Impacts of Meeting Carbon Budgets*, March 2017.

¹⁴⁷ *Ibid.*

¹⁴⁸ *The Conservative Party General Election Manifesto 2017*, 18 May 2017, <https://www.conservatives.com/manifesto>.

¹⁴⁹ Committee on Climate Change, *Energy Prices and Bills- Impacts of Meeting Carbon Budgets*, March 2017.

¹⁵⁰ *Ibid.*

¹⁵¹ Jenkins, C., *What is Driving Energy Price Rises?*, Institute for Fiscal Studies, 2014.

expensive. As a result, UK households are spending a larger proportion of their income on energy.

Transport

Transport, although not essential in the same way as food or housing, is still vitally important for households. Furthermore, spending on transport represents the joint highest category of household expenditure, accounting for 14 per cent of weekly household expenditure.¹⁵²

A review of the academic literature reveals the importance of transport, especially to households on low incomes. For example, Ohnmacht *et al*, and Lucas, have argued that a lack of transport is linked to social disadvantage and exclusion.^{153 154} Moreover, Bauman has stated that those lacking the resources and transport options required for being able to move become deprived from interacting with the opportunities offered by society.¹⁵⁵

Furthermore, successive governments have recognised the importance of transport as it relates to living standards. For example, a white paper issued by the Department for Transport in 1998 stated:

Being unable to afford transport can limit everyday life. Job, training, and education opportunities are more limited and there is less choice in shopping, adding to family budgets of those least able to bear the cost.¹⁵⁶

In addition, the guidance to the Child Poverty Act 2010 stated:

Transport infrastructure, and accessibility to local service for children and parents, and employment opportunities for parents, are important in all local areas and are likely to be particularly so for those living in more remote or rural areas where the effects of growing up in poverty may be compounded by poorer access to services.¹⁵⁷

Driving

A major expense associated with owning and driving a car is the cost of petrol and diesel.

The average household spends £19.40 each week on petrol and diesel which amounts to 3.7 per cent of weekly expenditure.¹⁵⁸

The price of petrol is expensive in the UK by international comparisons when compared to other countries in the EU and the OECD.¹⁵⁹

However, the price of petrol in the UK would be one of the lowest in the EU and the OECD if it were not for the government. This is because the government levies fuel duty on petrol at a rate of 57.95 pence per litre and also VAT at a rate of 20 per cent.¹⁶⁰ When compared to other countries, total duty as a proportion of the price of petrol paid by consumers in the UK is one of the highest in Europe and is the highest in the OECD.¹⁶¹

As the graph below demonstrates, the reason why petrol prices are so expensive in the UK is because of the taxes levied upon petrol by the government. Without these taxes, petrol in the UK would be amongst the least expensive in the EU and the OECD and so households would face much lower costs.

¹⁵² ONS, *Family spending in the UK: financial year ending March 2016*, 16 February 2017.

¹⁵³ Ohnmacht, T., Maksim, H. & Bergman, M., (eds), *Mobility and Inequality*, (Aldershot: Ashgate, 2009).

¹⁵⁴ Lucas, K., *Transport and Social Exclusion: Where are we now?*, *Transport Policy*, 20, 105-113, 2012.

¹⁵⁵ Bauman, Z., *Liquid Modernity*, (Cambridge: CUP, 2000).

¹⁵⁶ Department for Transport, *A New Deal for Transport: Better for Everyone*, White Paper, 1998.

¹⁵⁷ *Child Poverty Act 2010*, <http://www.legislation.gov.uk/ukpga/2010/9/contents>.

¹⁵⁸ ONS, *Family spending in the UK: financial year ending March 2016*, 16 February 2017.

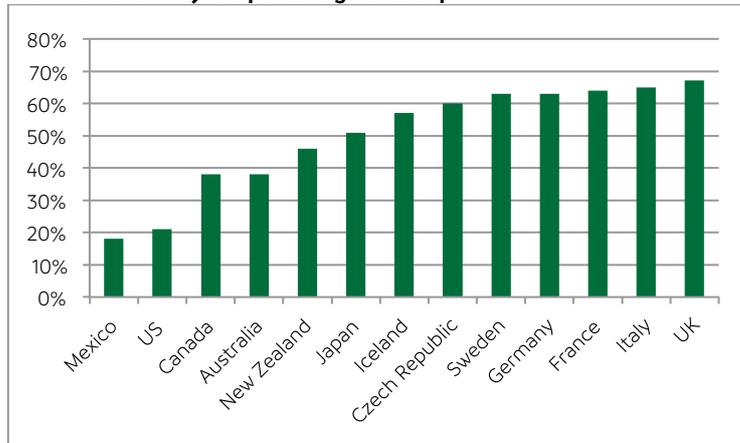
¹⁵⁹ International Energy Agency, *Energy Prices and Taxes Second Quarter 2017*, 11 July 2017.

¹⁶⁰ *Ibid.*

¹⁶¹ *Ibid.*

Given that the average price of petrol in the UK is 114.7 pence per litre,¹⁶² and the total duty including VAT levied upon it is 67.2 per cent,¹⁶³ if duties on petrol were abolished, then motorists in the UK would be paying only 37.62 pence per litre for petrol. Therefore, motorists in the UK would be paying 77.08 pence less per litre for petrol.

Chart 20: Total duty as a percentage of total price



Source: International Energy Agency

As the average price of diesel in the UK is 115.4 pence per litre,¹⁶⁴ and the total duty levied upon it is 66.9 per cent,¹⁶⁵ then if duties were abolished, motorists in the UK would be paying only 38.20 pence per litre for diesel. Therefore, motorists in the UK would be paying 77.20 pence less per litre for diesel.

As discussed above, having access to transport is incredibly important, especially for those on low incomes. However, the evidence would appear to suggest that duties on petrol and diesel are having a devastating impact on the budgets of the poorest households.

For example, a recent report from the RAC found that around 960,000 of the very poorest car owning households spent approximately one-fifth of their disposable income on buying and running a vehicle in the last financial year and spent 22 per cent of their weekly disposable income on the purchase and operation of a vehicle.¹⁶⁶

However, it is not only the taxes levied upon petrol and diesel which increase the cost of living for UK motorists; the government further exacerbates the problem by imposing vehicle excise duty upon motorists.

Three groups of charges apply, based on the date of registration of the vehicle: on or after 1 April 2017; before 1 March 2001; and between those dates.

VED on cars registered since April 2017 has an initial one-off rate in the first year based on bands of CO₂/km emissions, with a discount for alternative fuel cars. Rates in subsequent years are based on whether the list price is above a threshold (£40,000 in 2017-18) and whether the power is petrol/diesel, electric or alternative.

Cars registered before April 2017 pay one of 13 bands based on CO₂/km emissions (with lower rates for alternative fuel cars) unless they were registered before March 2001, in which case only two rates apply, based on whether the engine size exceeds 1549cc.

¹⁶² The AA, *Fuel Price Report: July 2017*, July 2017.

¹⁶³ International Energy Agency, *Energy Prices and Taxes Second Quarter 2017*, 11 July 2017.

¹⁶⁴ The AA, *Fuel Price Report: July 2017*, July 2017.

¹⁶⁵ International Energy Agency, *Energy Prices and Taxes Second Quarter 2017*, 11 July 2017.

¹⁶⁶ RAC Foundation, *Transport Poverty*, 02 March 2017.

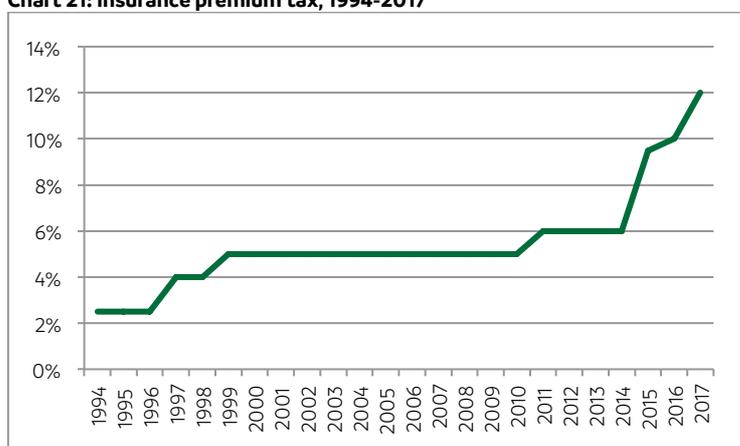
Four bands apply to motorcycles and two to tricycles, based on engine size. Light goods vehicles pay a single rate except some historic vehicles which comply with Euro 4 or Euro 5 emissions standards. Heavy goods vehicles pay VED and HGV road user levy based on the weight, number of axles and suspension type.¹⁶⁷

Vehicle excise duty places an extra burden on households as it increases transport costs. Moreover, vehicle excise duty has a disproportionately high impact on the lowest earning households as, according to Professor Stephen Glaister, they are less likely to be able to afford to purchase newer vehicles with lower emissions.¹⁶⁸

The government places even more strain on the household budgets of motorists by imposing insurance premium tax. Motorists pay insurance premium tax when they take out car insurance which is levied at a rate of 12 per cent.¹⁶⁹ The rate was relatively low and stable between 1997 and 2010, but has since increased significantly under both the coalition and Conservative governments.¹⁷⁰

Therefore, it is clear that the government exacerbates the financial difficulties faced by motorists. It does this by levying fuel duty and VAT on petrol and diesel, and by imposing vehicle excise duty and insurance premium tax.

Chart 21: Insurance premium tax, 1994-2017



Source: ABI

Trains

Despite receiving huge subsidies from the taxpayer, rail fares are still the most expensive in western Europe. For example, commuters into London can expect to spend an average of £387 per month, compared with £61 in Rome or Paris.¹⁷¹

Given that rail prices are so high in the UK, and that commuters are spending a significant proportion of their income on travelling by train and the detrimental impact that this has on their standard of living, the future of the rail industry in the UK has been the subject of much political debate.

For example in its 2017 general election manifesto, Labour pledged to renationalise the railway industry in the UK.¹⁷² Moreover, the results of polls conducted over the past few years suggest that renationalising the railway industry would be a popular policy.¹⁷³

¹⁶⁷ HM Government, *Calculate Vehicle Tax Rates*, 2017.

¹⁶⁸ RAC Foundation, *Cost of Motoring Hits Low Earners*, 11 December 2008.

¹⁶⁹ ABI, *The raid on the responsible continues- third rise in Insurance Premium Tax in under two years heaps more pressure on "just about managing" families*, 30 May 2017.

¹⁷⁰ *Ibid.*

¹⁷¹ European Commission, *Study on the Prices and Quality of Rail Passenger Services*, April 2016.

¹⁷² *The Labour Party General Election Manifesto 2017*, 16 May 2017, <http://www.labour.org.uk/index.php/manifesto2017>.

¹⁷³ A 2013 poll by YouGov revealed that 66 per cent of the public supported nationalising the railway industry.

Furthermore, there have been frequent calls from pressure groups and the media for the government to do more to stop rail fares increasing; the two which seem to gain the most traction involve the government capping rail fares and the further subsidising of the railway industry.

However, as we have already seen in this paper, government intervention is a key factor in why the cost of living is so expensive; train fares are no exception.

Further subsidising rail fares is not a sensible solution. Rail fares in the UK are already heavily subsidised and this places a very heavy burden on the taxpayer.¹⁷⁴ As we will see later in this paper, tax paid by the lowest earners already has an incredibly detrimental impact on their standard of living.

This raises the question of whether it is morally right for taxpayers to further subsidise train fares. Trains are more likely to be used by people on higher incomes, whereas those on lower incomes are far more likely to travel by car or by bus. The fact that the wealthy are far more likely to travel by train led the then transport secretary Philip Hammond in 2011 to admit that the railway is a “rich man’s toy”.¹⁷⁵

As discussed above, those on lower incomes who drive are already spending a significant proportion of their income on fuel duty, it is wrong that they should also have to subsidise train fares. It cannot be right that a cleaner from Huddersfield should have to subsidise the daily commute of a stockbroker from Sevenoaks to the City.

Moreover, subsidies could actually be contributing to high rail fares. For example, subsidies reduce the price of train tickets which provides an incentive for people to travel by train when they might not ordinarily choose to do so.

As discussed in the section on housing, when demand outstrips supply, upward pressure is placed on prices. This results in the market price of rail fares increasing.

Furthermore, calls for the government to place even more caps on train fares are also misguided. Train fares are already heavily regulated with approximately 45 per cent of fares set by a formula based on the retail price index figure for the previous July. Price caps have not eased the burden on commuters or taxpayers as they have done nothing to address the underlying market price.

In a free market, rail companies would be able to manage demand pressures by use of the price mechanism, but due to caps on rail fares enforced by the government, the train companies are unable to do so. As a result, they have focused on supplying new infrastructure to cope with demand. The cost of this spending on infrastructure is then reflected in the price of train fares.

It is not just rail subsidies which place a burden on taxpayers. The government also increases the pressure by embarking upon incredibly expensive infrastructure schemes such as HS2. Up to September 2016, the government had already spent £1.4 billion on the programme.¹⁷⁶ The Department for Transport’s latest figures assumes the total cost of the project, including rolling stock, will amount to £55.7 billion (2015 prices).¹⁷⁷ The National Audit Office calculated that the final cost for phase one (London to Birmingham) will be £27 billion.¹⁷⁸

¹⁷⁴ Office of Rail and Road, *Rail Finance Annual Statistical Release*, 2017.

¹⁷⁵ Millward, D., ‘Trains “Rich Man’s Toy” Admits Transport Secretary’, *The Telegraph*, 13 September 2011.

¹⁷⁶ Fairhead, H., *Rich man’s toy: The case for scrapping HS2*, TPA, July 2016.

¹⁷⁷ *Ibid.*

¹⁷⁸ National Audit Office, *High Speed 2 (HS2), Phase One*, House of Commons Library, June 2017.

The cost is set to continue to spiral out of control. An as-yet-unreleased report from the Cabinet Office found that the total cost could now rise to £104 billion.¹⁷⁹

We have seen that transport is vitally important for households as it enables them to reach employment and educational opportunities and allows them to engage with, and contribute to, society.

We have also seen that spending on transport represents the joint highest category of household expenditure, accounting for 14 per cent of weekly household expenditure. However, despite its importance to households, government policies have raised transport costs which have had a negative impact on household budgets, with poorer households being disproportionately affected.

¹⁷⁹ Hannan, D., 'We saddle our children with ideas from the past, like HS2, and debts from today. Where is the vision for the future?' *The Telegraph*, 22 July 2017.

Holidays

Another area of household expenditure to consider is holidays abroad. As with expenditure on restaurants and hotels, this can be classed as discretionary. However, holidays are very important to households. This is evidenced by the fact that there were 70.8 million foreign trips by UK residents in 2016, with UK residents spending £43.8 billion on visits overseas. The most frequent reason for these visits was for holidays.¹⁸⁰

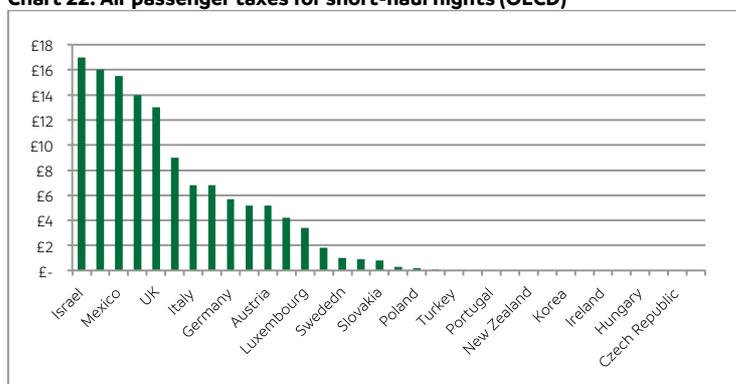
As a percentage of household expenditure, holidays abroad fall under the recreation and culture category. For the country as a whole, this was the third highest in terms of a proportion of household expenditure, and was the category with the highest spending for the North East, the North West, and Yorkshire and the Humber.¹⁸¹ These three regions spent 14 per cent of their total expenditure on recreation and culture, compared with 11 per cent in London.¹⁸² This disparity was driven by these regions spending a higher proportion of expenditure on package holidays abroad.¹⁸³

Despite the high value placed on holidays by households, the government makes them more expensive. One way in which the government does this is by imposing a sky high rate of air passenger duty on passengers departing from the UK.

APD in the UK is the highest aviation tax levied on passengers departing from airports in the EU, Norway, and Switzerland for both short-haul and long-haul flights in all classes.¹⁸⁴ UK APD is significantly higher than comparable taxes applicable elsewhere in Europe. For example, it is more than three times the rate in France, more than twice the rate in Germany, and almost twice the rate in Italy.¹⁸⁵

Furthermore, when compared to other OECD countries, UK APD is amongst the highest taxes applicable for travel in economy for short-haul journeys.¹⁸⁶

Chart 22: Air passenger taxes for short-haul flights (OECD)



Source: British Air Transport Association

Moreover, it is the highest for travel in economy for long-haul flights, and is the highest tax applicable for travel in higher classes.¹⁸⁷

Globally, on a per-passenger-kilometre basis, the UK ranks below countries in Africa and Latin America for short-haul journeys but above all other regions of the world.¹⁸⁸ As for long-haul flights, the UK ranks highest globally.¹⁸⁹

¹⁸⁰ ONS, *Family spending in the UK: financial year ending March 2016*, 16 February 2017.

¹⁸¹ *Ibid.*

¹⁸² *Ibid.*

¹⁸³ *Ibid.*

¹⁸⁴ Steer Davies Gleave & British Air Transport Association, *Flying High? How Competitive is air passenger duty?*, March 2016.

¹⁸⁵ *Ibid.*

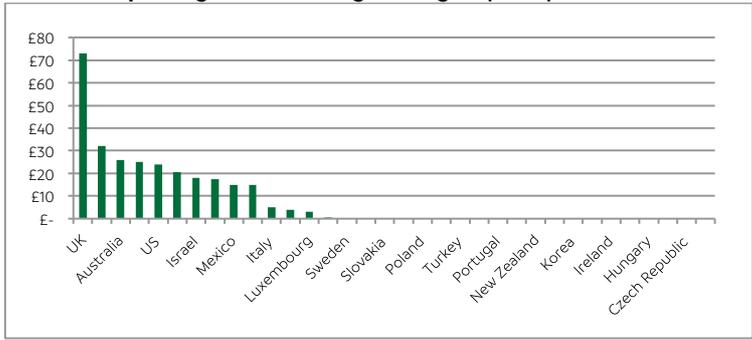
¹⁸⁶ *Ibid.*

¹⁸⁷ *Ibid.*

¹⁸⁸ *Ibid.*

¹⁸⁹ *Ibid.*

Chart 23: Air passenger taxes for long-haul flights (OECD)



Source: British Air Transport Association

APD has resulted in inflated costs for UK holidaymakers. For example, an average family jetting off to Spain this summer would have spent £26 on APD.¹⁹⁰ As for a family travelling to Florida, they would have spent £150 on APD.¹⁹¹

It is patently clear that APD raises the cost of holidays abroad for UK households. This puts further pressure on the budgets of already stretched households.

¹⁹⁰ Wild, A., *The Tax on Summer Holidays 2017*, The TaxPayers' Alliance, 14 August 2017.

¹⁹¹ *Ibid.*

'Sin' taxes

Alcohol and tobacco are considered demerit goods due to the health risks to the consumer associated with excessive consumption of these products, and also for the burden that this can place on society.

As a result, the government levies duties on tobacco and alcohol products which are essentially a Pigouvian tax designed to discourage their consumption and to also offset the negative externalities generated by their consumption.

Tobacco

In the UK, approximately 7.6 million adults smoke tobacco.¹⁹² Smoking rates are at an historic low with male smokers on average smoking 12 cigarettes each day and female smokers 11 cigarettes on average each day.¹⁹³ Average weekly spending on tobacco in 2015/16 was £3.60; this includes £2.80 average spending on cigarettes.¹⁹⁴

Smoking is significantly more common among those on low incomes, the unemployed, those suffering from mental health conditions, and the homeless. Data analysed by the ONS found that people who are unemployed are twice as likely to smoke as employed people.¹⁹⁵

Moreover, research by the Mental Health Foundation has revealed that smoking rates among people with depression is twice as high as among people without depression.¹⁹⁶ As for people suffering from schizophrenia, the smoking rate is three times higher than among people who do not have schizophrenia.¹⁹⁷ Furthermore, research by Baggett *et al* found that the homeless are far more likely to smoke than the general population.¹⁹⁸

Not only are the poorest in society most likely to smoke, they also tend to smoke more frequently and are less likely to quit.¹⁹⁹

Tobacco duty results in cigarettes being much more expensive. For example, a duty is levied at 16.5 per cent of the retail price plus £207.99 per 1,000 cigarettes. Therefore, for a packet of 20 cigarettes that amounts to £4.15 plus the 16.5 per cent.²⁰⁰

When one considers duty on tobacco as a percentage of disposable income, the average household spends 0.9 per cent.²⁰¹ The bottom quintile spends 2.2 per cent.²⁰² The second spends 1.8 per cent.²⁰³ The third spend 1.4 per cent.²⁰⁴ The fourth 0.7 per cent²⁰⁵ and, the top quintile spend 0.3 per cent.²⁰⁶

Given that the annual average income for households in the UK is £26,300, the average household spends £236.70 each year on tobacco duty.

¹⁹² ONS, *Adult Smoking Habits in the UK: 2016*, 15 June 2017.

¹⁹³ *Ibid.*

¹⁹⁴ ONS, *Family spending in the UK: financial year ending March 2016*, 16 February 2017.

¹⁹⁵ ONS, *Smoking Trends in Great Britain Since 2000*, 26 September 2013.

¹⁹⁶ Mental Health Foundation, *Smoking and Mental Health*.

¹⁹⁷ *Ibid.*

¹⁹⁸ Baggett, T., Tobey, M., & Rigotti, N., 'Tobacco Use among Homeless People- Time to Address the Neglected Addiction', *The New England Journal of Medicine*, 369: 201-204, 2013.

¹⁹⁹ Peretti-Watel, P., & Constance, J., "It's All We Got Left". Why Poor Smokers are Less Sensitive to Cigarette Price Increases', *International Journal of Environmental Research and Public Health*, February 2009.

²⁰⁰ HMRC, *Excise Duty- Tobacco Duty Rates*, 8 March 2017.

²⁰¹ ONS, *The effects of Taxes and Benefits on UK Household Income: Financial Year Ending 2016*, 25 April 2017.

²⁰² *Ibid.*

²⁰³ *Ibid.*

²⁰⁴ *Ibid.*

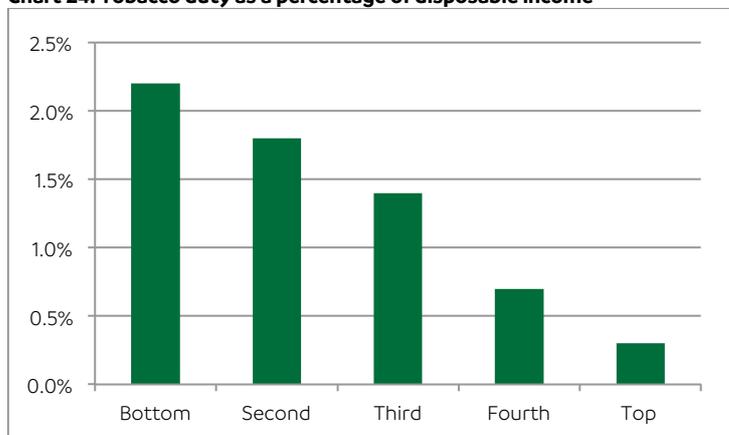
²⁰⁵ *Ibid.*

²⁰⁶ *Ibid.*

However, the situation may be even starker for those on the lowest incomes than the official statistics would suggest. This is because there is a significant amount of underreporting for tobacco consumption.

For example, research by Brewer & O'Dea revealed that approximately 40 per cent of all recorded tobacco sales show up in expenditure surveys.²⁰⁷ Moreover, average figures mask the fact that many people do not smoke.

Chart 24: Tobacco duty as a percentage of disposable income



Source: ONS

Research conducted by Snowden has attempted to calculate the impact on the lowest earning households of tobacco duties. He concludes that:

A smoker in the bottom income quintile who smokes an ordinary popular brand of cigarettes would tend to smoke around 19 cigarettes per day and would spend 21.8 per cent of their household disposable income on cigarettes, with the taxes alone taking up 16.8 per cent of their disposable income²⁰⁸

Therefore, the research would appear to suggest that taxes on tobacco are an even greater burden on the poorest households than the official statistics would appear to suggest.

Alcohol

As with tobacco, the government makes drinking alcohol more expensive for consumers by imposing a duty upon it. For example, alcohol duty means that a pint of beer is 52 pence more expensive²⁰⁹ and a pint of cider is 22 pence more expensive.²¹⁰ As for wine, a 750 millilitre bottle is £2.08 more expensive²¹¹ and a bottle of sparkling wine is £2.67 more expensive.²¹² A 70 centilitre bottle of whisky is £7.74 more expensive due to alcohol duty.²¹³

The average household spends 1 per cent of their disposable income on alcohol duty, which is equivalent to £263 each year.²¹⁴

In contrast to smoking, alcohol consumption tends to increase in line with income.

The bottom 40 per cent of earners are significantly less likely to drink than those on a higher income.²¹⁵ However, despite the rich consuming more alcohol than the lowest

²⁰⁷ Brewer, M., & O'Dea, C., *Measuring Living Standards with Income and Consumption: Evidence from the UK*, IFS, 2012.

²⁰⁸ Snowden, C., *Aggressively Regressive: The 'Sin Taxes' That Make the Poor Poorer*, IEA, October 2013.

²⁰⁹ HMRC, *Guidance- Alcohol Duty Rates*, 13 March 2017.

²¹⁰ *Ibid.*

²¹¹ *Ibid.*

²¹² *Ibid.*

²¹³ *Ibid.*

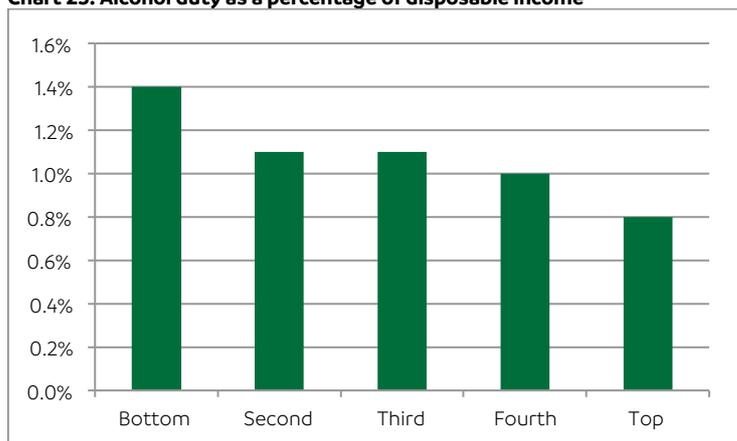
²¹⁴ ONS, *Family spending in the UK: financial year ending March 2016*, 16 February 2017.

earners, alcohol duties and VAT levied on the duty accounts for 2 per cent of the disposable income of the bottom quintile, but only 0.8 per cent of the income of the top quintile.²¹⁶

When one considers alcohol duty as a percentage of disposable income, the data reveals the following:

- The average household spends 1.0 per cent.²¹⁷
- The bottom quintile spends 1.4 per cent.²¹⁸
- The second quintile 1.1 per cent.²¹⁹
- The third quintile 1.1 per cent.²²⁰
- The fourth 1.0 per cent.²²¹
- The top quintile 0.8 per cent.²²²

Chart 25: Alcohol duty as a percentage of disposable income



Source: ONS

However, as is the case with tobacco, the official statistics may not reveal the whole picture. Brewer & O'Dea found that approximately 50 per cent of all recorded alcohol sales show up in expenditure surveys.²²³ Furthermore, average figures mask the fact that many people do not consume alcohol.

Research by Snowdon has attempted to calculate the true impact on the poorest households of taxes on alcohol. He found that:

The average drinker in the low quintile, if self-reporting was correct, would spend an average of 2.5 per cent of their income on alcohol taxes, rising to 3.7 per cent if drinkers underestimate by 50 per cent.²²⁴

Therefore, the research would appear to suggest that taxes on alcohol are having a significant impact on the budgets of households. Moreover, this impact could be far greater than what the official figures would appear to suggest.

Excessive alcohol and tobacco consumption can be detrimental to the health of those who abuse them. Moreover, excessive consumption can also result in costs to the health service, the police, and the courts and prisons. Therefore, it is fair from a Pigouvian perspective that there is some level of taxation on these products.

²¹⁵ ONS, *Adult Drinking Habits in Great Britain: 2005 to 2016*, 3 May 2017.

²¹⁶ ONS, *The effects of Taxes and Benefits on UK Household Income: Financial Year Ending 2016*, 25 April 2017.

²¹⁷ *Ibid.*

²¹⁸ *Ibid.*

²¹⁹ *Ibid.*

²²⁰ *Ibid.*

²²¹ *Ibid.*

²²² *Ibid.*

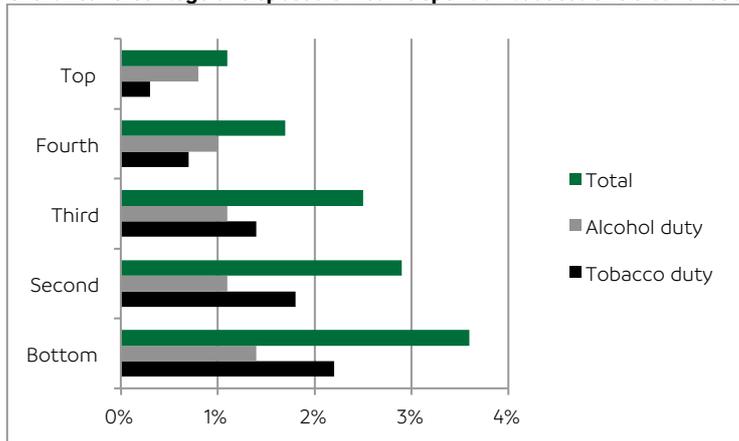
²²³ Brewer, M., & O'Dea, C., *Measuring Living Standards with Income and Consumption: Evidence from the UK*, IFS, 2012.

²²⁴ Snowdon, C., *Aggressively Regressive: The 'Sin Taxes' That Make the Poor Poorer*, IEA, October 2013.

However, the current level of taxation on these products far exceeds the damage caused by alcohol and tobacco consumption. Duties on alcohol and tobacco are excessive and have a disproportionate impact on those with the lowest incomes.

The government places taxes on the consumption of alcohol and tobacco, in part to discourage excessive use of these products, and also in order to raise revenue for HM Treasury. As discussed above, although a proportion of the duties go towards offsetting the potential damage caused to the individual and society by excessive use of these products, the amount of money raised by HM Treasury far exceeds the cost resulting from excessive use.

Chart 26: Percentage of disposable income spent on tobacco and alcohol duty by quintile group



Source: ONS

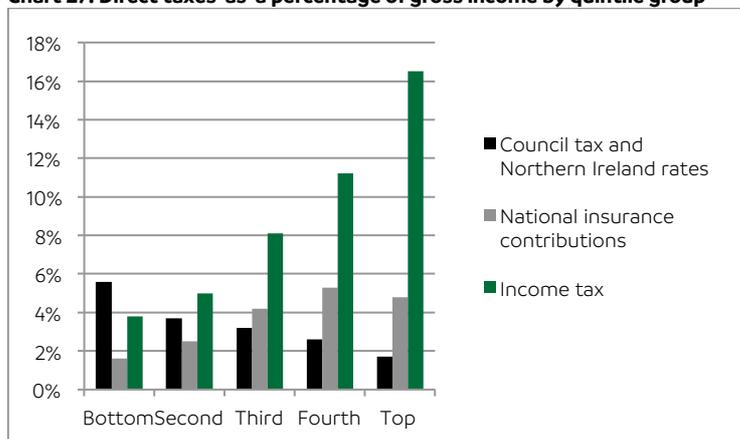
Furthermore, the evidence reveals that duties on alcohol and tobacco have a detrimental impact upon household budgets and, in the case of tobacco in particular, this is felt most keenly amongst poorer households. Moreover, it is highly probable that this impact on household budgets is even greater than the official statistics would appear to suggest.

Direct taxation

Direct taxation is a unique section in this paper as it does not relate to goods or services purchased by households. Rather, in the case of income tax and national insurance contributions, it is extracted from household incomes by the government.

It can also not be considered a choice as with many of the other items of expenditure. Instead, households have no choice but to pay their taxes, to do otherwise would result in sizeable fines, their property being confiscated, and even a prison sentence.

Chart 27: Direct taxes as a percentage of gross income by quintile group



Source: ONS

In 2016, households paid on average £7,800 per year in direct taxes, equivalent to 18.7 per cent of their gross income.²²⁵

The richest fifth of households paid on average £20,100 per year, which corresponds to 23.0 per cent of their gross income. The majority of this (16.5 per cent of gross income) was paid in income tax.²²⁶

The average tax bill for the poorest fifth of households was £1,600 per year, which is equivalent to 11 per cent of their gross household income.²²⁷

In this section we will consider three types of direct taxation which most households face: income tax; national insurance contributions; and council tax.

Income tax

Income tax in the UK operates through a system of allowances and bands of income.²²⁸ For example, those earning up to £11,500 per year pay no income tax. There is a basic rate, a higher rate, and an additional rate.²²⁹

Therefore, as soon as somebody starts earning more than £11,500 then they have to pay 20 per cent income tax.

The evidence would appear to suggest that this produces disincentives for people to work more hours. For example, Weber has argued that this was the case for men,²³⁰ and Ryznar found that this is also the case for married women where the husband is employed.²³¹ A similar point has also been argued by Harvard professor Gregory

²²⁵ ONS, *The effects of Taxes and Benefits on UK Household Income: Financial Year Ending 2016*, 25 April 2017.

²²⁶ *Ibid.*

²²⁷ *Ibid.*

²²⁸ Pope, T., & Waters, T., *A Survey of the UK Tax System*, IFS, November 2016.

²²⁹ *Ibid.*

²³⁰ Weber, M., *Measuring Disincentives to Formal Work*, World Bank, 2015.

²³¹ Ryznar, M., 'To Work or Not to Work? The Immortal Tax disincentives for married Women', *Lewis & Clark Law Review*, Vol. 13:4, 2009.

Mankiw.²³² According to the OECD, this is particularly true for the lowest earners.²³³ As a result, households on lower incomes are discouraged from working extra hours and so have less disposable income.

National insurance contributions

National insurance was originally introduced with the aim that only people who made national insurance contributions should receive benefits. The idea was that anyone paying the same, flat-rate premium would receive the same, flat-rate benefits if they became ill, lost their job, or reached retirement age.²³⁴ However, it now acts simply as a further tax on income which is used to fund the welfare state.

National insurance contributions represent a further burden on taxpayers and increases pressure on household budgets. For example, the poorest fifth of households paid on average of £240 in national insurance contributions in 2016.²³⁵ This is money which could have been spent by these households which are already struggling to make ends meet on other essential items.

Council tax

A further way in which the government increases the burden on households is through council tax. In the UK, domestic residences are banded according to an assessment of their market value; individual local authorities then determine the overall level of council tax, while the ratio between rates for different bands is set by central government.²³⁶

As with income tax and national insurance contributions, council tax places extra pressure on household budgets. The money spent on council tax could have been spent on other essentials such as food, rent, transport or on other important services such as childcare.

Moreover, the evidence would suggest that not only is council tax a burden on all households, but it is also exacerbating the financial difficulties faced by the poorest in society. For example, the data reveals that council tax made up the largest proportion of direct taxes for the lowest earning households, accounting for half of all direct taxes paid by them, 5.6 per cent of their gross income on average.²³⁷

It is right that a reasonable amount of money is paid in taxation to fund essential services and to provide opportunities for the most disadvantaged in society. However, taxation places a burden on households and prevents them from spending money on essential goods and services.

232 See, for example, this article: Mankiw, G., 'I Can Afford Higher Taxes. But They'll Make Me Work Less', *New York Times*, 9 October 2010.

233 OECD, 'Taxation and Employment', *OECD Tax Policy Studies*, No. 21, 2011.

234 Beveridge, W., 'Social Insurance and Allied Services', 1942.

235 ONS, *The effects of Taxes and Benefits on UK Household Income: Financial Year Ending 2016*, 25 April 2017.

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VAT

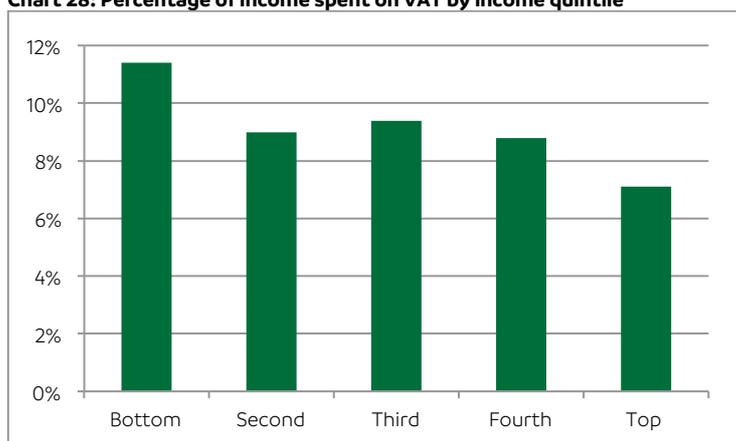
The standard rate of VAT has been 20 per cent since 4 January 2011.²³⁸ A reduced rate of 5 per cent applies to domestic fuel and power, women's sanitary products, children's car seats, contraceptives, certain residential conversions and renovations, certain energy-saving materials, and smoking cessation products.²³⁹ A number of goods are either zero-rated or exempt.²⁴⁰

The richest fifth of households paid nearly three times as much in indirect taxes as the poorest fifth (£9,700 and £3,500 per year, respectively).²⁴¹ This reflects greater expenditure on goods and services subject to these taxes by higher income households. However, although richer households pay more in indirect taxes than poorer ones, they pay less as a proportion of their income.

For example, the richest fifth of households paid 14.4 per cent of their disposable income in indirect taxes including VAT, while the bottom fifth of households paid the equivalent of 27 per cent of their disposable income.²⁴² Again, the proportion of disposable income that is spent on VAT is highest for the poorest fifth and lowest for the richest fifth.

The average of all income groups for VAT as a percentage of disposable income by quintile groups is 8.4 per cent.²⁴³ For the bottom quintile it is 11.4 per cent.²⁴⁴ For the second quintile it is 9 per cent.²⁴⁵ For the third it is 9.4 per cent.²⁴⁶ For the fourth it is 8.8 per cent,²⁴⁷ and for the top quintile it is 7.1 per cent.²⁴⁸ This means that the average household spends £2,209.20 on VAT each year.

Chart 28: Percentage of income spent on VAT by income quintile



Source: ONS

Therefore, we can see that in terms of a percentage of disposable income, it is those on modest incomes who pay the most and who are most adversely affected by VAT.

As with direct taxation, it is right that the government raises some revenue in order to fund legitimate schemes and essential services. However, VAT does increase the cost of goods for services. As a result, increased pressure is placed on household budgets, with the poorest households being the most adversely affected.

²³⁸ Pope, T., & Waters, T., *A Survey of the UK Tax System*, IFS, November 2016.

²³⁹ *Ibid.*

²⁴⁰ *Ibid.*

²⁴¹ ONS, *The effects of Taxes and Benefits on UK Household Income: Financial Year Ending 2016*, 25 April 2017.

²⁴² *Ibid.*

²⁴³ *Ibid.*

²⁴⁴ *Ibid.*

²⁴⁵ *Ibid.*

²⁴⁶ *Ibid.*

²⁴⁷ *Ibid.*

²⁴⁸ *Ibid.*

Conclusion

In this paper we have seen that households in the UK face costs for a variety of goods and services. Many of these are essential, whilst others are not as important for survival but are still of great importance to households.

As for taxation, this is an unavoidable cost for households. We have also seen that prices associated with these goods and services place a burden on low and middle income households.

In light of the financial difficulties now faced by people on modest incomes, politicians and the media are understandably concerned. As a result, there is now a consensus amongst the major political parties of the UK that the government should be doing more to ease the burden.

However, we have seen in this paper that such a position, although based on good intentions, is unwise. Having analysed the impact of various government policies in different sectors we have seen that rather than ameliorating the burden on households, government policies have actually compounded it.

Trips to the supermarket, travelling to work, holidays abroad, energy bills, and providing care for children are all more expensive due to various government policies. Furthermore, the cost of buying or renting a home is now simply unaffordable for many people due to planning regulations. Finally, the government augments the pressure on households by reducing their incomes through taxation.

It is patently clear that government intervention is one of the main reasons why the cost of living is so high in the

UK and why many households are struggling to make ends meet.

Therefore, if we want to alleviate the financial hardships faced by households in the UK then the answer is not more government action. If we want to see the cost of living come down then the government needs to do less, not more.

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