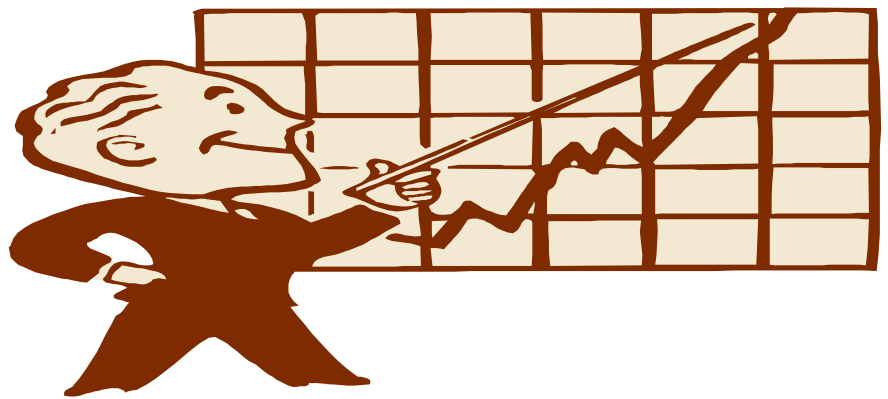
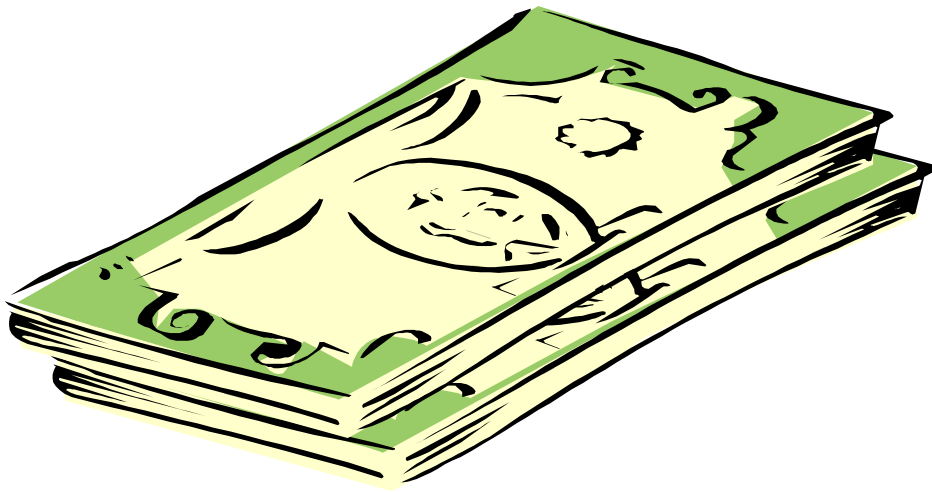


# TAXATION



By

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## **WHAT IS DIRECT AND INDIRECT TAX?**

**Direct tax:** *These are taxes that are collected by the Department of Inland Revenue. A direct tax is one that is deducted (taken out) from your salary or wages e.g. income tax.*

**Indirect tax:** *These are collected by the Customs and Excise Department. These taxes fall mainly on expenditures, that is, they are paid when money is spent on goods and services. They are known as indirect tax because it is possible for the person who pays the tax to pass the burden of the tax on to someone else.*

## *Why are taxes levied?*

*A tax is a levy paid by citizens and organisations to their government. There are several reasons why the government imposes tax.*

- ✦ To raise money to pay for public expenditure, most public spending is paid for taxes. The rest is paid for by royalties on North Sea oil, national insurance contributions; other sources, such as profits from nationalised industries or rents from council houses; and government borrowing.*
- ✦ To affect economic behaviour. For instance, taxes on cigarettes discourage smoking. Taxes on petrol encourage motorists to economise on fuel.*
- ✦ To help redistribute income between different individuals and between different sectors of the economy.*
- ✦ To help control the economy.*

## **WHAT ARE THE MAIN TYPES OF TAXES LEVIED IN THE U.K.**

### **INDIRECT TAXES: CUSTOM AND EXCISE TAX**

#### **VALUE ADDED TAX (VAT)**

*This is a tax on expenditure. There are different rates of tax. Essential commodities-food, water, children clothing, books, newspapers and public transport-are tax exempt (i.e. there is a zero rate). Domestic fuel (gas, electricity, heating oil and coal) is taxed at 8%. All other goods and services are taxed at 17.5%. VAT is collected by business and is imposed on the value added to a product by that business.*

#### **EXCISE DUTY**

*Excise duties are taxes levied on fuel, alcohol and betting. They are calculated not on value but on the volume sold. So excise duty is paid per litre of petrol or per bottle of wine for instance.*

#### **SPIRITS AND TOBACCO TAX**

*They are paid on quantity rather than value. For example the duty on a bottle of wine is the same whether the bottle cost £2 or £200. Where VAT on a £200 bottle would be 100 times as much as on a £2 bottle.*

### **DIRECT TAX**

#### **INCOME TAX**

*This is direct tax on a person's income, for example a single person is allowed to earn over £4335 free of tax. This sum of free tax is called tax allowance. Money earned on top of the tax, is taxed at 22%. So if an employee earned £10,000 and had a pay increase of £1000, £220 of that £1000 would go to the government's income tax. As the level of income increases the taxpayer pays higher rates of tax.*

#### **CORPORATION TAX**

*This is a tax on a company's profits. The rate of tax is 28% on profits over 1.5 million per annum. However companies can claim numerous allowances.*

#### **CAPITALS GAINS TAX**

*This is a tax on real capital gains- the difference between the buying price and selling price of an asset adjusted for inflation. Most goods and services are exempt, including the buying and selling of a person's home. It is paid mainly on stocks and shares.*

*INHERITANCE TAX*

*This is a tax on the value of assets left on death by an individual. The first £250,000 of any inheritance is tax-free. Thereafter it is taxed at 40%.*

## **EXPLAIN WHAT HAS HAPPENED TO THE AMOUNTS COLLECTED AS DIRECT AND INDIRECT TAX?**

### **A SHIFT FROM INCOME TAX TO VAT**

*The rate of VAT has increased from 8% to 15% in the budget of 1979. The tax allowed the government to raise extra revenue and at the same time allowed them to decrease income tax for millions of people from 60% down to 40%.*

*The government main aim is to reduce income tax and raise more money from VAT type taxes and excise duties on tobacco, petrol and spirits. In 1992 the government increased VAT again from 15% to 17.5% to help pay for the increased spending by the local councils.*

### **HAS THE TAX SYSTEM BECOME MORE REGRESSIVE?**

**Regressive:** *this is when people's income gets less but they may be paying more in taxes than before.*

*Since 1979 tax systems have shifted the amount of tax paid by the richer people to the less well off people who are now paying more taxes than before. The tax that has increased is VAT, which is paid on all goods, especially by poor families who may drink and smoke, more than well off people.*

### **PROGRESSIVE, REGRESSIVE AND PROPORTIONAL TAXATION**

**Progressive:** *The higher a person income the more tax they will have to pay. Income tax because the more people earn the more they pay in tax at different income levels (Capital Gains Tax is progressive), if you earn £6,000, you might have to pay 10% in Income Tax and if you earn £30,000, you might have to pay 30% in Income Tax.*

**Corporation tax and capital gains tax** *are also progressive in their structure. Corporation tax is paid on profits made by companies and shareholders of the company. Capital gains tax is very progressive and only paid by richer families who have enough financial assets. Inheritance tax is also progressive and only paid by richer families who have enough financial assets. Inheritance tax is also progressive because*

*this is only paid if you die and have more than £250,000 in assets and do not leave a will.*



## **HOW HAS THE CHANGE AFFECTED PEOPLE WHO PAY TAXES?**

*Indirect tax is usually regressive. A much higher proportion of low-income households budget is alcohol, tobacco and betting than that of high income households therefore excise duties are regressive. Items will form a disproportionate part of low-income budget, as food and public transport, are zero-rated therefore VAT is progressive. High-income earners save a large amount of their income compared to low-income workers. The balance of low income paid in VAT decreases and the income increases making a regressive effect.*

## **CONCLUSION**

*Taxation has shifted from better to a worse situation. This is because of the cuts in higher rate income tax. This has made income tax less progressive. In 1979, the rate of VAT increased from 8% to 15%. By 1991, it increased to a further 17.5%, which made the tax system more regressive. Hence, council tax is now more regressive compared to the rating system placed in 1979. People are taking advantage of the government, because they know they are guaranteed money if they do not have a job, therefore people just sit at home or work without informing the government therefore collecting two incomes.*

## **REFERANCE**

- ✦ *Source of tables (Inland Revenue Statistics)*
- ✦ *Text book (Economics for GCSE)*
- ✦ *Notes provided by the teacher*