

PAYSLP METHODOLOGY SERIES

Chapter 1 — Literature Review

Income Tax — England, Wales & Northern Ireland

*A thematic synthesis of statutory, regulatory
and policy literature*

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ABSTRACT

This literature review examines the statutory, fiscal and policy literature underpinning the calculation of personal income tax for employees and pensioners in England, Wales and Northern Ireland for the 2026/27 tax year. Synthesising primary sources from HM Revenue and Customs, the House of Commons Library, HM Treasury and the Low Incomes Tax Reform Group, the review identifies four cohering themes: the architecture of the Personal Allowance, the three-band rate structure, the Personal Allowance taper above £100,000, and the fiscal drag arising from the threshold freeze extended through April 2031 by the Autumn Budget 2024. The review argues that the published 'headline' rates of 20, 40 and 45 percent materially understate the effective marginal rate of tax for taxpayers in the £100,000–£125,140 income range, where the compounding effect of allowance withdrawal produces a 60 percent effective rate. This finding directly informs the implementation of the ukTax calculation engine. The review concludes with implications for tax-calculator design and identifies areas where the literature reveals enduring policy tensions.

Keywords: income tax, personal allowance, fiscal drag, PAYE, 2026/27, UK tax

1. Introduction

The taxation of personal income in the United Kingdom rests upon a body of primary legislation, secondary instruments, and annual fiscal events that together determine the liability of approximately 33 million income taxpayers (HMRC, 2026). For those whose income arises in England, Wales or Northern Ireland, income tax remains a wholly reserved matter, levied at rates and thresholds set by the United Kingdom Parliament at Westminster, notwithstanding the devolution of the Welsh Rates of Income Tax (WRIT) since April 2019, which to date have been set so as to produce no divergence from the UK figures (Welsh Government, 2026, as cited in House of Commons Library, 2026).

This chapter undertakes a thematic literature review of the principal materials informing the 2026/27 income tax calculation as implemented in the Payslp methodology. The review is necessarily synthetic rather than exhaustive: it draws on four core sources—the HMRC technical guidance on rates and personal allowances (HMRC, 2026), the House of Commons Library research briefing on direct taxes (CBP-10618), the HM Treasury Autumn Budget 2024 publication, and the Low Incomes Tax Reform Group's practitioner-oriented commentary on the personal allowance—and synthesises the position they collectively describe.

The chapter is structured as follows. Section 2 sets out the scope and methodological approach. Section 3 presents the literature review under four thematic headings: statutory architecture, the personal allowance and its taper, the rate-band structure, and the impact of threshold freezing as a mechanism of fiscal drag. Section 4 synthesises the literature and considers its implications for tax-calculator implementation. Section 5 concludes.

2. Scope and Methodological Approach

The literature reviewed in this chapter is restricted to materials directly bearing upon the calculation of income tax liability for an individual taxpayer resident in England, Wales or Northern Ireland for the tax year commencing 6 April 2026. Scottish income tax, governed by the Scottish Rate Resolution process

under the Scotland Act 2016 (c. 11), is considered separately in Chapter 2 of this Methodology Series. The review deliberately privileges primary statutory and governmental sources over secondary academic commentary: this prioritisation reflects the calculator’s purpose, which is to reproduce the figure a taxpayer would in fact be liable to pay rather than to advance theoretical perspectives on tax incidence or optimal design.

Four categories of source are drawn upon. First, official HMRC guidance, which represents the administering authority’s interpretation of the legislation as applied through Pay As You Earn and Self Assessment. Second, parliamentary research, particularly the House of Commons Library briefings, which offer independent technical exposition. Third, primary fiscal statements from HM Treasury, notably the Autumn Budget 2024 document, which contains the policy decisions that crystallised the 2026/27 rates and thresholds. Fourth, practitioner commentary from the Low Incomes Tax Reform Group (LITRG), which is particularly valuable for its accessible explication of interaction effects.

The review excludes commentary issued after the close of the May 2026 evidence window, on the basis that subsequent developments—such as any in-year administrative changes or Court rulings on individual liability disputes—do not ordinarily disturb the underlying statutory framework that the calculator must implement.

3. Literature Review

3.1 Statutory architecture and the source of legal liability

The Income Tax Act 2007 (c. 3) provides, at sections 3 to 10, the fundamental architecture under which income tax is imposed. Section 6 establishes the basic, higher and additional rates; section 10 fixes the basic-rate limit at £37,700 of taxable income. These figures are explicitly defined relative to taxable income, which is to say income net of the personal allowance, rather than relative to gross income—a distinction whose significance becomes acute in the personal allowance taper zone discussed below. HMRC’s technical guidance (2026) faithfully reproduces these statutory figures but tends, for accessibility, to describe rates by reference to the gross income at which they begin to bite (for example, that the higher rate ‘starts at £50,270’). The House of Commons Library (2026, CBP-10618) is more rigorous on this distinction and accordingly more useful for calculator implementation, which must operate on taxable rather than gross income.

The Income Tax (Earnings and Pensions) Act 2003 (c. 1) supplements ITA 2007 in respect of employment and pension income, providing the rules under which earnings are charged to tax under PAYE. Together these two statutes provide the legal basis for the great majority of the calculations a tax tool must perform.

3.2 The Personal Allowance and the taper above £100,000

The personal allowance for 2026/27 stands at £12,570, frozen at this level since 2021/22 and now scheduled to remain frozen until April 2031 following the policy reaffirmed in the Autumn Budget 2024 (HM Treasury, 2024). The Low Incomes Tax Reform Group (2026) emphasises that the personal allowance is not merely a deduction but a structural feature of the rate scale: its presence converts what would otherwise be a proportional tax into a progressive one even before the rate-band structure is considered.

More consequential, however, is the operation of the taper introduced by Finance Act 2009. Under section 35 of the Income Tax Act 2007 (as amended), the personal allowance is reduced by £1 for every £2 of adjusted net income above £100,000, ceasing to be available at all once adjusted net income

reaches £125,140. The House of Commons Library (2026) describes this device as the ‘hidden 60 percent rate’, and rightly so: an additional pound of income in the taper zone attracts the headline higher rate of 40 percent plus a further effective 40 percent arising from the withdrawal of fifty pence of allowance (taxed at the higher rate, yielding twenty pence) on top of the lost gross income. Sixty pence of every additional pound is therefore consumed by the Exchequer in the taper zone.

This is not an obscure technicality. According to HMRC’s personal tax statistics, approximately 1.1 million taxpayers have incomes in the affected range, and the LITRG (2026) observes that affected taxpayers frequently fail to understand the rate they actually face. The calculator must therefore implement the taper not as a separate adjustment but as an integral part of the income tax function.

3.3 The three-band rate structure

Above the personal allowance, three rates apply: 20 percent on the first £37,700 of taxable income, 40 percent on the next £87,440 (taking taxable income to £125,140) and 45 percent thereafter. The House of Commons Library (2026) presents these in the technically correct ‘taxable income’ basis; HMRC (2026) in the more colloquial ‘gross income’ basis. The discrepancy matters at the boundaries: a gross-income basis treats the higher-rate threshold as £50,270 (i.e. £12,570 + £37,700) and the additional-rate threshold as £125,140, but only the first of these is invariant. When the personal allowance tapers, the gross-income point at which the higher rate begins to apply shifts downward, while the band width in taxable income terms remains fixed at £37,700.

This subtlety has direct implementation consequences: a calculator that holds the gross-income band edges fixed at £50,270 and £125,140 independently of allowance tapering will systematically under-tax incomes in the taper zone. The Payslp implementation, following the House of Commons Library’s more rigorous formulation, expresses the bands in taxable income terms throughout.

3.4 Threshold freezes and fiscal drag

The Autumn Budget 2024 (HM Treasury, 2024) confirmed the extension of the freeze on the personal allowance and the higher-rate threshold to April 2031, a continuation of policy initiated by the then Chancellor in 2021. The House of Commons Library (2026) characterises this as the dominant fiscal policy lever of the current Parliament. Frozen nominal thresholds, when overlaid on positive nominal wage growth, produce ‘fiscal drag’: the gradual movement of taxpayers into higher rate bands without any explicit legislative increase in rates. LITRG (2026) emphasises the regressive distributional pattern that results, with the highest proportional impact falling on those whose income growth is concentrated near the higher-rate threshold.

4. Synthesis and Implications for Calculator Implementation

The four primary sources converge on a consistent picture of the 2026/27 income tax regime for England, Wales and Northern Ireland, but diverge in their framing of two issues particularly material to calculator implementation. The first is the basis of rate-band quotation, where the House of Commons Library’s technically correct taxable-income basis must be preferred over the HMRC guidance’s gross-income basis, on pain of error in the personal allowance taper zone. The second is the visibility of the effective marginal rate: the published 40 percent rate dramatically understates the position of taxpayers in the £100,000–£125,140 corridor, where the compounding of statutory rate and allowance withdrawal yields an effective 60 percent rate.

These findings produce three implementation requirements. First, the calculator must compute taxable income net of any tapered allowance before applying the rate bands. Second, it must hold band widths

invariant in taxable-income terms rather than treating the gross-income equivalents as fixed. Third, the user-facing presentation should make the effective marginal rate visible where it materially diverges from the headline rate. The Payslp implementation realises the first two requirements within the ukTaxWithPA function and pursues the third through the explanatory commentary displayed in the calculator results panel.

The literature also identifies a more diffuse but no less important policy context: the threshold freeze through April 2031, by maintaining fixed nominal thresholds against rising nominal wages, will progressively expand the pool of taxpayers facing higher rates. Calculator design must therefore anticipate not only the current legal position but the trajectory of liability as wage growth proceeds against frozen thresholds.

5. Conclusion

This review has synthesised the principal statutory, administrative and policy literature underpinning the calculation of personal income tax in England, Wales and Northern Ireland for 2026/27. The literature is internally consistent on the headline parameters—a £12,570 personal allowance, a £37,700 basic-rate band, a 40 percent higher rate to £125,140, and a 45 percent additional rate beyond—but reveals two areas in which differing presentation can mislead a non-specialist reader: the basis on which band thresholds are quoted, and the existence of the ‘hidden 60 percent rate’ arising from the personal allowance taper. Calculator design must accommodate both. The threshold freeze to April 2031 ensures that the practical importance of these features will grow rather than diminish over the remainder of the current Parliament.

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