Thursday 19 October 2006

TPA RESPONSE TO THE TAX REFORM COMMISSION REPORT

Comment from the TaxPayers' Alliance

Matthew Elliott, Chief Executive of the TaxPayers' Alliance, said:

> *"The Conservative Party has lacked a credible tax policy for some time, but this problem will be dealt with if they adopt Michael Forsyth's excellent report.*
>
> *"These proposals are a good first step towards reducing tax bills for ordinary families and giving the economy a boost by reducing taxes on businesses. As the report shows, other countries have benefited greatly from lower taxes. Britain can too."*

Summary

The TaxPayers' Alliance welcomes today's report by the Tax Reform Commission, which furthers the case for lower and simpler taxes in Britain.

The implementation of its proposals by any Government would be an important first step in the right direction for Britain. It would reduce the burden on families, improve competitiveness and help to stop businesses relocating abroad.

There are a number of proposals we think are particularly important:

- We support the proposals to reduce the basic rate of income tax to 20 per cent, raise the threshold at which people start paying income tax, abolish inheritance tax and exempt the family home from any tax on death, and cut the main corporation tax rate to 25 per cent. They would reduce tax bills for ordinary families and bring business taxes down to more competitive levels.
- We support the proposals to simplify business, personal and capital taxes and get rid of some of the senseless reliefs that clog up the system. We think that national insurance is another tax on income and moves to align the two will help people to see that. We hope that the proposed "Office of Tax Simplification" would do its job and reduce the ridiculous size of Britain's tax code.

- We are also delighted that the Commission has adopted our proposal to set up a dynamic model for the UK economy, which would show how tax changes really affect economic activity and government revenues. (The TaxPayers' Alliance has been making the case for the creation of a "Dynamic Analysis Division" within the Treasury for some time – we coordinated a letter to the Chancellor from 40 economists calling for this back in June).

Whilst we welcome the report, the TPA would have gone further in a number of areas, which we believe the Conservative Party and others should look at addressing in the future. For example:

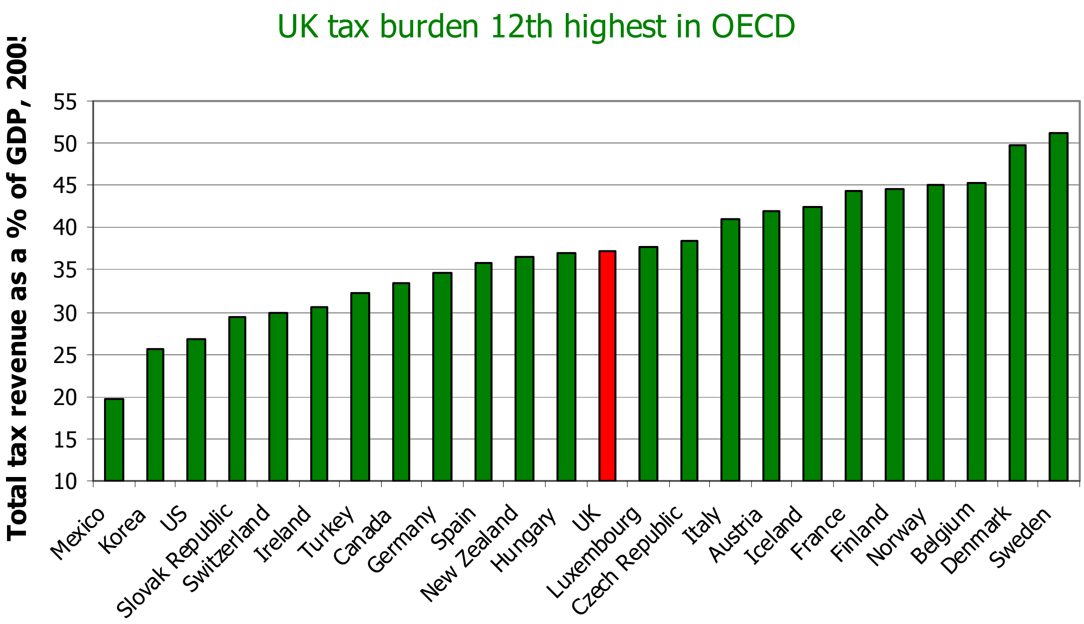
- Exempting the main home from any sort of tax on death, as the report proposes, would mean less unfair double taxation than currently with inheritance tax. But families would still have to pay tax on other assets that the deceased has held for less than ten years under the reformed capital gains tax. A "rollover relief", as there is in Ireland, would mean that tax is only paid if the family sells the deceased's assets.
- Raising the absurdly low threshold at which people pay top rate income tax would take middle earners, such as policemen and teachers, out of top rate tax.
- Reducing the main rate of corporation tax to 20 per cent as quickly as possible would mean that Britain was ahead of most European countries (although Ireland's main corporation tax rate is only 12.5 per cent).
- Fully merging national insurance and income tax would reduce administrative burdens for small businesses and mean that people would see how much tax they truly pay.

Why the Tax Reform Commission report is necessary

The relative health of the British economy over the last decade or so – compared to the sluggish economies of the Eurozone – has masked the fact that taxes have gone up significantly. Over time, this has begun to seriously affect families and businesses across the country. This rise in the tax burden needs to be addressed fast.

The scale of the rising British tax burden

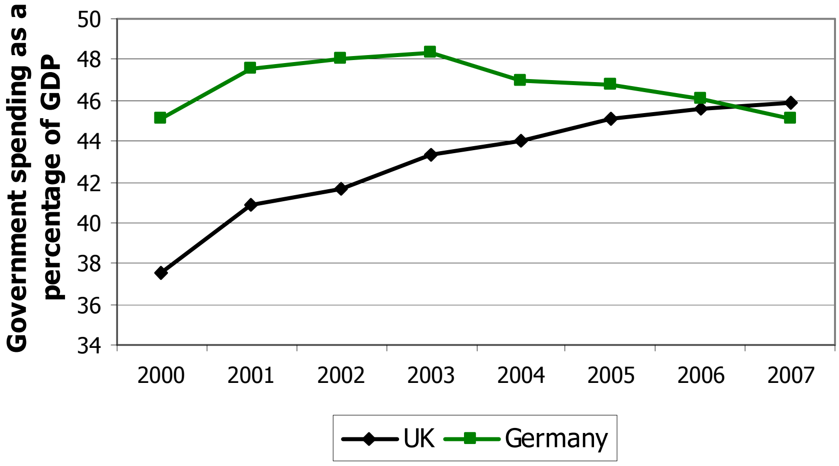
- Last week's OECD Revenue Statistics report showed that Britain's tax burden was the 12th highest in the OECD in 2005. Britain now has a higher tax burden than Germany.



Source: Table A, OECD Revenue Statistics 2006, October 2006. NB: data for 2005 is not yet available for six OECD countries.

- The same OECD report found that between 2004 and 2005, the UK's tax burden rose by 1.2 per cent of GDP. Only two OECD countries saw a faster rise in their tax burden. Separate OECD figures show that the UK's main rate of corporation tax is uncompetitive. It is now above the OECD average.
- The OECD's latest biannual Economic Outlook publication showed that Britain's public spending is set to overtake the level in Germany next year.

UK public spending overtaking Germany



Source: Annex table 25, OECD Economic Outlook No. 79, June 2006

The effects on families

The rising tax burden is making everyday life more difficult for ordinary families across the country.

- Figures published in July by accountants Ernst and Young showed that households' discretionary income (the amount that families earn after paying unavoidable expenses such as taxes and household bills) has fallen by 10 per cent since 2002.
- The number of higher rate taxpayers has increased from around 2 million in 1997 to 3.2 million today because tax thresholds have not risen in line with average earnings.
- New TaxPayers' Alliance research shows that the average household pays over £600,000 in direct and indirect taxes over a lifetime. A household in the poorest fifth pays almost £250,000.
- New research by the think tank Reform shows that young people pay a marginal tax rate of almost 50 per cent once student loan repayments and planned compulsory pension contributions are included.

People are becoming increasingly aware that the serious rise in the tax burden has not delivered what they were told it would deliver – better public services. An ICM Direct poll for the TaxPayers' Alliance in August showed that by 56-17 per cent, people believe that "if Britain reformed public services and cut waste it could lower taxes without having to cut spending on vital services".

The effects on businesses

- The rising tax burden is contributing to Britain's fall down the world competitiveness league tables. Since 1997, Britain has fallen from 7th to 13th in the World Economic Forum's ranking and from 9th to 21st in the Institute of Management and Development's index.
- Higher taxes and falling competitiveness are leading to businesses considering leaving Britain. A number of high-profile companies have already moved some of their operations overseas – including British Airways, high street bank Abbey, Norwich Union, Prudential and Royal & Sun Alliance. Others may follow. Reports suggest HSBC has may move its headquarters overseas in response to falling tax competitiveness (*Financial Times,* 6 October).
- The Director General of the CBI recently warned that the current "trickle" of companied relocating abroad may become a "flood". He said: *"Current corporation tax levels are unsustainable. Either companies will relocate or corporate taxes will have to come down"* (*Financial Times,* 9 October).
- In a global business tax roundtable on 25 September organised by the *International Tax Review* magazine, the Chairman of the Hundred Group of Britain's largest companies, Philip Broadley, said that there would be fewer compelling reasons for businesses to base their operations in the UK in future, and that this was partly due to the worsening tax system.
- As a *Financial Times* leader on 11 October warned: *"In the UK, the biggest and most productive sectors are also the ones that can most easily relocate abroad. To keep them in the country will require simpler, lower and better applied taxes."*
- Businesses are also being hit by the *complexity* of the current tax system. The Tax Reform Commission's survey of businesses found that *19 per cent are considering transferring operations outside of the UK because of the complexity of Britain's tax system.* The survey found that 78 per cent think the tax system has become more complex in the last five years and 60 per cent are having to increase spending on tax planning, law and advice.
- The trend of companies leaving Britain is also affecting individuals. An ICM Direct poll for the TaxPayers' Alliance in August 2006 found that one in five people knew of someone whose job had been affected by companies moving abroad.

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