Tax reform recommendations: what the think tanks think...

General Features



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Nine think tanks have suggested areas for revenue-neutral tax reform.

In advance of the 26 November Budget, nine think tanks published a list of seven areas where they recommended tax reform (see, for example, cps.org.uk/research/tax-reforms-for-growth). In all cases, the proposals are suggested as revenue-neutral to the Exchequer, which means that in return for a relief from tax in one area, tax would rise in a related area.

The think tanks covered a range of political views and are CenTax, the Institute for Public Policy Research, the Joseph Rowntree Foundation, Dan Neidle (Tax Policy Associates), the New Economics Foundation, Labour Together, the Adam Smith Institute, the Centre for Policy Studies and Bright Blue.

Real-world impacts

In most cases, these proposals look highly unlikely to be adopted – but I'm writing before the Budget, and you are reading this afterwards! There are three main reasons, I'd suggest:

- In most cases, the transitional implications are just too significant.
- Some involve increasing tax rates beyond levels generally accepted.
- Some ideas are a matter of opinion rather than a definitive economic view.

Many people have pointed out that council tax valuations in England and Scotland were set in 1991 – and everyone will be aware that while almost all properties have risen in value, the differentials between properties across the UK have changed substantially. A revaluation to current day values would mean millions of winners and millions of losers. Residential stamp duty land tax (and the devolved equivalents) amounted to £8.6 billion in 2023-24, compared to council tax of £44.5 billion. This would require a 20% increase in overall council tax to cover lost revenue. The challenge that governments would need to consider is how taxpayers would manage very significant additions to their annual tax liabilities – as well as the disruption to the property market while values adapted to changes, which couldn't be implemented immediately.

The capital gains tax proposals are based on the theory that investors use their capital to buy an asset – but it ignores the often more important entrepreneurial gains, where typically the individual has little capital to invest. Gordon Brown specifically introduced business asset taper relief to deliver a low capital gains tax charge to entrepreneurs. Abandoning that group by charging gains at 45% could encourage entrepreneurs to develop their business ideas elsewhere.

I would, however, like to see a change to the removal of childcare benefits once the taxpayer's income reaches £100,000. It cannot be right that earning a pound more costs many thousands in the withdrawal of tax-free childcare and nursery places. Unfortunately, the government has not published the cost of this, or how many households are affected, but fixing it is probably the cheapest thing on the list.

Package 1: Reform property taxes: This proposes abolishing stamp duty land tax, basing business rates on site values while removing empty property relief, and basing council tax on current house values with regular revaluation. Revenue neutrality would be achieved by adjustments to business rates and council tax to offset the loss of stamp duty revenue.

Package 2: Lower VAT and broaden the VAT base: This proposes broadening the VAT base to cover more types of spending and lowering the headline rate, with targeted compensation for lower income groups to offset higher costs on basic goods. The broader base would raise additional revenue, which would be returned through the reduced rate and targeted compensation for lower income groups.

Package 3: Address marginal income tax rates: This proposes reducing the marginal rate that applies to the removal of childcare subsidies, introducing a gradual taper for child benefit removal, and keeping marginal rates low for those on low incomes or moving off benefits. Revenue neutrality could be achieved by increasing the higher or additional rates or lowering their thresholds.

Package 4: Tax all income from work equally: This proposes merging employer and employee NICs with income tax, as proposed by the Mirrlees Review. Income tax rates would be adjusted to achieve neutrality.

Package 5: Tax landlords on profits as other income: This proposes allowing a full deduction for mortgage interest or equivalent borrowing costs, with an added top-up to account for NICs. Revenue neutrality would be maintained by adjusting headline income tax rates as needed.

Package 6: Do not distort incentives to invest in assets which grow in value: This proposes introducing an ‘investment allowance’ for capital gains, a carryover basis at death, and taxing only gains accrued in the UK with rebasing on arrival and deemed disposal on departure. Headline capital gains tax rates should be adjusted as needed to maintain revenue neutrality.

Package 7: Reform corporation tax: This proposes giving upfront relief for all business expenditure, ending the capital/income distinction and the bias toward debt over equity, and removing limits towards debt over equity investment. Headline corporation tax rates would be adjusted to ensure the reform remains revenue neutral.

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