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The future for taxes?

1 November 2019

George Crozier reports on the latest developments at the 2019 party conferences

Party conferences can be frenetic and feverish at the best of times. With a new prime minister locked in battle with MPs and the courts, party dynamics and public opinion reaching new peaks of volatility, an emergency return of a bad-tempered Parliament, and Brexit and an election both looming, this year's conference season was even more fractious and febrile than usual. Perhaps unsurprisingly, with everything else going on, it was a quiet year for new tax policy (Lib Dems aside), but there were still some helpful signs of what to expect in party manifestos if we do go to the polls this autumn.

Lib Dems in Bournemouth

The Liberal Democrat conference in Bournemouth backed radical changes to corporation tax, including restrictions to reliefs, a boost to capital allowances and extending the tax to cover highly profitable partnerships and other unincorporated businesses. Freelance workers and small unincorporated sole traders would continue to be taxed through the income tax and national insurance systems.

The new tax would be based on accounting profits with minimal adjustments. Standard tax incentives would be restricted to a maximum of 50% of taxable profits, meaning that no established profitable business should have an effective tax rate of less than 10%. The party would, though, retain cash R&D tax credits to support businesses as they develop.

The Lib Dems also propose substantial reforms to investment incentives, arguing the current regime has big dead weight costs, pushes businesses to take 'sub-optimal planning decisions' to tick boxes, enables undeserving businesses to shelter profits from taxation, is unnecessarily complex and lacks the transparency needed to judge whether incentives are providing value for money. Among the changes, the party proposes replacing patent box and entrepreneurs' reliefs with new incentives that better support early stage businesses.

Internationally the Lib Dems are committed to continuing the OECD BEPS project, but conclude that, ultimately, we will need a globally agreed system for allocating business taxes. This would – among other principles – recognise that businesses generate value from all the societies in which they operate and not just in their 'home' country (or adopted low-tax 'home').

In the meantime, the Lib Dems would make a number of changes to tackle aggressive tax planning by multinationals operating in the UK. These would include taxing profits where the business activity takes place following actual commercial reality and not legal form, and adopting a wider definition of permanent establishment. In particular, this would be aimed at ensuring that businesses selling advertising aimed at UK consumers or generating value from UK subscribers are captured within the UK business tax system. The party reckons this will raise an additional £2 billion a year. Perhaps surprisingly, the party does not endorse the government's plans for a digital services tax, being sceptical about both sector-specific taxes and taxing company revenues.

These changes to business taxation supplement far-reaching personal tax policies agreed by the party last year. These include taxing capital gains and dividends through the income tax system, abolishing the separate tax-free allowances for both, and turning inheritance tax into a progressive large gifts tax.

Labour in Brighton

The Labour Party outlined plans for widespread nationalisation, higher public spending and taxes and greening the economy, at its conference in Brighton.Tax had a relatively low profile at the conference. A number of Labour policies dating from the 2017 election manifesto were affirmed, including raising corporation tax for most companies back up to 26% and raising income tax for those earning more than £80,000. There appears to be little appetite within Labour for broader tax increases. Speaking at a fringe meeting, James Meadway, an economist who until recently was chief economic adviser to shadow chancellor John McDonnell, said the message that all but the highest earning 5% will not see an increase in income tax or national insurance had been effective in 2017 and would be again.

The biggest tax-related announcement around conference time was made the previous week, when McDonnell stated that he would abolish non-dom status in his first Budget. Labour will consult on whether they should make an exception for foreign residents who live in the UK only for a short period of time.

Other news from the fringe? McDonnell repeated his well-known enthusiasm for a financial transaction tax and reaffirmed Labour's proposal for a levy on overseas companies owning property in the UK. Shadow financial secretary Anneliese Dodds reaffirmed Labour's commitment to review council tax and business rates. Shadow chief secretary Peter Dowd said a Labour government would launch a public enquiry into tax evasion and avoidance and oblige anyone earning more than £1 million a year to make their tax returns public.

The place where most Labour economic policy is gestating is not Parliament but the think tanks of the left, most notably the New Economics Foundation (NEF) and the Institute for Public Policy Research (IPPR). NEF have been behind ideas such as the 'Green New Deal' – a motion passed by the conference said the cost of decarbonisation should be 'borne by the wealthiest through progressive taxation'. They are currently arguing for replacing the income tax personal allowance with a weekly cash payment of £48 a week, as well as using 'the levers of the state', including corporation tax, to incentivise businesses to reward their workers fairly. IPPR, of course, produced last year's 'Plan for the New Economy' setting out radical tax proposals across the board.

Conservatives in Manchester

There were no big tax announcements at this year's Conservative conference, but plenty of hints of what the new prime minister and chancellor would like to do, once Brexit is out of the way. Writing up its eve of conference interview with the prime minister, The Sun reported that: 'Boris Johnson told hard-up Brits to expect tax cuts in the upcoming Budget.' The Sun thought, however, that they could detect 'a strong hint that fuel duty would be frozen again or cut'.

The chancellor, for his part, hinted that he would like to cut inheritance tax, telling a fringe event: 'You pay taxes already through work or through investments and your capital gains in other taxes. There is a real issue with then asking them to, on that income, pay taxes all over again.' Cutting IHT would be tremendously popular among the Tory faithful. At a standing-room only fringe meeting, calls for the tax to be scrapped won rousing cheers.

For further hints on reforms which might be under consideration, it's worth recalling what the prime minister and chancellor said when they were leadership contenders a few months ago. Back then Boris Johnson argued for raising the threshold for the higher rate of income tax to £80,000 (later downgraded to an 'ambition'), raising the NIC threshold to align it with the income tax basic rate threshold, and raising the annual investment allowance threshold further. Sajid Javid, meanwhile, said in the summer that he was willing to scrap the 45p rate in a bid to inject more 'dynamism' into the economy, but his priority was to cut taxes for the low paid. He also said that fuel duty should be frozen for at least two more years and that he was looking at 'various options' for reforming SDLT.

There was a lot of support around the conference for the notion that the government should prioritise tax cuts that would have the biggest impact on economic growth. This means principally tax cuts for business – especially delivering the corporation tax cuts already promised (and more if possible). One radical possibility discussed on the fringe was a proposal for a single consolidated tax for small business. The idea is that companies with revenue of under £1 million should be given the option to replace corporation tax, business rates, VAT and employer's national insurance with a simple levy on turnover, charged on a cash basis. It came out of a report written earlier this year by a former special adviser to Javid, and Javid (then home secretary) praised the report's ideas at the time as 'compelling'.

SNP in Aberdeen

The final conference of the season saw the SNP meeting in Aberdeen. Derek Mackay, Scotland's finance secretary, used his keynote speech to defend the Scottish government's income tax changes, which mean lower earners (income of less than £27,000 a year) in Scotland are paying slightly lower tax than people on the same salary living elsewhere in the UK, while higher earners are paying more. 'While [Boris Johnson's Conservatives] plan tax cuts for top earners, we will always prioritise the communities who continue to bear the scars of a decade of Tory austerity,' he vowed.

A CIOT-sponsored fringe event debated how tax devolution was faring 20 years on from its inception. Pollster Mark Diffley presented evidence from a new poll of Scottish voters, which found that awareness of Scottish taxpayer status and where respective tax powers lie is low and falling. At the same event, Tom Arthur MSP acknowledged the challenges inherent in the current model of devolution, citing legal challenges preventing the devolution of air departure tax and aggregates levy and the anomalous 53% marginal tax rate because of the misalignment between the Scottish higher rate of income tax and the upper earnings limit for national insurance as examples. He suggested that this could facilitate future debates on the devolution or merging of NICs with the income tax regime.

Conclusions

The political environment seems to change from day to day. By the time you read this we may have Brexited (or not), may have had a Budget (or not), and may be in an election campaign (or not). But looking at a period of years rather than weeks, the economic battleground is becoming clearer. Everyone favours – at least rhetorically – simplification, tackling avoidance and international co-operation against profit-shifting. But there is a growing divide between a Conservative agenda which argues that the route to prosperity is low taxes, especially for business, and a Labour agenda that is increasingly ambitious for public services and will need to tap business and high earners – though not, it maintains, the average voter – to pay for them. There is also a divide between sympathy among non-Conservative parties for greater taxation of wealth and land, and most Tories' desire to roll back what taxes we already have in this area. Plus, there must be doubts about whether either main party can afford to deliver its spending plans without additional, yet to be announced, tax rises. Perhaps post-Brexit tariffs will help fill the gap? Only time will tell.

Full reports on each of the party conferences' tax discussions can be read on the CIOT website [1].

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[1] https://www.tax.org.uk/media-centre/blog