



The Freedom Association

The 50p tax rate - What it is and why it should be abolished

"Our 50p rate is higher than in Germany, France, the US, Switzerland, China... it's a long list. We've got to get a commitment that it will come down."

Boris Johnson, Mayor of London.

Written by Hasan Afzal

Introduction

Before the 50p tax rate came into force, there were three taxable bands from 10% to 40% of income tax with a personal allowance of £6,475. However, there are now four taxable bands, from 10% to 50% of one's income. The table below shows that the new 50% tax rate came into force in financial year 2010/11¹:

Rate	2009-10	2010-2011	2010-11
10%	£0 - £2,440	£0 - £2,440	£0 - £2,440
20%	£0 - £37,400	£0 - £37,400	£0- £35,000
40%	Over £37,000	£37,401-£150,000	£35,001-£150,000
50%	Not Applicable	Over £150,000	Over £150,000

The tax rate was proposed by the outgoing Labour administration of Gordon Brown and was confirmed in the Chancellor's budget of 2010 of the Coalition government.

This briefing paper sets out to explain why the 50p tax rate should be abolished and the government should introduce tax reforms concentrating on removing much of the tax burden facing Britons.

Budgets Out Of Control

At the time of the conception of the 50p tax rate, there was a considerable effort by politicians to show they were 'tough on the banks' as the Labour administration had saved a number of failing British banks including RBS and Northern Rock at the expense of massive government taxpayer spending.

As a result of the massive taxpayer spending, British public debt was £424 billion in 2005 but recent data puts British public debt to £932 billion for financial year 2010² with public net debt estimated to reach £1284 billion in 2015 (estimate from HM Treasury 2010 budget).

The high level of debt is also complimented with a continued and sequential increase in government spending from financial year 2011 to 2015 as general government debt is expected to increase by 14.7%³ with so-called 'government cuts' in effect.

¹ HM Revenue & Customs. "HM Revenue & Customs: Income Tax Allowances." *HM Revenue & Customs: Home Page*. Web. 30 Jan. 2011. <<http://www.hmrc.gov.uk/rates/it.htm>>.

² UK Public Spending. "Public Spending Chart for United Kingdom 2000-2015 - Central Government Local Authorities." *UK Central Government and Local Authority Public Spending 2012 - Pie Charts Tables*. Web. 30 Jan. 2011. <<http://www.ukpublicspending.co.uk/>>.

³ UK Public Spending. "Public Spending Chart for United Kingdom 2000-2015 - Central Government Local Authorities." *UK Central Government and Local Authority Public Spending 2012 - Pie Charts Tables*. Web. 30 Jan. 2011. <<http://www.ukpublicspending.co.uk/>>.

With such levels of government debt and spending to commit, it may seem rational for government policymakers to increase taxation in an attempt to bring more revenue to the treasury. However, this view is flawed as history suggests when government increases tax, the results are often to the detriment of economic growth.

Betting Against The Trend

Historically, tax increases do not increase government revenue. They have the opposite effect.

In the United States, when President Ronald Reagan enforced tax cuts for the public, at a time when the country had record inflation and high public debt, the share of income tax contributions actually increased for the highest 10% of taxpayers climbing from 48% in 1981 to 57.2% in 1988⁴.

Whilst in Ireland, capital gains tax was substantially cut by 40% to 20% in 1997 and, as a result, net receipts went from £83.7m in 1996 to £132.4m, £193.1m and £356.2m in 1997, 1998, 1999 respectively⁵.

By taxing the rich, the definition of 'rich' being anyone who earns over £150,000, the government inhibits the incentive of highly wealthy and highly mobile individuals in investing in the United Kingdom.

As a result of negative sentiment towards wealth-creators, Britain's position as a top location for Foreign Direct Investment (FDI) has been hurt substantially. In a Sunday Times article in 2006, the UK was quoted as being 'the top choice for Foreign Direct Investment' with an increase of £98.2 Billion of investment in just one year⁶.

The position of Britain's FDI has been hurt substantially as a result of the economic crisis. The United Nations Conference on Trade and Development claims that Britain's FDI flow plummeted well below global averages in 2009 from \$91Bn in 2008 to \$46Bn⁷ - a decrease of 49% percent with the global average being 37%. These cuts were attributed without the heavy burden of the 50p tax rate, Britain's high tax burden can not have a positive effect to attracting Foreign Direct Investment into the country creating jobs and prosperity.

⁴ The Heritage Foundation. "The Historical Lessons of Lower Tax Rates | The Heritage Foundation." *Conservative Policy Research and Analysis | The Heritage Foundation*. Aug. 2003. Web. 30 Jan. 2011. <<http://www.heritage.org/research/reports/2003/08/the-historical-lessons-of-lower-tax-rates>>.

⁵ Adam Smith Institute. *Estimated Revenue Losses from Capital Gains Tax Increases*. Briefing Paper. Web. <<http://adamsmith.org/files/CGT-II.pdf>>.

⁶ Duncan, Gary. "UK Becomes Top Choice for Foreign Direct Investment - Times Online." *The Sunday Times*. 29 June 2006. Web. 30 Jan. 2011. <<http://business.timesonline.co.uk/tol/business/economics/article1095140.ece>>.

⁷ United Nations Conference on Trade and Development. "UnctadStat - Table View." *United Nations Conference on Trade and Development*. 2008. Web. 30 Jan. 2011. <<http://unctadstat.unctad.org/TableViewer/tableView.aspx>>.

Parliamentary Activity

The 50p tax has been mentioned a number of times in the Houses of Parliament. In January 2011, the Business Secretary, Vince Cable, made clear his own dissatisfaction of the tax⁸:

Andrew Bridgen (North West Leicestershire, Conservative): *Does the Secretary of State agree that although the 50p rate of tax may be necessary in the short term, it will have a detrimental effect on economic growth in the UK in the medium to long term? It scares away foreign investors, acts as a disincentive for home-grown entrepreneurs to start businesses and offers a massive incentive for some of our brightest and best business brains to leave this country and pay less tax elsewhere.*

Vince Cable (Secretary of State, Business, Innovation and Skills; Twickenham, Liberal Democrat): When I was in opposition I spent quite a lot of political energy arguing against a 50p tax rate. However, in the present context we have to understand that the burdens of the very difficult period through which we are passing have to be shared fairly, and that is why the tax remains in place.

Vince Cable's answer is an accurate representation of the standard government response when ministers are pressed for an answer on reform on the 50p tax reform. The Prime Minister has offered a similar answer⁹. There is little different to the answer the previous administration used to provide.

Charlie Elphicke (Dover, Conservative): *Does the Prime Minister, like the shadow Chancellor, believe that the 50p tax rate should be temporary?*

David Cameron (Prime Minister; Witney, Conservative): *Yes, I agree with the shadow Chancellor. The interesting question is whether he agrees with the Leader of the Opposition ...*

In the House of Lords, there has been debate focused on just how 'temporary' the 50p tax rate is. Below is a series of questions directed at the former Parliamentary Secretary to HM Treasury, Lord Myners¹⁰:

⁸ HC Deb, 13 January 2011, c427

⁹ HC Deb, 24 November 2010, c264

¹⁰ HL Deb, 1 February 2010, c4

Baroness Valentine (Crossbench): *The Chancellor recently stated that the 50p top rate of income tax was not a matter of ideology. If in practice it will do little to increase tax revenue and instead may drive away many of those contributing the most to the Exchequer, what is it a matter of?*

Lord Myners (Parliamentary Secretary, HM Treasury; Labour): *It is a matter of meeting the finance requirements at a time when the public sector has a very large deficit. The broadest shoulders must, quite rightly, bear the greatest burden. We are talking about less than 2 per cent of the population by income, a section which has enjoyed an increase in earnings at more than double the median rate over the past 10 years. However, it is not a commitment of ideology. This Government wish to see a reduction in the higher rate of taxation as soon as it makes sense, from the point of view of prudent macroeconomic management.*

Lord Forsyth of Drumlean (Conservative): *My Lords, can the Minister indicate whether the first Minister, Secretary of State, et cetera, et cetera-the noble Lord, Lord Mandelson was speaking for the whole Government when he said that the top rate of income tax at 50 per cent was going to be a temporary measure?*

Lord Myners (Parliamentary Secretary, HM Treasury; Labour): *In her supplementary question the noble Baroness has already quoted the Chancellor of the Exchequer, saying it is not a matter of ideology. I have also said that we wish to see a reduction in the top rate of taxation as soon as it makes economic sense. I suggest to the noble Lord, Lord Forsyth, that it is not possible to drive a wedge between the First Secretary, the Chancellor and myself on these matters: we are at one. That gives us greater credibility. It may well be a route that the Opposition Front Bench wants to try- although as I warned last week, we have to continue to listen to our wireless very carefully to keep up to date with Tory thinking on matters. We have seen this over the weekend: now we are looking forward not to an age of austerity but to one of slow and modest cuts in public expenditure.*

The exchange shows that even in the Brown Administration, the duration of which the 50p tax rate would apply for was a mystery with ministers giving very similar responses to today's administration.

Also in February 2010, Baroness Noakes attacked the high levels of taxation that the previous New Labour administration had enforced whilst in office¹¹.

Baroness Noakes (Shadow Minister, Shadow Minister; Conservative): *My Lords, according to the World Economic Forum's report on competitiveness, the UK was ranked fourth in terms of the lowest tax burden and tax evasion in 1997, and 84th in 2009-10. Does this have something to do with the Government's policies of high taxation?*

Lord Myners (Parliamentary Secretary, HM Treasury; Labour): *The UK has the lowest rate of corporate tax in the G7 at 28 per cent. The tax-to-GDP ratio is 36.1 per cent, which continues to be below the EU15 average and the G7 rate. At 18 per cent, the CGT rate is extremely low, and we continue to take measures through the tax system to encourage new business. I do not think the answer lies in taxation.*

Despite the fact that the Coalition government has increased taxation whilst in office, the above exchange is case in point on the effects of high taxation and endless bureaucracy on businesses. It is hoped this government will honour its commitment to cut petty bureaucratic procedures that are a blight to the business community.

Voices of reform

A number of politicians, policymakers and organisations have publicly criticised the 50p tax rate and many have done so for the reasons stated above.

The British centre-right think tank 'Reform' commented on the Budget 2010 briefing adding that the tax rates increase 'complexity and reinforcing perception of UK as [a] hostile tax jurisdiction'¹².

The Mayor of London, Boris Johnson, has added his support for reform of the 50p noting 'Our 50p rate is higher than in Germany, France, the US, Switzerland, China... it's a long list. We've got to get a commitment that it will come down.'¹³

The Liberal Democrat Member of Parliament David Laws has also expressed support for the withdrawal of the 50p tax rate as he criticised the Leader of the Opposition, Ed Miliband,

¹¹ HL Deb, 1 February 2010, c5

¹² Haldenby, A., P. Nolan, L. Parsons, and N. Seddon. *Briefing Note: Budget 2010*. Rep. Mar. 2010. Web. 30 Jan. 2011. <<http://www.reform.co.uk/portals/0/Documents/Budget%25202010%2520Briefing%2520FINAL.pdf>>.

¹³ Blackhurst, Chris. "The MT Interview: Boris Johnson - Leadership, Business and Management News, Tips and Features from MT and Management Today Magazine." *Management Today*. 01 Jan. 2011. Web. 30 Jan. 2011. <<http://www.managementtoday.co.uk/news/1047368/MT-Interview-Boris-Johnson/?DCMP=ILC-SEARCH>>.

position 'that cuts should be delayed and that high tax rates (including the 50% tax rate) should be retained'.

The quotes are welcomed by The Freedom Association as they show a healthy tradition of classical liberalism with influential policymakers and politicians but also show a strong cross-party consensus can be established between both coalition partners.

Conclusion

It is recognised that the government does, at times, have legitimate reasons to increase taxation for the purpose of increasing government revenue. However, the line of which government taxation begins to substantially hurt the prosperity and the growth of the UK economy is somewhat of an art more than an exact science.

In respect to the 50p tax rate, the above evidence shows that the sentiments and foundations behind the tax hike are to the detriment of entrepreneurship and innovation to the UK economy. The tax was brought in as a result of a need to politically manoeuvre the former Labour administration to the populist position of 'bashing bankers'.

The result of the implementation of the tax has resulted in the view that business in Britain has become more difficult and more expensive to the risk-takers who ultimately provide the capital for jobs and investment.

In conclusion, as a result of the reasons set out above, the Freedom Association recommends the 50p tax hike be abolished as soon as possible.