

TAX POLICY: A FULLY PROGRESSIVE TAX SYSTEM

At Labour's heart is the commitment to create "a community in which power, wealth and opportunity are in the hands of the many not the few, where the rights we enjoy reflect the duties we owe". Our tax policy must reflect this and address popular concerns to ensure that under Labour:

- 1) The inequality gap closes via a fully progressive tax system
- 2) All taxpayers pay a fair amount of tax on their income and capital gains
- 3) The UK's international reputation is not undermined by harmful tax competition or a perceived lack of morality in tax.

This paper focusses on the first of these concerns.

Income Tax

From 1913-1980, Britain's fully progressive tax system was central to increasing income equality. In 1978/79 UK income tax rates spanned 25-83%. This became 30-60% from 1980/81 on, as Conservative governments abolished the reduced rate tax for Britain's poorest and slashed the higher rate of tax. By 1988/89 a two-step 25-40% income tax system was entrenched. Subsequently, income inequality has risen sharply.

To reduce income inequality it is necessary to return to fully progressive tax rates graduated across all income bands. This must be established as a permanent change in policy.

Voters seek a mature discussion on tax, having been persuaded by arguments where any "pain" is seen to fall most on those with the broadest shoulders. Fully progressive rates can be re-introduced over successive years simply by reversing the pattern followed from 1978/79 to 1988/89, with suitable indexation or uprating of income bands. For example, if the 50% band is to begin at £150,001 the 60% band might begin at £250,001.

Capital Gains Tax

Simultaneously, capital gains must be taxed at the rate levied on an individual's top slice of income. This will prevent the avoidance of tax by shifting income into gains.

Relief for pension contributions

Tax relief for contributions into a pension scheme should be limited at the ceiling of a tax band containing median male earnings.

Deductibility of mortgage interest

Buy-to-let investments have skewed the UK housing market. Labour should support a review of the tax deductibility of mortgage interest against rents and property income. A wider review of letting agents' charges should also be considered.

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Corporation Tax

In 1979 the UK's mainstream corporation tax rate was 52%; by 1986 it was 35% - having been reduced to 50% in 1983 and again in three 5% tranches annually from 1984. After a further small reduction in 1990-91, it settled at 33% until 1996. Later, from 1999-2007 it was held at 30%. The Coalition has reduced the inherited 28% rate and is working towards a 22% rate for Financial Year 2014.

Cuts to the corporation tax rate from 1997-2010 alone lost the Exchequer an estimated £50bn in revenue. Labour must return the UK's mainstream corporation tax rate to 30% over three financial years and should also introduce an alternative minimum tax like the USA.

Ultimately, mainstream corporation tax rates must be restored, so that company income and gains are taxed at a rate equivalent to that levied on an individual paying a higher rate of tax. This will prevent the avoidance of tax via the use of personal service companies without the need for complicated and unpopular regulations such as IR35. The small companies' rate prevents an undue burden falling on new or developing companies.

Labour should work internationally to agree minimum levels of corporation tax to prevent harmful tax competition. A starting point would be an EEA-wide agreed minimum tax rate of 30%.

VAT

Labour should commit to reducing VAT immediately to 17.5%, with a priority of reducing VAT to 15%.