

Baroness Jo Valentine's speech in the Lords taxation debate

28 January 2010

(Lord McNally to call attention to the case for a fairer and more progressive tax system)

My Lords, I declare an interest as chief executive of London First, a non-profit-making business membership organisation that works to secure London's competitiveness as a location for globally mobile business.

I congratulate the noble Lord, Lord McNally, on securing this debate. From a business perspective, taxes fund investment, which is vital to our competitiveness: from heavy infrastructure such as Crossrail through to essential social services such as education. Notwithstanding the debate raging in America, few businesses in the UK would covet the health insurance bills that American businesses pay, and by providing the resource for a safety net they create the necessary social support for flexible labour markets. I therefore firmly believe that taxes, with a redistributive element, are the price that we pay in Britain for an effective economy as well as a civilised society.

There are, however, very different views of what constitute fairer taxes and where the incidence of progression should lie, which is where the nub of this debate lies.

Many of the arguments for progressive taxation were forged in the Britain of 100 years ago when there was a large, poor working class, a relatively small middle class and a geographically immobile upper class, many of whom sat in your Lordships' House. Now Britain has a vastly expanded middle class. In 1939, 10 million people paid income tax; now the number is around 30 million. The rich-I might even say the nouveau riche-generates their wealth from geographically mobile talents and capital.

Colbert, Louis XIV's Finance Minister, said that taxation was the art of plucking a goose while generating the least amount of hissing. Like it or not, the rich these days will not come to or stay in this country if they are in for a disproportionate plucking.

The recent KPMG study, showing that £1 million earners in the UK keep less of their income than in any other developed economy, was read worldwide. Would anyone who earns, or aspires to earn, that sort of money not be discouraged by such a cap on ambition?

Of course, London and the UK score highly on many other factors, including quality of life, language, and multiculturalism. Who wants to go out on the town in Zurich?

While we can afford to have top rates which are not the lowest, we cannot afford to have the highest. In any case, there just are not enough rich people to provide us all with the levels of public expenditure we might like. The PBR estimates that the yield from income tax this year will be around £130 billion. The Treasury forecasts that the 10 per cent increase in the top rate from 40 per cent to 50 per cent will raise around £2.5 billion.

That, too, is contested because it does not take account of other lost revenues; for example, through VAT when the money is spent. The Treasury may underestimate the dynamic effect of people working less hard, reorienting their tax exposure or just plain leaving the country. Nor does it take account of companies with headquarters outside Europe which are considering where to locate a European regional office, but which may discount the UK because it is considered to be a tax unfriendly jurisdiction. Treasury models never take account of what they cannot see.

The 50 per cent higher rate of income tax represents an important psychological milestone. According to colleagues who regularly work across the Atlantic or in the Far East, it is perceived as a reason why not to come to London.

The Institute for Fiscal Studies calculates workplace tax rates for the highest earners at 66 per cent. If this issue is not addressed, we will see the converse of the Thatcher reduction in income tax; that is, a steadily declining contribution from the rich to the Exchequer in the medium term.

By comparison, an increase in the basic rate of just 1 per cent raises £4 billion, according to the latest Treasury ready reckoner.

The inconvenient truth is that funding good-quality public services requires substantial contributions from the many, not just the few. As we move to close the deficit, how we go about this matters.

My premise is that we want to close the deficit in the manner which does least damage to sustainable economic growth—the first and best way of raising revenue for the Exchequer and creating prosperity. International experience suggests that a mix of roughly 80 per cent spending cuts and 20 per cent tax increases may be the most sustainable way of achieving this outcome.

So how will the 20 per cent from tax increases be realised?

The Government need to be very wary of taxes which inhibit economic growth over the next few years. We have a high mountain of debt to climb and without economic growth we will be on a slippery slope rather than the cable car to the top. Those taxes which threaten

international competitiveness-indeed, which fail to build on our unique position in the world- and those which discourage enterprise or corporate investment should be touched with extreme caution.

If we consider areas where our tax system is less fierce internationally or where we might provide leadership, two taxes merit further consideration. First, VAT could be brought more in line with the rest of the EU, particularly if it is levied on items where purchase is discretionary rather than essential. Secondly, if the UK led international moves towards green-based taxes it would raise revenue while discouraging unsustainable behaviour by business and consumers.

Whatever the next Government decide is the right solution to this conundrum, a vital component is the clear signalling of the way forward. There should be no sudden changes of tack and a thorough consultation with the marketplace to avoid those easy unintended consequences.

The uncomfortable truth is that the heavy lifting may have to be done by taxes with a broad base, such as the basic rate of income tax or the standard rate of VAT. But I suspect that this is a view which is most easily expressed from the Cross Benches.