Global Counsel

Britain’s higher tax future?

Blog post by Head of UK Leo Ringer, 28 June 2017

Tax rises are now back in the centre ground of the UK economic discourse, in a way they have not been for at least a decade. This shift should put businesses and investors on notice - the era in which they could safely assume an ever-friendlier approach to taxation may be at an end.

Those wanting more tax and spending in the UK now outnumber those wanting a continuation of the status quo for the first time since the financial crisis, according to new survey data released today. This underscores a general election result which saw 40% of voters back a Labour manifesto which committed to a higher tax, higher spend fiscal policy. It marks the first time since the crisis that a UK political party has been able to talk about higher taxation with electoral credibility.

The driver appears to be a shift in the public’s attitude towards spending cuts in particular, as opposed to deficit reduction *per se*. In fact, the election saw all of the parties commit, one way or another, to balancing the books, even if the economic debate was much weaker than usual. The real change evident in the election result was about *how* the books should be balanced on a day to day basis.

Labour was explicit that its plan involved substantial tax rises – to the tune of £49bn – primarily as a way to fund real terms growth in public services spending, while still meeting its deficit reduction pledge. This contrasts with the post-crisis orthodoxy in which spending cuts were the predominant driver of consolidation, with a very minor role for tax rises (at a ratio of circa 85:15 between 2010 and 2017).

From 2010 onwards, there has been a consistent stream of voices calling for a greater role for tax rises in helping to balance the books, including from Vince Cable as business secretary. Their argument was that public services would bear less of the brunt if tax rises filled some of the gap between revenues and spending. But they failed to generate traction, and the idea never gained political or electoral relevance. Discussions around the Cabinet table took comfort from the apparent resilience of public services to cuts. The public now appear to disagree with that assessment, and it has at least two big implications.

The first, is that the shift will – or should – give serious pause for thought at Conservative Campaign Headquarters. The strategy of deficit reduction driven by spending cuts has been a hardy perennial for the Conservatives, winning the political and electoral argument hands-down, year in, year out. For the first time since then, they face an electorate that now appears to worry as much, if not more, about the state of public services than it does about the level of taxation in the country. Even Oliver Letwin, former Conservative Cabinet Office minister and policy enforcer is reportedly talking seriously about the need for a change of approach.

Second, in a world where tax rises are a serious part of the fiscal discourse, the question of “who pays” will come into sharper focus. The vast majority of Labour’s £49bn (around £40bn) would have come from businesses, rather than households. Just under half of this would have simply unwound cuts in corporation tax driven through in the past decade, but the other half would be “new” business tax measures. This would tilt the balance of tax rises back towards businesses and away from households, in an economy where businesses typically pay around 30% of the overall tax bill.

It is not year clear how the Conservative Party will evaluate this month's result. Chancellor Philip Hammond has stuck to his guns so far, with plans to continue to cut corporation tax while delivering deeper public spending cuts. Only last week in his Mansion House speech, he argued that "higher taxes will slow growth, undermine competitiveness, and cost jobs". But he and the Party must fear that this tax-lite strategy, if perceived as equating to lower public services spending, may not survive another electoral test. Either way, the centre ground in the debate on taxation has shifted – businesses should beware.