withersworldwide

Funding the coronavirus response in the UK

03 JUNE 2020

CATEGORY:
ARTICLE

Click here to read more on how we can support you beyond the coronavirus crisis.

With a shift of focus from the current health crisis to a future economic crisis, the Office for Budget Responsibility is predicting a deficit of £280 billion for the 2020-21 financial year, while The Financial Times estimates the deficit could exceed £337 billion. The obvious but painful question is 'how do we pay for all of this?'. Some changes to UK taxation policy are surely to be expected (though it is inconceivable that the government will try to clear all the deficit through increased taxes, especially given the current low costs of borrowing), so without attempting to predict the future, we consider various options the government could be considering. It is clear that to the extent that there are tax increases these are unlikely to be levied on businesses, as the government looks to them to drive the country out of recession, and so it is individuals who will bear the brunt of the potential changes.

Income Tax

The Conservative Party manifesto pledged not to increase income tax, national insurance or VAT. However, given that income tax accounts for nearly 25% of tax receipts in the UK, it seems unlikely that there will be no adjustments at all. It is also relatively easy to see how such a departure from the manifesto could be justified given the extraordinary current circumstances.

One rumoured change is an incremental increase in income tax rates. This could be by as little as 1% on the basic rate, 2% on the higher rate, and a 3% increase on the additional rate, which, if presented as an increase to fund our NHS front-line heroes, might not be too unpalatable. Alternatively, it could be a flat 1% increase (although this would only raise an estimated £5.6 billion per year). The Government could technically avoid increasing income tax rates by lowering the threshold that higher and additional rates kick in – for example, reducing the additional threshold from £150k to £120k.

Income taxes could also be increased by abolishing higher rate reliefs for pension contributions.

National Insurance

When Rishi Sunak launched the self-employment income support scheme in April, he alerted self-employed people to a future increase in their National Insurance contributions ('NICs'). They currently pay NICs at 9% compared to 12% for employees, which the Chancellor said was now 'harder to justify'. The Institute for Fiscal Studies has even argued that the self-employed should pay a rate of NICs aligned with the combined rate of employer and employee contributions, although this would surely be an unpopular move amongst the UK's 5 million self-employed.

As well as increasing the rate of NICs for the self-employed, another option would be to increase the Upper Earnings Limit above which a lower rate of NICs is levied and this would also have the impact of increasing the NICs take.

VAT

Again, notwithstanding the manifesto pledge, it is possible that there could be an increase in the rate of VAT. Even a small increase here would make for a large increase in receipts.

Capital Gains Tax

Capital Gains Tax ('CGT') is currently at a very low rate and, given it was not included in the Conservative manifesto, there is definite scope for an increase in the rate at which it is paid. This could mean a new flat rate (potentially aligned with income tax rates, though more likely somewhere between where the rate is now and the 40% rate of income tax), rather than the current arrangement where basic rate taxpayers pay CGT at 10% (18% for property), and higher and additional rate taxpayers pay CGT at 20% (28% on property). Reducing the current CGT annual allowance would also be an easy way to raise additional revenue. There has also been some talk of introducing CGT on unrealised gains though this is much more difficult to implement in practice than a simple rate increase and would be deeply unpopular.

Wealth Tax

A 'wealth' tax, or a levy on net wealth either as a one off windfall, or an ongoing measure, appears to be broadly supported by the public and is already something that much of Europe are familiar with. If we followed the continental model, it would involve taxing a small percentage of people's net wealth, though some experts have suggested it could be taxed at the same rates as income, raising up to £174 billion a year in tax receipts. This could hasten the reallocation of capital towards more income generating investments and assets, such as dividend paying trading businesses rather than real estate held for capital gain – a windfall for a government looking to restart the economy. However, it should be noted that a wealth tax of this sort is completely alien in the UK and it is much more likely that any such tax, if introduced, would be based on the taxation of real property. See here for a more detailed look at the possibility of a wealth tax and what it would mean .

It is highly unlikely that any changes to taxation will happen while lockdown is still in place and we do not expect to see any new measures until the Chancellor's autumn statement at the earliest. It is likely that the government will aim to reduce a lot of the deficit through a combination of quantitative easing (the printing of money) and hoping that the economy improves so as to increase the tax take (austerity is unlikely to be the primary driver this time round), but politically there will have to be some changes to the tax system so watch this space.

We will be looking at this topic in more detail during a live webinar on 7 July. For more information and to register, click here.

Authors

Phineas Hirsch

SENIOR ASSOCIATE | LONDON

Private client and tax

+44 20 7597 6484

phineas.hirsch@withersworldwide.com

Georgie Moule

TRAINEE | LONDON

Family

+44 20 7597 6190

georgina.moule@withersworldwide.com