CPS Pre-Budget Briefing

By James Heywood

The first budget for nearly 18 months is due to be delivered on Wednesday, with a new Government and an even newer Chancellor of the Exchequer. Rishi Sunak faces a tough balancing act, with manifesto promises for more spending to be kept on the one hand, and the Conservatives' reputation for fiscal rectitude to be maintained on the other.

Beyond the immediate questions of tax and spend, the Chancellor will no doubt have in mind the other fundamental issues which need to be addressed in the UK economy. The housing market is still dysfunctional and excludes many younger people from any chance of owning their own home. Productivity has been stagnant, and wages are only just back to pre-crisis levels. There is significant inequality between the different regions of the UK.

In addition to all this, there is now a backdrop of growing unease over the COVID-19 coronavirus outbreak and the impact it will have both on the world economy and on our daily lives here in the UK.

Measures to consider in the event of an economic shock from coronavirus

It now seems likely that the coronavirus will be a dominant theme in next week's Budget. The Government has already taken steps to mitigate the impact, including through changes to the rules on statutory sick pay. But the Chancellor will need to consider what other measures may be necessary if the number of UK cases grows considerably and begins to have a major economic impact.

- **Provide substantial support for the provision of short-term credit to businesses**

If the coronavirus outbreak leads to a significant number of infections in the UK, businesses will be affected by workers and customers staying at home or indeed being sick themselves. This could be an extremely testing time for some firms, and businesses which may otherwise be perfectly viable could go to the wall, with all the disruption and unemployment that entails. Even without a major outbreak in the UK, the disruption to supply chains for some businesses here as a result of the outbreak in China has already been felt.

To combat this, the Government should look to significantly relax the rules around lending to businesses. This could include incentives for banks to provide more generous overdraft facilities and repayment relief for loan or mortgage payments, or even a formal insurance scheme. This would be particularly important for small and family businesses which do not have the same access to finance as larger corporations.

- **Give businesses 25 per cent off their business rates and employer's NICs bills for one year**

If the cashflow shock for businesses is very substantial, the Government could announce a year-long business rates cut for all small businesses. Every business with a turnover below £5 million (representing 98 per cent of all businesses) could be given a 25 per cent cut in their business rates bill in 2019/20, as well as 25 per cent off their employer's National Insurance bill to prevent the need for lay-offs. The CPS proposed similar measures in the event of an economic hit from a 'no deal' Brexit last year (*A Budget for No Deal*, CPS, March 2019)

There are obviously other measures which might need to be taken depending on the severity of the outbreak - we aim to publish future work on this topic if needed.

Other measures the Chancellor should consider

- **Take the lowest paid out of tax by raising the National Insurance threshold for employees**

In a November 2018 report the CPS proposed a renewed focus on cutting taxes for working people by aligning the threshold where workers start paying National Insurance Contributions with the income tax personal allowance.

Increasing the employee NICs threshold to £12,500 would deliver a tax cut of nearly £500 per year to all full-time employees. This would be a significant increase in the amount workers can earn tax-free. We termed this the 'Universal Working Income', and polling by YouGov found that 76 per cent of people supported it, with 41 per cent strongly supportive.

The idea was endorsed by all of the leading candidates for the Conservative leadership last summer, and we are delighted that it made its way into the Conservative manifesto at the general election. The Chancellor should stick by that commitment and set out how the threshold will rise over the coming years and be aligned with the income tax personal allowance, given that the Conservative manifesto only costed the initial rise to £9,500.

For more information on this policy see *Make Work Pay* (Tom Clougherty, CPS, November 2018)

- **Level-up left-behind regions with a new generation of free ports and opportunity zones**

The Government has already shown an encouraging appetite for creating free ports – a policy which the CPS is proud to have put on the national agenda through a 2016 CPS paper authored by the now Chancellor, Rishi Sunak.

The free ports programme should specifically target deprived areas so that they benefit from special business and tax regimes to encourage investment and economic activity in those places, creating a new wave of 'opportunity zones', as further proposed by the CPS. As Rishi Sunak's original paper pointed out, such measures fit perfectly with the "levelling up" agenda: of the UK's 30 largest ports, 17 are in the bottom quartile of local authorities when ranked by the ONS's Index of Multiple Deprivation.

For more information on this policy see *The Free Ports Opportunity* (Rishi Sunak, CPS, November 2016) and *A Rising Tide* (Nick King and Eamonn Ives, CPS, October 2019)

- **Take 90 per cent of properties out of Stamp Duty to boost the housing market**

Most economists agree that Stamp Duty Land Tax is a very bad tax. The increased cost of moving means fewer people move for work, which causes inefficiencies in the labour market, and also means people are less likely to vacate properties which are larger than they need, meaning the housing stock is allocated less efficiently.

The CPS has proposed a radical reform to take all properties below £500,000 out of SDLT altogether, which accounts for around 90 per cent of properties in England, and for rates payable on properties above £500,000 to be reduced sharply. Due to the impact we expect this would have on the number of housing transactions and on housebuilding, this would only cost around £1.6 billion in lost revenue, while the benefits for the housing market would be considerable.

For more information on this policy see *Stamping Down* (Alex Morton, CPS, October 2019)

- **Start an infrastructure revolution by setting up a new National Infrastructure Fund**

The UK has invested much less in its infrastructure than other developed countries over many decades. Investment in the UK as a share of GDP has ranked in the lowest 10 per cent of OECD countries for 16 of the last 21 years.

The Government has rightly said it wants to address this, and is due to bring forward a National Infrastructure Strategy. As part of this, a new National Infrastructure Fund should be set up to work alongside the National Infrastructure Commission, as proposed in a CPS paper last year. The Fund would not just invest in transport infrastructure but also in digital connectivity, energy and other utilities, as well as into the infrastructure to help us tackle climate change and to unlock and support new industries. This would help coordinate the Government's plans for an infrastructure revolution.

For more information on this policy see *A Rising Tide* (Nick King and Eamonn Ives, CPS, October 2019)

- **Help first-time buyers by encouraging a new market in long-term, fixed rate mortgages**

The average cost of a monthly mortgage payment is now less than the average monthly rent. This means that many of those currently forced to rent could in fact afford to be homeowners, but are shut out of the property market by the hurdle of a deposit and by strict lending rules. Since the 2008 crisis, average loan-to-value rates have fallen from 95 to 85 per cent, effectively tripling deposits.

The CPS has set out how the Government and the financial sector can help to promote a market in fixed rate mortgages which only require 5 per cent deposits. We welcome the fact that the Conservative manifesto made a commitment to do this, which could help almost 2 million households into ownership, and hope the Budget contains concrete commitments to take this policy further.

For more information on this policy see Resentful Renters (Graham Edwards, CPS, December 2019)

- **Encourage businesses to invest by raising the Annual Investment Allowance**

The Annual Investment Allowance allows companies to write off capital investment against their tax bills, removing a disincentive for firms to make productive investments. A lack of this sort of investment by companies has been identified by many economists as a key factor in the UK's sluggish productivity growth since the financial crisis.

Philip Hammond announced a temporary increase in the AIA to £1 million in the 2018 Budget, but as things stand, the AIA is set to fall by 80 per cent back down to just £200,000 at the end of 2020.

In a 2019 paper the CPS recommended making the AIA unlimited for investments in plant and machinery, and making this increase permanent. This would be a pro-growth reform which would increase business investment and help to boost UK productivity. A research paper published this week by the CPS, written by one of America's leading tax economists, shows how substantial the economic benefits could be based on the US experience, and suggests that the measure would more than pay for itself in the medium term.

For more information on this policy see *A Budget for No Deal* (Tom Clougherty, CPS, March 2019) and *Boosting Growth as the UK Leaves the European Union* (Stephen J. Entin, CPS, March 2020)

- **Help renters into home ownership via reforms to Capital Gains Tax**

Since 1997, the number of households renting in the private sector has more than doubled, and the UK's home ownership rate is now one of Europe's lowest. With property prices and rents rising substantially, huge amounts of capital have been diverted to the buy-to-let market and many landlords have made substantial gains on the value of their properties.

The CPS has proposed using these gains to give a tax incentive to landlords to sell to their tenants, and to help the tenants with the deposit. The Government should turn the Capital Gains Tax payable by a landlord when selling to a sitting tenant into a rebate shared between landlord and tenant. The landlord would get a third off their tax bill, and the tenant would receive support for two-thirds of a 10 per cent deposit on the property. This could have a major impact on reversing the UK's declining home ownership rate.

For more information on this policy see *From Rent to Own* (Alex Morton, CPS, October 2018)

- **Massively simplify tax for small businesses through a Simple Consolidated Tax**

Small businesses are the backbone of the British economy, employing around 13 million people and with a combined turnover of some £1.4 trillion. A report by the Federation of Small Businesses in 2018 showed that small firms are spending £5,000 and losing three working weeks on average on tax compliance each year.

In a 2019 paper the CPS proposed a new simple levy on turnover, a 'Simple Consolidated Tax', which businesses with a turnover below £1 million could opt into as an alternative to Corporation Tax, Employer's National Insurance, VAT and business rates. More than two thirds of businesses surveyed for the report who expressed a view said they would support the introduction of such a system. This reform would allow smaller firms to substantially reduce the burden of tax compliance. The report also proposed a variety of other reforms to support small businesses, such as changes to the late payment regime.

For more information on this policy see *Think Small* (Nick King, CPS, May 2019)