

Muse Three

Direct Taxes: Back to Basics

The whole structure of payments received for services rendered – including basic wages and salaries – has changed so much from the levels and standards previously pertaining that my original muse cannot now be considered to offer credible alternative.

At first I was inclined to remove this muse, but an unexpected contribution to You Tube by the Prime Minister - 24hrs before the Chancellor was due to make his budget speech – made me believe there was still some relevance.

Thus, I am revising the whole muse. Clearly, whenever and however any changes are suggested they will be met with strong opposition from political and other vested interest groups.

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I am well aware of the iniquities that exist within the present Tax System: I once earned three times The Average Wage, then to have it erode over a period of 10 years to 60% of the Average. I have always made comparisons between my own experiences and the alleged position of the Vestey Family: it was reported that they had paid no more than £700 in Taxes while amassing £700,000,000 in Capital Wealth.

I was still paying Tax on an Income of less than a half of The Average Wage.

The existing structure and system of Income Tax and National Insurance collection is unnecessarily complex.

The introduction of Self Assessment would have been an appropriate time to effect the introduction of simpler systems. **Alas an opportunity lost!**

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The solution offered here is but one of many by which an improvement could be effected - as per Maxim Seven.

In order to ensure long term stability the system must comply with Terms of Reference that have been subject to an all-party agreement: such an agreement binding until replaced by another all-party agreement.

Suggested Terms of Reference

- The yield of Tax should not be significantly different from that prevailing.
- Those earning less than Twice the Average Wage will not be subject to more Tax – in monetary terms – than they did before the change.
- The effects of step anomalies should be minimised.
- Tax Allowances will be limited to the tax free threshold that can be considered as one of the adjustables required to maintain stability into the long term.
- Those earning more than Twice the Average Wage should not have to pay a higher Maximum percentage than currently stated.

- The system must be capable of adjustment by use of variables without change to the terms of reference.
- The true variables will be the tax-free threshold, the Maximum Rate of Tax and the incremental tax rates on the incomes above £40,000.
- There will be categories to which different tax levels will apply, but these will be defined by The Mode Wage; The Median Wage and the Average Wage.
- The tax rate applicable within these categories is defined by the Actual Gross Wages earned by each individual according to the system agreed in the original, or, revised all-party discussions.

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For the purpose of this muse I have included a few other prescribed conditions that makes it relevant to certain expressed opinions – pro and contra - of the major political activists.

- When the numbers employed and self employed was 31million, the expected Income Tax take was £170 billion. These remain as the basis for this muse. For the record this indicates – if allowance is made for mode and median wages - that 25 million averaged £18,000 per year and 6million averaged £72,000.
- On the 2007 to 2008 conditions the typical median individual would pay £2,200 income tax; compared with £26,000 for the individual on £72,000: the relevant percentages paid are 12% and 36% of their gross income. There are of course inbuilt iniquities in that the lower income person may possibly qualify for tax credits and income support and many of the higher paid may have the potential to legitimately offset some of their tax.
- Arguably, the deletion of the lower tax rates was not based upon a credible basis; it being almost certain that it was based upon average wage rates rather than the mode wage and median wage that are critical to the 50% who earn less than the median wage.
- There seems little point in keeping the tax threshold lower than that which attracts tax credits and income support
- Thus in this example I have set a tax threshold of £10,000 believing that anomalies arising from differing 'family' circumstances would be best dealt with by the use of tax credits.
- It is probably not in the long term interest of a majority to not have the security of a National Insurance payment record. Thus the prevailing conditions for initial payment is retained.
- Up to an, and including an annual income of £40,000; the 20% tax rate is replaced by a percentage figure equivalent to the first two numbers of the Annual Income net of the tax threshold e.g. at £(11),000 the tax rate is 11%; at £18,000 it is 18% at £22,000 it is 22%; etc. until at £39,000 it would be 39% and at £40,000 it would be 40%.
- For incomes above £40,000 there will be an added 1% for each added £10,000; thus at £50,000 the tax rate becomes 41% such that a 50% tax rate becomes applicable at £140,000.
- Thereafter, if 50% is the assigned maximum, all income would be taxed at that rate. If, however, a 60% rate were considered 'reasonable' the rate could increase by 1% per £50,000 of additional income up to the maximum threshold of £690,000.
- There is a perceived unfairness attached to deducting NI contributions from post taxed income: thereby paying tax on those contributions. There is a case for deducting the NI contributions from the Gross Income.

- Arguably, for simplicity, the NI contributions percentages should be compounded with the tax rates. I have not, in the examples given below taken this step in order to minimise the critical contentions that will inevitably arise.

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The following examples are given to clarify the system, but it should be remembered that any anomalies arising are correctable by adjusting the variables in order to give the desired Tax: take: presumably that which is obtainable under the present system: any incremental anomalies are correctable by the use of tax credits.

Example A (Employee Only)

Gross Income £11,000 (Equivalent to 38 hours per week on the Minimum Wage)

Less Tax Threshold of £10,000

Less NI Contributions at 11% of £1,210

Taxable Income is -(£210) I.e. No Tax payable.

This compares with +£910 under the present system I.e. a net gain of £910 per annum. This is 8.27% of the Gross Income that can be used to offset loss of tax credits and possibly income support.

Nett Income is £9,790 per annum. 89% of Gross Income.

Example B (Employee Only)

Gross Income £16,500 I.e. equivalent to the Mode Wage.

Less Tax Threshold £10,000

Less NI Contributions £1815

Taxable Income is £4685 at 16.5%

Tax Payable is £773 per annum compared with £2010 under the present system I.e. a net gain of £1,237. This is 7.5% of gross income that can be used to offset loss of tax credits and possibly income support.

Nett Income is £13,900 per annum. 84% of Gross Income.

Example C

Gross Income of £23,000 I.e. equivalent to the Median Wage.

NI Contributions £2530

Taxable Income is £11,470 at 23%

Tax payable is £2638 per annum compared with £3,310 currently I.e. a gain of £672. This is 2.9% of gross income.

Nett Income is £17,840 per annum. 77.5% of Gross Income.

Example D

Gross Income of £30,000 I.e. equivalent to the Average Wage.

NI Contributions £3,300

Taxable income £16,700 at 30%

Tax payable is £5,010 compared with £5,020 currently I.e. no gain or loss as one would expect for the average wage situation when the tax take is to remain the same.

Nett Income is £21,690 per annum. 72.3% of Gross Income

Example E

Gross Income of £45,000 I.e. approx twice the Median Income I.e. 1½x the Average Income and is the upper limit threshold for the 11% NI Contribution.

NI Contributions £4950

Taxable income £30,050 at 40%

Tax payable is £12,020 compared with £10960 currently I.e. a net loss of £1,060 per annum equal to 2.35% of gross income.

Nett Income is £28,030 per annum. 62% of Gross Income.

Example F

Gross Income of £70,000 I.e. 3x the Median Income.

NI Contributions £5200

Taxable Income £54,800 at 43%

Tax Payable is £23,564 compared with £20,910 currently I.e. a net loss of £ 2,654 per annum equal to 3.8% of Gross Income.

Nett Income is £41,236 per annum. 59% Of Gross Income.

Example G

Gross Income of £100,000 I.e. approx 4x the Median Wage.

NI Contributions £5,500

Taxable Income £84,500 at 46%

Tax payable is £38,870 compared with £33,020 currently I.e. a net loss of £5,850 per annum equal to 5.85% of Gross Income.

Nett Income is £55,630 per annum. 55.6% of Gross Income.

Example H

Gross income of £140,000 I.e. approx 6x the Median Wage.

NI Contributions £5,900

Taxable Income £124,100 at 50%

Tax payable is £62,050 compared with £49,000 currently I.e. a nett loss of £13,050 per

annum equal to 9.3% of Gross Income.

Nett Income is £72050 per annum. 51.46% of Gross Income.

Example I

Gross Income of £190,000 I.e. approx 8x the Median Wage.

NI Contributions £6,400

Taxable Income £173,600 at 50%

Tax Payable £86,800 compared with £ 69,370 currently I.e. a nett loss of £17,400 per annum equal to 9,10% of Gross Income.

Nett Income is £96800 per annum. 50.9% of Gross Income.

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Obviously those currently earning more than the True Average Wage are net losers under this system: thus a level of disgruntlement is inevitable.

Those who gain, namely those below the True Average Wage, all gain: the gains received increasing as the income decreases: this will not guarantee there will be an absence of complaint.

These would appear to be a reasonable results for the proposed system, particularly when another test is applied. The 25,000,000 earning less than the Average wage would under this system pay £16.8 billion less Income Tax and the 6,000,000 earning more than the Average Wage would pay £15.8 billion more as the examples are presented; thus giving a nett reduction of Tax Take of £1billion: offsetting this is the savings made by dismantling the Tax Credit System and redefining the Income Support System. Clearly a closer match is obtainable by tweaking the controlling variables, but at 0.6% difference it is truly statistically irrelevant. Additionally one should not underestimate the extent to which those earning more than £140,000 per annum are able to legally reduce their tax liabilities.

On this count alone there is justification that the system should benefit the lower earners. However, it must be remembered that there should be accompanying reductions of income from Tax benefits and income support. These I am not in a position to assess. I stand open to correction but the following is suggested by the information included above.

- 66% of all earners receive less than the Average Wage:
- 15% of all earners receive between the Average Wage and £70,000. (This is possibly the Median Wage of those receiving more than the Average.
- 10% earn between £70,000 and £100,000 per annum.
- Possibly 6% to 7% earn between £100,000 and £150,000 per annum.

Balancing 2% to 3% earn between £150,000 and the arguably obscene earnings of Premier footballers and some Financial Executives.

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I include these estimates only to emphasise that it is unlikely that any system can allow for the skews imparted by excesses; such that one has to take particular care to ensure that low wage earners are not unjustifiably disadvantaged.

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It may of some interest that the disposable incomes of all Members of Parliament includes them in the top 2% to 3% earners in society, even if additional non-parliamentary earnings are ignored. I stand open to correction.

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I note that the media reported that the Chancellor admitted that the proposed 50% rate applying to earnings above £150,000 per annum was not based upon a 'scientific' rationale but upon his own personal opinion.

I see no criticism in this as intuitive response is mostly superior to contemplative response. This is discussed in Part Two of my Book Five. See Book Section.

Additionally the figures contained in the above examples plot out to give graphs from which derived formulae can be obtained. To this extent the proposed system could be deemed 'scientific' and this assume some measure of 'virtual' respectability.

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