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Reform Tax System, says leading world economist in Politeia pamphlet. As tax payers flee high tax regimes, Irwin Stelzer urges curbing income tax and moving to consumption taxes.

As the abolition of the 10p tax rate brought tax to the centre of politics, the Chancellor, Alistair Darling announced he is appointing a high-level panel to devise a tax system that makes the UK competitive at a global level. Like other politicians, Darling is re-learning the old lesson that tax and the levels of tax matter. Politeia's new pamphlet suggests that for the future a new direction may be needed as tax revenues become ever more constrained.

In *Taxes in a Global Economy – Efficiency, Fairness and Incentives,* Irwin Stelzer, explains that Governments may have reached the limits of tax revenue. Today's global economy leads to greater mobility of both labour and capital. High earners can flee high tax regimes. Investors can move capital to tax friendly countries. Those who remain will not wish to pay ever higher tax. How then can Governments maintain, or even raise, their income?

Governments, Dr Stelzer explains, have three options. They can:

- *Cut spending*. Western welfare states may find this difficult. Defence spending is already tight; and politicians refuse to rein in welfare budgets. Here in the UK all parties are pledged to the existing size of the welfare state.
- *Shift the burdens of spending to the private sector.* Ministers can compel private companies to fund social programmes, e.g. parental leave or minimum wages. But, in the long run that might threaten competitiveness.
- *Shift the tax base.* If raising tax or curbing spending are not an option, they can shift the tax base to consumption. Consumption taxes, which cause less damage to incentive, can hit poorer people disproportionately.

Stelzer considers the principles underlying tax. The three goals, of efficiency, fairness and the shaping of society, are often in conflict. The advice to politicians is clear: not only does tax matter, but so does how it is spent. It should be clear, simple, bring good value for money, and be levied on 'bads' not 'goods' with increases on 'bads' offset by lowering tax on 'goods'. Above all they should remember its impact on growth. Tax on income should be kept low and taxes directed at consumption, with exemptions to reduce regressive tax.

Irwin Stelzer's guide for future tax …

- Tax competition and how taxes are spent will increasingly matter. The combination of 'high taxes and shoddy services is likely to prove lethal'.
- Complexity is as big a deterrent to investors as high taxes.
- Tax on business is now around the norm of 25-30 percent. Complexity, uncertainty and changes in the tax code have a cost: and the headline rate may bear little relation to the effective rate.
- 'Sensible estimates' should be made of the effect of proposed tax changes.
- Taxes should be concentrated on 'bads' not 'goods'.
- Tax increases aimed at 'bads' such as pollution should be offset by lowering taxes on 'goods'.
- Above all the effect of taxes on economic growth must not be forgotten. Given the mobility of resources needed to grow any economy 'it is often wise to keep taxes on incomes low, lest the taxpayer flee, and concentrate on taxing consumption' with exemptions to reduce regressive tax.

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Taxes in a Global Economy – Efficiency, Fairness and Incentives is available online from Politeia (www.politeia.co.uk) or on request to secretary2@politeia.co.uk