Funding the Future

Tax After Coronavirus (TACs) : Capping total ISA contri...

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The reasons why wealth needs to be subject to additional taxation has been discussed in another Tax After Coronavirus (TACs) post, with all links being supplied there and so it will not be repeated here.

What was also discussed in that post was that the necessary short term changes to wealth taxation fall into three groups. They are, firstly, to equalise tax rates on equivalent sources of income or allowances. Second, it is by reconsidering those things that should be taxed that are not but might be if the goal of greater equality is to be achieved, and vice versa. In other words, those parts of available tax bases subject to exemptions and reliefs need to be reviewed. Third, it is about creating a more progressive tax system by changing

Capping total ISA contributions

Individual Savings Accounts (ISAs) were introduced in 1999 by the then Labour government. They replaced a previous tax incentivised savings scheme created by the previous Conservative government. What they create is low tax rates on wealth that fuel **the inequality in tax rates between labour and unearned income sources.**

Although the details of ISA savings rules have changed over the years the logic has remained largely consistent throughout. Any adult person is (subject to minor limits for some types of account) allowed to save in ISA accounts to an annual total limit, which is currently £20,000, and the sums saved are held in accounts where the incomes and capital gains arising are all tax-free. There is, however, no tax relief on transferring sums into the

accounts and so no tax charge on any withdrawal from them. Various types of account are now permitted but the limits apply across the types. The sums may be invested in cash and shares to the agreed limits (with minor rule changes having happened over time).

The purpose of ISAs was to encourage savings. The logic was that this helped fund investment in the economy. This is not necessarily true. Savings have, however, been seen to be virtuous and so to be rewarded by generations of politicians. ISAs are one response to that and, as a matter of fact, having access to some savings does increase household resilience and there is likely to be a social benefit to that.

Within the context of discussion on tax and inequality the problem with ISAs is that although there are annual limits to contributions that can be made there are no lifetime limits. As such after twenty years of operation there are now reported to be ISA millionaires i.e. people who have tax-advantaged savings in such accounts amounting to more than £1 million. This means that the tax relief being provided is disproportionately benefitting those already wealthy. This would seem to be an inappropriate use of tax relief if the tax system as a whole is meant to reduce inequality, as its appearance of having a progressive nature implies to be the case.

The solution to this problem is relatively straightforward. A lifetime contribution limit should be introduced. The sum could be discussed, but when £100,000 represents significant savings within the UK at present a cap at this limit would seem appropriate and could be applied from now on, preventing anyone with this sum in ISA accounts from making further contributions in the future.

Notice could then be given to those holding ISA balances of greater than this sum that they must reduce their balances held within a prescribed period or become taxable on returns on balances in the future. The permitted balances that might be retained might be in excess of the £100,000 contribution limit to allow for growth in the balance held since the investment was made over time, but should not be excessively so. A retained balance limit of £150,000 would seem to be entirely fair. This way greater equity could be restored to the savings market and the tax system would cease to subsidise wealth as heavily as it does at present.