

Is Truss signalling that she wants flat taxes for the U...

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I heard Liz Truss say to Laura Kuenssberg that she wanted a simpler UK tax system this morning. I immediately tweeted this:



Then I noticed that Simon Clarke, her Levelling Up Secretary had tweeted:



Clarke confirmed what I thought: there is a flat tax agenda amongst the Tories who are now (supposedly) running the UK.

I last write in-depth about the dangers of flat taxes in 2006, when commissioned to do so by the Association of Chartered Certified Accountants - the ACCA. [That paper is here.](#) In it I said that flat taxes were:

WHAT ARE FLAT TAXES?

According to the UK Treasury (2005), flat taxes are 'tax structures that have a single positive marginal tax rate'. Technically this could cover income tax, corporation tax on company profits or VAT and some are even suggesting such an arrangement should include national insurance. Most of the time though the taxes remain distinct and the term flat tax refers to a replacement for the existing income tax rules incorporating two key features:

I concluded:

THE ISSUES

A recent survey among SMEs in the UK suggests that the complexity of the UK tax system and the frequent changes that occur within it have helped create interest in flat taxes among this group (Tenon Group 2005). In the accompanying press release, however, it is warned: 'No one knows yet exactly what a flat rate tax system will look like...there are a number of dangers [and]... flat rate tax could quickly become as complicated as the current system...' (Tenon Group 2005).

The theory of flat taxes suggests significant simplification of the tax system; the assessment of

those systems undertaken for this report suggests they may be as complicated for small businesses and individuals and require as much or more form filling as the current UK tax system. In addition, flat tax systems appear likely to impose costs on government and to redistribute incomes in ways that require political judgement to be exercised, an issue beyond the scope of this report.

In consequence, introducing a flat tax would not be a simple issue. The complex issues are discussed in detail in this report, which pinpoints key questions such as:

- What is the role of the state and of government in taxation and the management of the economy? How does opinion on this affect the design of a flat tax system?
- Should tax be charged on income or consumption in a flat tax system? If on income, should that from overseas and that from savings be taxed?
- The UK has complex rules on both residence and domicile. The latter is relatively unusual and believed by the UK to provide it with competitive advantage. Would this advantage be lost under a flat tax system?
- Most countries, including the UK, have many international double tax treaties and other obligations. To what extent should any tax reform be designed to meet such international obligations along with the needs of the domestic market?
- Should small business be treated differently from large business?
- How will trusts be taxed in a flat tax system?
- What is the future of inheritance tax? Can a flat tax

I was trying to be objective back in those days, reflecting the wishes of those sponsoring my work.

I unpacked my arguments [in a separate blogpost](#), which was one of the first I ever wrote for this site. In it I said:

The report was paid for by ACCA research funds and as such had to meet strict, objective academic research standards, including (as is essential for a professional institute) a neutral approach. But this article is not subject to those constraints, and I can therefore be more straightforward about what the evidence I uncovered when writing the report reveals.

The first conclusion I reached was that there are no "flat tax states". Those countries that claim this title in Eastern Europe have tax systems that are nothing like the flat tax model as laid out by Alvin Rabushka and Steve Forbes in the USA, who are the main political promoters of this idea. At best they have single rate income tax, capital gains tax and corporation tax systems with all the resulting complexity that flow from retention of such structures. In fact, Russia, Lithuania and Serbia even manage multiple rates of income tax, which somewhat negates the claim to have flat tax systems.

Secondly, the tax systems that these states operate are not simple. They all retain complex rules for calculating income, the treatment of capital allowances and the consideration of capital gains. They also have a wide variety of allowances and reliefs available for ordinary citizens to claim against their personal income including, in most cases, relief for pensions, mortgage interest, education costs, home to work travel, union and other dues, charitable contributions and so on, and on (in some cases).

Next, these systems do not appear to reduce the administrative burden on the tax payer, as is claimed. In Estonia 84% of adults submit a tax return each year; in the UK it's 16%. And in the same country details of benefits in kind supplied by an employer to their employees have to be made monthly, which makes the annual P11D routine in the UK seem like a positive panacea in comparison.

These departures from the myth that is promoted around flat taxes might have been acceptable if the claims for their economic performance had been shown to have any support. Unfortunately that was not the case either. It is widely claimed that tax revenues increase when flat taxes are introduced. No evidence was found to support this claim. Income tax revenues fell in countries introducing flat taxes if other obvious factors (such as Russia's oil boom, the creation of which can hardly be attributed to a tax change) are taken into account. Indeed, if tax revenues did increase it was almost entirely of VAT and NIC, as was the case for example in Slovakia and Romania, where income tax revenues fell.

Nor can this increase in indirect tax be attributed to economic growth resulting from the adoption of a flat tax. Indeed, the Estonian Ministry of Finance specifically warned

against making an assumption that this was possible. Their spokesman when interviewed for the report said of flat tax "it's a tax; it's not a medicine for the economy."

And the IMF and Institute for Fiscal Studies did not find the rich in Russia were more tax compliant after the introduction of a flat tax, as its proponents claim they should have been. But curiously though those on low pay who actually saw flat taxes increase their tax burden in that country were more tax compliant, counter intuitively to the claims of those who propose such taxes.

Finally, although the UK's leading exponent of flat taxes, Richard Teather of Bournemouth University claimed that his proposals for a flat for the UK would not help the rich in the UK and would only benefit the less off, my work showed that the data he used when coupled with HMRC data could not support that view. In fact, those earning less than £22,000 might save an average of about £200 a year (before NIC changes, which are likely to increase their bills based on the precedent of other flat tax states), those between about £22,000 and £74,000 would see their tax bills rise by up to £2,000 whilst those earning over £74,000 might see their tax bills reduce by over £7,000 an average. This is a clear indication that this system will favour the rich, as all other surveys in the UK and the range of data I reviewed for other countries also showed to be true.

So, the evidence failed to support any of the claims made by the flat tax lobby. In which case I have, outside the framework of the report considered what that lobby want. I conclude that they wish to promote these four things:

- 1: Reduced taxes for the rich
- 2: Increased taxes for working people
- 3: Reduced tax on companies
- 4: Reducing the role of government.

As some indication of this two quotes from Alvin Rabushka, the man who invented flat tax are illuminating. Both come from the interview with me for this research, which he consented to be published. About the redistributational effects he said:

"The only thing that really matters in your country is those 5% of the people who create the jobs that the other 95% do. The truth of the matter is a poor person never gave anyone a job, and a poor person never created a company and a poor person never built a business and an ordinary working class guy never drove economic growth and expansion and it's the top 5% to 10% who generate the growth for the other 90% who pay the taxes to support the 40% in government. So if you don't feed them [i.e. the 5%] and nurture them and care for them at the end of the day over the long run you've got all these other people who have no aspiration for anything more than, you know, having a house and a car and going to the pub. It seems to me that's not the way you want to run a country in the long run so I think that if the price is some readjustment and maybe some people in the middle in the short run pay a little more those people are going to find their children and their grandchildren will be much better off in the long

run. The distributional issue is the one everyone worries about but I think it becomes the tail that wags the whole tax reform and economic dog. If all you're going to do is worry about overnight winners and losers in a static view of life you're going to consign yourself to a slow stagnation."

I think that pretty much supports my first two claims, and since the third is part of the same metric, it's covered by the same evidence.

As for the role of government he said:

"I think we should go back to first principles and causes and ask what government should be doing and the answer is "not a whole lot". It certainly does way too much and we could certainly get rid of a lot of it. We shouldn't give people free money. You know, we should get rid of welfare programmes, we need to have purely private pensions and get rid of state sponsored pensions. We need private schools and private hospitals and private roads and private mail delivery and private transportation and private everything else. You know government shouldn't be doing any of that stuff. And if it didn't do any of that stuff it wouldn't need all of that tax money so that's the fundamental position and as long as you're going to have government do all that stuff you're going to have all those high taxes."

As he also made clear, that then let's you have a flat tax. But in that case what I wrote for the Guardian last year is true:

"Flat tax is not a serious attempt at taxation, but is instead an exercise in social engineering. That is why its innocent appeal is so dangerous."

That 'social engineering' process is designed, as Rabushka himself say, to 'take the tax code out of the economy'. In other words, it leaves people wholly dependent upon market forces. The consequence happens to be that politics is neutered on the way because as anyone who follows general elections knows, at the end of the day politics is about the economy. Rabushka and the right wing want to stop that. And if you don't believe me, John Meadowcroft who writes for the Institute of Economic Affairs, a think tank Margaret Thatcher still supports, said recently when asked if he thought democracy a 'market institution' (when undertaking an interview on www.transformingbusiness.net) that :

"Democracies and free societies tend to go hand in hand. Having said that, democracy tends to lead to socialist policies, such as protectionism. If democracy leads to property rights and the rule of law, then yes, you need democracy. But otherwise, democracy is not a prerequisite for a market economy. Democracies tend to create very large states. In most European countries, including the UK, nearly half of GDP goes to the state. This is not good for the creation of free markets."It seems fair to conclude that some in the mainstream the right wing now think democracy can be sacrificed to the market, and I believe that flat tax is part of that process. Which leads to the conclusion that two

writers (Hettich and Winer) have put forward that:
"it is possible to have a flat tax, or to have democracy, but not both"

I agree with that. Nothing has made me change my mind since 2006.