

[Capital tax fiasco](#) [1]

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The proposed increase in Capital Gains Tax, inherited by the coalition from the Liberal-Democrats, has attracted a measure of criticism. It has been denounced because it will hit quite small savers, especially if the threshold is lowered from £10,100 to £2,000, as featured in the Lib-Dem manifesto.

Critics have pointed out that some of the 'gain' has resulted from inflation, and that in some cases the tax will be more than any real increase in value. Others have identified inherited 'second homes' as likely to pull quite ordinary households into the tax's net.

The Adam Smith Institute has now published [research](#) [3] pointing to an even bigger drawback: the tax increase will produce less revenue for the Treasury, not more. Drawing on the experience of other countries, the ASI report, *The Effect of Capital Gains Tax Rises on Revenue*, shows how it has been decreases in the rates of capital gains tax which have produced additional revenue, while increased rates have diminished it.

The evidence is overwhelming. When capital gains taxes are increased, people are less ready to realize gains and expose them to tax, so the tax base is diminished, and so are revenues. The effect is likely to be even more stark in the UK, where the increase will be widely regarded as temporary. Unlike income, people can choose to postpone capital gains, and do so when the tax on them increases.

By making capital investment less attractive, increased capital taxes result in lower levels of investment. The productivity gains produced by investment are reduced, as are the wage increases which they bring in their wake, and the price reductions enabled by lower unit costs.

The proposed increase in Capital Gains Tax made no economic sense when it first appeared in the Lib-Dem manifesto. Now that it has been examined and analyzed, it makes even less. If the government goes ahead, it will subject the economy to a self-inflicted wound, and will have nothing to show for it in return. Unlike some disasters, this one is entirely voluntary and should be avoided.

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