UK banks act as subsidisers of the welfare state

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From Prof Tim Congdon.

Sir, Was I your only reader to be struck by the discrepancy between your **"UK bank losses will hit tax bill and public purse"** (May 12) and the main letter in your correspondence section on the same day headed **"Step up competition for banks and rating agencies"**?

According to your news report, the UK's banking, finance and insurance sectors paid corporation tax in 2005-06 of £11.6bn, about a quarter of the total. The figure is impressive, because the financial sectors certainly do not account for a quarter of employment.

On the face of it these sectors make a disproportionately large contribution to tax revenues. But in his letter Eric De Keuleneer, **taking his cue from Martin Wolf** (May 7), claims that finance relies on "regular state subsidies", because – in his words – it receives "a massive subsidy in the form of free insurance against systemic risk". He apparently believes that governments and central banks "bail [the banks] out in the bad times".

What is Prof De Keuleneer talking about? If he is referring to a central bank loan to illiquid commercial banks on lender-of-last-resort terms, he is simply wrong. A loan of that kind is at a penalty rate and must be repaid.

To the extent that it is not repaid and the borrowing bank has a capital deficiency, the shareholders suffer a loss and are not bailed out. But what otherwise can he mean by "regular state subsidies"?

The exposure of banks' shareholders to market forces has been demonstrated rather conclusively in recent months by the rights issues announced by the Royal Bank of Scotland, HBOS and Bradford & Bingley, as well as by the government's apparent determination to steal Northern Rock from its shareholders even if its lender-of-last-resort loan is repaid in full.

The truth is that our banking and financial industries are very large subsidisers of the British welfare state. Indeed, the corporation tax payments are only part of the story. It should also be remembered that the highly-paid individuals who work in the City of London also make substantial income tax payments, with their share of total income tax revenues again being out of all proportion to their numbers.

These individuals and their employers may or may not want to remain indefinitely in our country. Much will depend on the regulatory and fiscal regimes they confront in future.

Tim Congdon,
Huntley Manor,
Huntley, Gloucs GL19 3HQ, UK