Local Government and Communities Committee

Consideration of the Council Tax (Substitution of Proportion) (Scotland) Order 2016

Submission from Professor Kenneth Gibb

The Local Government and Communities Committee have asked for responses regarding the above approach to reforming the Council Tax. On their website they seek views on:

• To what extent will the Government’s proposed reforms make the system of Council Tax fairer?
• To what extent will the changes be straightforward for local authorities to implement?

In this short paper I will do the following. First, I go back to the Commission on Local Taxation and consider its brief, analysis and its main recommendations). Second, I highlight the main points of the proposed SSI and the related changes to the council tax reduction scheme. Third, I reflect on the proposed reforms and seek to both answer the above questions and set them in a wider frame.

The Commission

The Commission on Local Tax Reform (co-chaired by the Scottish Government and COSLA) was announced in the Programme for Government at the end of 2014. It sat, took evidence, consulted and then reported in December 2015 The remit of the Commission was to ‘identify and examine alternatives that would deliver a fairer system of local taxation to support the funding of services delivered by local government’. The all-party commission (minus the Scottish Conservatives who were undertaking their own low tax commission) was expected to consult widely in communities across Scotland and to take account of income and wealth inequalities for individuals and households, the wider demographic, macroeconomic and fiscal impacts (including the housing market), revenue-raising capacity, administrative (including any transitional arrangements) and the impact of any proposed reforms on local democracy and accountability.

During this process, working with Linda Christie, I presented several times to the commission, undertook an international evidence review, facilitated a seminar with an international expert on local government finance (Prof Enid Slack, University of Toronto), was a member of a group evidence session to the Commission from the Scottish Property Tax Reform Network and, also prepared a submission on behalf of
Policy Scotland¹.

The Commission concluded that the problems of the council tax were sufficiently severe that what was required was a new approach to local domestic taxation based on property but including an element of income taxation. Their diagnosis of the council tax was based on the following points². First, it is regressive geographically. Evidence from England indicates that low value regions in the north pay higher proportions of household income on band D properties than do households in the South. Second, a growing proportion of dwellings pay less than the standard council tax liability because of discounts and exemptions. Third, and perhaps most importantly, the council tax is regressive across income bands (as indicated 10 years ago by the Commission chaired by Sir Peter Burt) but particularly so in terms of the amount of tax paid as property values rise. Fourth, apart from Ireland who recently imitated the UK, no other OECD country has a banded property tax. The bands themselves are very odd, as indicated in Table 1, since their weights flatten the tax liability across different property values such that a band A property pays a 1/3 of a band H property yet the latter may be at least 15 times the value of a band A property.

Table 1 – The Structure of the Council Tax

<table>
<thead>
<tr>
<th>Band</th>
<th>% of all dwellings (2013)</th>
<th>Value Range (1991)</th>
<th>Percentage of D</th>
</tr>
</thead>
<tbody>
<tr>
<td>A</td>
<td>21</td>
<td>Up to £27,000</td>
<td>67</td>
</tr>
<tr>
<td>B</td>
<td>24</td>
<td>£27,001-35,000</td>
<td>78</td>
</tr>
<tr>
<td>C</td>
<td>16</td>
<td>£35,001-45,000</td>
<td>89</td>
</tr>
<tr>
<td>D</td>
<td>13</td>
<td>£45,001-58,000</td>
<td>100</td>
</tr>
<tr>
<td>E</td>
<td>13</td>
<td>£58,001-80,000</td>
<td>122</td>
</tr>
<tr>
<td>F</td>
<td>7</td>
<td>£80,001-106,000</td>
<td>144</td>
</tr>
<tr>
<td>G</td>
<td>5</td>
<td>£106,001-212,000</td>
<td>167</td>
</tr>
<tr>
<td>H</td>
<td>1</td>
<td>£212,001 or more</td>
<td>200</td>
</tr>
</tbody>
</table>

Critically, the council tax has not been revalued since 1991 which creates all manner of anomalies and leaves the market distribution of property value increasingly divorced from the historical 1991 distribution - it is widely recognised internationally

¹ http://localtaxcommission.scot/tell-us-what-you-think/
² http://scottishpropertytaxreform.org/?page_id=34
that regular revaluation is essential to a sustainable property tax system\(^3\). These problems accumulate over time and reinforce each other so that the council tax system decays into greater disorder or entropy over time.

The Commission recommended that the council tax should be replaced and the freeze ended\(^4\). The Commission’s local tax reform proposals were relatively abstract, favouring a (regularly revalued) property tax solution but one that could be augmented by an element of income taxation. The Commission suggested that further work would be required to assess the practical basis for a land value tax as an alternative to a more conventional property tax. The Commission also made it clear that they expected the main political parties to respond in their (2016) Scottish election manifestos in how they would secure local tax reform and build on the Commission’s recommendations.

- The Scottish National Party moved away from their long term support for a local income tax and instead proposed a modest set of reforms entailing a reweighting of the bands so that higher value properties pay more, an additional high value band, an end to the freeze, some additional support for low income households in higher value bands, and consultation over assigning locally a proportion of future Scottish income tax receipts. There would be no general revaluation.
- The Conservatives low tax commission proposed broadly similar though less progressive reweighting of bands to the SNP proposal.
- Scottish Labour suggested a new property tax, one which included a fixed element but with higher percentage tax rates on properties above a certain level. This would operate locally in terms of rate-setting and would retain a national system of rebates.
- Liberal Democrats moved from their long standing support for a local income tax toward property taxation and, in particular, land value taxation.
- The Scottish Greens proposed a five-year transition to a property tax with a long term vision of using this as the basis for a future land value tax. The proposal also included a £10,000 allowance, a revaluation (which would distinguish land from buildings) and higher tax yields from more expensive properties.

**The Scottish Government's Proposals**

The new SNP administration brought forward a draft Statutory Instrument in September 2016. While this and the associated proposals for the Council Tax

---

\(^3\) Chris Leishman in research for the Commission found that around 60% of properties were in the wrong band, split roughly equally between too high and too low.

\(^4\) The council tax freeze which cost £630 million in its ninth year of operation (and several billions cumulatively) has been in place across Scotland for nine years and is expected to be ended in the imminent draft budget for 2017-18.
Reduction Scheme, are the main focus, they need to be placed in a wider frame.

First, the Scottish Government propose to increase the weights or multipliers on the top four bands (E, F, G and H), rising respectively by 7.5%, 12.5%, 17.5% and 22.5%. The Government estimates that will generate an additional annual £100 million. Second, however, households living on low income (defined as net incomes below the Scottish median - £25,000 per annum) will be entitled to an exemption through the Council Tax Reduction Scheme (CTRS). This would benefit 54,000 such households currently on Bands E to H properties. It is estimated that this will cost £7 million a year. An Equalities Impact Assessment was undertaken for the Council tax reweighting but not as regards the changes to CTRS on the basis that it was assessed when it was established. Neither the council tax weighting nor the CTRS changes were deemed to warrant other impact assessments (business regulatory or strategic environmental).

Third, the extra £100 million generated by the reweighting will not go to councils but is instead being ring-fenced as extra money for school-level education (a national Government priority). Fourth, the Scottish government has indicated that it had the desire to consult over (at some point in the future) assigning a proportion of devolved income tax receipts locally (further discussed in a submission to this evidence inquiry by Marco Biagi, former chair of the recent Commission and local government minister in the last Parliament). Fifth, it was announced separately that legislation will allow councils to charge full council tax on second homes (and keep the extra resources). Finally, the previous Scottish Government also implied that there may be further reform to local taxation in the future.

Reflections on Reform and Beyond

Is the proposal package more progressive (i.e. ‘fairer’)? It makes a regressive tax less regressive and offers significant exemption and hence compensation (albeit through a means-tested route) to all of those on below median incomes. The changes proposed do not appear on reflection to be massively difficult for councils to implement though there will inevitably be opportunity and transaction costs. However, I think there re wider questions and concerns.

While there was not complete consensus on the Commission for the action recommended there was agreement on the need to end the council tax and the freeze. What is being proposed, especially given the absence of a general revaluation, is clearly what the Scottish Government, in carrying through manifesto

---

5 The exemption is calculated by augmenting the current calculation of CTRS. Household income is determined as for normal CTRS cases, but then compared with a threshold amount derived from the equivalised median net income figures for that household type corresponding to an annual net income of £25,000. If the income level is below the relevant threshold then such households are entitled to the relief (see the Council Tax Reduction Policy Note).
pleads, feels it can do. But what is maximal for them is less than the minimum in the context of the reasonable expectations generated by the Commission. My worry is that without further commitment to substantive reform we will back in five years saying here is a property-based tax which sets values on market levels from 30 years in the past. The weighting may be more fair but the values that place properties in bands will be in most cases wrong and increasingly illegitimate. It is hard not to see this as a political fudge which does not resolve the underlying problems indicated above.

A second point is that fairness with property taxation is complex. It is not just about tax in relation to current income (important as that is) but it is also about the importance of inequality transmitted and reflected in the housing market and the relative failure to tax housing as an owner-occupier investment. While we repeatedly hear of the importance of social justice and tackling inequality, one of the key sources of that inequality (as well as damage through market volatility to economic productivity) is apparently sacrosanct. Moreover, as John Muellbauer at the University of Oxford pointed out, there are other ways to support low income households pay their local taxes, such as through allowances (like the Greens proposed), deferred payments as well as well-designed benefit systems.

Third, while the CTRS reform is in many ways a neat solution to compensating those in low incomes in higher value properties, it does add a further layer of means-tested complexity, and it is not clear at this point what will be done to ensure the highest levels of take-up. This is all the more germane given that the exemption would go much further up the income scale to immediately below median net incomes. There is a tension here with government policy elsewhere which will likely lead to councils setting full council tax on second properties on the basis to bring properties into more efficient use, yet at the same time CTRS is being used to help households stay in properties that are often only marginally affordable, if that.

Fourth, I was surprised that it was deemed unnecessary to carry out an equality impact assessment for the CTRS and that no wider assessments were required for either the tax change or the CTRS. The £7m figure for the additional cost of the CTRS must have assumptions about take up rates – it would be interesting to know more about these – as I think there would be grounds to think that rates might be relatively low. Additionally, aren’t the lessons from the land building transactions tax introduction that these sorts of tax changes do have market effects at the upper end of the housing market and that this is likely to have some degree of impact on when people decide to move how and could conceivably affect the labour market decisions of higher net worth households. I would have thought that was something working looking into.

Fifth, while ending the freeze and giving councils back the power to charge full council tax on second homes provides more discretion locally, this is offset by the
implementation of ring-fencing the extra £100 million to a national government priority.

Professor Kenneth Gibb
Director, Policy Scotland
University of Glasgow