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Council Tax Proposals in the Scottish Election 2011

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Abstract: this paper looks at the proposals for taxing property put forward by the political parties prior to the May 2011 Scottish election. It examines the effects on the overall Scottish budget and also the distributional impacts on all households and pensioner households. It finds that there are very large negative effects on local authority budgets arising from a council tax freeze and the proposals for discounts to pensioners have complicated interactions with the council tax benefit system.

Summary

This note analyses the proposals that were made by the political parties for changes in council tax in Scotland in the 2011 Holyrood Election Campaign. The proposals were as follows:

Conservatives

- a four-year council tax freeze
- a proposal to give residents the power to stop bills rising faster than inflation
- a pensioner discount of £200 per household from 2013-14
- no change in council tax bands or the ratios between these bands

Greens

- Replacement of both Council Tax and the Uniform Business Rates with a Land Value Tax

Labour

- a two-year council tax freeze
- students to be exempt from paying council tax

Liberal Democrats

- a two-year council tax freeze
- no pensioner on less than £10,000 has to pay any council tax, benefiting 20,000 pensioners in Scotland at a cost of £10 million
- long-run objective to replace the council tax with a local income tax

Scottish National Party

- a five-year council tax freeze
- a long-run objective to replace the council tax with a tax based on "ability to pay"

These proposals were subject to limited scrutiny during the election campaign. This paper examines the proposals put forward by the parties and argues that:

1. COSLA has substantially underestimated the costs of freezing the council tax in money terms. If councils were given the freedom to set their own council tax, one might reasonably assume they would ensure that its real value did not fall. The difference between holding council tax fixed in real terms as opposed to money terms could amount to more than £500 million per annum by 2015-16.
2. The freeze on council tax generally benefits middle income households rather than the poor.

3. A council tax freeze reduces the amount of council tax benefit payable in Scotland and therefore reduces the sum that will be transferred to the Scottish Government when housing and council tax benefit regulations change in 2013.
4. The Liberal Democrat proposals to exempt pensioners earning less than £10,000 would benefit low income households (but not the poorest households). Council tax bills would fall by £120m as a result of this policy. But net bills would only fall by £65m because there would be a reduction of £57m in council tax benefit payable by DWP. This is because the reduction would mainly impact on households already receiving council tax benefit. If their council tax bills are reduced to zero, then so is the amount of council tax benefit they receive. The cost of this policy would be around £120m, significantly more than the £10m published in their manifesto.
5. The Conservative policy would reduce council tax bills by £97m, but would cause a much smaller reduction, £24m in council tax benefit. This is because the Conservative proposals affect all pensioner households, the majority of whom do not receive council tax benefit. The Conservative policy would cost councils £97m and reduce payments by pensioner households by £73m. The Liberal-Democrat proposal would cost councils £120m and reduce council tax bills by only £65m.
6. The Liberal Democrat proposals would particularly benefit poorer pensioner households. The Conservative proposals would benefit middle income pensioner households proportionately more.
7. There is a growing body of support for the introduction of a land value tax.

Before discussing these findings, it is worth recalling some of the key features of property taxes in general and council tax in particular, few of which were discussed during the course of the election campaign:

1. In 2009-10, local authorities' revenue from council tax was £2.28 billion. This comprised only 17.7 per cent of net revenue expenditure by local authorities. They are compensated for the loss of income due to council tax rebates and council tax benefit by payments from the Department of Work and Pensions. Of this, £1.91 billion was collected directly from Scottish households. The remaining £0.37 billion came from council tax benefit subsidies paid by the Department of Work and Pensions. As mentioned previously, the model takes into account household circumstances and incomes so that council tax benefits and rebates can be calculated by household.
2. The council tax is a "hybrid tax", incorporating elements of both an income tax and a property tax. The income-related aspect comes from the operation of council tax benefit, a benefit paid by the Department of Work and Pensions, which offsets the cost of council tax for lower income households. It can also be viewed as a surrogate wealth tax or as a tax on the imputed value of housing services enjoyed by owner occupiers.

Finally, it also has some of the features of a poll tax in that a single-person's discount is available.

3. Council tax may be capitalised into property values if consumers are forward-looking, implying that the burden of such taxation may fall on the initial owners of the property¹.
4. Very few jurisdictions do not have some form of property tax. Since its tax base is immovable property, council tax is less likely to distort economic activity than most other forms of taxation. Arnold (2008)² argues that taxes on property have less adverse impact on economic growth than other forms of taxation. The recession has also focused attention internationally on the relative merits of property taxes. Having a wide tax base makes an economy more resilient to unanticipated falls in revenues from individual taxes. Thus for example, Ireland has recently introduced a property tax. In his advice to the Irish Government, OECD Secretary General Angel Gurría, argued that:

"Ireland cannot afford to go into another economic cycle without a reform of property taxation. Property taxes are an efficient way of raising revenue and the Commission on Taxation has recommended their introduction." Gurría (2009)³

5. The only part of the United Kingdom to make a significant change to property taxation in the last decade has been Northern Ireland. It replaced its domestic rates with a system based on the capital value of every residential property in Northern Ireland, using evidence from housing market sales. This is effectively a property tax. Every five years properties are to be revalued.
6. In Scotland, the Local Government Finance Review Committee⁴ recommended the introduction of a property tax, arguing that:

"We recommend a new progressive Local Property Tax (LPT) be introduced, based on the capital value of individual properties and payable by households occupying properties (whether as owner-occupiers or as tenants) and by owners of second homes and unoccupied properties. LPT satisfies our criteria." (Executive summary, para. 17)

This proposal pre-dated the introduction of a similar system in Northern Ireland, but no significant changes were made to Scotland's council tax system following this review.

¹ Feldstein, M. S. (1977), 'The Surprising Incidence of a Tax on Pure Rent: A New Answer to an Old Question', *Journal of Political Economy*, 85, 349–60.

² Arnold, J., (2008) "Do Tax Structures Affect Aggregate Economic Growth? Empirical Evidence From A Panel Of OECD Countries", *Economics Department Working Papers No. 643*, OECD, Paris

³ Gurría, A. (2009) "Launch of Economic Survey of Ireland", OECD, Paris [Accessed at: http://www.oecd.org/document/26/0,3746,en_21571361_44315115_44014874_1_1_1_1,00.html]

⁴ [Local Government Finance Review Committee](#) (2006)

7. Council tax in Scotland is based on 1991 property valuations. These are substantially out of date and do not reflect subsequent changes in the relative value of housing in different parts of Scotland. As evidenced by the experience of Northern Ireland, it is now technically feasible to regularly assess the value of individual properties. The current banding system for council tax does not adequately capture variation in property values.
8. There are a number of apparently anomalous exemptions from business rates, including agricultural buildings.
9. The UK has one of the highest rates of taxation on property among OECD countries if one includes taxes on both domestic and commercial property. Boadway et al.⁵ suggest that there is limited scope for increases in *real* revenue from this source.
10. Council tax revenues are highly predictable and provide a stable source of income for government. Other forms of revenue are much less predictable. This was evident in 2008 when UK revenues from income tax, corporation tax and stamp duty all declined at an unexpectedly rapid rate.
11. Due to the interaction of council tax benefit, council tax rebates and the structure of property valuations, council tax bears most heavily on households just below median income.
12. Research already reported by the Local Government Finance Review Committee⁶ on the increase in personal income tax rates necessary to replace the revenue lost should council tax be abolished and replaced by a local income tax indicated that an increase of 4.5p would be required. This exactly corresponds with recently reported estimates by Scottish government economists⁷.

⁵ Boadway, R., Chamberlain, E. and Emmerson, C. (2010) "Taxation of Wealth and Wealth Transfers", Chapter 8 of "Dimensions of Tax Design: the Mirrlees Review of UK Taxation" Mirrlees, J. (Chair), Oxford University Press

⁶ See: Bell, D. and King, D. (2006) "Modelling the Effects of Tax Options", Committee on Local Government Finance (2006) [Executive Summary](#), [Main Report](#)

⁷ [Glasgow Herald](#), April 11, 2011, [The Telegraph](#), April 8, 2011, [Scotsman](#) April 8, 2011

Analysis of the Party Proposals

1. The Council Tax Freeze

All of the parties propose to freeze the council tax for some, or all, of the next Parliament. Labour and the Liberal-Democrats propose a two-year freeze, with the Conservatives suggesting four years and the SNP proposing to freeze council tax throughout the next Parliament. But how much will this cost?

The difficulty with estimating the cost of the council tax freeze is that there is no readily available counterfactual. What would the council tax have been had a freeze not been in place? To estimate costs, one needs to establish a plausible alternative scenario for how council tax revenue would have changed had there not been a freeze.

I have approached this in two ways. The calculations lead to broadly the same conclusions.

- First, I look at how council tax revenues in England have grown since a council tax freeze was introduced in Scotland in 2008-09 and how they are forecast to grow by the Office of Budget Responsibility (OBR) over the next four years.
- Second, I have forecast changes in council tax liabilities at a household level assuming that council tax will grow at the same rate as the Consumer Price Index (CPI). This is based on CPI forecasts produced by the OBR. This exercise uses a similar microsimulation model to that utilised by the Institute of Fiscal Studies and by the Scottish government in the assessment of the relative costs of council tax and a local income tax. This method allows a proper assessment of the interaction of the council tax freeze with council tax benefits and rebates. Unlike the IFS, our model does not allow for a proportion of individuals not to take up benefits to which they are entitled.

a) The English Comparison

Table 1 shows the major sources of the local authority income in Scotland between 2005-06 and 2009-10. Over this period, revenue grants from government increased in value from £8.9 billion to £10.8 billion. Council tax revenue increased from £1.7 billion in 2005-06 to £1.9 billion in 2008-09. From 2007-08 to 2009-10, following the introduction of the council tax freeze, total council tax revenue in Scotland stayed stable at around £1.9 billion. Non-domestic rates, payable by businesses, rose throughout the period from 2005-06 to 2009-10.

In England, council tax rose revenues rose by 20% between 2005-06 and 2009-10. The equivalent increase in Scotland was 11%. Thus the burden of council tax has grown less rapidly in Scotland than in England. In particular, between 2007-08 and 2009-10, average council tax in England increased by 7% while in Scotland, there was no significant change.

Table 1: Scottish Local Government Income by Source

	£ Million				
	2005-06	2006-07	2007-08	2008-09	2009-10
Revenue Income					
Revenue Grants	8,862	9,284	9,834	10,377	10,845
<i>Of which:</i> <i>Council tax Benefit</i>	354	359	354	351	368
Council Tax	1,720	1,812	1,890	1,909	1,910
Non Domestic rates	1,897	1,884	1,860	1,963	2,165

Suppose that, instead of freezing council tax, Scottish local authorities followed their counterparts in England over this period in increasing council tax levels. Therefore in 2008-09, Scottish councils would have raised council tax rates by 3.9%. If the stock of housing in Scotland stayed fixed, total council tax revenue would have increased by £74 million. This is close to the £70 million⁸ agreed between the Scottish councils and the Scottish government as compensation for freezing the council tax in 2007-08.

Then in 2009-10, average council tax in England grew by 3 per cent. This is a *further* 3 per cent *in addition* to the 3.9 per cent in the previous year. Compared with a frozen council tax budget, Scottish councils could have expected to raise an additional £132m in 2009-10 compared with 2007-08. This shortfall is well in excess of the £70m compensation. And if council taxes again followed England in 2011-12, Scottish local authorities could have expected to raise £193m more than they would under a council tax freeze based on 2007-08 council tax bills.

Clearly, increasing council taxes at the same rate in Scotland as in England would not have been politically popular in Scotland, but the costs to local authorities have been high. They have not been fully compensated for the lost revenue and have become more dependent on grants from the Scottish Government to finance their activities.

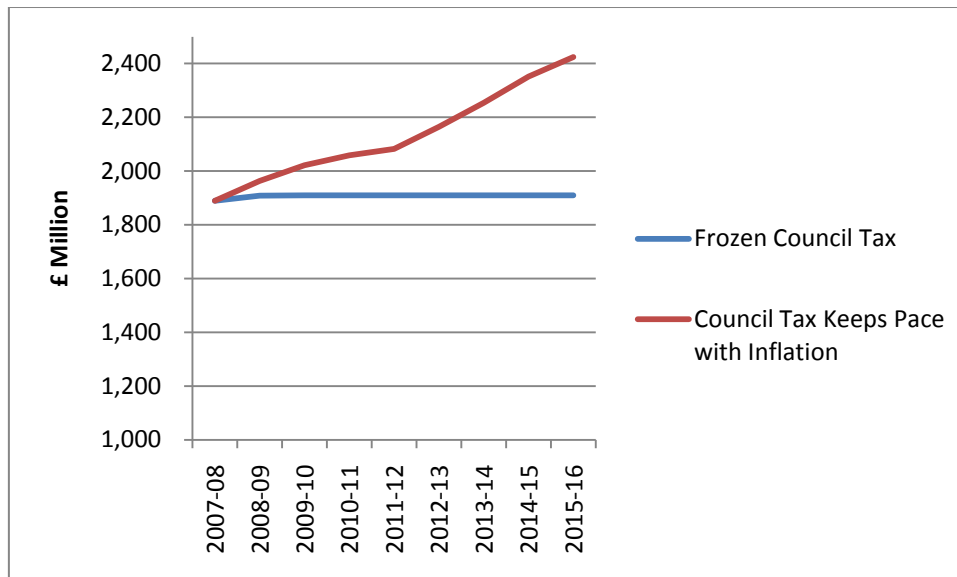
Now consider the costs of the council tax freeze over the next Parliament. Comparisons with England are more difficult since English local authorities do not preannounce council tax rates for more than a year in advance. However, the OBR does forecast future council tax revenues. These forecasts form part of the OBR assessment of the UK government's fiscal stance and the credibility of its attempts to reduce the UK structural deficit. The OBR forecast is that total council tax revenues in the UK will rise from £25.3bn in 2010-11 to 29.8bn in 2015-16, a 17.8 per cent increase. This is consistent with an assumption that council tax revenue stays constant in real terms, where price inflation is measured by the Retail Prices Index (RPI). The RPI is expected to increase by 18 per cent over the same period. In the past, one would have expected wages and benefits to keep pace with or exceed the RPI. This would mean that even with an 18% rise, the real burden of council tax on households would be falling.

Figure 1 shows the paths of total council tax revenue in Scotland from 2007-08 to 2015-16 based on (a) a council tax freeze and (b) increases in council tax based on the increases that

⁸ See: [Scottish Government](#) (2009)

took place in England from 2008-09 to 2010-11 and forecasts of growth from 2010-11 to 2015-16 based on OBR forecasts of council tax revenue.

Figure 1: Actual and Forecast Council Tax Revenues Scotland 2008-09 to 2015-16



Due to the recession, wage growth is unlikely to match the RPI increase over the next few years, suggesting that the OBR forecast implies that the real cost of council tax to UK wage earners will increase between 2011 and 2015. The income of those dependent on pensions and/or benefits, will be increasing with the CPI rather than the RPI following recent budgetary decisions by the Coalition Government. This means that if the OBR forecast was accurate, there will be a 6 per cent increase in the real cost of council tax between 2011 and 2015 for pensioners and benefit recipients. This is because the OBR forecast is that RPI growth will exceed CPI growth by 6 per cent over this period. This implies a growing real burden of council tax payments which would undoubtedly be politically unpopular throughout the UK. On the other hand, a council tax freeze implies that the real cost of council tax will diminish and therefore that other taxes will have to bear a greater share of the burden of reducing the UK budget deficit. Further, councils will become increasingly dependent on central government grants. And the implication from the OECD (2008) research is that an increase in property taxation would be less harmful to economic recovery than any other form of tax increase.

For Scotland, this calculation implies that the gap between frozen council tax revenues and the OBR-based forecasts of council tax revenue will grow from £193 million in 2010-11 by a further £342m by 2015-16. This means that, if one assumes that councils were able to keep their council tax revenues fixed in real terms, the rather than in money terms, but the annual cost of freezing the council tax at its 2007-08 level will equal £535m by 2015-16. This is substantially in excess of previous estimates of its costs. Clearly the size of the shortfall declines with the length of the council tax freeze. A two-year freeze would be substantially less costly than a five-year freeze.

b) The Scottish Calculation

One criticism that can be levelled at the above calculation is that it does not take account of interactions between the council tax and the tax and benefits system. One way to remedy this is to simulate how Scottish household council tax bills would change if, instead of freezing the council tax, local authorities decided to increase its level in line with inflation.

To do this, we use a tax-benefit model developed at the University of Stirling. It is based on anonymised household data from the 2008-09 Family Resources Survey. The model calculates tax liabilities, tax credits and benefits based on individual and household circumstances. The model is first updated to 2011-12 from 2008-09 by applying known rates of increase in incomes and prices. Known budgetary changes to tax rates and benefits between 2008-09 and 2011-12 are also applied. For forecast periods, we apply any changes to rates and allowances made in the most recent budget.

We ignore any change in household behaviour that might result from the policy changes. Thus, for example, we make no assumption that households move to houses in different council tax bands because their council tax bills might change. We also assume that council tax benefit regulations do not change.

We assume that earnings and benefits in Scotland grow in line with the OBR forecast for the UK. The growth in earnings means that some households receive less council tax benefit if the household council tax bill is frozen. Their earnings rise, but with a fixed council tax bill they qualify for less council tax benefit. As a result, the aggregate amount of council tax benefit payable in Scotland falls. On the other hand, if council tax is not frozen and instead increases with inflation, there will be relatively little variation in aggregate council tax benefit. This reduction in aggregate council tax benefit will have implications for the Scottish budget once responsibility for housing and council tax benefit is transferred to Scotland. This was signalled in the 2010 Spending Review by Chancellor George Osborne:

“We will give local authorities greater flexibility to manage council tax together with direct control over Council Tax benefit, within an overall budget that will be reduced by 10% from April 2013.”⁹

In Scotland, the transfer will not be to local authorities, but to the Scottish Government.

The main components of the differences arising from a frozen council tax and one based on the OBR forecasts of earnings and inflation is shown in Table 2 below:

⁹ HM Treasury (2010) The 2010 Spending Review, Chancellor’s Speech, [Accessed at: http://www.hm-treasury.gov.uk/spend_sr2010_speech.htm]

Table 2: Difference Between Scottish Council Tax Revenues based on OBR CPI Forecast and Frozen Council Tax 2015-16

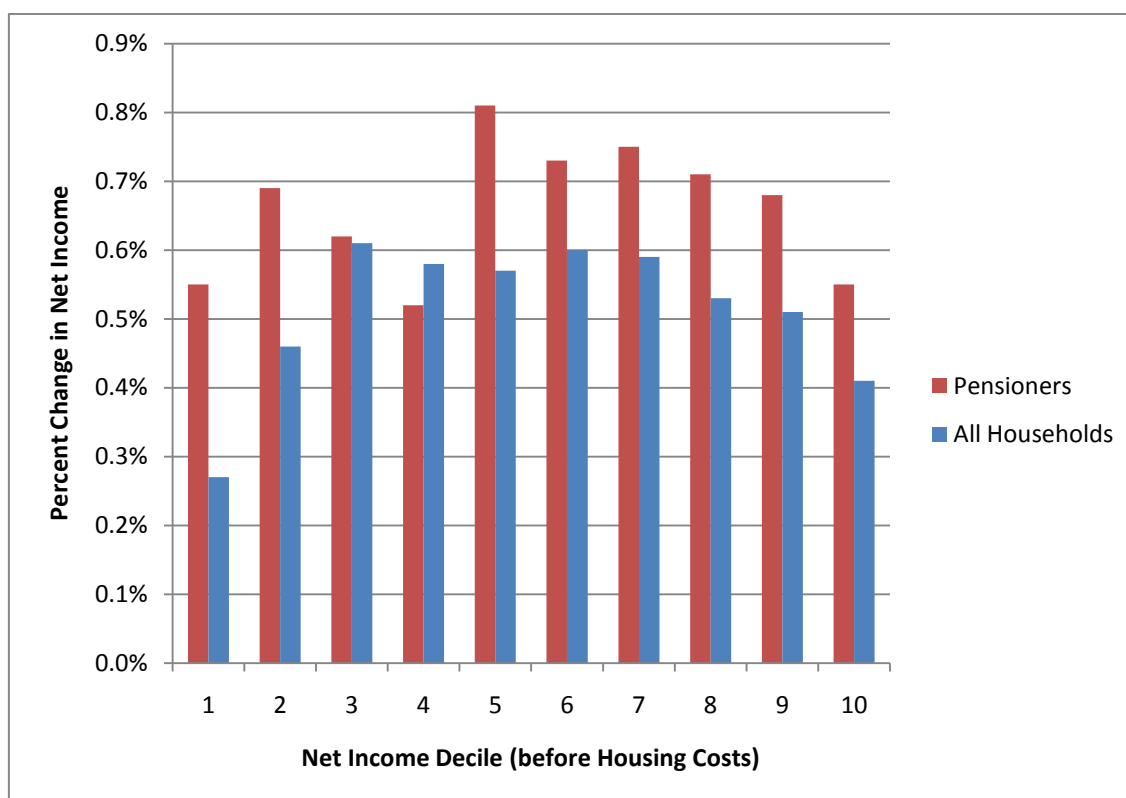
	Difference in 2015-16
Gross Council Tax Bill	£383m
Net Council Tax Bill	£327m
Council Tax Benefits	£57m

The implied change in net council tax is £327m. This is somewhat less than the estimate in the previous section. The difference is explained by the increased council tax benefit caused by the higher council tax bills. The net effect on local authority income between 2011-12 and 2015-16 is to increase it by £326m.

Figure 2 shows how the difference between a frozen and an indexed council tax affects Scottish households with different incomes. It is based on an ordering of households by net income from poorest to richest. We divide this range into ten deciles. Each decile is therefore a grouping of households with similar incomes. The first decile comprises the poorest 10% of households; the second decile is the next poorest 10%, and so on up to the 10th decile which comprises the richest 10% of households. We then calculate the average change for each decile in average weekly household income caused by freezing the council tax as opposed to increasing it with the CPI. We do this both for all households and pensioner households (households with one adult aged over 65). Pensioner households have a lower average income than all households.

A number of findings are clear from Figure 2. First, pensioner households gain more than households as a whole from the council tax freeze, largely because council tax makes up a large proportion of their outgoings. Second, households in the middle of the income distribution tend to gain more than those at the top or bottom. The relatively poor do not spend a high proportion of their net income on council tax, since their low income qualifies them for council tax benefit. The relatively rich spend only a small proportion of their income on council tax and therefore the imposition of the freeze benefits them less than middle income households.

Figure 2: Increase in Net Household income as Result of Council Tax Freeze 2015-16



Source: Family Resources Survey and Stirling Microsimulation Model

Thus the policy of freezing the council tax has distributional consequences as well as affecting council budgets, particularly benefiting those close to median household income and benefiting pensioner households more than households in general.

2. The Conservative and Liberal-Democrat Proposals for Council Tax Rebates

Now we consider specific proposals for Council tax affecting pensioner households only from the Conservatives and Liberal Democrat parties. The Conservatives propose to give each pensioner household in Scotland a £200 annual rebate on council tax bills¹⁰. The Liberal-Democrats propose to abolish council tax for pensioners with incomes below £10,000¹¹.

Our assumption is that the Liberal-Democrat proposal applies to households since the council tax liability applies to houses rather than to individuals. If it applied to individuals, one would have the anomalous position that households with two incomes of £9000 would be exempt from council tax, while one with a single income of £11,000 would be fully liable.

We estimate that there are around 488,000 pensioner households in Scotland in 2011-12 where these are defined as households with one adult aged over 65. Table 3 shows that

¹⁰ See: <http://www.scottishconservatives.com/downloads/common-sense-on-council-tax.pdf>

¹¹ See: <http://www.scotlibdems.org.uk/news/2011/03/purvis-and-scott-launch-policy-lift-low-income-pensioners-out-council-tax>

around 64 per cent of Scottish pensioner households are single person, while 36 per cent comprise two adults¹². Among two person households, only 6.4 per cent of couples have a household income of less than £10,000. On the other hand, more than half of single pensioners have an income of less than £10,000. The Liberal-Democrat proposal would principally benefit single pensioners, the majority of whom are women, while the Conservative proposal would affect more men. Our estimate is that there are 170,000 pensioner households with incomes less than £10,000, while there are 526,000 individual pensioners whose personal incomes are less than £10,000.

Table 3: Pensioner Households in Scotland

	Number of Pensioner Households	Share	Number of Pensioner Households with income under £10000	Share
Single	312,000	64%	159,000	50.7%
Couple	175,000	36%	11,000	6.4%
All	488,000		170,000	34.8%

The model described in the previous section is run for the year 2011-12 with and without the policy proposals of the Conservatives and the Liberal-Democrats. We use these runs to analyse changes in net household income for 2011-12 resulting from their proposed policies. We also assume that the proposals do not affect the existing system of council tax benefits and rebates. Any other form of adjustment would require changes to council tax benefit and rebate regulations that would probably require the involvement of the UK government.

We apply the policies after having taken account of council tax rebates, but before calculating council tax benefit. This does not matter for the Liberal-Democrat proposals, which are solely based on incomes. For the Conservative proposals, it is less clear. If the £200 discount is applied *after* taking account of, say, a council tax rebate of 25 per cent, then its value will be £50 greater than if the rebate was made *before* the application of the rebate. We have assumed the more generous interpretation that the discount is applied after the rebate.

Council tax bills would fall by £120m as a result of this Liberal-Democrat policy. This is significantly more than the £10m estimate in the manifesto. But net bills would only fall by £65m because there would be a reduction of £57m in council tax benefit. The removal of council tax for households with incomes below £10,000 would mainly impact on households *already* receiving council tax benefit. If their council tax bills are reduced to zero, then they would no longer receive council tax benefit.

The Conservative policy would reduce council tax bills by £97m, but would cause a much smaller reduction, £24m in council tax benefit. This is because the Conservative proposals affect all pensioner households, the majority of whom do not receive council tax benefit. The Conservative policy would cost councils £97m and reduce payments by pensioner

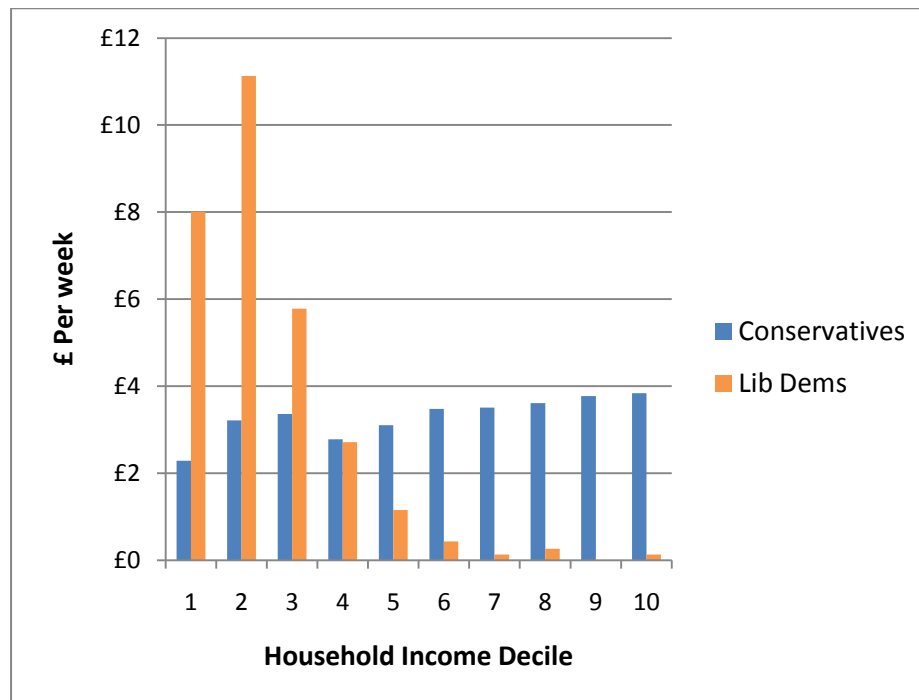
¹² There are a very small number of pensioner households that comprise more than two adults.

households by £73m. The Liberal-Democrat proposal would cost councils £120m and reduce council tax bills by only £65m.

Scottish councils would lose 5.1 per cent of their council tax revenue under the Conservative proposals and 6.3 per cent of the net council tax revenue under the Liberal-Democrat proposals. Given that the overall Scottish budget is shrinking, these amounts would have to be found from elsewhere in this diminishing budget. Local councils would wonder how they would be compensated for this loss of income, particularly when there is already concern about the effects of the council tax freeze on local government budgets.

We have also calculated the effects of the Conservative and Liberal Democrat policies on different types of pensioner households. In particular, we have concentrated on their impacts on the disposable incomes of poor and rich pensioner households as measured by their net household income. We again order the incomes of pensioner households from poorest to richest and divide this range into deciles. We have then calculated the average effects of the policies in terms of the change in net weekly household income on those within each decile, taking into account council tax rebates and council tax benefit. Results are shown in Figure 3

Figure 3: Change (£) in Weekly Net Household Income by Income Decile (Pensioner Households)



Source: Family Resources Survey and Stirling Microsimulation Model

Pensioner households at the lower end of the income scale benefit less from a blanket £200 subsidy to council tax than do those on higher incomes. This is because many of those on low income have council tax liabilities of less than £200. These will particularly include single pensioner households, which receive a 25% rebate as well as often being eligible for council tax benefit. Thus, Figure 3 shows that the increase in weekly net income arising from the

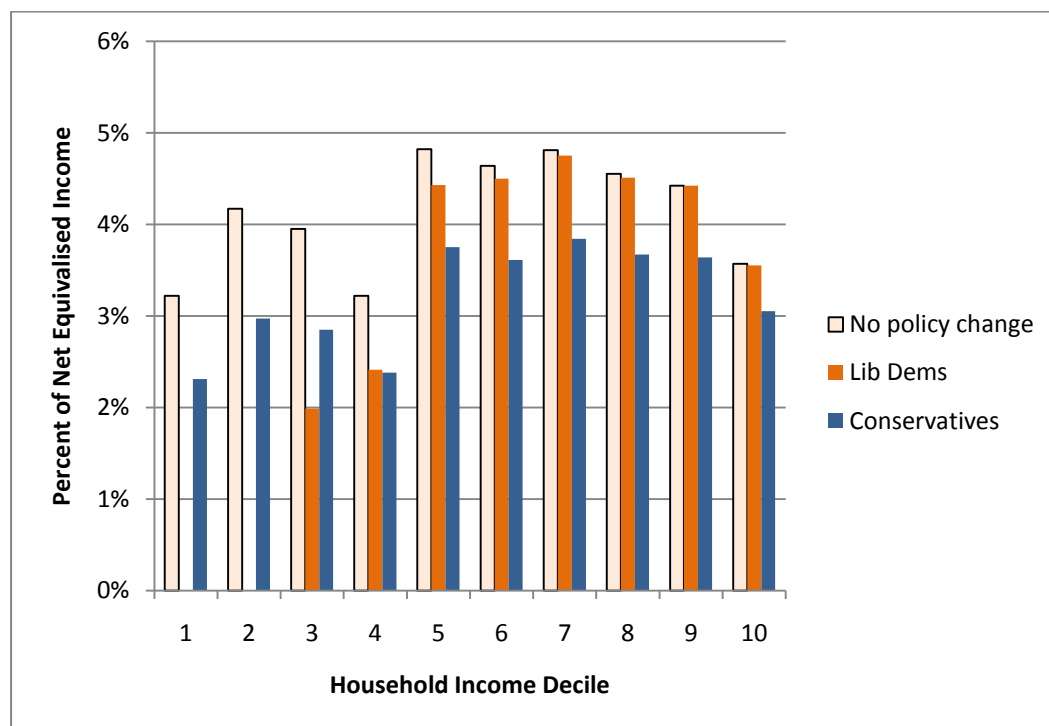
Conservative proposals is consistent at just under £4 per week across most income deciles, but is somewhat lower among poorer pensioner households.

In contrast, the Liberal Democrat proposals concentrate assistance on lower income deciles. Figure 3 shows that the largest net gain in weekly income of £11 per week would be made by those in the second income decile. The impact of the Liberal Democrat proposals on those pensioner households at or above the fifth income decile is negligible.

Another way to consider the effects of the policies is to estimate their effects on the share of their income pensioners households have to set aside to pay council tax. This is shown in Figure 4, which gives net council tax as a share of "equivalised" net household income. Incomes are adjusted or "equivalised" to take account of differences in household composition. This adjustment is principally used to take account of the real spending power available to families with different numbers of children and does not have much effect on calculations involving pensioners.

Figure 4 shows that it is those in the middle of the pensioner income distribution that have the largest council tax burden. Households in the sixth, seventh and eighth income decile pay just less than 5% of their net income in council tax. This share is lower among better off pensioner households because although they are likely to be liable for larger council tax bills, their income grows proportionately faster. The share is again smaller among poorer pensioner households due to the effects of rebates and council tax benefits.

Figure 4: Net Council Tax as Share of Equivalised Net Household Income before and after Policy Changes



Source: Family Resources Survey and Stirling Microsimulation Model

Figure 4 shows that the Liberal Democrat policy removes those in the first and second income decile from council tax payments entirely. Those in the third and fourth deciles gain significantly, while those in the fifth or higher income deciles gain very little from the policy of removing households with incomes below £10,000 from council tax.

Figure 4 also shows that the Conservative policy provides some significant benefits to those in lower income deciles, but they still pay between 2 and 3 per cent of their net income in council tax. For those in the fifth income decile or above, the Conservative policy still reduces the share of net council tax in net income. As one would expect, these reductions are somewhat greater than those from the Liberal Democrat policy.

Both Conservative and the Liberal Democrat policies clearly benefit pensioner households. While these benefits are spread across the income distribution with the Conservative proposals, the Liberal Democrat proposal would concentrate assistance in the first few income deciles where council tax benefit is already focused.

The Scottish Greens Proposal – A Land Value Tax

The proposal to reform the council tax system and replace it with a land value tax is radical. But it is not without merit or support. The Mirrlees Review of the UK tax system argues that:

“The use of land values rather than property values is preferable when considering taxation since land is relatively more immobile than property. This is because the taxation of land, unlike that of property, does not provide a disincentive for individuals to add to the value of their home through extensions and other such changes. However, while calculating the value of land might be more difficult, and potentially less transparent, than using market property values these problems do not seem insurmountable.” (Boadway et al. 2010)¹³

The Green’s proposal would be based on land values – not on the value of buildings. So it would not deter improvements to properties, on which homeowners anyway pay VAT. In this it differs from the new Northern Ireland tax and the proposals of the Local Government Finance Review in Scotland which both focus on property values. Introduction of a new land value tax would also provide be an opportunity to unify business and personal property taxation and to address some of the many anomalies in the existing system – such as the failure to revalue for two decades, the arbitrary nature of the existing council tax banding structure and the exemptions given to agricultural buildings etc. Even if domestic property and businesses were taxed at different rates, there would be economies of scale in data collection for valuations. A land value tax would also deter individuals and companies from hoarding land.

¹³ Boadway, R., Chamberlain, E. and Emmerson, C. (2010) “Taxation of Wealth and Wealth Transfers”, Chapter 8 of “Dimensions of Tax Design: the Mirrlees Review of UK Taxation” Mirrlees, J. (Chair), Oxford University Press

Conclusions

This paper has examined the proposals for changing council tax over the course of the next Scottish Parliament. It argues that the effects of the council tax freeze have been significantly underestimated. Compared with a scenario where council tax was fixed in real terms, a council tax freeze in money terms will reduce the local authority revenues from council tax by over £500 million by 2015-16.

Payments for council tax benefit will be reduced as a result of the freeze on council tax. This will mean a smaller amount of income will be transferred to the Scottish government when the Department for Work and Pensions hands over the responsibility for the distribution of council tax benefit to the Scottish government in 2013.

The Conservative and Liberal Democrat proposals to reduce pensioners' council tax bills have differing effects across the distribution of pensioner household incomes. The Liberal Democrat proposals cost more but are more targeted on poorer pensioner households. However because these households generally already receive council tax benefits there would be a substantial reduction in payments by DWP to local authorities. The Conservative proposals are less progressive but do not cause such a large reduction in Council tax benefit payments.

There is certainly some merit in proposals for a land value tax and it should be considered as one of the options should the Scottish government revisit the issue of property taxation in Scotland. If Northern Ireland can effect significant change in the way it taxes property, it is difficult to see why successive Scottish Governments have been unable to make any change the way in which property is taxed in Scotland.