

Briefing No. 3

WHAT'S WRONG WITH THE COUNCIL TAX

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The Local Tax Commission is undertaking a fundamental review of the Council Tax. But what exactly are the problems associated with the current form of local taxation in Scotland?

Summary

- Council Tax was a hasty, political compromise to overcome the poll tax fiasco. In such a febrile context, what seemed workable in the short term looks much less sensible now.
- The main problems with the council tax start with the deliberate decision to not revalue and to stick to 1991 property values, which is now untenable.
- No other property tax system bands payments into property value bands and this serves to compress the distribution of payments compared to the distribution of property values. This is one cause of the unfairness of council Tax – low value properties pay more in tax than higher value properties. Evidence from the Burt Review also suggests regressivity measured against household income. Moreover, higher housing value regions pay less in council tax as a percentage of property value and than lower priced regions.
- Because of the Council Tax freeze and the lack of a general revaluation, the tax lacks buoyancy (compared to economic and income growth) and has a diminishing yield (compared to general house prices).

Introduction

The Scottish Local Tax Commission is undertaking a fundamental review of the Council Tax. It may recommend structural reform of the present tax or indeed some new form of domestic taxation to fund local government. This reflects the fact that many are highly critical of the tax. But what is it that people do not like about Council Tax? To understand the main criticisms we need to first say a little bit about its context and its design or structure.

The Council Tax in Context

The Council Tax emerged quickly in the aftermath of the fall of Mrs Thatcher in late 1990. It was a political solution to the many problems of the poll tax, not least of which was the non-collectability of the Community Charge and the remaining hostility to a return to the old Rates system, which politicians believed was unacceptable to home-owners. The objective was to neutralise the political toxicity of local taxation but to do so in such a way as to retain the less salient but nonetheless attractive features of the poll tax system of local government finance, such as personal discounts for single adults and single person households (at least this was the view at the time from the perspective of central government).



The Council Tax was therefore something of a political compromise, a fix that would allow normal political life to resume. Of course, from the vantage point of a number of years later it is easy to say that this was unlikely to work well over time, if measured against sensible criteria (technical feasibility, fairness, wider impacts, local accountability, etc.); however, the setting up of the council tax had much shorter time horizons, it was done very quickly and did not carefully consider its longer term impact.

There are several key features of the council tax as it applies in Scotland today. First, it is based on property values set as they were in 1991 (or if built subsequently they are valued back to an imputed 1991 value). Only in Wales have council tax valuations been updated since 1991. This principle of not carrying out a general periodic revaluation stems from the political desire to avoid the previous problems with rates revaluations, which were perceived to be so unpopular with (voting) home-owners.

Second, and trying to retain some of the more attractive elements of the poll tax, personal discounts were offered to single adult households. Along with exempted properties, this means that around only 55% of Scottish dwellings are liable for the full Council Tax charge.

Third, properties were banded into 8 bands such that each property within a band faced the same liability. Moreover, the actual payments for each band were deliberately compressed in terms of their differentials (another olive branch to home owners). As Figure 1 describes, this meant that those with the lowest values (under £27,000 in 1991 values) paid 2/3 of the reference Band D and those in the highest Band (H), with properties exceeding £212,000 in 1991 values, paid twice the level of Band D. We can also see from the figure in the Annex that the bandings do not relate well to the proportions of properties in each band with more than 3/5 of all properties in the lowest three bands and only one percent in the top band. The Burt Review in 2006 noted that they could not find any other country that taxed property, also used a banding system of some kind. Comparing Band A with Band H, we see that properties are at least nine times more expensive but pay only three times more in Council Tax (and thereafter more expensive properties for instance in excess of a million continue to pay only three times more than the lowest valued properties).

Fourth, Council Tax is a hybrid in that it has property tax and personal tax elements but it also had a rebate system to help those on low incomes providing up to 100% support for those on social security such as income support. This changed after the 2010 UK General Election when in England Council Tax Benefit was cut by 10% and decentralized. In Scotland, the Scottish Government chose to pay the 10% from the Block and broadly retain the old system under the new name of Council Tax Reduction.

Problems with the Council Tax

- The absence of a general revaluation. While we can probably understand the political calculation of simply not revaluing, the long-term effect is corrosive. Not only is increasing resource required to value new properties back to 1991 values; but more importantly we have no sense of the adequacy of the banding today. Have properties and their neighbourhoods remained static in relative terms and

not risen or fallen with economic and social change? This is highly unlikely – some neighbourhoods did not even exist in 1991 whilst others have been radically recast by processes of development, gentrification and absolute decline. The Burt Review noted that between broadly 1993 and 2005 Scottish house prices rose by around 90% while in the same period Band D council tax increased by 10%. Yet this also masks wider local variation. This is actually an argument about fairness – property taxes can only work if they are regularly and consistently revalued and this is set in stone by statute.

- Council Tax has regressive features. As a percentage of property value, lower valued properties pay a larger proportion of their value in Council Tax than do higher valued properties. To the extent that the distribution of property values proxy for wealth this would seem to be unfair. This is a direct consequence of the banding system. Work done by the Burt Review in 2006 also suggests that lower decile income groups tend to pay an increasing share of their income in Council Tax but that it falls once we are over the median level of income. Households in the top two deciles pay the lowest proportion of their income in Council Tax. It is also the case that the poorest 10% appear to pay more than anyone else despite income-related assistance. This may reflect greater labour market insecurity and self-employment within this group – a segment likely to have grown since Burt was published just before the financial crisis. It will also reflect the savings cap on assistance
- Council Tax also appears to have perverse effects across regions. In [work for the Joseph Rowntree Foundation](#), Chris Leishman and colleagues report that Council Tax as a proportion of property value was higher in low value northern English regions compared to the Home Counties.
- All local taxes have to meet certain technical criteria if they are to be sustainable. They need to be collectable and Council Tax scores reasonably well on that score. But it does less well in terms of buoyancy and yield. Buoyancy concerns the extent to which the tax base rises with general economic growth and incomes. Retaining 1991 values does not help this, of course, and we saw that the yield has trailed well below house price growth despite the net additions to the housing stock. Moreover, in Scotland we have had eight years of Council Tax freeze, reducing the real cost of the Council Tax and its share of local government revenue.

Conclusion

The Council Tax was designed to be the most inoffensive possible tax to salve unruly home-owners but in so doing it undermined its long term coherence as a valid form of taxation. The implication for the Local Tax Commission is whether adjustments to the Council Tax in the form of re-banding, re-weighting bands and offering a commitment to regular general revaluations, would be sufficient to establish a durable, fair and efficient form of taxation, or whether it is necessary to look at more radical alternatives?

Reference

Local Government Finance Review Committee (2006) [Report of the Local Government Finance Review Committee](#) (Burt Report), Edinburgh: LGFRC

Annex The Council Tax in Scotland

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