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Reforming Council Tax

A summary of the options

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1. THE PROBLEM AND ITS CAUSES

Council tax represents a growing burden for many people on limited incomes. This is because, over recent years, the percentage rises in the tax have exceeded the percentage rises in both average earnings and retail prices, (to which some, but not all, pensions are linked). It is obvious therefore that council tax must be taking a growing proportion of most people's incomes. Anybody who was already on a tight budget a few years ago must be finding things even harder today.

The fundamental reason for the excessive rises in council tax is that central government has loaded more responsibilities onto local government - but has not provided the full funds necessary for discharging those responsibilities.

However, as well as causing hardship, the council tax is also "unfair" in two important respects:

- People on broadly similar **incomes** often pay very different amounts in Council Tax. In the worst cases the difference can be more than 30%. It all depends upon **where** you live - not on **what** you live in.
 - Indeed, people living in very similar **properties** can also end up paying widely different amounts in council tax. This is because the band appropriate to otherwise similar properties varies enormously from place to place - and the government tries to equalise the tax on properties in the same **band** wherever they are in the country.
- There is no direct relationship between the average council tax paid by any community and the amount that their local councils are able to spend on them. Many people pay more council tax for less or poorer services than others do.
 - In fact, there is a tendency for the more extravagant / higher spending local authorities to charge their residents less in tax than the more frugal ones. This is a direct consequence of the way in which central government funds are distributed - in particular the equalisation noted above.

The result of all this is that many of the "middling poor" people in the richer areas of the country end up subsidising the "middling rich" in the poorer areas of the country. People are actually forced to subsidise others who in both real and monetary terms are in fact better off than they are themselves. People are, in effect, being taxed, (or subsidised) on the basis of their neighbours' well being, (or ill being), and not on the basis of their own means.

None of this has anything to do with how extravagant or frugal any particular local authority is. The variations between local authorities in the council tax levels for the same band are far too small for that. The cause of the unfairness is that the banding structure, together with the equalisation of council tax for any band, makes the incidence of council tax haphazard - both with respect to people's incomes and with respect to the type of property that they occupy.

The haphazard nature of the tax means that many of the “knee jerk” proposals for change - typically making the tax more progressive - simply won't work. Some people will be helped, but this will only cover a few of those who really need it. A substantial minority of those who would be hurt, and hurt badly, by such a change are **already** suffering unfairly under the present system. Because of the haphazard way in which council tax works, even quite substantial changes to the system, such as increasing the tax on the more highly banded properties and reducing it on the more lowly banded ones, (or adding extra bands at the top and bottom), would have very little effect on the overall progressiveness of the system. There would be roughly equal numbers of winners and losers at **all** levels of income under any such changes of this type.

2. SOME POSSIBLE SOLUTIONS

There are a number of possible ways in which the unfairness and hardship associated with the council tax could be reduced. Those that I have investigated include:

- Abolishing the council tax in whole or in part and replacing it with increases to national taxation - income tax and VAT being the favoured candidates.
 - Simply funding locally determined expenditure from the proceeds of an unreformed council tax and financing those activities for which local government merely acts as the agent for central government out of national taxes would result in a substantial reduction in council tax bills. With such a reduction, people would probably not be so concerned about the unfairness of the tax.
- Abolishing the council tax in whole or in part and replacing it with other forms of local taxation. Only a local income tax would appear to be a viable option for replacing a significant proportion of the money raised from council tax.
 - A conventional local income tax, where local authorities would be responsible for setting the **rates** of tax, would be administratively complex and quite possibly economically damaging - as would local sales taxes. However, if local authorities were allowed to determine tax **allowances** instead, then the cost of administration would be very low and the economic effects minuscule.

Changing the way in which central government grants are distributed - from one based on the banding structure in each local authority to one based on the incomes of its residents while leaving the rest of the council tax system unreformed.

- I have investigated a whole range of options in this area. One particular option works by setting the council tax per dwelling based on a formula involving the mean and median gross personal incomes of the residents of each authority. This produces a very substantial improvement in the fairness of the tax in terms of income and a smaller, though still useful, improvement in terms of the fairness of the tax on similar properties.
- Changing the mix of bands within local authorities - i.e. making bands depend on relative local property prices and not relative national property prices, (which inevitably include properties a long way away). I have investigated a number of options of this type.

- One particular promising approach involves using the same (carefully chosen) mix of bands in **all** authorities, changing the ratios between council tax charged at different bands and modifying the central government grant allocation algorithm. This particular model eliminates virtually **all** the **systemic** unfairness of the tax. I can of course do nothing about people who live in better houses than their income “warrants” when compared with other people in the same local authority.
- Another approach is to deliberately force fit the banding profile in each local authority to the income profile. The main attraction of this approach is that, if it is coupled with a government grant algorithm based on mean and median incomes, we can then make the incidence of council tax much more progressive or regressive against income without causing any of the problems associated with doing so within the current banding and grant allocation approach.

None of the options of this type can be implemented without a full scale revaluation exercise. Unfortunately, the government has decided that no such revaluation will take place in the near future.

- I have also investigated the possibility of having locally determined ratios between the council tax bills for different bands - instead of the uniform national system that we have at present.
 - While this does improve fairness and reduce hardship, I have not been able to come up with a system that does as well as changing the banding structure does in this respect. However, this approach does have value in that it could be implemented without any property revaluation.

Some of these possible solutions can be combined with others to produce a hybrid approach. Others can not. However, even with those that can, I find that the optimum results from a combination generally have different values for the various parameters than when the options are considered separately. For example, if we only change the distribution of central government grants, the ideal values of those grants from the point of view of “fairness” are rather different from the ideal values when we also modify the banding mix within different local authorities.

This is deliberately only a summary of some of the statistical research and modelling that I have undertaken. I intend publishing much fuller details on each of these options on the Isitfair website in the near future.