Briefing Note

Local Income Tax

Background

The political impetus for a Local Income Tax as a means of providing a contribution towards local government finance derives from widespread public dissatisfaction with the Council Tax. Council Tax bills in Scotland rose substantially in excess of the cost of living between its introduction in 1993 and the SNP/COSLA agreed Council Tax freeze which came into force in April 2008.

Local government finance is a devolved responsibility of the Scottish Government and governments north and south of the border have in the past commissioned research into the options for replacing the Council Tax. In Scotland such a review, chaired by Sir Peter Burt, reported in November 2006 and recommended that the Council Tax be replaced by a property value tax, similar to that operated in Northern Ireland. This recommendation found little support among the political parties in the run-up to the May 2007 Scottish Parliamentary elections and the report was quickly sidelined.

The widespread public anger at the cost of the Council Tax resulted in this topic being a key battleground in the 2007 Scottish elections. The Labour Party fought on a policy of retaining the Council Tax but re-banding it to ensure smaller bills at the lower end of the scale and higher bills at the upper end. The Conservatives also favoured the retention of the Council Tax, but with a 50% discount for the over 65s. Both the Scottish National Party and the Liberal Democrats proposed a Local Income Tax, with the SNP favouring a flat national rate, while the Lib Dems wanted to see local variation across Scotland's 32 local authority areas.

The Scottish National Party Government

On assuming office in May 2007, the SNP Government restated its commitment to introduce a Local Income Tax to replace the Council Tax within the lifetime of the current parliament, i.e. by May 2011. In March 2008, the Scottish Government published its proposals for a Local Income Tax to launch a consultation on the policy, which ran until July of this year. Scottish Chambers of Commerce discussed the issue of a Local Income Tax at its July Council meeting and a submission was subsequently made to the consultation.

In November 2008, the Scottish Government published its response to the public consultation, restating its commitment to the introduction of a Local Income Tax and pledging to bring forward a Bill in the Scottish Parliament by June 2009. This view was reiterated by the Cabinet Secretary for Finance and Sustainable Growth, John Swinney MSP, at a private meeting with Scottish Chambers of Commerce and the other Scottish business organisations on 27 November 2008.

The Scottish Parliament

The subject of a Local Income Tax has been debated four times in the Scottish Parliament, with the following motions having been agreed:

21 June 2007 - "That the Parliament believes that local income tax, which is based on ability to pay, is a fairer system of local taxation than the discredited and unfair council tax and notes the position of the Green Party in regard to land value taxation."

April 17 2008 - "That the Parliament notes the Scottish Government's consultation on the future of local taxation; recognises that this consultation is not due to close until 18 July 2008; notes the wider range of possible options, including local income tax, land value tax, property tax and reform of the council tax; recognises that the existing system of local government taxation is discredited, bureaucratic and unpopular; agrees on the urgent need for substantial changes to the system of local taxation, and agrees that, in developing this future system, due consideration should be given to fairness, local accountability, the need to reduce tax avoidance and the wider social, economic and environmental impact of any proposed system of local tax reform on communities across Scotland."

October 2 2008 - "That the Parliament calls on the Scottish Government to publish in detail, prior to the introduction of a council tax abolition Bill, how it proposes to allocate to each local authority local income tax revenues and all other sources of funding, including revenue support grant and non-domestic rates income, together with indicative figures for each local authority for the first year of operation of local income tax, and how stability of funding is delivered to ensure that no local authority loses revenues directly because of the introduction of the new tax system in the event of the Bill being enacted, and believes the UK Government should agree that Council Tax Benefit money forms an integral part of local government finance and should be available to local government as part of decisions by the Scottish Parliament to reform local taxation in Scotland."

4 December 2008 – "That the Parliament notes the intention of the Scottish Government to introduce legislation to reform the system of local government taxation and calls on it to ensure that the scope of the Bill when introduced is sufficiently wide as to enable members to debate and vote on all options, including reform of the council tax, a land value tax, a local income tax with variable rates determined locally and the Scottish Government's own proposals."

It is clear that in the Scottish Parliament, there is no clear majority in favour of any single method of recovering a domestic contribution for local government finance. The SNP, supporting a Local Income Tax with a nationally set rate, have 47 votes, and the Lib Dems, supporting a locally set LIT, have 16 votes. If they manage to broker a deal, that will give them a voting block of 63, two short of the 65 needed for an overall majority. Labour have 46 votes and share the goal of a reformed Council Tax with the Conservatives who have 16 votes, leaving them 3 short of an overall majority. The balance of power therefore rests with the votes of the 2 Green MSPs (who support a Land Value Tax), the Independent MSP Margo MacDonald, who supports an income based solution to local taxation, but not that proposed by the Scottish Government, and the Presiding Officer, who only has a casting vote which would presumably be cast in favour of the status quo if the voting was split 64-64.

The Scottish Parliament's most recent vote on LIT was the motion of 4 December. This was a Conservative motion for a wider consideration of methods of local government finance. The Tories were supported by Labour, the Greens and Margo MacDonald, with the vote being passed by 65 votes to 60.

SCC's Position

Scottish Chambers of Commerce have steadfastly maintained an opposition to a Local Income Tax since it was first mooted by the Scottish Government. Our reasons for opposing this have been:

- **The direct administrative cost to Scottish businesses for its implementation, estimated by the Burt Review to be £60 million in the first year and up to £18 million per year thereafter.**

- **The threat LIT would pose to inward investment in Scotland, with anecdotal reports suggesting that some businesses are holding back from investment decisions as a result of uncertainty over LIT.**

- **LIT could prejudice Scotland's ability to attract headquarter operations to Scotland, as a result of the income tax differential on higher paid staff.**

- **The LIT is a tax on labour, not on wealth.**

- **Employment patterns can change quickly and this may prejudice the ability of local authorities to plan budgets strategically. This is especially important with councils now playing a more central role in economic development.**

- **The replacement of a property tax with a labour tax may create in imbalance in the housing market, making workforce mobility more difficult.**

- **Questions over the co-operation of HM Revenue & Customs in recovering the Local Income Tax remain to be resolved, as does the issue of the repatriation of revenue to the Scottish Government.**

SCC has deliberately not taken a position on the Council Tax or any other alternative method of funding local government. Our opposition to the Local Income Tax is based upon its potential to adversely affect the competitiveness of Scottish businesses and its potential harm to the Scottish economy.

Scottish Chambers of Commerce
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