

COUNCIL TAX

The Case For Reform

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Peter Kenway and Guy Palmer

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ABOUT THE AUTHORS

Peter Kenway is Executive Director of the New Policy Institute.

Guy Palmer is Director of the New Policy Institute.

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New Policy Institute
109 Coppergate House
16 Brune Street
London E1 7NJ

Tel: 0171 721 8421
Fax: 0171 721 8422
Email: info@npi.org.uk
Web site: www.npi.org.uk

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FOREWORD

It would not be an exaggeration to say that the Community Charge or Poll Tax brought down Mrs. Thatcher. It is not surprising that the Labour government has left the replacement Council Tax well alone. There have been neither riots nor a widespread refusal to pay, and it enjoys a legitimacy that the Community Charge did not.

Yet there is much that is wrong with the Council Tax and if the government continues to 'leave well alone', it will miss an opportunity.

The fundamental problem with the Council Tax is its regressivity. Bigger and more expensive properties on average pay proportionately less than smaller, cheaper ones. As a principle for taxation, this is not acceptable. It is the opposite of how income tax works, where higher incomes pay proportionately more tax than lower incomes. And it is worse than VAT, where the tax is a constant proportion of expenditure.

The essence of this paper by the New Policy Institute is that we can reform the Council Tax system by lowering the burden of the tax on smaller, less-valuable properties without increasing the tax for the majority in middle-sized properties. This can be done because so much of the tax for the poorest households is actually paid by the government in the form of Council Tax Benefit. The immediate beneficiaries of this reform would be the low-paid, who are a key group for government policy.

Reform could also have benefits of a quite different kind, by making it easier to increase the share of local authority revenue that is raised locally, via the Council Tax, without hurting lower income groups.

As it is, a shift from central to local funding has been going on ever since the Council Tax was introduced, and this has meant that redistribution is going on now, but in the wrong direction!

Reform of the Council Tax could also provide a platform for bigger changes in society. Why can a household's liability for Council Tax not also be used as the basis for levying other charges that fall naturally on households? The television licence, for instance, is at present levied uniformly on almost all households. Why not use a reformed Council Tax as the basis for a new licence fee system to pay for digital expansion?

Other examples are the standing, or fixed, charge elements of bills levied on households by gas, electricity and water companies as well as telephone and even cable companies. A move from uniform to (relatively) progressive fixed charges could also make sense for the companies involved, making it easier to increase the fixed element of bills overall while reducing the additional charges levied per unit of the service consumed.

It is important to recognise that the call being made here is limited to one of reform of the Council Tax, rather than its abolition. There is a good reason for this, which is that although strongly regressive, the Council Tax is built on the principle that the amount paid should to some degree reflect household wealth and income. The principle only appears in a weak form, but it is present, and as such stands in contrast to the Community Charge which explicitly rejected the principle. And as this paper makes clear, there is considerable potential within the Council Tax system to reform it. There is both a need for change and an opportunity to effect it.

Jim McAuslan

Deputy General Secretary,
Public and Commercial Services Union

SUMMARY

INTRODUCTION

This paper discusses the future of the Council Tax and how, if at all, it should be changed. As such, it aims to stimulate a long overdue debate surrounding the Government White Paper on local government finance published in summer 1998.

The paper is one of two commissioned by the Public and Commercial Services Union, the other of which analysed the impact of moving water charges onto a Council Tax basis. In this context, it is worth noting that the potential use of Council Tax goes far beyond being just a means for raising part of local authority income, certainly to water charging and possibly to other utility pricing. But such extensions in the use of Council Tax, and indeed the possible expansion of its role in local authority finance, depend on it being fair and just. This paper demonstrates that this is currently not the case, but also that the government has the means to hand to make it the case.

Three terms recur throughout the report:

- **Revaluation.** The assignment to each dwelling/property of a Council Tax band, any of A through H. Properties were originally valued for Council Tax purposes in 1991 and that valuation still stands.
- **Re-banding.** A change in either the number of Council Tax bands (currently 8) or the range of property values which each spans.
- **Re-multiplying.** Changing the proportions or multiples that are used to calculate the level of the Council Tax for any particular band in comparison with the tax for the middle band (band D).

THE GOVERNMENT'S ARGUMENT AGAINST REVALUATION

In their July 1998 White Paper, *Modern Local Government In Touch with the People*, the government argued against a revaluation of properties for Council Tax purposes during the lifetime of this parliament. The essence of its argument, in which re-banding plays a subsidiary role only, was that:

- The Council Tax is working well, with no fundamental problems needing urgent attention.
- Major changes in relative property prices would be needed before significant numbers of households are badly treated. The current valuation base is broadly acceptable and is likely to remain so for the next few years.
- The fairness of the system will be kept under review, and a revaluation carried out if necessary in the next parliament. If necessary, the number and width of the bands can be reviewed then too.

Our analysis does find some evidence that could support the case for revaluation; for example, the considerable disparity between rateable values and Council Tax valuations. Overall, however, we do not seek to make an argument for revaluation in its own right.

OUR ARGUMENT FOR RE-BANDING

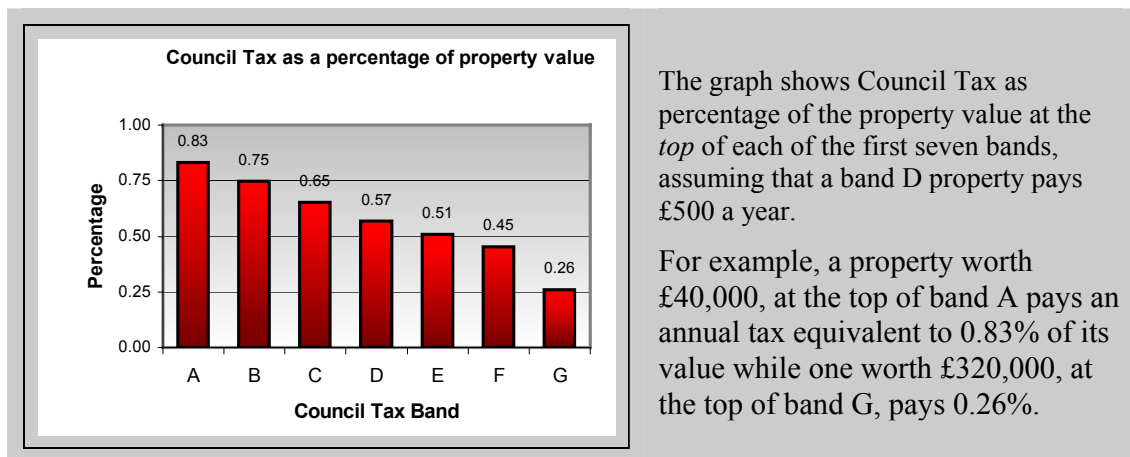
Instead of concentrating on revaluation, our paper puts forward a case for reform of the Council Tax in which re-banding is crucial and revaluation is subsidiary:

- There are many, somewhat arbitrary, unfairnesses in the current system and there are opportunities for a more proportionate system. Reform could help the less wealthy; help to ‘make work pay’; and strengthen local autonomy.
- Such gains can only come from re-designing the bands, changing both their number and their width. Any re-design of the bands automatically opens up the question of what the multipliers should be.
- Re-design of the bands then requires a revaluation, in order to assign properties to the new structure.

Whereas, the Government’s argument centres on problems, ours is more focussed on opportunities: if it has the will, the Government certainly has the means to bring about significant change. In particular, the setting of the bands and the multipliers rest in its hands. Furthermore, because a sizeable proportion of those in lower bands receive Council Tax benefit, the *net* cost of cutting tax at the bottom is much reduced. As a result, as our analysis shows, desirable solutions are feasible.

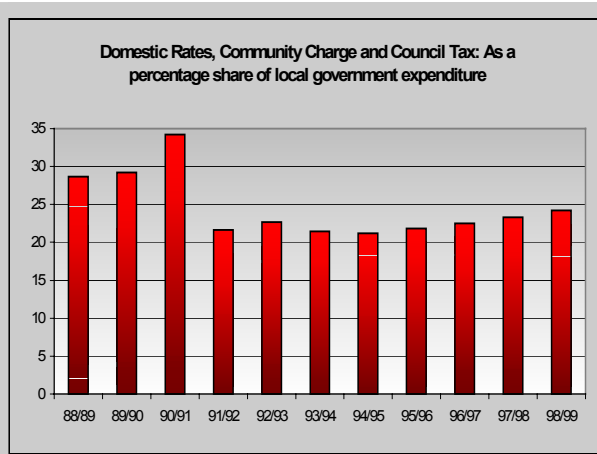
THE CASE FOR REFORM

Unlike income tax, Council Tax is regressive. With income tax, both the *amount* of tax and the *rate* of tax generally *rise* as income rises - income tax is a progressive tax. By contrast, within any local authority, whilst the *amount* of Council Tax *rises* as the value of the property rises, the *rate* this represents as a share of the property’s value generally *falls* as the value rises.



Another way of expressing the fact that more valuable properties pay proportionately less is that, while the ratio between property values in the top and bottom bands is at least 8 to 1, the ratio between the amounts of tax they pay is only 3 to 1. Council Tax is more progressive than the Community Charge which it succeeded, but not all that much more so. It is also significantly more regressive than the pre-1989 system of rateable values.

Since Council Tax is more regressive than income tax, shifting the share of local authority funding away from central taxation towards local taxation penalises those living in smaller properties to the benefit of those on higher incomes. Since its introduction in 1993, Council Tax has been rising as a share of local authority revenue, but it is still substantially below the proportion that both domestic rates and Community Charge represented, before the collapse of the latter in 1991/92.

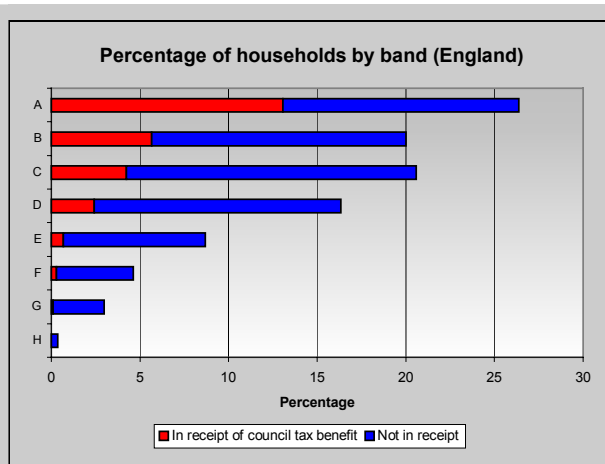


The graph shows Council Tax (and its fore-runners) as percentages of local government revenue.

From over 34% in 1990/91, the Community Charge fell to just 22% of local government revenue in 1992.

Council Tax provided about 22% of local government revenue when introduced in 1993, rising to about 24% in 1998/9. Since its introduction, it has represented around 4% of the total taxes paid to government.

The regressivity of the Council Tax system also deepens the benefit trap and adds to the benefit bill, given that the great majority of those receiving benefit live in homes in the lowest bands.



The graph shows the properties by band, divided according to whether they get Council Tax benefit, whether full or partial.

Around a quarter of all households, and almost half in band A, are in receipt of Council Tax benefit.

87% of all households in receipt of Council Tax benefit are in bands A to C.

Finally, as the government itself observed (in its April 1998 Consultation Paper, *Water Charging in England and Wales - A New Approach*), properties especially in the northern regions of England are concentrated overwhelmingly in just one or two bands, rather than being spread reasonably uniformly. This accentuates the extent to which the Council Tax actually resembles a flat tax in many parts of the country.

THE OPPORTUNITY FOR REFORM

The regressive nature of the Council Tax is not inherent to a property tax; nor is it inevitable. Rather, it arises from the particular parameters chosen for it, in terms of the bands into which properties are placed and the multipliers used to calculate the amounts levied on each band.

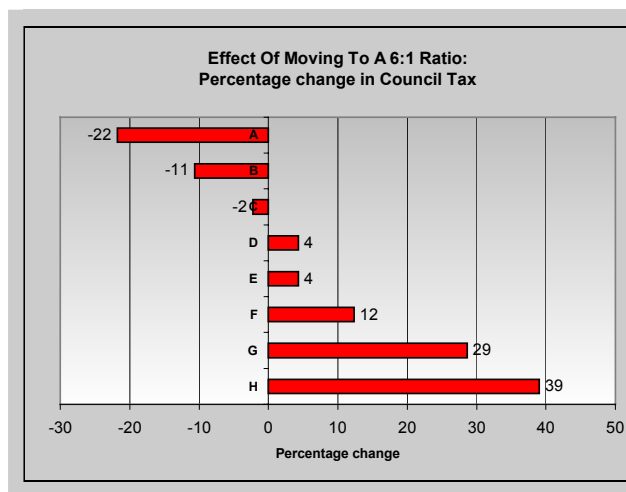
It could well be argued that the current bands and multipliers have a strong degree of arbitrariness, having been quickly chosen as a politically acceptable replacement for the Community Charge. However, this arbitrariness also points to a flexibility in the Council Tax system that neither the Community Charge nor domestic rates possessed: by selecting the banding and the multipliers, government has the opportunity to reform Council Tax so as to reduce the unfairness and its side effects. Government has more scope to amend the Council Tax than it had to amend either of its predecessors.

THE PRACTICABILITY OF REFORM

As well as there being a good case for reform, our analysis demonstrates that there is scope to do so in a way that can both reduce the benefit bill and return money to the poor in work, while still leaving the great majority of Council Tax payers unaffected.

The paper analyses a number of options to illustrate the effects that reform of the Council Tax could bring:

- In terms of the number of bands, the paper argues a minimum reform case which increases the number of bands from 8 to 10, by splitting the lowest band, A, and the second highest band, G.
- In terms of the multipliers, the paper suggests a new set that tilt the burden of tax in favour of the lowest three present bands at the expense of the highest three, while leaving the middle two untouched. Instead of the present 3 to 1 ratio between the top and bottom bands, the paper considers options up to ratios of 6 to 1.



The graph shows the percentage change in bills by Council Tax band resulting from the implementation of a 10 band structure, using multipliers where the ratio between top and bottom is 6 to 1.

The calculation assumes a uniform rate of tax across all authorities, and is therefore illustrative only.

To achieve revenue neutrality, a 4% rise in band D's Council Tax is needed.

In this example, and in terms of the impact among those who pay the Council Tax in full (as opposed to those who receive Council Tax benefit):

- The 13% of full tax payers in band A enjoy reductions of about £1.90 a week, the 14% in band B enjoy reductions of 80 pence, and the 16% in band C enjoy reductions of 25 pence a week.
- The 4% in band F face an increase of £2.40 a week, the 3% in band G face an average weekly increase of £6.30 and the 0.5% in band H face an increase of £10.30 a week.
- The 22% in bands D and E lose between 60 and 70 pence a week.

Those who do not pay any Council Tax (i.e. their tax is paid directly in the form of Council Tax benefit) are not helped *directly* by such reform. However, they are helped *indirectly* as soon as they move into work which takes their income above the Council Tax benefit threshold. For those in the lower bands, a reform of this kind helps to lower the benefit trap thereby lessening the disincentives for moving into paid work.

The analysis also shows that there would be a fall of about 10% (£220 million) in Council Tax benefit. This does not save the government money since the calculation assumes a matching increase in revenue support grant. However, it does point to the reason why a relatively benign outcome is possible, because a significant proportion of the Council Tax revenue from the lowest bands is actually met by the government from general taxation.

Our analysis of this question is only intended to be illustrative; there are, for example, important inter-regional aspects which would need to be considered. However, its central message is that a reasonably modest reform can bring significant gains to tax payers in bands A and B while leaving the almost 50% of households in C, D and E virtually untouched.

CONCLUSION

The argument for Council Tax reform is not based on there being any great administrative problem that needs to be addressed or overcome. Rather, the argument is that the tax is unfair, especially to those on low incomes above the benefit thresholds, but that thanks to its design, the government has the opportunity to undertake reform. In particular, the bands and multipliers can ultimately be set at will while the fact that a sizeable proportion of those in lower bands receive Council Tax benefit means that the net cost of cutting their tax is much reduced. Thus, there are both means to hand and desirable solutions which are likely to be feasible.

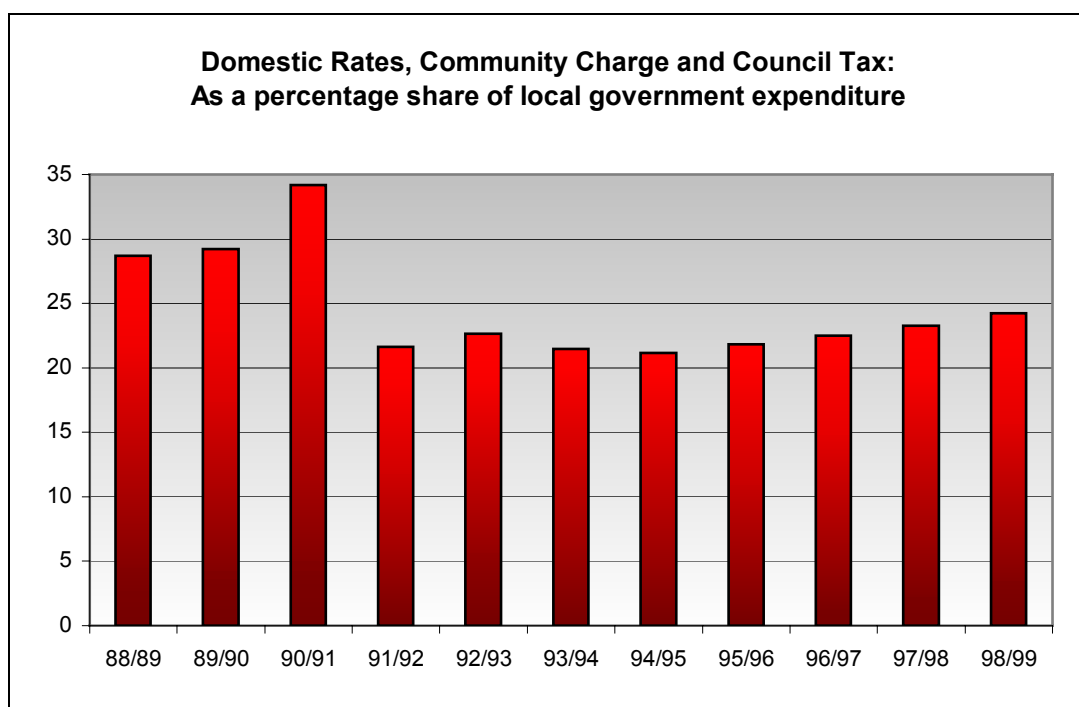
It was once said, only half in jest, that when the Chancellor, Nigel Lawson, reduced the top rate of income tax in the 1988 budget from 60% to 40%, his ultimate aim was to get the 'top' rate of tax below the standard rate. That idea sounds extreme, until it is realised that that is exactly what happens with the Council Tax as it is now structured.

1. INTRODUCTION

In this chapter, we discuss some of the important characteristics of the Council Tax system.

COUNCIL TAX AND ITS IMPORTANCE

Council Tax is a hybrid tax which mixes elements of a tax on property value, a tax on people (as the first two adults both affect the liability) and a tax on income (due to the tax rebates for low income households).



Source: Local Government Financial Statistics 1998, table 9.5. The figures are gross of all rebates, relevant benefits and transitional relief schemes.

The graph shows the percentage that Council Tax or its predecessors represent as a share of local authorities' revenue expenditure.

- From a peak of 34% in 1990/91, the Community Charge fell back to being just under 22% of local government revenue in 1991/92.
- Council Tax provided just under 22% of local government revenue when introduced in 1993/94, rising to just over 24% in 1998/99.
- In addition, Council Tax has represented around 4% of the total taxes paid to central and local government since its introduction.

Almost all European nations have some form of property tax. As a share of local government income, property taxes range from under 10% in Austria and Denmark to over 30% in France, Belgium and Spain. The UK is therefore in the middle of this range.

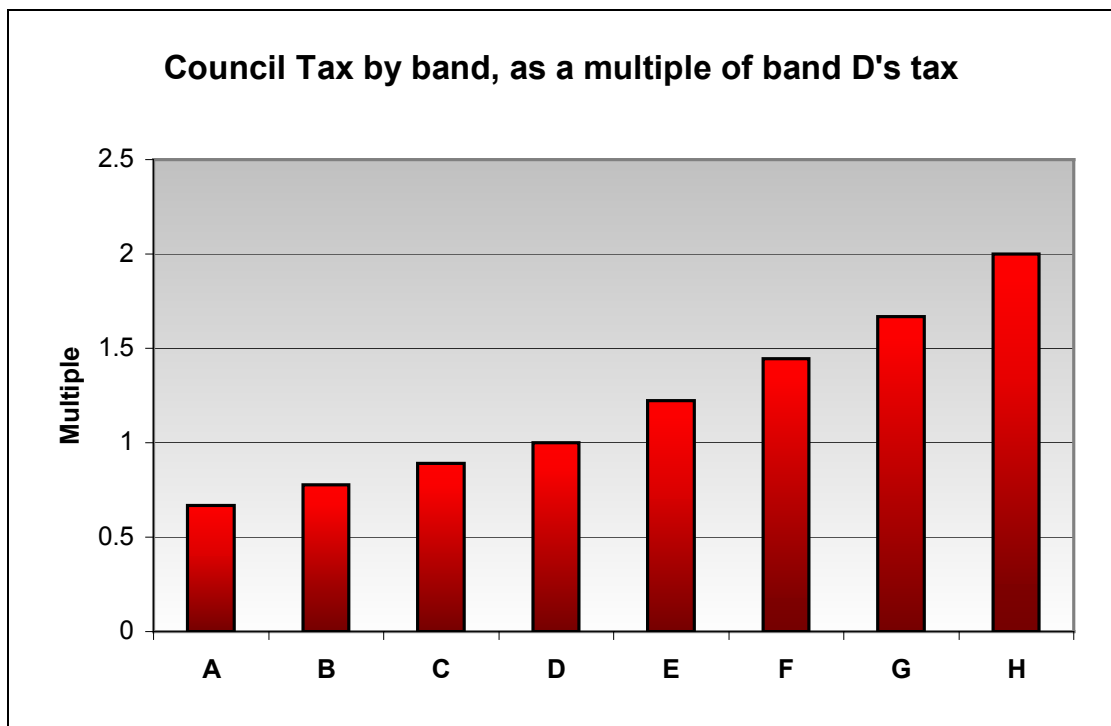
KEY ELEMENTS OF THE SYSTEM

The two key elements of the Council Tax system are the *bands* and the *multipliers*.

There are eight bands and each property is put into one of them according to an assessment of its value in 1991. The bands are:

Band	Properties value in 1991 for England
A	Below £40,000
B	From £40,000 to £52,000
C	From £52,000 to £68,000
D	From £68,000 to £88,000
E	From £88,000 to £120,000
F	From £120,000 to £160,000
G	From £160,000 to £320,000
H	Above £320,000

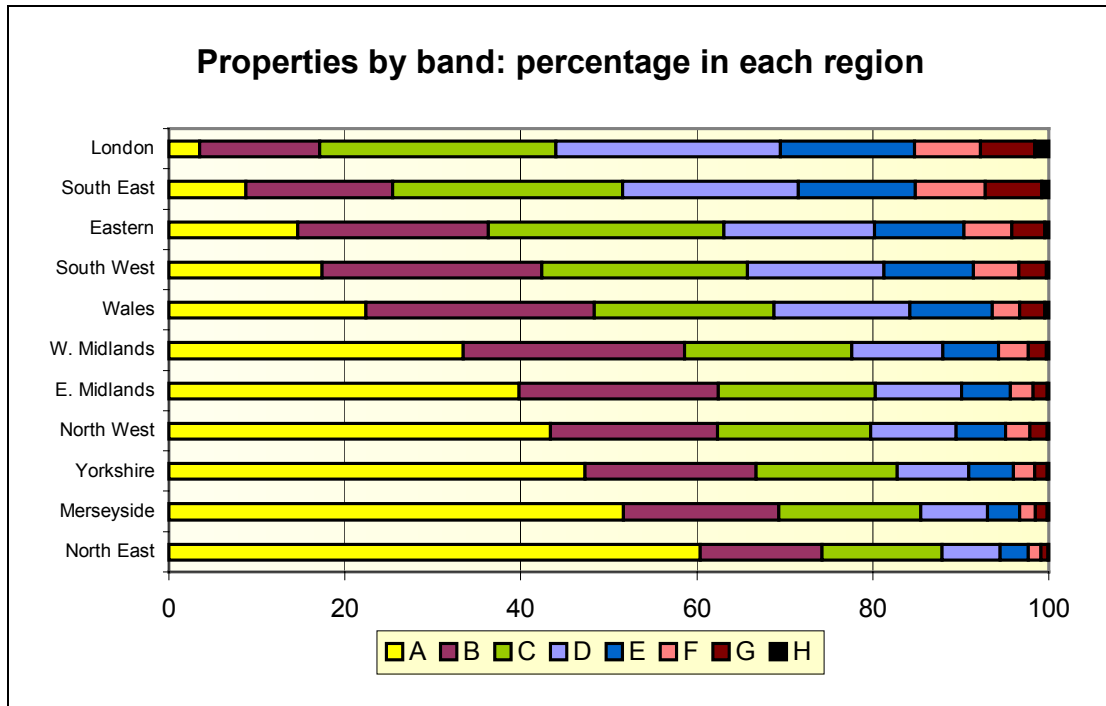
The *multipliers* express the Council Tax in any given band as a proportion or multiple of the tax paid in band D. These multipliers range from 2/3rds for band A to 2 for band H.



Although debate about the future of the Council Tax usually focuses on the question of the underlying valuation of properties, the more fundamental questions about it concern the banding and the multipliers.

REGIONAL VARIATION IN THE DISTRIBUTION BETWEEN BANDS

The distribution of properties across the bands varies hugely between the different regions.



Source: Local Government Financial Statistics 1998, table 5.1 (for the English regions); Family Resources Survey 1995/6 (for Wales).

The graph shows the percentage of properties in each band for each of the 10 English regions and Wales.

- In the four southern-most regions, the distribution is broadly symmetric, with most properties falling in bands C, D and E.
- By contrast, in the four northern-most regions, between two-thirds and three quarters of properties fall in bands A and B.

The differences in property prices between different regions means that the Council Tax takes on a very different character in the north, where most properties are concentrated in the lowest bands, from elsewhere. In the original design of the Council Tax, this could have been avoided by having more bands, especially covering the current band A, which is of particular importance in the north.

Alternatively, bands could have been set differently for different regions. In fact, this is exactly what was done for Wales and Scotland, where the property values defining the various bands are different from those for England.

THE FLEXIBILITY OF THE SYSTEM

This last point hints a very important characteristic of the Council Tax system, which is that there is really quite a lot of scope to make adjustments. Comparison with both the Community Charge and the Rates shows quite how flexible the Council Tax system is.

<i>Tax system</i>	<i>Degrees of freedom</i>	<i>Elements</i>	<i>Set when and by whom</i>
<i>Community Charge</i>	1	The charge per head in each local authority	By the local authority each year
<i>Domestic Rates</i>	2	The charge per pound of rateable value in each local authority The rateable value of each domestic property	By the local authority each year During a periodic revaluation exercise
<i>Council Tax</i>	5	The band D charge in each local authority The multipliers relating charges in different bands The number of bands and the values each covers The single person discount The band to in which each property is put	By the local authority each year (subject to government guidance) By parliament in the legislation By parliament in the legislation By parliament in the legislation During a periodic revaluation exercise

In addition, each system also includes arrangements for providing relief from the tax for low income households, currently provided by the means-tested Council Tax Benefit.

Particularly noteworthy is the comparison between the flexibility of the Council Tax system and the rigidity of the Community Charge system.

CONCLUSION

The practical conclusion here is that the Council Tax is in principle a very flexible system. If it wished to, government could use this flexibility to achieve particular outcomes. The Council Tax's potential in this regard is much greater than that of either the Community Charge or the Rates. Dissatisfaction with the way the Council Tax works at the moment, therefore, does not mean that we have to think about abolishing it and replacing it with something else. Instead, there appears to be considerable scope for reform.

2. ISSUES OF REVALUATION

In this chapter, we consider the case for a general revaluation of properties.

When the Council Tax system was set up, every dwelling or property was assigned a to one of the eight Council Tax bands, A through H. This valuation took place in 1991 and those valuations still stand.

Revaluation in principle need involve no reform of either the number of bands, the values that define them, or the multipliers.

Any system of property-based taxation requires a periodic revaluation of all properties. One of the problems with the Rating system which lasted until 1989 was that there was no general revaluation after 1973.

THE GOVERNMENT'S VIEW

The question of a new valuation of properties for the purposes of Council Tax was considered by the government when it came to power in 1997. Their view of the matter was set out in the 1998 White Paper, *Modern Local Government In Touch with the People*, which stated that:

- The Council Tax is working well, with no fundamental problems needing urgent attention.
- In a banded system, major changes in relative property prices are needed before significant numbers of households are badly treated.
- The current valuation base remains broadly acceptable and is likely to remain so for the next few years; there will be no revaluation during the current parliament.
- The fairness of the system will be kept under review, and a revaluation carried out if necessary during the next parliament.
- If necessary; the number and width of the property bands can be reviewed then too.

The most important thing about this argument is that treats *revaluation* as the central issue for the future of the Council Tax.

REGIONAL VARIATIONS IN HOUSE PRICE CHANGES

If all house prices rose by exactly the same percentage, and if the upper and lower limits that define the bands were adjusted accordingly, then a general revaluation would leave everybody's Council Tax bill unchanged. On the other hand, evidence of substantial relative movements in property prices since 1991 would contribute towards the case for a general revaluation.

Some information on differential prices is available at the regional level using data on the percentage change in prices between 1991 and 1998 for each of five different types of residential property: terraced, semi-detached, detached, flats and bungalows. For each region, the table shows the largest and smallest changes.

	<i>Smallest Change</i>		<i>Largest Change</i>	
South West	34%	Flats	59%	Semis
London	27%	Detached	51%	Terrace
South East	17%	Flats	28%	Terrace
Yorkshire	2%	Semis	21%	Flats
West Midlands	4	Bungalows	15%	Semis
East Anglia	3%	Flats	14%	Terrace
East Midlands	6%	Flats	12%	Terrace
North West	(2%)	Bungalows	12%	Flats
North	4%	Semis	11%	Flats

Source: Nationwide Building Society

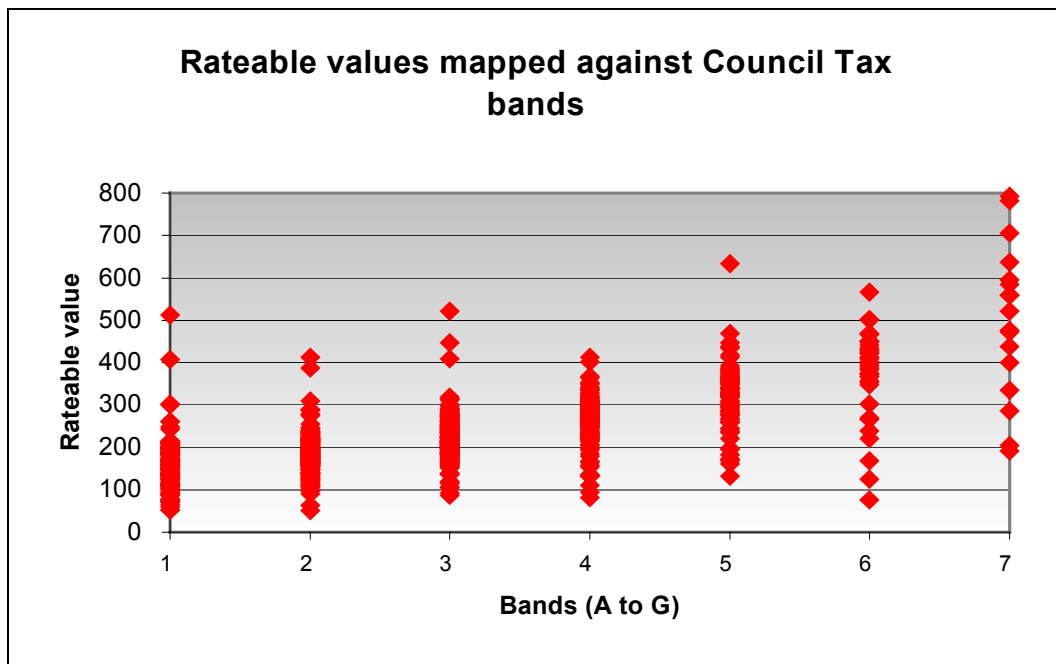
Two points can be seen:

- The disparity in ***overall average price rises***, with the south rising at two to three times as fast as other regions (inter-regional variation in house price changes).
- The disparity in the extent of the ***spread of prices rises*** within a region, in excess of 20% in London, the South West and Yorkshire (intra-regional variation in house price changes).

The first of these points does not in itself add to the case for a general revaluation, since the government could achieve the same effect on local authority finances that would arise from such a revaluation by adjusting local authorities' revenue support grants. The second point does, however, add to the case: properties whose values have risen by less than the average are now paying too much tax while those who have risen by more than the average are paying too little.¹

DISPARITY BETWEEN RATEABLE AND COUNCIL TAX VALUATION

Data from water companies, who still use the old rateable values as the basis for charging most of their customers for water, can be used to compare rateable values and council tax bands for a selection of properties. The following graph, for a sample of Severn-Trent plc's customers, shows that there is only a rather weak connection between the two.



Source: Severn-Trent data, supplied by Oxera Ltd.

The graph plots the rateable values of each of the properties in the Severn-Trent data-set against its Council Tax band (shown here as bands 1, i.e. A, to 7, i.e. G).² The lack of match between rateable values and Council Tax bands can be seen in the fact that properties with rateable values of both £200 and £400 can be found in every one of the seven Council Tax bands.³ Some possible explanations for the poor fit between the two, and the implications are:

- That rateable values were simply a mess. If this were the case; the poor fit shown here would not contribute towards a case for a Council Tax revaluation.
- That the 1991 Council Tax valuation exercise, done in something of a hurry, was crude and inaccurate. If this were the case, then the poor fit could be an argument for revaluation.
- That rateable values, while sound in 1973, had become a mess because of relative changes in property prices. If this were the case, then it would contribute to an argument for the regular revaluation of each property's Council Tax band.

Clearly, the disparity between rateable values and Council Tax valuations could be an argument for a revaluation. We have not, however, found any other evidence that would support such a conclusion. Moreover, it should be borne in mind that the while there are other interpretations available that would not point in the same direction.

CONCLUSION

We have found some evidence that could be interpreted to support revaluation, particularly the large relative house price movements in the south of England since 1991. A charitable interpretation of the discrepancies between Council Tax bands and rateable values is that, over time, there is a lot of relative movement in house prices. House prices have continued to grow in 1999, with reports of particularly rapid growth in some “hot spots”. Taken together, these suggest that the case for revaluation is bound to grow stronger over time.

Nevertheless, it is perhaps unsurprising that the government has not found the evidence sufficiently compelling to initiate a revaluation, especially in view of the £100 million that it would cost.

3. THE CASE FOR REFORM

In this chapter, we consider deeper reasons for reform of the Council Tax system.

AN ARGUMENT BASED ON VALUES AND OPPORTUNITIES

There are perhaps three types of reason why government might be motivated to act to reform the tax:

- **Popular pressure**, in response to popular opposition or protest.
- **Administrative propriety or convenience**, to remove/reduce anomalies, inaccuracies and inconsistencies or to allow the system to be used elsewhere (e.g. for water charging).
- **Political values**, to alter aspects of the system that conflict with certain basic principles or objectives.

There is clearly no popular pressure for action.

The government's argument against revaluation can be construed as denying that there is any administrative need for action, at least as far as the Council Tax itself is concerned.

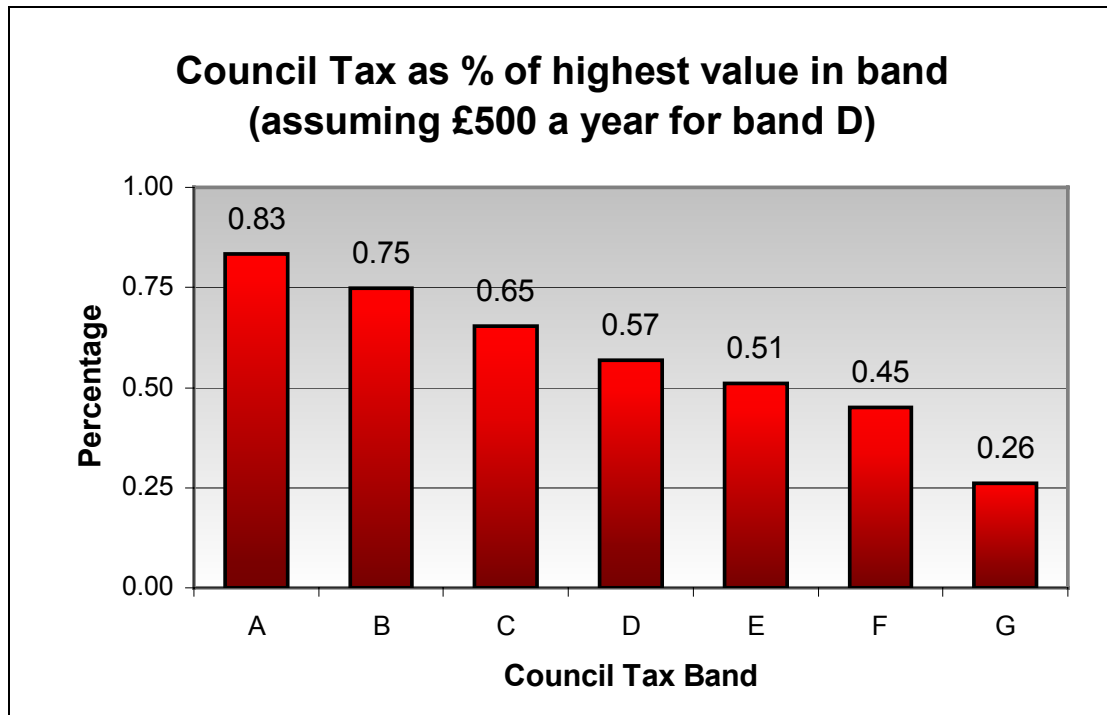
Thus, the case for reform is connected with values, particularly relating to the regressivity of the tax. This regressivity is in contrast to other major taxes: with income tax, the higher a person's income, the higher is the proportion of their income paid in tax and thus income tax is a progressive tax; with VAT, the amount of tax paid always represents a constant proportion of the cost of the item and VAT can therefore be thought of as a **neutral** tax, at least in relation to expenditure.⁴

Values that would stimulate reform include:

- **Reducing unfairness**. Although more progressive than the Poll Tax, the Council Tax is not that much more progressive, betraying the continuing influence of the principle that underlay the Poll Tax.
- **Helping the less wealthy**. Reform of the kind considered here would benefit those in cheaper properties at a cost to those in the most expensive, i.e. a modest redistribution on the basis of property wealth.
- **Helping those on low incomes**. While those whose tax is wholly met by Council Tax benefit would not gain directly, it would help many on low income above the benefit threshold. It would also help to reduce the 'benefits trap', i.e. it would enhance the extent to which 'work pays'.
- **Strengthening local autonomy**. Reducing the regressivity of Council Tax will make it fairer to shift the balance of local authority funding towards locally collected revenue away from central grants.

THE OVERALL REGRESSIVITY OF THE SYSTEM

A key measure of the character of the system is the changing relationship between the multipliers and property values across bands, expressed by the tax paid as a percentage of the property value. The more that these percentages fall as the underlying property value rises, the more regressive the tax is.



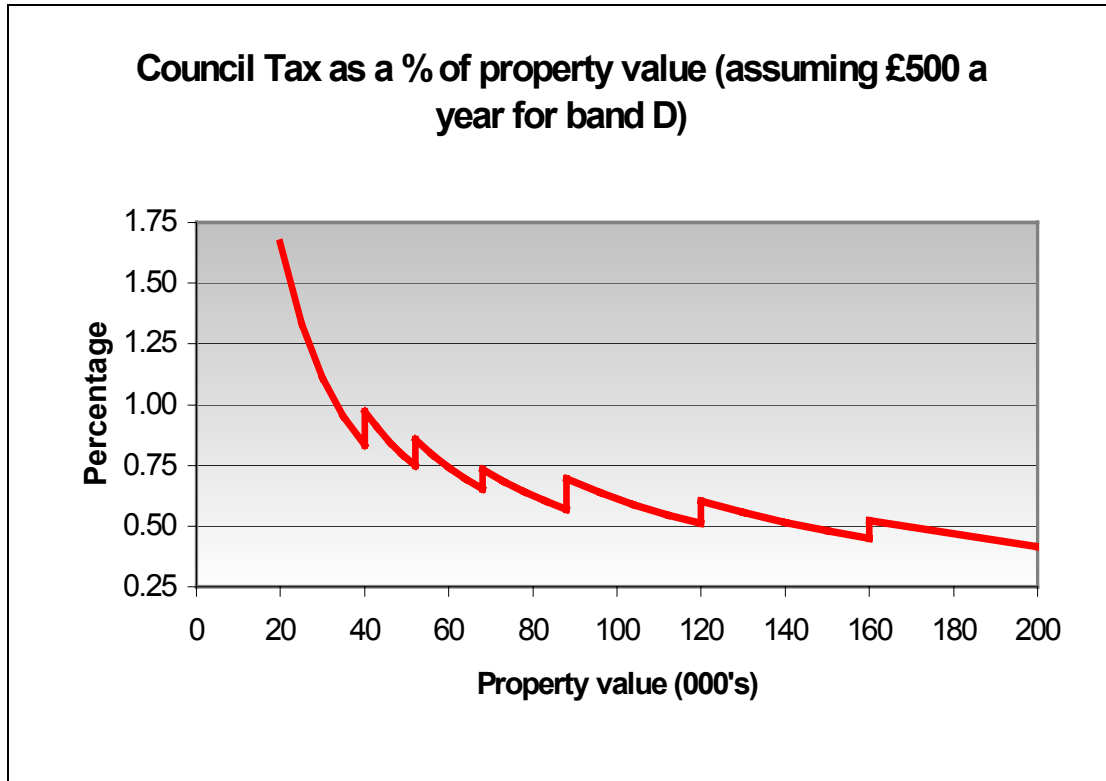
The graph shows the percentage of the property value paid in Council Tax by properties at the top of each of the first seven bands (and assuming that a band D property pays £500 a year).

- A property worth £40,000, at the top of band A pays an annual tax equivalent to 0.83% of its value while one worth £320,000, at the top of band G, pays 0.26%. Thus, the rate of Council Tax decreases as the property value increases.
- On average, from band to band, every 1% increase in the value of a property decreases the rate of Council Tax by about ½%.
- In comparison, this latter figure would be 1% for a flat rate tax (such as the Community Charge) and 0% for a neutral tax (such as the old rateable value system) where the tax rises proportionately with the underlying valuation.

Thus the Council Tax is sharply regressive relative to property values within any one tax collecting authority. While the actual *amount* of tax always rises from one Council Tax band to the next, the *share* that amount represents as a percentage of the underlying property values generally falls. There is a social justice case for adjusting the multipliers to remove (or at least reduce) this effect.

LOCALISED PROGRESSIVITY IN THE SYSTEM

The previous graph treated all properties in a band as if they had exactly the same value. Removing that assumption does not alter the overall picture, but it does introduce important new detail.



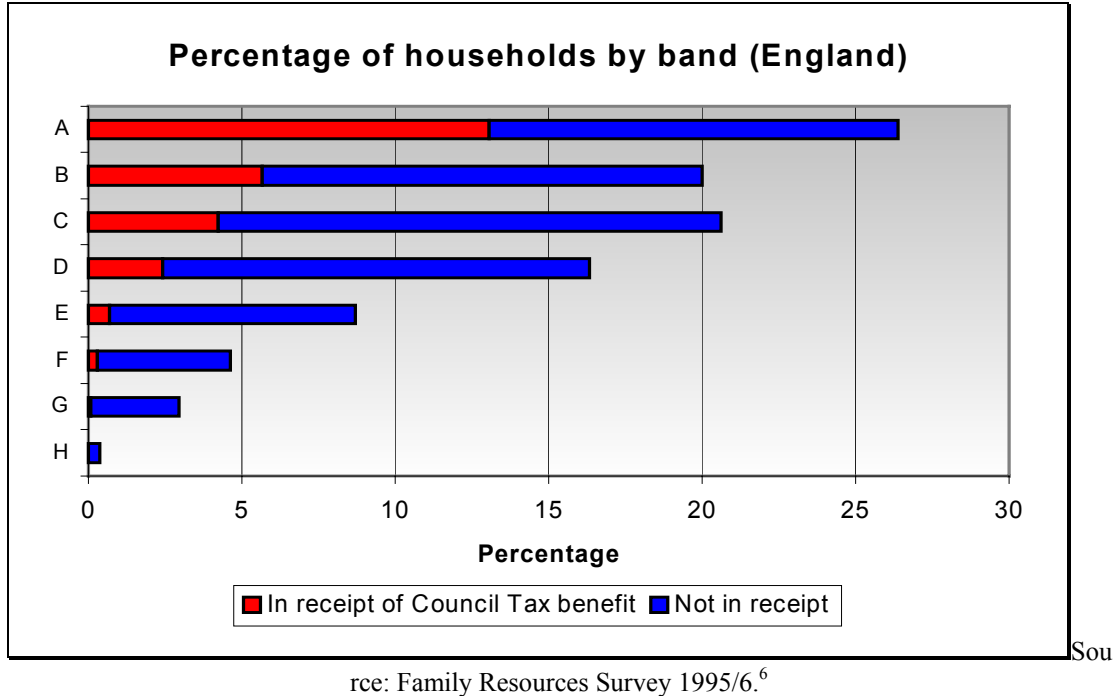
The graph plots the same ratio as plotted in the last graph, but here for a range of values in each band instead of just for the upper boundaries. The key points are:

- The overall regressive, trend is still present.
- There is a very strong degree of regressivity *within* bands, especially band A.
- The upward spikes as each higher band kicks in, shows a considerable degree of localised progressivity. within an overall regressive system. For example, a property in the middle of band B is paying much the same percentage Council Tax as a property at the top of band A.

As a rule of thumb, properties in the lower half of a band are paying a higher percentage Council Tax than properties at the very top of the band below. This *localised progressivity* has little to recommend it when set against the *overall regressivity*.

COUNCIL TAX BENEFIT

A key feature of the Council Tax system is that a significant proportion of the Council Tax bill is met by the means-tested Council Tax Benefit.⁵



The graph shows the distribution of properties by band, and whether they receive Council Tax benefit.

- Around a quarter of all households, and almost half in band A, are in receipt of Council Tax benefit.
- 87% of all households in receipt of Council Tax benefit are in bands A to C.

Council Tax benefit plays an important role in ameliorating the adverse effects of Council Tax among the poorest. The worst effects are felt among those towards the middle of the income distribution, especially those who are in work but who are not in any sense well paid. The incentive to work more is also lessened for those receiving the benefit, since some of any extra earnings will be “lost” in the form of reduced benefit.

CONCLUSION

The case for the reform of the Council Tax rests above all on its regressivity: those in smaller, cheaper properties pay proportionately more tax than those in larger ones. On these grounds, the Council Tax is better than the Community Charge, or Poll Tax, but the influence of the Poll Tax experiment is still very evident in the Council Tax’s regressivity.

However, the fact that a large proportion of bands A, B and C receive Council Tax benefit means there would be a smaller net revenue loss from reducing the multipliers for lower bands. This makes adjusting the multipliers in the lower bands' favour easier to accomplish, opening up the prospect that reform within tight fiscal limits might be feasible.

4. THE FEASIBILITY OF REFORM

In this chapter, we consider how might a re-design of the bands and multipliers underlying the Council Tax system might work. The examples put forward are only designed to illustrate the possibilities. In particular, they treat Britain as a whole. In practice, a complete assessment would need to take account of the shift in revenue between local authorities that would occur as a result of re-banding.

PRINCIPLES

Any re-design of the bands should have two objectives:

1. To ensure that there is a regular progression within the bands (with an associated regular progression to the associated multipliers too). The present set of bands displays this regularity, at least for bands B through F.
2. To ensure there are no undue concentrations of properties within just one or two bands. Without this, the tax effectively reverts to being a flat, or an almost flat tax.

A MINIMUM RE-BANDING SCHEME

A *minimum* re-design to meet these criteria would be to split A and G, giving a total of 10 bands (band H only includes 0.4% of all properties; splitting it is not considered further here).

- The case for splitting G is that the 2:1 ratio between its upper and lower limits (£320,000 and £160,000) is much larger than the ratios for any of the other bands B to F which are typically 1.3:1.
- Exactly this argument applies too for splitting A, assuming it contains £20,000 properties.
- The other argument for splitting A is that both nationally and in 6 of the 10 English regions, it contains by far the largest percentage of properties. Even when split in half (at £30,000), the new bands A1 and A2 would still each contain the highest percentage of properties in 5 of those 6 regions.

In view of the heavy concentration of properties in band A, it may be that 10 bands are too few if there is to continue to be a single set of bands for all the English regions.

Applying these principles leads to the following illustrative 10 band scheme, whereby the present band A is split into two at £30,000 and the present band G split into two at £225,000. As can be seen from the table, this results in a reasonable degree of uniformity between the different bands in terms of the ratio between the top of each band and the bottom.

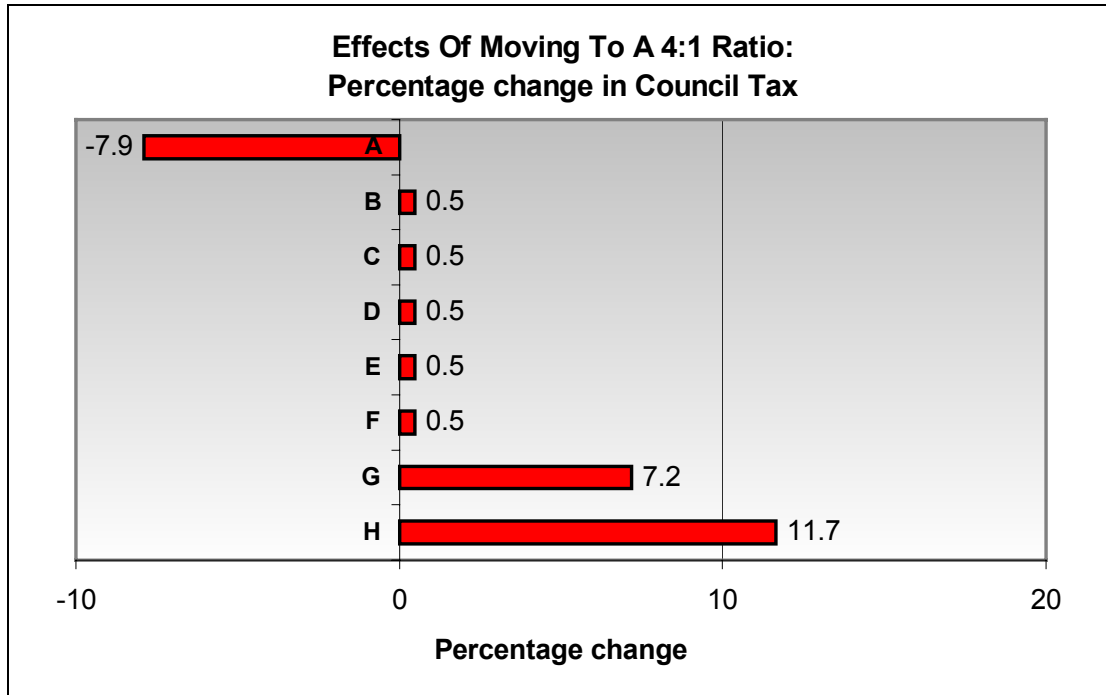
The table also shows three sets of multipliers:

- The present multipliers - the base case - with a ratio between the highest and lowest multiplier of 3:1.
- A set where this ratio is increased to 4:1. This is a minimal change since the only bands where the multipliers are different from the base case are A1, G2 and H.
- A set where this ratio is increased to 6:1. This is a more extensive change, since almost all multipliers are different from the base case values, with those in A1, A2, B and C being lower than in the base and those in F, G, G2, and H being higher than in the base.

Band	Lower Threshold	Upper Threshold	Ratio between upper and lower threshold	Current multipliers (overall 3:1 ratio)	New multipliers 1 (overall 4:1 ratio)	New multipliers 2 (overall 6:1 ratio)
A1		£30,000	-	6/9	5/9	4/9
A2	£30,000	£40,000	1.33	6/9	6/9	5/9
B	£40,000	£52,000	1.30	7/9	7/9	6/9
C	£52,000	£68,000	1.31	8/9	8/9	7½/9
D	£68,000	£88,000	1.29	1	1	1
E	£88,000	£120,000	1.36	11/9	11/9	11/9
F	£120,000	£160,000	1.33	13/9	13/9	14/9
G1	£160,000	£225,000	1.41	15/9	15/9	17/9
G2	£225,000	£320,000	1.42	15/9	17/9	20/9
H	£320,000	-	-	18/9	20/9	24/9

THE EFFECTS OF A 4:1 RATIO

Using a model calibrated with data from the Family Resources Survey, an illustration of the effects of shifting to set of multipliers yielding a 4:1 ratio overall (with individual multipliers as given in the previous table) is as follows:



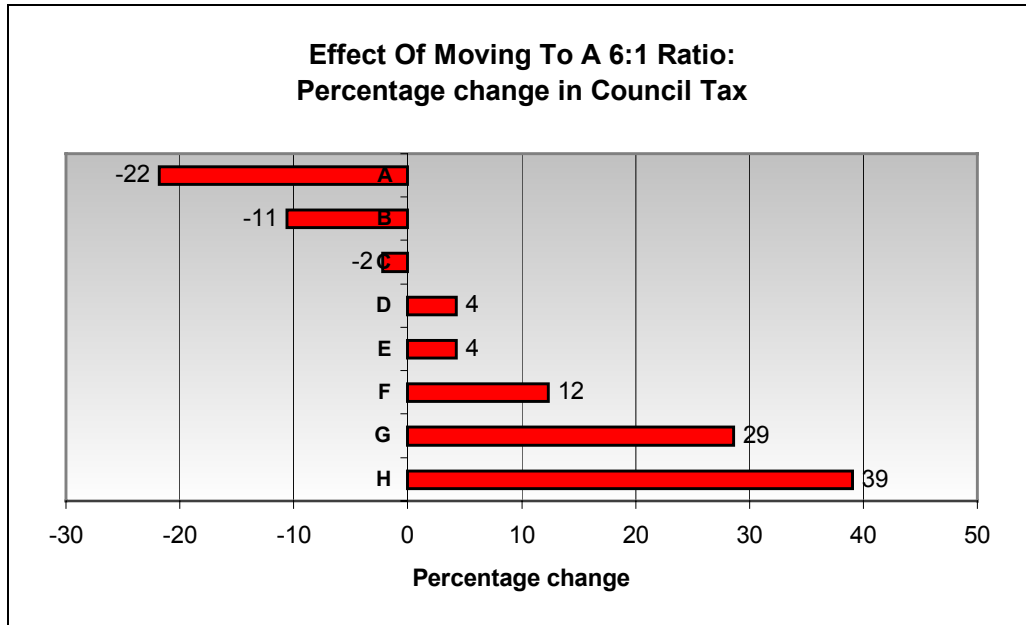
The graph⁷ shows the percentage change in each band's tax. The calculation assumes a uniform rate of tax across all authorities with bands A and G split equally into two bands each.

- Revenue neutrality requires an increase of 0.5% in the Council Tax for band D.
- The 13% of full tax payers in band A enjoy reductions of about 70 pence a week.
- The 3% in band G face an average weekly increase of about £1.60 and the 0.5% in band H face an increase of £3.10 a week.
- All others lose less than 10 pence a week.

In conclusion, a 4:1 ratio with maintained Council Tax revenue permits modest gains to band A while leaving the more than 50% of households in bands C, D, E and F virtually untouched.

THE EFFECTS OF A 6:1 RATIO

Using the same model, an illustration of the effects of shifting to set of multipliers yielding a 6:1 ratio overall (with individual multipliers as given in the table at 1.10) while maintaining Council Tax revenue is as follows:



The graph⁸ shows the percentage change in each band's tax. The calculation assumes a uniform rate of tax across all authorities with bands A and G split equally into two bands each.

- Revenue neutrality requires an increase of 4% in the Council Tax for band D.
- The 13% of full tax payers in band A enjoy reductions of about £1.90 a week, the 14% in band B enjoy reductions of 80 pence, and the 16% in band C enjoy reductions of 25 pence a week.
- The 4% in band F face an increase of £2.40 a week, the 3% in band G face an average weekly increase of £6.30 and the 0.5% in band H face an increase of £10.30 a week.
- The 22% in bands D and E lose between 60 and 70 pence a week.

A 6:1 ratio with maintained Council Tax revenue permits significant gains to bands A and B while leaving the almost 50% of households in C, D and E virtually untouched.

CONCLUSION

The Council Tax system offers government *opportunities* to undertake reform. First, the bands and multipliers can ultimately be set at will. Second, the fact that a sizeable proportion of those in lower bands receive Council Tax benefit means that the *net* cost of cutting their tax is much reduced. So there are both means to hand and desirable solutions which are likely to be feasible.

Just as the case for reform depends on values rather than administrative convenience, the nature of that reform should focus on re-banding and re-multiplying rather than revaluation:

- The real gains come firstly from changing the multipliers and secondly from re-designing the bands so as to avoid the concentration of properties in just one or two bands, as is seen in the north.
- In practice, any radical change to the multipliers cannot happen without redesigning the bands, while any redesign of the bands automatically opens up the question of what the multipliers should be.
- Any re-design of the bands probably then requires a revaluation in order to assign properties to the new structure.

Ultimately, re-banding is the key that unlocks the door to the reform - and indeed strengthening - of the Council Tax, since it both raises the question of the multipliers and requires a revaluation in order to be put into effect. In our view, the case for re-banding rests on the need to greatly improve the fairness of the Council Tax system.

It was once said, only half in jest, that when the Chancellor, Nigel Lawson, reduced the top rate of income tax in the 1988 budget from 60% to 40%, his ultimate aim was to get the 'top' rate of tax below the standard rate. That idea sounds extreme, until it is realised that that is exactly what happens with the Council Tax as it is now structured.

ENDNOTES

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- ¹ This remark is subject to a number of qualifications. The ‘lumpiness’ of the system, caused by the banding, means that a property with a value towards the bottom of a band could rise in value by typically up to 30% more than the rate of general inflation and still remain in the same band. The amount that the government distributes in revenue support grant, and the formula that it uses to determine how much to give each local authority, would still be a very big factor in determining whether individual bills rose or fell.
- ² The data-set contains no properties in the top band, band H.
- ³ A very similar pattern to that shown here for Severn-Trent can be seen in data on 10,000 households provided to us by Southern Water.
- ⁴ The fact that items like food are not liable for VAT qualifies this slightly.
- ⁵ As The Institute For Fiscal Studies observes, this makes the Council Tax unique among our taxes in that it is the only one that has its own means-tested benefit. In summary, their overall assessment of the effectiveness of the benefit is that in principle, it is well designed to help those most in need and that in practice, it does help many poorer households. On the other hand, partly as a result of its complexity, there is a significant problem of low take-up. See: Clarke, T., C. Giles and J. Hall, *Does Council Tax Benefit Work?*, Institute For Fiscal Studies, 1999.
- ⁶ These figures correspond closely with published figures from quarterly claimant count. (Department of Social Security, Social Security Statistics 1997, Table A4.06).
- ⁷ The gains and losses by band use the average band D Council Tax for 1997/98 of £688 (Local Government Financial Statistics, 1998 table 5.2) and apply the multipliers specified in the text. The calculation of the change to the band D rate itself necessary to ensure revenue neutrality derives from a model which takes as inputs:
- i) the distribution of dwellings by band in England in March 1998 (Local Government Financial Statistics 1998, table 5.1);
 - ii) the proportions within each band in receipt of Council Tax benefit (Family Resources Survey 1995/6);
 - iii) the proportion in which Council Tax benefit stands to Council Tax for those in receipt of benefit (Social Security Statistics, 1996/7).
- The application of the relevant multipliers to this model then yields a figure showing how much Council Tax revenue *net* of Council Tax benefit is altered by the application of these multipliers, and therefore how much the band D rate needs to rise.
- By way of a check on the model’s validity, it should be noted that for the year 1997/8, when gross Council Tax revenue reached £11.24 billion (Local Government Financial Statistics, table 9.5), the model implies a level of Council Tax benefit of £2.32 billion, compared with an actual figure of £2.50 billion (DSS Web site, ‘Key Statistics’). While this is an error of some 7%, it is only a second order effect (worth about 4 pence a week to band D in the ‘worst’ scenario considered here) and has thus been ignored.
- ⁸ See footnote above.