

“A Fairer Local Tax for Scotland”

Ministerial foreword

For too long the people of Scotland have faced the burden of high and unjust local taxes. Now is the time for a new approach.

The abolition of the unfair Council Tax and its replacement with a fairer local tax based on ability to pay forms a key part of our vision for a flourishing Scotland. The Government believes that the fairest solution is a local income tax; a commitment on which we were elected to office.

We are proud to form Scotland's first minority government, and as a minority government we must convince Parliament and wider society that our approach is the correct way forward. The first step in this process is a consultation that sets out our plans in detail and invites comments on them. This consultation also opens up discussion on alternative approaches. As a minority government we are happy to hear the ideas of others and have our own position tested in open public debate. I am eager to listen to all views and welcome the chance to engage constructively and build consensus on a way forward.

The move to our proposed local income tax will take time to implement, and in the interim period I have signed an historic agreement with COSLA, which represents Scottish local authorities, to freeze Council Tax levels throughout Scotland. The Council Tax freeze will work to shelter vulnerable individuals from further Council Tax increases as we work to address longer-term reform. It will also protect families and individuals from another increase in household costs at a time when fuel and food prices are rising. Our proposals are part of a number of important taxation reforms that we have undertaken to put before Parliament and the people of Scotland. Whilst moving towards fairer taxation for individuals, we will also be pursuing a fairer environment for businesses.

These proposals represent a substantial overall reduction in taxation in Scotland. It is vital that taxes are lower and fairer to create a more prosperous country. This Government's fresh approach to taxation in Scotland is a cornerstone of our plans to create wealth and enable people to share fairly in that wealth.

Our proposals for a local income tax will need the support of the Scottish Parliament, local authorities across Scotland and Government departments elsewhere in the United Kingdom. We cannot deliver this in isolation, and will need the input of our colleagues across the public sector to make these proposals a reality. I welcome comments on our proposals from all the bodies involved. I am especially keen to hear the views of members of the public who will be affected most by our proposals.

The Government wants taxation in Scotland to be fairer and based on ability to pay. I believe that a local income tax will support this aim and I look forward to the people of Scotland reaping the benefits that this change will provide.

John Swinney

Cabinet Secretary for Finance and Sustainable Growth

Contents

An Outline of Our Proposals

Section 1 – How much Local Income Tax will People Pay?

Section 2 – How will Local Income Tax be Collected and Administered?

Section 3 – What will be the Impact of a Local Income Tax on our Economy and People?

Section 4 – How will a Local Income Tax pay for Local Authority Services?

Section 5 – How will Empty and Second Homes be Taxed?

Section 6 – How will Domestic Water Charges be affected?

Section 7 – Are there other Taxation Systems that should be considered?

Section 8 – Information about the Consultation Process

Annex A – Calculating your Local Income Tax

Annex B – Income Tax Liability

Annex C – Useful Links

Annex D – Partial Regulatory Impact Assessment

Annex E – Local Taxation in Other Countries

Annex F – Household Impact of a Local Income Tax

Annex G – List of Consultees

Annex H – Response Forms

An Outline of our Proposals

The Scottish Government believes that the Scottish people have the right to change the way local authorities are funded from local taxation and also to change the nature of that local taxation. That is why the current Government stood for election with a clearly stated proposal to abolish the council tax and replace it with a fairer local tax based on ability to pay. This consultation is the first part of making that proposal a reality, and we are asking for your views. Our proposals for a new local taxation system to fund local authority expenditure include:

- A tax free personal allowance that matches the UK personal allowance levels
- A 3% rate applied to the income that is subject to basic and higher rates of UK income tax
- Collection that complements the existing national system of collection through Pay as You Earn (PAYE) and self assessment
- Exemptions for savings and investment income
- A tax for second homes, which will be subject to local requirements, and broadly comparable to the current council tax on second homes.

We will seek UK Government cooperation in administering a local income tax. We want to deliver these reforms as quickly as possible and within the term of the current Scottish Parliament. This will be a challenging task, but with the cooperation of the UK Government, we can achieve the implementation of the proposals outlined in this consultation document.

For 2007-08, we estimate that under our proposals households would on average be better off in all but the top income decile, although it is important to note that the impact on individual households will vary according to their particular circumstances. The table below shows weekly earning bands for each income decile.

Weekly Earning Bands for Income Deciles (2007-08)	
Bottom 10%	< £164
Decile 2	£165 - £206
Decile 3	£207 - £256
Decile 4	£257 - £309
Decile 5	£310 - £379
Decile 6	£380 - £455
Decile 7	£456 - £558
Decile 8	£559 - £680
Decile 9	£681 - £901
Top 10%	> £902

Annex F also provides a detailed analysis of how our estimates were derived and further evidence of the impact of the proposals.

Table 1 (below) shows the results across each income decile rounded to the nearest

10 pence and as a percentage of households' after tax income.

Table 1- Average weekly change in net income for each income decile

Income Decile	Bottom 10%	Decile 2	Decile 3	Decile 4	Decile 5	Decile 6	Decile 7	Decile 8	Decile 9	Top 10%
Average Weekly Change (£)	£6.70	£6.80	£8.10	£8.80	£10.30	£9.70	£6.90	£6.00	£0.90	-£15.10
Change as % of after tax income	5.7%	3.7%	3.5%	3.1%	3.0%	2.3%	1.4%	1.0%	0.1%	-1.2%

Table 2 shows the estimated average weekly change in net income according to seven family types.

Table 2 - Average weekly change in net income by family type

Family Type	Single non-pensioner	Married without children	Married with children	One-parent families	Single pensioners	Married pensioners	Households comprising "Multiple Taxpayers"
Average Weekly Change (£)	£3.30	£3.40	£3.10	£5.40	£7.30	£13.80	£2.50
Change as % of after tax income	1.1%	0.5%	0.5%	1.7%	3.3%	3.4%	0.4%

*Note: Households comprising "Multiple Taxpayers" (also known as Multiple Tax Units) involve a number of different household types, the main of which are – young adults living together, adult children living at home with parents and parent(s) living with their adult children.

Responding to our Consultation

There is no need to attempt to each question as it arises in the consultation paper itself. All the questions are listed in order in the final Annex to the consultation paper (Annex H) and you can therefore respond to them together by completing Annex H at the end. There is also an online response form at www.scotland.gov.uk/afairertax.

Section 1 – How Much Local Income Tax Will People Pay?

1. This section explains our main proposals for how local income tax will be calculated.
2. Local authorities receive funding through a range of sources. The bulk of their funding comes from the Scottish Government in the form of grant. They also collect council tax and Non-Domestic rates (business rates) locally and they receive certain other income from fees and charges. They also receive some funding from the UK Government (such as Council Tax Benefit). Our aim is to replace the council tax by an alternative local income tax.
3. We want a local income tax, that is efficient, easy to understand and that will cut the burden of taxation, benefiting most people in Scotland. The actual amount you may be required to pay will depend on your personal circumstances, though you can get an idea of the amount of tax you will pay by taking a look at Annex A, which explains how you can work out the amount of local income tax you are likely to pay.

Personal Allowance

4. Under the existing UK income tax system each taxpayer has a “personal allowance”, which is a tax-free amount of income. People who don’t earn more than their personal allowance don’t pay income tax. All income above the personal allowance threshold is subject to income tax.
5. The Scottish Government supports the existence of a personal allowance for a local income tax. Having a tax-free amount applied to the first part of income encourages people to work, and helps those on low incomes. It will also mean that many pensioners, students and others working part time or part of the year will not pay any local income tax at all.
6. We see clear administrative advantages to linking the Scottish local income tax personal allowance to the UK income tax personal allowance. This will make it easier to collect by the existing “Pay As You Earn” (PAYE) and self-assessment systems. Matching the Scottish local income tax to the UK tax structure in this way minimises the administrative burden on employers and government. This should make implementation as quick and easy as possible.
7. Alternatively, the Scottish local income tax personal allowance could be higher or lower than the UK income tax personal allowance. A higher personal allowance could encourage people to work because they would not pay local income tax on more hours. However, it would also mean that fewer people would be paying local income tax. The fewer people there are paying local income tax, the higher the rate would need to be in order to raise enough money to pay for essential public services.
8. A lower personal allowance would result in more people paying local income tax, and would mean that the rate could be slightly lower than 3%. However, a lower personal allowance could lead to financial difficulties for those on the lowest incomes because they would pay local income tax on more hours. On balance we think the Scottish

local income tax personal allowance should mirror the UK income tax personal allowance.

Question 1 - In your view, should the local income tax personal allowance be the same, higher or lower than the UK income tax personal allowance?

The Same

Higher

Lower

Don't Know

The Local Income Tax Rate and Bands

9. We propose that people pay 3% on all their income (except income from savings and investments) over the personal allowance. We think that a flat rate is the best way to raise funds efficiently and fairly without placing a large administrative burden on employers, and without compromising our goals of encouraging economic growth and entrepreneurship. A single rate across Scotland would provide certainty and consistency.

Other Kinds of Local Income Tax

10. A single rate would not be the only way to introduce a local income tax. It would be possible for local authorities to set their own rate for local income tax, and for this to apply to those who live in their area. This is the position of the Scottish Liberal Democrats and we would be interested to hear views on alternative approaches such as this.
11. Councils could be given the power to set any rate of local income tax they choose, or the power to vary the rate within a defined range. This level could be within a range – for example, 3% plus or minus ½%. A more limited power to vary the LIT rate, similar to the Liberal Democrat proposal, might be introduced. For example, a rate of 3p could be set and local authorities could be allowed to vary the tax rate BELOW this level, but not ABOVE it. This would allow for a degree of local variation while not breaking our commitment to a LIT rate no higher than 3p
12. A local income tax set by councils could have advantages. In particular, local authorities would have the power to determine the tax paid by their residents and vary the rate they charged to increase or decrease their own financial budget. When residents voted for their local councillors, they would do so knowing that their vote could directly influence how much local income tax they would pay.
13. In our view, however, the advantage outlined above is outweighed by the disadvantages. A locally variable rate would require extensive and expensive bureaucracy. This is because there would need to be a way of collecting up to 32 different variable tax rates from people living in Scotland, according to which local authority area they lived in. This could prove expensive and confusing for employers, councils and taxpayers.
14. There are also many different ways in which the tax could be structured. The tax could be capped for high earners, so that no one pays more than an agreed level. The rate could also be varied for those who are 'higher' rate taxpayers or it could be capped at a certain level, to be set by Scottish Ministers. We believe that the

advantages of a simple, easily administered tax outweigh the benefits of any variations.

Question 2 - Do you think a flat rate of 3% is too high, too low or about right?

Too high

Too low

About right

Don't Know

Question 3 - Would you be inclined to pay more Local Income Tax (i.e. above 3%) to provide for better quality local services?

Yes No Don't Know

Question 4 - Do you believe the level should be set locally or nationally?

Locally Nationally Don't Know

If you believe the level should be set locally, should Scottish Ministers be able to cap the rate?

Yes No Don't Know

Income subject to Local Income Tax

15. We propose that earned income of the type currently subject to UK income tax should be subject to local income tax. This is income from employment, pensions and other sources of income. An illustrative list is at Annex B. It excludes income from savings and dividends and other types of unearned income, such as gifts or loans.

Income from Savings and Investments

16. Some people receive income through interest on savings in banks and building societies and other investments (please see Annex B for information). Some may argue for a local income tax on this income, but we are not proposing that this should apply.

17. Our main concern is that the cost of collecting a local income tax on these types of income may be more expensive than the amount of money we will raise, as recently concluded by an independent committee when they examined available evidence. Additionally, we want to encourage people to save for their future and invest in business in Scotland to promote economic growth. A local income tax on these types of income may discourage saving and investment.

Exemptions and Discounts

18. Other than the personal allowances for a local income tax, we do not propose that there should be any exemptions or discounts. We believe that any person earning enough to become liable for a local income tax should make a contribution. A complicated system of exemptions and discounts could lead to appeals and disputes between taxpayers and Her Majesty's Revenue and Customs (HMRC), adding to the costs and bureaucracy of the new system. Reducing bills for some people in this way could mean that the overall local income tax rate would need to be higher than 3% in order to compensate.

Question 5 - Among the following, which should or should not be taxed as part of Local Income Tax?

- **Earned Income / Wages?**
Yes No Don't Know
- **Income from Pensions?**
Yes No Don't Know
- **Income from Savings?**
Yes No Don't Know
- **Income from Financial Investments?**
Yes No Don't Know
- **Income from Second Homes?**
Yes No Don't Know

Question 6 - In your view, do you think that there should be any special exemptions or discounts from a local income tax?

Yes No Don't Know

If yes, please state what for and share with us any thoughts on how you think these might be funded?

Residency Issues

19. People who have to pay local income tax will be "Scottish taxpayers". We intend to define a Scottish taxpayer using the definition already in the Scotland Act. Broadly, this is someone who lives in the UK for income tax purposes, and Scotland is the part of the UK with which they have the closest connection during the year. Someone has their closest connection with Scotland during a year if one or more of the following applies:

- a) The number of days they spend in Scotland equals the number spent elsewhere in the UK;
- b) They spend a part of the year in Scotland, and their main UK home is in Scotland and used as a residence;
- c) They are an MP for a Scottish constituency, an MSP or a member of the European Parliament for a Scottish constituency.

20. In practice this means that where a person's main home is in Scotland, but they spend more than half of the year living outside of Scotland, they may be liable for a local income tax. In addition, where the period of time spent in Scotland in the year is more than the period of time spent in the remainder of the UK, the person would be liable for local income tax.

21. Alternatively, local income tax could be linked to the proportion of the year a person lives in Scotland. In our view, that approach appears to build significant and unnecessary bureaucracy into the system.

Question 7 - Do you agree that a Scottish taxpayer should be defined using the definition already contained in the Scotland Act, described at paragraph 19 above?

Yes No Don't Know

If you disagree, how would you propose residency be defined?

Transitional Arrangements for Individuals

22. Most households will pay less under our local income tax proposals than they currently pay under council tax, but a minority will pay more. One way of making this change easier for those who will pay more would be to phase in their higher payments so that they would have more time to adjust. This type of phased approach is known as "transitional arrangements" and has been used elsewhere, such as in the Non-Domestic rates system. Phasing in the increases costs money because those making reduced payments will be paying less tax. This can either be paid for by national government, or by phasing in the changes for people who will pay less over the same time period.

23. We do not intend to introduce transitional arrangements. This is because we think the current council tax system is fundamentally unfair, and transitional arrangements will just continue this unfairness. We believe that transitional arrangements will result in richer people paying a reduced share of the total taxation bill at the expense of poorer taxpayers. We do not think that either government or other taxpayers should subsidise those who should rightly be paying more.

Question 8 - In your view should transitional arrangements for individuals apply?

Yes No Don't Know

If yes, please give your reasons and provide any comments on how you think transitional arrangements should be funded.

Section 2 – How will Local Income Tax be Collected and Administered?

24. This section explains how we propose to administer a local income tax.
25. Unlike general UK income tax, the local income tax will only be used to pay for local authority services. We think a local income tax should fit into the current arrangements for administering UK income tax and be collected by Her Majesty's Revenue and Customs (HMRC). This is the most efficient way of delivering a local income tax because HMRC already hold relevant data and has the experience and systems that we need to collect a local income tax. We will seek UK Government cooperation to deliver this method of collecting a local income tax. We believe it is reasonable for the Scottish Government to pay HMRC to administer a local income tax.
26. In 2006-07 (the latest year for which figures are available), gross expenditure by local authorities in Scotland on administering the council tax collection system was £62 million (offset by £21 million in fees, charges and other income). Gross expenditure on administering Council Tax Benefit for the Department of Work and Pensions (DWP) in the same year was £36 million (of which the bulk was provided directly by the DWP). In addition, gross expenditure on council tax valuation was £12 million. The collection and administration costs to HMRC for administering local income tax under our proposals would be considerably less than this.
27. A significant minority of people already pay income tax through self-assessment. These people would add a local income tax to their payment. We could extend this system to require all others who are liable to submit an annual local income tax payment that they calculate themselves.
28. There are a number of other ways that a local income tax could be collected. These include:
- *A Scottish Government collection agency*
We could establish a new Executive Agency in Scotland with responsibility for collecting a local income tax. This Agency could be given similar powers and duties to the income tax related powers of HMRC. This would be a large financial and administrative commitment and the new Agency would be required to work with employers in the same way as HMRC does for UK income tax. We believe that this extra tier of bureaucracy and administration would represent duplication of effort by the public sector and would not be welcomed by businesses or individuals in Scotland.
 - *A private sector collection agency*
A private company could be employed through open tender to administer a local income tax. We do not think this would be appropriate, as it would entail handling highly sensitive data relating to individuals' incomes. It is not clear that sufficient expertise would exist in the private sector to adopt this approach, and the same issue of duplication of roles would also arise.
 - *Councils*
Councils are familiar with collecting business rates and council tax and we could utilise this existing expertise. However, we believe that this will duplicate public sector effort and be potentially even more inefficient than a new single collection agency, due to a replication of effort across our local authorities.

Question 9 - Which of the following do you think should collect a Local Income Tax?

- Her Majesty's Revenue and Customs (HMRC)?
- A Scottish Government collection agency?
- A private sector collection agency?
- Local authorities?
- Don't Know

Question 10 - Do you think local income tax should be collected at source or through payment?

- Collected at source
- Collected through payment
- A combination of collection at source and by payment
- Don't know

29. A different income tax in Scotland than to the rest of the UK is an issue for employers who provide data and taxes to HMRC. Employers will have to apply different rates for their employees who live in Scotland. We are committed to reducing the bureaucracy which businesses face. We can minimise the impact of these changes by providing clear guidance to employers and helping businesses to plan for the introduction of a local income tax. We will work with the UK Government to ensure that processes are thoroughly tested before implementation.

Question 11 – If the Government were to offer support to employers to implement these proposals, which would be the most appropriate medium of support in your view? Please tick all boxes that apply

- Information booklet for employers
- Designated advice hotline
- Designated advice e-mail
- Website with a section of “Frequently Asked Questions (FAQs)”
- Workplace visits

- **Roadshows for employers**
- **Media advertising**
- **None**
- **Other (please specify)**
- **Don't know**

30. The amount raised through local income tax will not be identical to that raised through the council tax. There would need to be an adjustment to local authority funding after the change to take account of the difference and ensure that public services are properly funded. This Government has pledged to work with local authorities to provide a stable funding environment to ensure that the people of Scotland can get the vital front-line services they need.

31. Many council staff are involved in administering the council tax and Council Tax Benefit. Scottish Assessors are responsible for the banding of properties. The Government, local authorities and the Assessors will need to work together as we move from one system to another, minimising disruption to staff and to the payments process to prevent a shortfall in income to the public sector.

Section 3 – What will be the Impact of a Local Income Tax on our Economy and People?

32. This section discusses some of the potential wider impacts of our proposals to abolish the council tax and introduce a local income tax.

Economic impacts

33. Over the three decades since 1975, Scotland's economic growth averaged 1.8% while the UK average was 2.3%. Between 1997 and 2006, Scotland's growth trailed the UK average in 9 out of 10 years. A reduction in taxes through the abolition of the council tax has the potential to provide a stimulus to the Scottish economy and contribute positively towards the Scottish Government's aim to make Scotland a 'Wealthier and Fairer' place.

34. Our modelling of the impact of our proposals indicates that most people in Scotland will be better off under our proposals. We estimate that 4 out of 5 households will be better or no worse off. In terms of income deciles¹, we estimate that on average, people in all income deciles will be better off, apart from those in the very top income decile. We also expect that on average, all the family types we have modelled will be better off. This means that we expect most single pensioners, pensioner couples, couples, couples with children, single people and one parent families will all be better off. (See Annex F for more detailed information on this topic.)

35. Some have suggested that a local income tax will lead to richer people leaving Scotland to live elsewhere in the UK, leading to lower tax revenues for Scotland than we have forecast and other negative economic impacts. However, the proposed local income tax will only increase the tax burden for a minority of people and a 3% local income tax will not have a significant impact on many of these people. People decide where to live for a variety of reasons, and we believe that the fairer and wealthier Scotland we are building will create an environment where our citizens will want to stay.

Question 12 - In your opinion, will the introduction of a local income tax have positive economic impacts for Scotland?

Yes No Don't Know

Question 13 - To what extent would the tax rate influence your decision to live in Scotland?

A Lot A Little Not at all

¹

	Weekly Earning Bands for Income Deciles (2007-08)									
Decile	Bottom 10%	Decile 2	Decile 3	Decile 4	Decile 5	Decile 6	Decile 7	Decile 8	Decile 9	Top 10%
Net income	< £164	£165 - £206	£207 - £256	£257 - £309	£310 - £379	£380 - £455	£456 - £558	£559 - £680	£681 - £901	> £902

Work choices

36. Changes to taxation can result in people making different choices about their work, such as changing the number of hours they work each week. These choices have an impact on peoples' quality of life, as well as the overall size of the workforce, and the total tax revenue collected. In particular high rates of income tax may result in people working less. Our assessment is that the local income tax is unlikely to cause people in Scotland to change their current working patterns. We know that most people will be financially better off under our proposals for this new low rate of tax.

Question 14 - To what extent do you agree with the following statements about the impact that a local income tax might have on your working patterns? (select on a scale of 1- 5 where 1 is strongly agree and 5 is strongly disagree)

I am likely to work more hours

1 2 3 4 5 Don't Know

I am likely to work fewer hours

1 2 3 4 5 Don't Know

I am likely to work in a different location

1 2 3 4 5 Don't Know

I am likely to change jobs to a different sector

1 2 3 4 5 Don't Know

It will have no impact on my work patterns

1 2 3 4 5 Don't Know

Other work impacts (please specify)

(Note: 1 is strongly agree and 5 is strongly disagree)

Impact on Democracy and Accountability

37. The abolition of the locally set council tax and its replacement with a nationally set local income tax may be seen by some as reducing local democracy and accountability. We do not agree that this is the case. Politicians are accountable to their electorate through the proper democratic process, based on the decisions they make. Locally elected officials will continue to decide how funding for their area is spent and make locally devolved decisions affecting the welfare of their constituents. Clearly alternative proposals such as a locally variable rate of local income tax will have an effect on this issue.

Question 15 - On a scale of 1 - 5, where 1 is strongly agree and 5 is strongly disagree, how important is it that your local authority has the power to set a tax?

1 2 3 4 5 Don't Know

Question 16 - Please provide any comments you may have about local income tax and accountability and democracy.

Equality Considerations

38. Equality is about creating a fairer society where everyone can participate and has the opportunity to fulfil their potential. No one should be denied opportunities because of irrelevant differences. The Scottish Government wants to make sure that we do not make tax changes that will unfairly impact on people simply because of their race or ethnicity, their disability, their gender or sexual orientation, their age or religion.
39. The Scottish Government, along with all public bodies, is subject to a number of legal duties relating to equality, and we will of course make sure that we comply with these.
40. We will undertake a full equality impact assessment of our proposals and report our findings to the Scottish Parliament as part of the legislation to bring about these changes. Assessing the likely impact of our proposals will involve collecting and analysing data, considering adaptations to the policy because of any negative impacts, and putting in place monitoring arrangements.

Question 17 - If you have any specific comment about the impact of our proposals on equality issues, please tell us what these are.

Section 4 - How will a Local Income Tax Pay for Local Authority Services?

41. Unlike general UK income tax, the local income tax will only be used to pay for local authority services. This section considers issues relating to the financial implications of abolishing the council tax and introducing the local income tax.

Sharing Local Income Tax revenue across councils

42. As indicated earlier, our preference is for HMRC to collect the new local income tax. There are different ways in which HMRC might provide the money so collected for local authorities. One way would be for local income tax revenue for the whole of Scotland to be distributed to councils according to their relative need, as part of the existing arrangements for funding local government. Or it could be distributed according to the population in each area. A third way would be to distribute it according to how much local income tax is paid by those who live in their areas.

Funding of council services when we are moving from council tax to Local Income Tax

43. Council tax is paid over the year, giving local authorities a steady stream of money. However under the income tax system, self-employed people do not always pay throughout the year, and instead often pay a lump sum after the tax year has ended.

44. We will discuss with the UK Government ways to make sure that councils get their local income tax money as quickly as possible. We will also take steps to adjust grant payments to local authorities, as appropriate, so that they receive a steady flow of income over the year.

Question 18 - Do you feel that the money raised from a Local Income Tax should be distributed to councils according to:

- **Need?**
- **Population in each area?**
- **The amount of local income tax raised in each area?**
- **Don't know**
- **Other (please specify)**

Council Tax Benefit

45. Council Tax Benefit provides help with paying council tax for people on low incomes. Council Tax Benefit, as with all benefits, is controlled by the UK Government. It is administered by councils, but paid for by the Department for Work and Pensions (DWP), which gives the money straight to councils.

46. The latest figures (May 2007) from DWP indicate that 533,300 households in Scotland were receiving Council Tax Benefit (either full or partial). Under existing

arrangements, over £1.1 billion will be due to be paid in the next three years by DWP to Scottish Councils. We will negotiate with the UK Government as to the future of this Council Tax Benefit money on three grounds.

47. The first is that, according to the current Statement of Funding Policy for the devolved administrations (published by HM Treasury in October 2007), Council Tax Benefit is listed as a component of the Scottish Block, post devolution.
48. The second is as regards a mechanism to reimburse the Scottish Government with an amount equal to the saving in reduced Council Tax Benefit which is described in the Statement of Funding Policy. The UK Government has not operated this mechanism fully for some years and funding was suspended after settlement of the 2003-04 claims. As a result, a significant level of funding, worth several hundred million pounds in total, that would have been due to the Scottish Government from the UK Government has never been paid. The Scottish Government will seek to reverse this decision by the UK Government.
49. The third is as regards a matter of principle. We believe that Scotland should continue to receive from the UK Government the level of funding currently paid as Council Tax Benefit once the council tax is abolished. The Scottish Government is clear that moving from a council tax to a Local Income Tax will not place any greater burden on the UK Exchequer and that, as a result, the UK Government should continue to make available an equivalent sum to Scotland after the abolition of council tax. Council Tax Benefit is paid to Scottish councils to provide financial support for the delivery of local services. The introduction of a local income tax does not change that requirement and that is why Scottish councils should continue to receive this flow of revenue under a new system.

Question 19 - To what extent do you agree that Scotland should receive equivalent monies to Council Tax Benefit, after the abolition of council tax? (where 1 is strongly agree and 5 is strongly disagree)

1 2 3 4 5 Don't Know

Section 5 - How will Empty and Second Homes be Taxed?

50. Some people own more than one home. When it is not anyone's main home, then it is considered to be a "second home". In some areas, the ownership of second homes can be beneficial for the local community, but in other places the amount of second homes can make it harder for local families to find affordable housing. Under the existing council tax regime, owners of second homes and long term empty properties pay up to 90% of the full council tax bill on that property.
51. The Government believes that a continuing tax specifically targeted on second homes and long term empty properties is fair – it is reasonable that those who are fortunate enough to have two or more homes pay an extra contribution towards taxation. Such a tax could also encourage owners of these homes to make them available for occupation so as to avoid paying the tax.
52. There are three main aspects to creating a fair second homes and long term empty properties tax:
- Identifying the properties
 - Setting a fair amount of tax
 - Collecting the tax

Identifying Second Homes and long term empty properties

53. Identifying these properties under the current council tax system is relatively straightforward. Every home in Scotland gets a council tax bill and to qualify for the second home discount the owner needs to demonstrate that their main home is somewhere else. When council tax is abolished, homes will no longer receive a council tax bill and there will be no incentive for people to tell us that a building is their second home or is a long term empty property. If we were to continue with a tax on these properties, we would need to find a new way of identifying them.
54. We already hold a detailed record of current second home and long term empty property ownership through the council tax system, and under a new tax, we would need to keep this up to date in the future. We understand that HMRC will need to undertake national exercises to verify Scottish residency and ensure accurate tax records. The land registry also maintains information about domestic property and ownership. There are therefore clear opportunities for us to work across government in identifying second homes by using data that already exist or will be required in the future to administer local income tax.

Setting a Fair Amount of Tax for Second Homes and Long Term Empty Properties

55. It is our general intention to raise about the same amount of money from taxing such properties as is currently raised under the council tax system. However, since Scottish Assessors may no longer be maintaining a council tax valuation list, it may not make good practical and financial sense for them to value second homes as the basis for taxation. There is a range of options to base a second homes tax on but because second homes affect various areas differently, a one-size fits all approach across the whole of Scotland may not be appropriate. We are interested in creating a

tax that would allow local authorities to play a role in determining how much tax owners of these properties in their areas pay, based on their superior knowledge of local circumstances. Local authorities for whom such properties have reduced the supply of affordable housing may wish to set a higher level of tax, which could be used to invest in local housing. Local authorities that wish to encourage second home ownership in their boundaries may wish to set a lower level of tax.

Collecting the Tax

56. We believe that the collection of tax on second homes and long term empty properties should be made through the existing system used for the collection of Non-Domestic rates. Under this system local authorities already send bills and collect tax due for many properties throughout Scotland, and have an outstanding record of doing so timeously and efficiently. Since local authorities already administer the second homes council tax payment and will have a continuing role with Non-Domestic rates it makes sense that they also collect a second homes tax.

Question 20 - To what extent do you agree that local authorities should play a part in setting a second homes tax? (where 1 is strongly agree and 5 is strongly disagree)

1 2 3 4 5 Don't Know

Question 21 - To what extent do you feel second homes tax should be collected by:

- Her Majesty's Revenue and Customs (HMRC)?

1 2 3 4 5 Don't Know

- A Scottish local collection agency?

1 2 3 4 5 Don't Know

- A private collection agency?

1 2 3 4 5 Don't Know

- Local authorities?

1 2 3 4 5 Don't Know

Section 6 - How will Domestic Water Charges be affected?

57. Currently, domestic water charges are billed and collected together with council tax by local authorities. While water charges are based on council tax bands, they do not vary by local authority area.
58. Abolishing the council tax requires a review of these arrangements. Consideration needs to be given as to whether local authorities would continue to be best placed to undertake the billing and collection of domestic water charges on behalf of Scottish Water, or whether Scottish Water might be in a better position to undertake this task, perhaps by utilising the expertise of other utility players such as the power companies.
59. There is an independent regulatory framework in Scotland for setting water charges. The Scottish Government is required to consult on the overall principles that apply to water charging over any given regulatory period. The current consultation, on the principles that should apply between 2010 and 2014, closed on 29 February 2008. There will be a further consultation on our proposals for the future billing and collection of domestic water charges. Please contact ian.alexander@scotland.gsi.gov.uk if you would like to receive this consultation.

Section 7 - Are there other Taxation Systems that should be considered?

Land Value Tax

60. The Government's proposal is for a local income tax to replace the council tax. Other proposals have been made and, in the interests of open discussion, some of these are set out here. One prominent alternative system of local taxation is a land value tax. In its simplest form, land value tax is a tax based on the value of *land* owned. This contrasts with our current methods of local taxation based largely on *properties*. For this reason, land value tax is usually proposed as an alternative to both domestic property taxation and Non-Domestic rates.

61. Land value tax can take many forms, such as being introduced in certain geographical (usually urban) areas only or being combined with, for example, a land improvement tax. Land value tax could have a range of economic impacts on the property and land markets. It would be likely to re-distribute the taxation burden, narrow the tax base and simplify the valuation process. More information on land value tax is available at: www.scotland.gov.uk/afairertax

Environmental Taxes

62. The Scottish Government is firmly committed to a greener Scotland and taking steps to secure a sustainable future. There have been a number of recent proposals to encourage sustainable behaviour through taxation measures, including a plastic bag levy and council tax discounts for energy efficiency changes to homes. We would welcome views as to whether there are taxation options we should consider to promote a greener Scotland.

63. The Scottish Government is committed to high levels of recycling. Many other countries with high levels of recycling have systems in place to charge householders for the amount of residual waste (i.e. waste that is not recycled) which they throw out. The charges for this residual waste vary, depending on the amount of waste involved.

Question 22 - Which do you feel is the fairest approach to taxation? (select 1 only)

- Council Tax
- Land Value Tax
- Local Income Tax
- Environmental Tax
- None of the above
- Don't know

Question 23 - Which approach do you feel will provide a more wealthy Scotland? (select 1 only)

- Council Tax

- Land Value Tax
- Local Income Tax
- Environmental Tax
- None of the above
- Don't know

Question 24 - If a Local Income Tax is introduced, what would be the most significant factor (good or bad) for you? (select 1 only)

- That the Council Tax will be abolished
- I / my household shall be better off
- I / my household shall be worse off
- That a Local Income Tax system would be fairer than the Council Tax
- That it will help to make Scotland a wealthier and fairer place to live and work
- Don't know
- Other (Let us know what the significant factor is)

Section 8 - Information about the Consultation Process

Consultation is an essential and important aspect of Scottish Government working methods. Given the wide-ranging areas of work of the Scottish Government, there are many varied types of consultation. However, in general Scottish Government consultation exercises aim to provide opportunities for all those who wish to express their opinions on a proposed area of work to do so in ways which will inform and enhance that work.

While details of particular circumstances described in a response to a consultation exercise may eventually inform the policy process, consultation exercises can not address individual concerns and comments, which should be directed to the relevant Scottish Government department or public body.

Typically Scottish Government consultations involve a written paper inviting answers to specific questions or more general views about the material presented. Written papers are distributed to organisations and individuals with an interest in the area of consultation, and they are also posted under the current consultations section of the website, enabling a wider audience to access the paper and submit their responses.

Copies of all the responses received to consultation exercises (except those where the individual or organisation requested confidentiality) are placed in the Scottish Government library at Saughton House, Edinburgh.

The views and suggestions detailed in consultation responses are analysed and used as part of the decision-making process.

Within the Consultation section of the Scottish Government website there is a full list of all closed consultations and a listing of forthcoming consultations. The "closed" section will, in the future, provide details about the outcome of consultations and have links to any reports produced from the consultation exercise.

If you have any queries about the consultation process within the Scottish Government please contact Tania Smith in the Constitutional Policy and Civic Participation Team:
Area G-A North, Victoria Quay, Edinburgh, EH6 6QQ

Consultation on “A Fairer Local Tax for Scotland”

Responding to this consultation paper

We are inviting written responses to this consultation paper by **Friday 18th July 2008**. Please submit your response on-line or send it to afairertax@scotland.gsi.gov.uk or post it to: A Fairer Local Tax (CRE 959), CSU, Spur U5b, Saughton House, Broomhouse Drive, Edinburgh EH11 3XD.

If you have any queries about this consultation paper, contact Eva Bru-Dominguez on 0131 244 7011 (or at the email above or by post to 3-J North, Local Government Division, Scottish Government, Victoria Quay, Edinburgh, EH6 6QQ).

We would be grateful if you would either use the consultation questionnaire provided or clearly indicate in your response which questions or parts of the consultation paper you are responding to, as this will aid our analysis of the responses received.

This consultation, and all other Scottish Government consultation exercises, can be viewed online on the consultation web pages of the Scottish Government website at <http://www.scotland.gov.uk/consultations>. You can telephone Freephone 0800 77 1234 to find out where your nearest public internet access point is. The Scottish Government now has an email alert system for consultations (SEconsult: <http://www.scotland.gov.uk/consultations/seconsult.aspx>). This system allows stakeholder individuals and organisations to register and receive a weekly email containing details of all new consultations (including web links). SEconsult complements, but in no way replaces distribution lists, and is designed to allow stakeholders to keep up to date with all consultation activity, and therefore be alerted at the earliest opportunity to those of most interest. We would encourage you to register.

Handling your response

We need to know how you wish your response to be handled and, in particular, whether you are happy for your response to be made public. Please complete and return the Respondent Information Form enclosed with this consultation paper as this will ensure that we treat your response appropriately. If you ask for your response not to be published we will regard it as confidential, and we will treat it accordingly.

All respondents should be aware that the Scottish Government is subject to the provisions of the Freedom of Information (Scotland) Act 2002 and would therefore have to consider any request made to it under the Act for information relating to responses made to this consultation exercise.

Next steps in the process

Where respondents have given permission for their response to be made public (see the attached Respondent Information Form), these will be made available to the public in the Scottish Government Library by October 2008 and on the Scottish Government consultation web pages by October 2008. We will check all responses where agreement to publish has been given for any potentially defamatory material before logging them in the library or placing them on the website. You can make arrangements to view responses by contacting the Scottish Government Library on 0131 244 4552. Responses can be copied and sent to you, but a charge may be made for this service.

What happens next?

Following the closing date, all responses will be analysed and considered along with any other available evidence to help us reach a decision on the proposed abolition of the Council Tax and its replacement with a local income tax. We aim to issue a report on this consultation process during autumn 2008. Our intention is to introduce legislation in the Scottish Parliamentary session 2008-09.

Comments and complaints

If you have any comments about how this consultation exercise has been conducted, please send them to:

Name: Raymond Convill

Address: Room 3-J North, Local Government Division, Scottish Government, Victoria Quay, Edinburgh, EH6 6QQ

E-mail: raymond.convill@scotland.gsi.gov.uk

Calculating your Local Income Tax

This Annex contains some information to help you work out your liability. You need to know:

- what your total taxable income is for the year. This information is generally contained in documents such as a “P60”
- what your personal allowance is. For tax year 2008-09 the following personal allowances apply (please note that the following data are taken from the HMRC website):

Income tax allowances	2008-09 (£)
Personal allowance	5,435
Personal allowance for people aged 65-74 (1)	9,030
Personal allowance for people aged 75 and over (1)	9,180
Married couple's allowance (born before 6th April 1935 but aged under 75) (1) (2)	6,535
Married couple's allowance - aged 75 and over (1) (2)	6,625
Income limit for age-related allowances	21,800
Minimum amount of married couple's allowance	2,540
Blind person's allowance	1,800

(1) - These allowances reduce where the income is above the income limit by £1 for every £2 of income above the limit. They will never be less than the basic Personal allowance or minimum amount of Married Couple's allowance.

(2) - Tax relief for the Married Couple's allowance is given at the rate of 10 per cent.

Once you have this information you need to do the following:

Step one:

Deduct your personal allowance from your gross annual salary – that is the amount you get paid before any taxes have been deducted.

Step two:

Calculate 3% of this figure. One way of doing this is to divide the figure by 100, and then to multiply it by 3.

Example (2008-09)

- You have a gross income of £20,000.
- You deduct your personal allowance, which is £5,435, leaving £14,565.
- You then calculate 3% of this:
 - £14,565 divided by 100 is £145.65
 - £145.65 multiplied by 3 equals £436.95

- The amount of local income tax you will pay over the year will be £436.95. You pay income tax through PAYE and you are paid monthly, so your employer will deduct £36.41 a month from your salary

Warning

The above method only gives you an indication of the tax you will pay. The actual amount may vary slightly. This is because there is a range of different ways in which the amount of tax you pay can be affected. For example, if you donate money to a charity through the "Give As You Earn" scheme, then this money is deducted from your gross salary, and so reduces the amount of income tax you will pay. It is impossible for us to produce a user-friendly calculator that can take into account all of the possible variations on individuals' tax amounts.

You can get a more detailed idea of your likely local income tax by looking at your payslip to see exactly how much of your income is liable for income tax.

If you pay by self-assessment then you will be able to see your taxable income from your last tax return.

While accurate at time of publication, the information above may change due to the Budget on 12 March 2008.

Income that Her Majesty's Revenue and Customs (HMRC) count as Taxable

Employment (including income from self employment)

- Full, part time and temporary

Pensions

- State Pension
- Private, personal and occupational pensions
- Retirement annuity

Rents

- From any second property
- From a lodger if more than £4,250 (£2,125 if split between a couple)

Interest on savings

- Bank & building society interest (not including ISAs and PEPs)
- National Savings & Investments accounts and bonds

Investment income

- Dividends (not including income from ISAs and PEPs)

State benefits

- Carer's Allowance
- Incapacity Benefit after week 29
- Weekly Bereavement Allowance
- Employment and Support Allowance (Contributory)

Other

- Pensioner bonds
- Trusts

Income that HMRC does not count as Taxable

State benefits

- Disability Living Allowance
- Attendance Allowance
- Lump sum Bereavement Payments
- Pension Credit
- Free TV licence for over 75s
- Winter Fuel Payments
- Housing Benefit
- Child Benefit
- First 28 weeks of Incapacity Benefit
- Income Support
- Employment and Support Allowance (Income related)

Interest on Savings

- All ISAs and PEPs
- Savings Certificates
- Premium Bonds

Rents

- First £4,250 from a lodger (£2,125 if split between a couple)

Tax Credits

- Working Tax Credit

Please note that this information is taken from HMRC's website, for example see <http://www.hmrc.gov.uk/leaflets/ir121.pdf> for more information.

Useful Websites and Links

The Scottish Government

<http://www.scotland.gov.uk>

<http://www.scotland.gov.uk/Consultations/Current>

www.scotland.gov.uk/afairertax

Her Majesty's Revenue and Customs (HMRC)

<http://www.hmrc.gov.uk/>

<http://www.hmrc.gov.uk/rates/it.htm> (Personal allowances)

Department for Work and Pensions (DWP)

<http://www.dwp.gov.uk/>

Central Office of Information - DirectGov - "Public Services all in one place"

<http://www.direct.gov.uk/en/MoneyTaxAndBenefits/index.htm>

http://www.direct.gov.uk/en/MoneyTaxAndBenefits/ManagingMoney/SavingsAndInvestments/DG_10014062 (National savings and investments)

Local Government Finance in Scotland

<http://www.scotland.gov.uk/Topics/Government/local-government/17999/>

Council Tax in Scotland

<http://www.scotland.gov.uk/Topics/Government/local-government/17999/11179>

Partial Regulatory Impact Assessment: Abolition of Council Tax and Introduction of Local Income Tax

Purpose and intended effect

Objectives

1. This Partial Regulatory Impact Assessment focuses on the accompanying consultation's core proposals to abolish council tax and replace it with a system of local income tax. The Scottish Government believes that this is best done by a 3% rate applied to the basic and higher income tax rates and collected by Her Majesty's Revenue and Customs (HMRC). It is intended that the Scottish Primary legislation to provide for this will be brought before the Scottish Parliament in 2009. The implementation of the proposals will also depend on the timing of UK legislation.

Background

2. The existing system of council tax takes no account of ability to pay, instead allocating taxation liability on the basis of broad notional historical domestic property values. The government believes that this basis for taxation liability is fundamentally unfair and any changes to the existing system, other than abolition, will not address the core issue of ability to pay. However, in the interim period before council tax abolition, the government has reached agreement with local government, through the Convention of Scottish Local Authorities, to freeze the council tax in each local authority at 2007-08 levels. This is intended to reduce the negative impact of the council tax.

Rationale for Government Intervention

3. If there were no government intervention on the current system of council tax, then existing anomalies in the taxation liability of individuals compared with ability to pay would continue.

Scottish Variable Rate

4. Under existing devolved powers, the Scottish Parliament is able to vary income tax by up to 3% - the "Scottish Variable Rate". Under the terms of the Scotland Act, this could only be applied to income taxable at the basic rate. It would not apply to the higher rate tax band. The Government does not propose to use the Scottish Variable Rate (SVR) to replace the council tax, even though the SVR could, in principle, be introduced relatively quickly. However, the Government believes that earlier preparations made by HMRC for the SVR at the time of devolution should provide a basis for the arrangements that will be needed to implement a local income tax.

Consultation

Within Government

5. We will consult with the Cabinet Office, HM Treasury, Her Majesty's Revenue and Customs (HMRC), the Department for Work and Pensions (DWP), the Ministry of Defence (MOD), the Welsh Assembly Government and the Northern Ireland Executive.

Public Consultation

6. We will publish the findings of our consultation with the public and key stakeholders.

Options

Do Nothing

7. If there were no change to the current system of council tax, then existing anomalies in taxation liability compared with ability to pay would continue, given the regressive nature of the council tax system. This would not accord with the government's aim to make Scotland wealthier and fairer. This would lead to large numbers of those on low incomes continuing to pay a high percentage of their income in council tax charges, leading to individuals having less money to buy many 'essential' goods such as food and fuel, with attendant risks to health. There is a clear risk that some of these individuals will not pay their full council tax liability, which causes problems for local government finance and the funding of local public services. Although those on the lowest incomes are eligible for Council Tax Benefit, the thresholds are low and there are many on relatively low incomes that do not qualify. There is some evidence to suggest that many people do not receive the Council Tax Benefit to which they are entitled.

Reform Council Tax

8. Council tax could be reformed in a number of ways including revaluation, adding new bands or changing the ratio burden between bands. All these methods of reform will alter taxation liability, but none of them will create a link between taxation liability and the ability to pay. There is evidence that changing the ratios or bands will not make the council tax system progressive. This means that no council tax reform will meet the objective of a fairer taxation system. Key high risks with this option are therefore a continuing unfair burden on those on lower incomes and the attendant risks to health and local government funding. Any major change to the council tax system would require Primary legislation and with consultation requirements, would be unlikely to be possible in less than 2 years at the very least. Additionally revaluation may cause uncertainty, increase appeals and cause some difficulty with local authority financial planning.

Locally-Set Local Income Tax

9. Local authorities could be given the power to determine the local income tax rates within their own boundaries. This would create the vital link between taxation

liability and ability to pay. However, such a system would be administratively more complex than a single national rate, by potentially requiring employers to adjudicate on where they determined an employee's residence to be and make taxation deductions of up to 33 different amounts (the number could be 33 if there were 32 separate rates set by Scotland's 32 councils in addition to a UK rate). There is a clear and strong risk of undue administrative burden on employers, which threatens economic growth and entrepreneurship.

Alternative Local Taxation Systems

10. There are a number of alternative taxation systems that could be implemented in place of council tax, including Land Value Tax or environmental taxes. The diversity of these taxation systems and the various ways they could be introduced means that it is not possible to provide a full discussion of each option here. The Scottish Government believes that an income tax provides the best link between taxation liability and ability to pay. All other known options are based on factors other than ability to pay and therefore do not achieve our core aim of making the taxation system fairer, by better reflecting ability to pay. Many of these options are untested in Scotland and we currently do not hold sufficient data to examine their risks.

Costs and benefits

Sectors and groups affected

11. These proposals will affect most individuals in Scotland and also employers, including public and private sector organisations. Some charities will also be affected. Further detail on costs and benefits will be collected as part of the consultation process.

Benefits

Individuals

12. Council tax liability will cease for all those domestic home residents or owners who are currently liable for council tax. Taxation liability is complex and related to benefit entitlement and therefore it is difficult to generalise about the impact on individual households based on the principle of ability to pay. However, the local income tax proposed will be more progressive than the existing council tax system, with those who earn more paying more in tax. Annex F contains further more detailed analysis of the impact on individuals.

Charities

13. Many charities owning or occupying domestic properties that are liable for full or partial council tax will have this financial burden removed. It is also possible that there will be some secondary impacts on charities as the taxation regime changes. For example, change to council tax has long been campaigned for by some organisations representing older people. These organisations will now be able to concentrate their resources in other areas of importance to them. Some charities

providing welfare support to those on low incomes, may find on their resources alleviated slightly as council tax related poverty is substantively removed.

Public Sector Organisations

14. Local authorities and other public sector organisations who own domestic properties will no longer be liable to pay council tax on properties that are empty or homes of multiple occupation.
15. There will be administrative savings both to Local Authorities and DWP as a consequence of abolishing the council tax and removing the need to administer Council Tax Benefit.

Private Sector Organisations

16. Private sector domestic housing providers will no longer be liable for council tax on empty properties or homes of multiple occupation.

Costs

Individuals

17. All Scottish residents earning more than the personal allowance for UK income tax will become liable for local income tax. Taxation liability is complex and related to benefit entitlement and therefore it is difficult to generalise about the impact on individual households based on the principle of ability to pay. A local income tax based on ability to pay will necessarily base liability on income and those households with a relatively high income will pay more. The Scottish Government believes that this is fair.
18. The government believes that all those with an income above the minimum threshold should be liable for local income tax as a matter of principle. We will gather more information about these impacts as part of the consultation process.
19. Many of those on the lowest incomes are eligible for Council Tax Benefit under the council tax system. Some of those in receipt of full Council Tax Benefit will not earn enough to be liable to pay any local income tax, and so will be no better or worse off as a consequence of the changes.

Charities

20. Businesses with charitable status that do not pay Corporation Tax may be liable for some income tax on their profits, and hence these profits will be subject to the new local income tax. However, charities can claim relief from tax on most income or gains and on profits from some activities.
21. Some of those on relatively higher incomes may experience an additional financial liability and seek advice from certain charities. Change to the taxation regime generally may lead to some individuals seeking advice from advocacy and citizen's advice organisations. Those charities specifically working with those affected by the

changes, for example groups that will lose their council tax exemptions, will need to ensure that these changes are understood by those they represent. We will consult these organisations on how we can support them with this.

Public Sector Organisations

22. We will be liaising with UK government departments as to their view on these proposals and how they will be affected. The key departments that will be affected are HMRC and DWP, for collection and benefits respectively. We expect to reimburse HMRC for the collection services they carry out on our behalf. The MoD will also be affected, as special arrangements currently apply for service personnel and council tax.
23. Scottish local authorities will experience a substantive change to their role in local taxation. Under our proposals, they will no longer bill and collect current council tax charges, although some on-going collection of historical council tax debt is likely. This may result in some reorganisation at local authority level.
24. The Scottish Assessors will no longer be required to maintain an up to date council tax list in its current form and we are currently considering whether an alternate domestic property value record will be required.
25. Other public sector organisations that own domestic properties or assist individuals with day-to-day living will be affected in various ways. Public sector organisations that employ staff will be required to change their payroll processes to collect local income tax. We will be collecting more information on these impacts as part of the consultation process.

Private Sector Organisations

26. Private businesses that do not pay Corporation Tax will pay income tax on their profits. Local income tax will therefore be levied on their profits over the personal threshold. The impact on this change in the taxation regime will depend on individual council tax liability and individual income/profits. Some private enterprises will be required to change their payroll processes to collect local income tax. Some may raise wages to compensate employees for the increase in income tax.

Small/Micro Firms Impact Test

27. The Scottish Government is committed to ensuring that there is a fair business environment where all firms are not subject to undue administrative burden. This is a key reason why we propose using existing HMRC systems to introduce and administer local income tax.

Legal Aid Impact Test

28. It is anticipated that these proposals will be implemented in liaison with HMRC, utilising existing appeals practices as far as possible. We will work with HMRC to identify any new procedures or rights of appeal and their impact on Legal Aid.

"Test Run" of business forms

29. We will work with HMRC to ensure that any new forms introduced are "test run" with business organisations to make sure they are as clear, simple and easy to complete as possible.

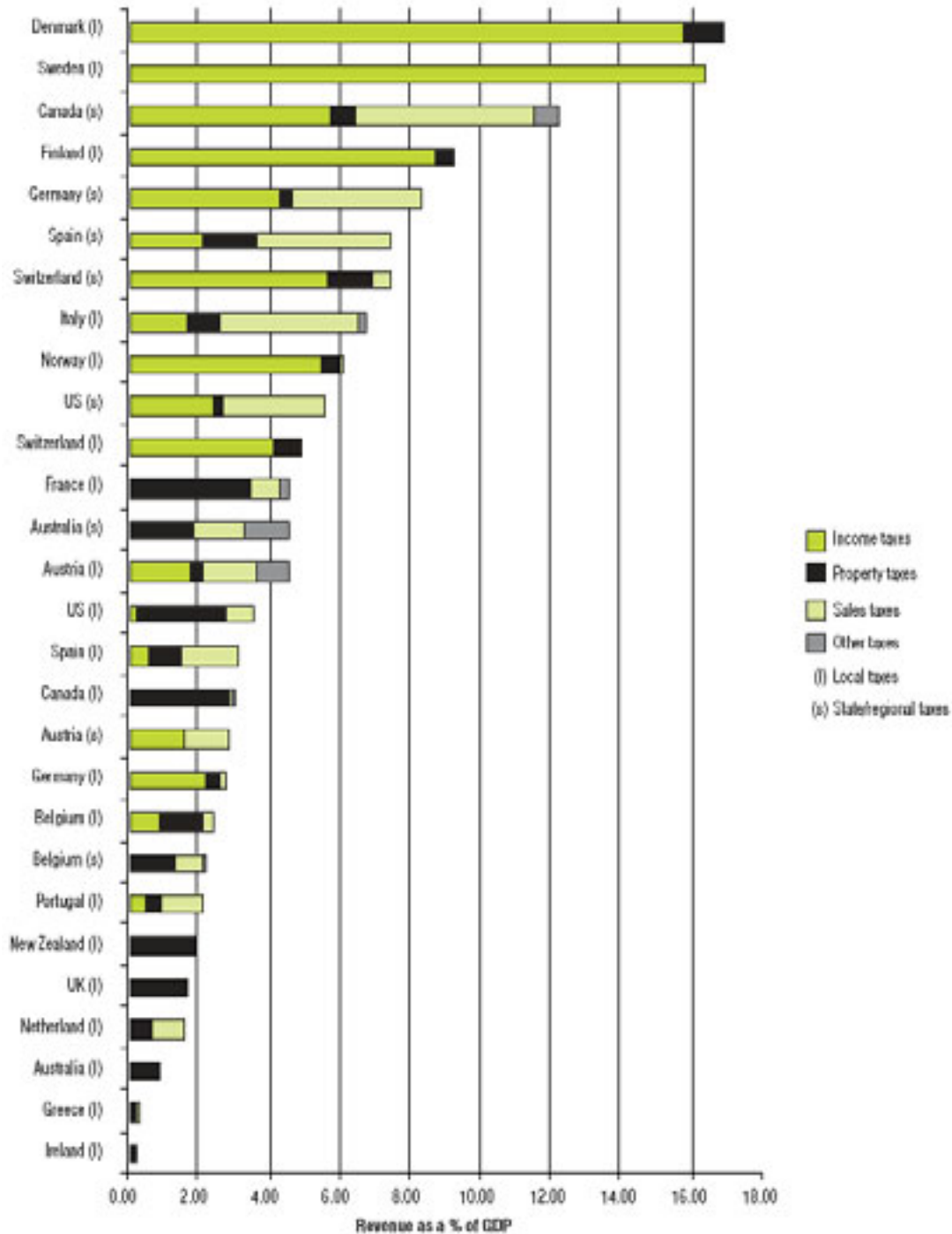
Competition assessment

30. We are not aware of any impact of our proposals on competition, as it is our intention that all administration is co-ordinated by HMRC, but we will continue to gather information on this aspect of our proposals as part of the consultation.

Local Taxation in Other Countries

In 2006, the Local Government Finance Review Committee published an analysis of the kind of local taxes that are levied in different countries. This analysis was based on data from the International Monetary Fund. It is reproduced below to help consultation respondents understand the international context of local taxation and how the proposed Scottish system compares with other countries. The analysis indicates that income tax is a common feature of local taxation.

Sub-national Tax Revenues by type of tax as a % of GDP



Household Impact of a Local Income Tax

Overview

1. This Annex outlines the methodology used to estimate what the impact of introducing a local income tax (LIT) would have been on Scottish households in 2007-08. This Annex also highlights the key results of the analysis.

Methodology

2. The assessment of the impact of a LIT was produced using a micro-simulation model of Scottish households². The model estimates Scottish household net income based on detailed information on the UK tax and benefit system. Using this information for 2007-08 we simulate household after tax income under a LIT of 3p levied on earned income for both the basic and higher rates. We compare this with household after tax income under the existing council tax regime.

3. In the modelling, we also estimate council tax benefit (CTB) take-up rates from the FRS (Family Resource Survey). We estimate a take-up rate of 73%. This estimation approach is designed to capture the fact that in reality not all households fully take-up their council tax benefits.

Results

4. Our analysis estimates that in 2007-08, under a LIT, 67% of Scottish households would have experienced an increase in net income, 18% a reduction and 15% no change (no change is defined as a change in weekly income of less than 5 pence).

5. The estimated average weekly increase in income would have been £4.90.

Distribution of Scottish households by income deciles

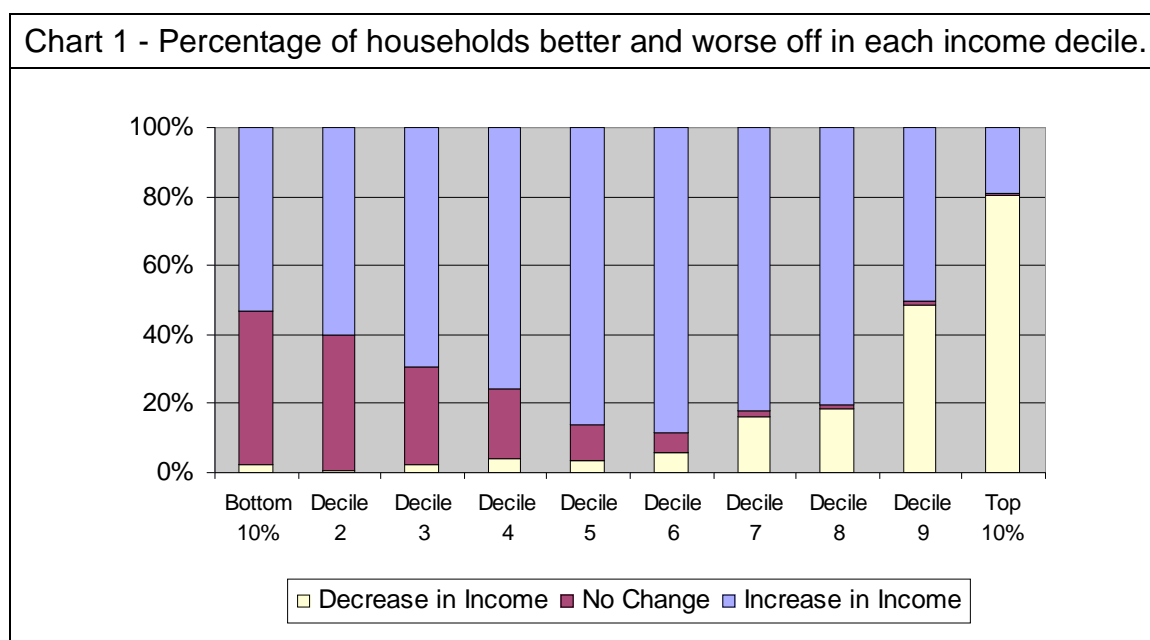
6. For 2007-08, it is estimated that the average household in nine out of ten income deciles would have been better off under a LIT. Households in the top income decile are forecast to have experienced, on average, a decrease in net income. Table 1 shows the results across income deciles rounded to the nearest 10 pence and as a percentage of households' after tax income.

² The model is based on the 2005-06 Family Resources Survey (FRS) which contains detailed information on income and expenditure information in approximately 4,500 Scottish households. Household income is based on UK earnings growth data supplied by HM Treasury to estimate income in future years

Table 1- Average weekly change in net income for each income decile³

Income Decile	Bottom 10%	Decile 2	Decile 3	Decile 4	Decile 5	Decile 6	Decile 7	Decile 8	Decile 9	Top 10%
Average Weekly Change (£)	£6.70	£6.80	£8.10	£8.80	£10.30	£9.70	£6.90	£6.00	£0.90	-£15.10
Change as % of after tax income	5.7%	3.7%	3.5%	3.1%	3.0%	2.3%	1.4%	1.0%	0.1%	-1.2%

7. It is important to note that the impact on individual households will vary according to their particular circumstances. Chart 1 presents the percentage of households within each income decile estimated to have experienced an increase, decrease or no change in net income.



³ The results for the top income decile are skewed by the change in income experienced by four outliers in the sample. When these observations are excluded from the analysis the estimated average change in household income for this decile is -£12.90 a week.

Distribution of Scottish household by family type

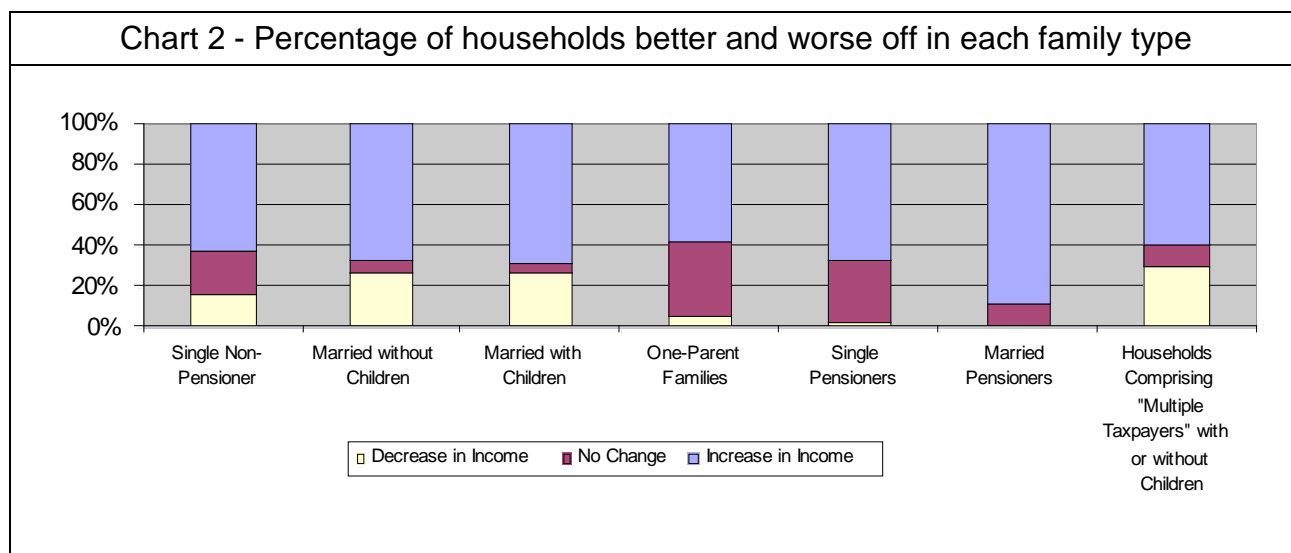
8. On average, in 2007-08, the majority of Scottish households across all major family types would have been better off under a LIT. Table 2 displays the estimated average weekly change in net income according to seven family types.

Table 2 - Average weekly change in net income by family type

Family Type	Single Non-Pensioner	Married without Children	Married with Children	One-Parent Families	Single Pensioners	Married Pensioners	Households comprising "Multiple Taxpayers" *
Average Weekly Change (£)	£3.30	£3.40	£3.10	£5.40	£7.30	£13.80	£2.50
Change as % of after tax income	1.1%	0.5%	0.5%	1.7%	3.3%	3.4%	0.4%

*Note: Households comprising "Multiple Taxpayers" (also known as Multiple Tax Units) involve a number of different household types, the main of which are – young adults living together, adult children living at home with parents and parent(s) living with their adult children.

9. In Chart 2, we present the percentage of households by family type estimated to have experienced an increase, decrease or no change in their net income as a result of the replacement of the council tax by a LIT.



10. Table 3 below gives estimates for 2007-08 which further illustrate the impact on the groups shown in Table 2 above.

	Pay Less	No Change	Pay More
Single Non-Pensioner	63%	20%	17%
Married without Children	67%	6%	27%
Married with Children	68%	4%	28%
One-Parent Families	57%	38%	5%
Single Pensioners	66%	30%	3%
Married Pensioners	88%	10%	2%
Households comprising "Multiple Taxpayers"	59%	11%	30%
Total Count	67%	15%	18%

Summary

11. For 2007-08, we estimate that under a LIT:

- 67% of Scottish households would have been better off, 15% would have been no worse off and 18% would have been worse off;
- The average change in household net income would have been £4.90 per week; and
- Pensioners and One Parent Families are estimated to benefit from the greatest increase in net income.

List of Consultees to whom the consultation is being sent initially

Accounts Commission	Joseph Rowntree Foundation
Action of Churches Together in Scotland	Law Society of Scotland
Age Concern Scotland	Legal Deposit Libraries UK
Association of Scotland's Colleges	Leonard Cheshire Scotland
Association of Scottish Business Women	Local Authorities Scotland (Chief Executives, Council Leaders and Directors of Finance)
Audit Scotland	Local Authority (Scotland) Advisory Committee, CIPFA
Barnardo's Scotland	Ministry of Defence
Black and Ethnic Minority Infrastructure in Scotland	Money Advice Scotland
Big Issue Foundation	National Farmers Union Scotland
Capability Scotland	National Pensioners Convention
Chartered Institute of Public Finance and Accounting (CIPFA)	Northern Ireland Executive
Child Poverty Action Group	National Union of Students Scotland
Child Support Agency	NCH Scotland
Children 1st	Older People's Consultative Forum
Children's Parliament	One Parent Families Scotland
Churches of Scotland	Oxfam Scotland
Citizens Advice Scotland	Policy Institute
Committee of Scottish Clearing Bankers	Positive Action in Housing
Confederation of British Industry Scotland	Poverty Alliance (Scotland)
Convention of Scottish Local Authorities	Prime Minister's Office
Council of Ethnic Minority Voluntary Sector Organisations	Registers of Scotland
Department for Communities and Local Government	Royal College of Nursing
Department for Work and Pensions	Rural Community Gateway
Dialogue Youth (Scotland)	Royal Institution of Chartered Surveyors
Engender (Scotland)	Royal National Institute of Blind People
Equality and Human Rights Commission	Scotch Whisky Association
Federation of Small Businesses	Scotland Office
Forum of Private Business in Scotland	Scottish Action Against Council Tax
Friends, Families & Travellers	Scottish Assessors Association
Health Boards in Scotland	Scottish Civic Forum
Help the Aged	Scottish Chambers of Commerce
Henry George Foundation	Scottish Churches Housing Action
HM Revenues & Customs	Scottish Committee of the Council on Tribunals
HM Treasury	Scottish Conservative & Unionist Association
Home Office	Scottish Consumer Council
Inclusion Scotland	Scottish Council for Development and Industry
Institute of Chartered Accountants of Scotland	Scottish Council for Voluntary Organisations
Institute of Directors Scotland	Scottish Council of Jewish Communities
Institute of Revenues Rating and Valuation	Scottish Disability Equality Forum
Isitfair – Campaign to Abolish the Council Tax (UK)	Scottish Financial Enterprise
	Scottish Fishermen's Federation

Scottish Government Library
Scottish Green Party
Scottish Grocers' Federation
Scottish Information Commissioner
Scottish Inter Faith Council
Scottish Labour Party
Scottish Liberal Democrats
Scottish Licensed Trade Association
Scottish MEPs/MPs/MSPs
Scottish National Party
Scottish Parliament Finance Committee
Scottish Parliament Information Centre
Scottish Parliament Local Government
and Communities Committee
Scottish Pensioners' Forum
Scottish Refugee Council
Scottish Retail Consortium
Scottish Rural Property and Business
Association
Scottish Senior Citizens Unity Party
Scottish Social Services Council
Scottish Socialist Party
Scottish Tenants' Organisation
Scottish Tourism Forum

Scottish Trade Union Congress
Scottish Water
Scottish Women's Convention
Scottish Youth Parliament
Sense Scotland
Shelter Scotland
Sheriff Officers Scotland
Society of Local Authorities Chief
Executives
Solidarity Scotland
Stonewall
Tenant Participation Advisory Service
(Scotland)
UNISON Scotland
Universities Scotland
Update (Scotland's National Disability
Information Service)
Valuation Appeal Committees
Welsh Assembly Government
Women@Work
Women Onto Work
Youthlink Scotland

Response Forms

You can respond online or you can access a printable version of the response forms via the website at www.scotland.gov.uk/afairertax