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LONG-TERM ALTERNATIVES TO DOMESTIC RATES

A formal review of Rating Policy in Northern Ireland was announced by the Minister for Finance and Personnel, Peter Robinson, in May 2007. The review is twofold in that it will assess the potential for short-term improvements to the existing system, as well as the possibility of longer-term alternatives. This paper is concerned with the latter aspect. It considers the feasibility of a number of local tax alternatives for implementation in Northern Ireland. Previous UK studies of local government taxation are outlined in this regard, and any implications for Northern Ireland, legislative or otherwise, are highlighted.

Contents

1. Introduction

In view of the forthcoming Rating Review, this paper considers the feasibility of various long-term alternatives to domestic rates for implementation in Northern Ireland (NI). Previous studies of local authority funding are considered, and the implications for Northern Ireland summarised in each case. The paper focuses on those options which have previously been considered viable in a UK context, namely taxes on property and income. It emerges that much of the recent evidence supports the existing rating system of "individual capital valuation".

2. Background

The new system of domestic rating, introduced in April 2007, has been heavily criticised[1]. The majority of criticism relates to the perceived unfairness of the system. Specific concerns include what is considered to be the lack of reliefs available (there have been calls for a single person relief) and the professed shortcomings / take-up of those that are on offer (student relief and disability relief).[2] Other criticisms have focused on the claimed inaccuracy of valuations and the related appeals process. It has also been argued that a property-based tax system is ineffective in the context of the pressurised local housing market. These issues have resulted in the recent announcement of a formal Rating Review[3].

3. Context

The review will be a two-fold one, and will be concerned with:

i. Identifying ways of improving the new system that can be implemented in April 2008; and
ii. Examining alternatives to the new system as a means of identifying options for *longer term* change.

This paper is concerned with the latter consideration, and will examine the following options for local taxation:

- Banding of house values (a Council Tax type system)
- Local income tax
- Income tax-varying powers (as per Scotland)
- Local sales tax
- Poll tax
- Tourist tax (as recommended in the Lyons report)
- Road charging
- Green taxes
- Land value taxation
- Derelict land taxation (as recommended in the Lyons report)

[1] Bills were not issued to customer until April 2007, however, notification letters were distributed in July/August 2006 indicating future rate liability – the first criticisms arose at this stage.
[2] Specifically, the student relief has been criticised on the basis that it will benefit landlords, not students (however, the scheme allows for this and requires proof that any savings are passed on to students via reduced rental costs). Disabled persons relief only applies to those individuals whose houses have been adapted because of disability – it has been suggested that this should instead apply to all disabled persons.
[3] Peter Robinson announcement 15 May 2007 http://www.ratingreviewni.gov.uk/

The previously undefined possibility of a local 'MOT charge' (an additional charge on the cost of MOT), as advocated by the Director of the Economic Research Institute of Northern Ireland (ERINI), Victor Hewitt, is considered under "Green taxes".

4. Legislative Implications

Under the Northern Ireland Act 1998, most issues of taxation are beyond the powers of a local administration and there can be no interference with, or duplication of, the national taxation system. The issues under consideration in this paper would therefore require new primary legislation and, in some cases (e.g. in relation to income tax and sales tax), a change to the original Act.

5. Previous Studies of Alternative Tax Options

Many of the options listed in Section 3 have been the subject of previous studies. The main UK-based studies on the alternative options for local funding include:

5.1 The Layfield Committee, 1976

Although published in 1976, the Layfield Report remains an influential document; researchers still refer to it in related studies. Described as "*a benchmark for subsequent studies*[4]" (into alternative local tax systems), this committee was formed in response to adverse reaction to inflationary rate rises in Britain in the early 1970s.[5] Reporting in 1976, the majority of the committee favoured a local authority system with greater financial autonomy. Layfield regarded local income tax as the only serious candidate for a new source of local revenue[6]. However, no reform took place; the post-1979 Conservative Government published a Green Paper in 1981, which again considered alternatives to domestic rates, as follows:

5.2 "Alternatives to Domestic Rates", 1981 Green Paper

A 1981 Green Paper dealt with the rating situation in England, Scotland and Wales, and considered the ways in which domestic rating might be improved / substituted. The study focused on three possible new forms of taxation[7]:

- a local sales tax;
- a local income tax; and
- a poll tax.

5.3 "Paying for Local Government" 1986 Green Paper

This Green Paper paved the way for the introduction of the Community Charge (the "poll tax") in 1989. The poll tax was introduced in Scotland in 1989, one year earlier than in England and Wales, following the abolition of domestic rates. The community charge was very unpopular and by January 1990, 421,400 cases of non-payment were being pursued[8]. Council tax was therefore introduced in the 1990s, in response to a 1991 Consultation Paper.

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[4] Bennett, Central Grants to Local Authorities, 1982
[5] Inflation in the early 1970s pushed local taxation up to high levels; in 1974, the average increase exceeded 30% (http://www.publications.parliament.uk/pa/cm200304/cmselect/cmodpm/402/40203.htm)
[6] "A Fairer Way", Report by the Local Government Finance Review Committee, Edinburgh, 2006
[7] A range of other taxes was considered, but it was decided that they were not worthy of further consideration. Those rejected included: local duties on petrol, alcohol or tobacco; local vehicle excise duty; charges for licences for the sale of alcohol or petrol; and local payroll tax
[8] "A Fairer Way", Report by the Local Government Finance Review Committee, Edinburgh, 2006

5.4 "A Fairer Way", Local Government Finance Review Committee, 2006

In their "review (of) different forms of local taxation" in 2006, the Scottish Government Finance Review Committee (the Committee) considered a variety of domestic tax options, which fell under the following four broad categories:

- Taxes on income (e.g. local income tax)
- Taxes on wealth, including land and property (e.g. domestic rates, land value tax)
- Taxes on people, usually at a flat rate (poll taxes)
- Taxes on transactions and products (e.g. local sales tax, specific additional taxes on fuel, tourism, chewing gum, alcohol)

The Committee concluded that only taxes on income and property were worthy of a more detailed consideration.

5.5 Lyons Inquiry into Local Government, March 2007

The terms of reference of this recently published inquiry, included: recommendations on the reform of council tax; consideration of shifting the balance of funding; and an analysis of other options for local taxation, including local income tax; non-domestic rates; and other local taxes and charges. Lyons made a series of recommendations (listed at Appendix 1) on various systems, which will be outlined in the appropriate sub-sections.

6. General Considerations in Assessing Different Tax Systems

A model of important criteria for a local taxation system has been provided in the Terms of Reference for the current Rating Review (refer last weeks pack). However, these do not directly equate with those identified as important in previous studies. The 2006 study "A Fairer Way" was required to "*review the different forms of taxation….against criteria set by the Executive*[9]". However the study identified other important factors which were not set out in the original criteria; they differentiated between the resultant criteria on the basis of importance; ranking them as 'high', 'medium' or 'lower'. The report identified the following factors as being of 'high importance'[10]:

- **Size of the Tax Base**: The size of the tax base (the number of people / households who would be liable) is important in ensuring that the burden of tax is spread as evenly as possible.

- **Fairness:** This emerged as by far the most important criterion amongst the Scottish public in their satisfaction, or otherwise, with council tax systems. Whilst clearly a highly subjective concept, a number of interpretations of 'fairness' were identified. 'Ability to pay' was the most common[11]. Other indicators included: 'effect on pensioners'; 'relationship between property value and rate liability' (the public indicating that this should be positive); and 'reliefs available for poor people'.

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[9] "A Fairer Way", Report by the Local Government Finance Review Committee, Edinburgh, 2006
[10] "A Fairer Way", Report by the Local Government Finance Review Committee, Edinburgh, 2006
[11] The committee recommended that 'ability to pay' be considered in both relative (it should be a progressive tax system) and absolute (individual bills should be affordable) terms.

- **Relationship to Benefits System:** A tax model's 'relationship to the Benefits System', and its reliance thereon, was identified as a vital consideration in providing a degree of fairness. For example, in Great Britain, Council Tax Benefit is considered crucial to the present council tax system; benefit is paid to those who are eligible for payment and deducted from their council tax bills by local authorities.

- **Ease of Assessment, Collection and Payment:** The "collectability" of different types of tax was identified by the Executive as an important issue. The ease of payment, for the taxpayer, was also considered noteworthy. For example, it has been argued that offering taxpayers more flexible payment terms can make a tax more affordable.

- **Stability and Predictability:** Tax revenue must be both predictable and stable; authorities must be assured of the funding they require to deliver services and to enable expenditure planning. Predictability is also important from the point of view of the taxpayer, enabling a reasonably clear expectation of tax liability.

- **Transitional Issues:** It is also important to consider how best to bring an "old system" to a close, and start a "new" one. For example, it might be considered whether a new system should temporarily run parallel to the old one, or should transitional arrangements be applied.

The Scottish study also identified a number of other considerations, which were classified as being of either medium or lower importance. Appendix 2 categorises the entire criteria by relative importance.

7. Comparative Analysis of Alternative Options

This section considers the various long-term alternatives to domestic rates, as summarised in Section 3. It will include the previously unspecified alternative of an 'MOT tax', as suggested by Victor Hewitt, Director of the Economic Research Institute of Northern Ireland, (ERINI)[12].

7.1 A Reformed Domestic Rating System: Banding of House Values

The current domestic rating system in NI incorporates an 'individual' (or 'discrete') assessment approach to capital valuation, (property values are assessed individually). This was selected in NI in preference to the alternative 'banding' methodology, despite the fact that banding is used in the council tax system in Great Britain. This section considers the arguments for changing the local rating system from an individual assessment basis, to a banded one.

The Rationale for Individual Capital Assessment in NI

It is suggested that individual assessment results in a more accurate and equitable outcome than banding, and that this explains its prevalence in various international

[12] Private communication: Victor Hewitt and Assembly researcher

countries[13]. In the NI case, the adoption of individual assessment was on the basis of a specially commissioned study.

In March 2003, the Government commissioned work by the University of Ulster entitled *'Examination of Options for a Capital Value System'.* The study analysed house sales data in NI over the period 1998-2002, adjusted to a common valuation date of 1 April 1999, (selling price was used as a proxy for capital value). The dataset contained 46,407 properties, representing approximately 7% of dwellings in NI. The study found that an individual approach was more progressive than a banded one, hence its implementation[14].

It is worth noting that there is a potentially debatable aspect to the decision to introduce 'discrete capital assessment' for NI. The study was undertaken in 2003, under very different property market conditions, using associated estimates of capital values. The applicability of this model to the current environment might be debated. Specifically, the analysis suggests that occupants of lower value properties (below £149,000) would be more likely to have lower rates bills – hence the assumption that is was more 'progressive'[15]. However, the entire distribution of property values has changed since the study. A survey by the University of Ulster in 2007 showed that the average house price in Northern Ireland is £215,590[16]. This is compared with the results of the same survey in 2003, in which the average value was reported at £105,779[17]. Substantially fewer properties would now fall within the 'below £149,000' range, within which a fall in rates was anticipated. This factor might be considered in the forthcoming review and in any re-assessment of the individual vs. banding approaches.

The Arguments For/Against a Banded Approach

The council tax system in Great Britain is a banded property tax. It was introduced in 1993 to replace the community charge (poll tax)[18]. Council tax involves allocating each residential property to one of eight bands, according to value. The band to which a property is assigned determines the basic bill for each household. There is a range of discounts, such as single person allowance, which has the effect of reducing tax liability by 25% for single adult households. The 'charge application ratio' is also enforced, which ensures that those in the top value band pay exactly 3 times the amount of those in the bottom value band (all other things being equal) – this avoids any disproportionately high tax bills.

In March 2007, the Lyons Inquiry, in its review of the existing system, recommended that: *"council tax should be retained as a source of revenue for local government",* thus endorsing its relative effectiveness on the basis of various criteria. However, this was inconsistent with the 2006 study "A Fairer Way", which recommended the abolishment of council tax in favour of an individual assessment property system. The Scottish study found that banding was less progressive, and less "fair". Lyons has also acknowledged the regressive nature of Council Tax. He acknowledges that

[13] The USA, New Zealand, Australia, Canada, the Netherlands and South Africa have all adopted a discrete capital value approach.
[14] "Examination of Options for a Capital Value System", University of Ulster, 2003
[15] A tax system is defined as 'progressive' if lower-income households pay a lower proportion of their incomes in tax, whereas it is 'regressive' if highest-income households are liable for the lowest proportion of their income (Lyons Inquiry, "Household Taxation and local charges", March 2007)
[16] "Average house cost over £215,000", BBC News, 1 June 2007 http://news.bbc.co.uk/1/hi/northern_ireland/6712089.stm
[17] http://news.ulster.ac.uk/releases/2003/990.html
[18] The poll tax replaced the domestic rating system in Great Britain in 1990 and in Scotland in 1989 ("Reform of the Domestic Rating System in Northern Ireland – Policy Paper")

the current system of Council Tax Benefit, whilst designed to offset this effect, does not *"noticeably alter"* this *"regressiveness"*[19].

However, to address this issue, he does not recommend individual assessment, rather the introduction of additional 'bands'. His argument for doing so is the considerable upheaval which would be associated with valuing individual properties.

For Northern Ireland, a key advantage of 'banding' over individual assessment, namely avoiding the need for (and cost / time implications of) individual valuations, is not applicable. Since the valuation process has already been carried out, there would therefore appear to be no benefit to moving to a 'banded' methodology, (however, upon revaluation in 2010 this would become a relevant consideration). An important aspect of council tax, which might be noteworthy for NI is the 'single persons relief'. The lack of this relief in NI has been the subject of significant criticism.

Summary Implications for Northern Ireland

- Changing distribution of property values might question robustness of original decision to introduce individual assessment;
- Benefits of property based tax system apply equally to individual / banded approaches (i.e. difficult to evade, reasonably simple and inexpensive to collect, provides a stable and predictable yield);
- The evidence is split: one study recommended the abolition of council tax, the other its retention;
- A banded approach is generally considered to be comparatively less progressive[20];
- Single Person's Relief might improve the perceived "fairness" of local system;

7.2 Local Income Tax

The previous UK-based studies have reported relatively favourably on the prospect of a local income tax; however none have actually recommended its implementation. In terms of the practicalities of enforcing a local income tax, the financial implications of full and partial income tax replacement (of council tax) are as follows[21]:

- **Full replacement:** To fully replace revenue earned from council tax (£22 billion) with an income tax would have involved an additional 7.7 pence on the basic rate of income tax in 2006-07;
- **Partial replacement:** To replace approximately half of council tax would require an average local rate of 3.9 pence on the basic rate of income tax[22].

The Layfield Committee gave qualified approval to one form of local income tax as a *supplement* to domestic rates, but not as a substitute. It concluded that this was *"the only feasible major new source of revenue"* for local authorities[23]. However, the Committee recognised the likelihood of problems and that the associated cost would be substantial. The 1981 Green Paper also defined income tax as amongst the potentially feasible options for England, Scotland and Wales. The most

[19] Lyons Inquiry, "Household taxation and local charges", March 2007
[20] A tax system is defined as 'progressive' if lower-income households pay a lower proportion of their incomes in tax, whereas it is 'regressive' if highest-income households are liable for the lowest proportion of their income (Lyons Inquiry, "Household Taxation and local charges", March 2007)
[21] Lyons Inquiry, "Household taxation and local charges", March 2007
[22] This option would also involve allowing band D council tax to be reduced to an average of £629 (£1,268 in 2006-7)
[23] Lyons Inquiry, "Household taxation and local charges", March 2007

straightforward means of implementing a local income tax was identified as being integration with the present national income tax system.

However, it was suggested that this would be a complicated undertaking, and that there would be difficulties arising from central and local government sharing the same tax base.

The Scottish study, 2006, also short-listed income tax as worthy of further consideration. Further, it revealed that there were higher levels of public satisfaction and lower levels of dissatisfaction (37% and 35% respectively) with income tax than with council tax, (21% and 60% respectively). The analysis found that any local income tax system, for practical reasons, would need to operate in parallel with the UK tax system[24]. This implied the use of the same allowances and tax bands, and assessment and collection procedures. It was concluded that a nationally set local income tax would be less complex and cheaper to apply than a locally set one.

However, in comparison with a property tax, the authors of "A Fairer Way" (2006) favoured property, suggesting that it was more difficult to evade and could be collected locally. It concluded that a local income tax should *not* be introduced, either as a replacement for council tax, or as a supplementary tax. Similarly, in March 2007, the Lyons review did not recommend the implementation of a local income tax in Britain in the short or medium term. Lyons highlighted that the public underestimated the impact that a move to income tax would have on tax liability. He explains that moving away from property-based taxation towards income tax would result in a significant redistribution of the tax burden, away from retired households, and onto the working age population. Nonetheless, Lyons did acknowledge that it was a theoretically feasible option for Britain, and that it remained a choice for future.

<u>Summary Implications for Northern Ireland</u>

- Some support for this type of tax, primarily based on the perception that it is "fair";
- Would be more progressive to overall income than council tax[25];
- Might be a feasible option for NI, however it has not been recommended by previous studies;
- Would result in significant redistribution of tax burden, away from retired households, onto working age population;
- Its use may be restricted to a supplementary role, rather than a direct substitute;
- Previous studies suggest that it would be best operated in conjunction with the national income tax system;
- The cost of implementation would be substantial;
- Amendment to primary legislation would be required.

<u>7.3 Income Tax Varying Powers</u>

Scotland is a region with devolved powers in respect of income tax; the Scottish Parliament holds limited power to vary the rate. This only applies to income earned at the basic rate; the Parliament can vary tax at this rate (upwards or downwards) by up to 3 pence in the pound. If raised by the full 3 pence, this would raise around 40%

[24] "A Fairer Way", Report by the Local Government Finance Review Committee, Edinburgh, 2006
[25] Lyons Inquiry, "Household taxation and local charges", March 2007

of the taxable income currently collected through income tax (an estimated £810 million in 2004-05)[26].

“A Fairer Way” found that in order to be “fair”, an income tax must apply to all taxable income. On this basis, local income tax varying powers, such as those held in Scotland, (and which only apply to income earned at the basic rate), would be considered less “fair”, and therefore might not be recommended.

Summary Implications for NI

- Powers would need to be devolved with respect to income tax;
- Assuming a similar system to that in Scotland, likely to be perceived as less “fair” than a property tax

7.4 Local Sales Tax

International comparisons show that sales taxes are used, although generally in combination with other taxes. In federal countries, such as Australia, Austria, Canada, Germany and the United States, they tend to form a significant share of tax revenues for state government (typically 25-40% and around 50% for USA), but considerably less for local government, (nil for Australia; less than 10% for Canada and Germany; 20-30% for Austria and USA)[27].

The possibility of a local sales tax has been considered in previous UK based rating policy reviews. It was analysed, in particular, by the Layfield Committee, which identified a number of strong arguments *against* it. A subsequent assessment was carried out by the Government in the 1981 Green Paper[28]. However, it was deemed unsuitable as a sole replacement for domestic rates, and potentially problematic as a supplement[29]. The 2006 study also eliminated sales tax as an option for Scotland.

“A Fairer Way” (2006) reported a mixed reaction from the Scottish public regarding a local sales tax. Whilst there was some support for this alternative, most was conditional. Key amongst these considerations were that the rate be set nationally to avoid cross-local authority boundary shopping, that basic goods should be exempted from the tax, as with VAT, and that it should only be used to supplement other taxes. The authors concluded (on the basis of evaluation against their criteria) that a sales tax should be ruled out as an option for Scotland.

One important issue raised in the Scottish study was the question as to whether a sales tax in addition to VAT would comply with EU law. The committee sought legal advice on the matter, which indicated that the legality of the tax would depend to a great extent on its structure. The more distinctive the tax appears to VAT, the greater the chance of compliance. For Scotland, it was considered likely that a separate rate of VAT would be *incompatible* with EU law, as it does not permit differential tax rates within states. This would clearly present a similar issue for Northern Ireland.

[26] “A Fairer Way”, Report by the Local Government Finance Review Committee, Edinburgh, 2006
[27] “A Fairer Way”, Report by the Local Government Finance Review Committee, Edinburgh, 2006
[28] The 1981 Green Paper looked at the possibility of either a single-stage sales tax or a multi-stage tax, akin to VAT (Value Added Tax). Whilst theoretically, a local sales tax could take the form of a full-scale VAT, levied on all the transactions currently subject to national VAT, this was deemed too complicated. The Government therefore concluded that any potential local sales tax would be of the single-stage variety. The two basic single stage models which were considered by the Government are outlined in Appendix 3
[29] Anticipated problems included; financial control problems, unpredictability of yield, distinguishing between domestic and business transactions, high costs of compliance, and questions of accountability and perceptibility.

Summary Implications for Northern Ireland

- Eliminated as a long term option by all three previous studies;
- Considerable practical difficulties would be anticipated;
- Would require amendment to primary legislation;
- May be incompatible with EU rules.

7.5 Poll Tax

A fixed annual charge could be levied on individuals living in a local authority area as a contribution to the cost of providing local services – i.e. a 'poll tax'. This concept operated in Scotland from 1989 to 1993, and similar charges have been used in the past in both the UK and other countries. According to "A Fairer Way", 2006, poll taxes (as they are generally defined) are no longer used as a significant source of revenue by any major countries. The Scottish study also revealed significant public and official opposition to the notion of a poll tax.

In summary, the study found no justification for considering a poll tax as a possible replacement for a council tax. Although it does offer some potential advantages (it could be stable and predictable, assuming high levels of compliance), the lack of any link with 'ability to pay' was considered to be likely to make it extremely unpopular. Furthermore, it would only be feasible in conjunction with an extensive benefits system and the costs associated with this would be likely to consume a very large proportion of the tax proceeds[30].

Summary Implications for NI

- Historical evidence suggests significant difficulties in collection;
- Not favoured by previous studies;
- Little relationship with 'ability to pay';
- May not be financially viable.

7.6 Tourist Tax

'Bed taxes' and other types of tourism tax (e.g. airport departure fees and taxes) are often used in other cities and countries, and are used in particular to assist the promotion and development of tourism locally[31].

"A Fairer Way" found, (from responses to the consultation paper), that a local tourist tax would be very unpopular amongst the Scottish public. Most local authorities were also against the concept. The British Hospitality Association (Scotland), a tourism industry body, made a submission strongly opposing tourism tax.

However, the Lyons report viewed a tourism tax more favourably; it recommended:

"that the Government should consult on the costs and benefits of providing a permissive power for local authorities to levy taxes on tourism, including a possible tax on accommodation, and whether local authorities would use such a power[32]"

[30] "A Fairer Way", Report by the Local Government Finance Review Committee, Edinburgh, 2006
[31] "A Fairer Way", Report by the Local Government Finance Review Committee, Edinburgh, 2006
[32] "Lyons Inquiry into Local Government – Final Report", March 2007

Nonetheless, Lyons stressed that a local accommodation tax would only be appropriate under certain circumstances.

Specifically, a local authority must be able to demonstrate that there is robust evidence that the local economy could support the tax, existing alternatives have been fully considered, there is local support for the tax, and that the scheme has been developed in partnership with local businesses and residents. He suggests that a tourism tax could have very little impact on tourist numbers in one location, but could be very damaging in another[33].

Summary Implications for NI

- Ability of local economy to support a tourism tax should be considered;
- Might be argued that tourism industry should be developed further to ensure robustness.

7.7 Road Charging

Congestion charging and road pricing were raised by a number of submissions to the Lyons Inquiry as a possible source of revenue for local authorities. Powers to operate congestion charging schemes were introduced for authorities outside London in the Transport Act 2000, in instances where charging would support the Local Transport Plan. These are relatively new powers and remain largely untested, with the notable exception of London's congestion charge. Lyons therefore suggested that the Government should consider removing restrictions on the use of road pricing revenues.

Summary Implications for NI

- Possible source of local revenue;
- Environmentally friendly

7.8 Green Taxes

The Director of the Economic Research Institute of Northern Ireland (ERINI), Victor Hewitt, has proposed a number of other revenue raising alternatives. His recommendations focus on the wide latitude that exists around introducing 'charges' which do not represent the modification / introduction of a tax resembling an existing national tax. He highlights the fact that such 'new' charges do not require amendment to primary legislation, but that they need to be assigned to specific areas.
Specifically, Victor Hewitt proposes an additional charge on MOT costs, to which it might be possible to attach an environmental surcharge. He suggests that this would generate revenue which could be spent on environmental issues associated with road transport. There are a number of advantages of this option, as follows:

- Perhaps most importantly, an 'MOT charge' would not require amendment to primary legislation, since it does not represent a modification of an existing national tax;
- MOT income goes to the local service centres; an associated tax might therefore produce revenue which could be retained locally;

[33] "Lyons Inquiry into Local Government – Final Report", March 2007

- It would be an environmentally friendly tax;
- The revenue stream would be quite stable and certain;
- It would be difficult to evade and quite enforceable.

However, potential disadvantages include:

- Properties are more fixed than vehicles, thus the tax base would be less stable and revenue less predictable;
- There may be issues around fairness, and specifically ‘ability to pay’. There is already an argument about how well domestic rates distribute the rates burden, since they are only payable by homeowners (thus excluding the contribution of some members of the public). This perception is likely to be exacerbated if the tax only applies to vehicle-owners. There might also be a fairness issue around the fact that MOTs only apply to cars of a certain age – this could be perceived as regressive.

Victor Hewitt has indicated that this type of tax system presents a viable means of at least supplementing local taxation revenue. However, he suggests that it would be most applicable for funding borrowing, rather than expenditure (due to unpredictable nature)[34].

Summary Implications for Northern Ireland

- No amendment to legislation required;
- Potential issues around ‘fairness’ / perception as ‘regressive’;

7.9 Land Value Taxation

Land-value tax (also known as “site value tax”) has two key features. The first is that the tax applies to the value of the land and not the value of any buildings on the land. The second is that it is the owner of the land, rather than the occupier, who pays the tax. The basic rationale of land value tax is that it encourages optimal use of the land, as the tax liability will be the same whether the land is left derelict or is fully utilised. Its supporters argue that standard property taxes create a disincentive to developing land and improving properties, since those developments result in tax.

According to “A Fairer Way”, more than 700 cities worldwide apply a land value tax in some form, including cities in Australia, eastern Europe and the US State of Pennsylvania. The study reported that, despite considerable evidence, there is no “ideal” model in operation, making an assessment of the effect of land value taxation difficult. The authors conferred with the Layfield Committee in their elimination of land-value tax as an option, instead favouring a property system based on capital values.

[34] Other similarly novel suggestions offered by Victor Hewitt include a charge on satellite dishes or a licence for selling chewing gum to help with the clean up costs. However, he acknowledges that the latter suggestion would be conducive to problems with smuggling.

Summary Implications for Northern Ireland

- May have specific applicability to shortage of housing in Northern Ireland, since it could avoid developers 'sitting' on land / promote development;
- The positive features of a land-tax are consistent with the general progressiveness of a property based system;
- Collection could be difficult; owners (unlike properties) can move and it might be difficult to pursue payment from some landlords;
- Public may find it difficult to accept considerable upheaval involved in reform of this nature;
- Previous studies found that a capital value based property system was preferable.

7.10 Derelict Land Taxation

Measures that were introduced in the 1970s to provide better incentives for the re-use of empty property have not been entirely successful. It has been argued that, when faced with penal rates of tax, owners often found it easier to make the property derelict rather than bringing it back into use[35]. Lyons suggests that this is an important lesson and that a tax on previously developed land would present a possible solution to this problem.

Specifically, this tax would relate to derelict property and brownfield land. However, Lyons acknowledges a number of potential stumbling blocks in the implementation of this tax: defining, identifying and valuing the land would be a significant task. Furthermore, resultant revenue may not be very substantial, since most derelict land is worth comparatively little. Nonetheless, the purpose of the tax would primarily be the creation of proper incentives for re-use of land, not revenue creation. The Lyons Inquiry therefore recommends that the Government should:

> *"develop proposals for the taxation of derelict property and brownfield land and consult on those with stakeholders"*

Summary Implications for Northern Ireland

- As with land value taxation, could help address housing shortage;
- Revenue implications would be limited.

[35] "Lyons Inquiry into Local Government – Final Report", March 2007

APPENDIX 1: LYON'S INQUIRY – SUMMARY RECOMMENDATIONS

CHAPTER 7 – HOUSEHOLD TAXATION AND LOCAL CHARGES

7.1 Council tax should be retained as a source of revenue for local government. The option of change in the longer term to shift the balance towards other taxes and changes remains open.
7.2 While not the most urgent priority, the Government should conduct a revaluation of all domestic properties for council tax. Transitional arrangements to ensure households do not face steep tax increases from one year to the next should be considered at the point of revaluation.
7.3 Subsequent revaluations should take place regularly and automatically at intervals of no more than five years.
7.4 At the revaluation the Government should introduce new property bands at the top and bottom of the current structure. It could also consider the introduction of separate bands for Inner London to reflect the unique shape of the property market in that region and to reduce turbulence there.
7.5 The Government should ensure the grant system reflects realistic data on the number of student households exempt from council tax in their areas. This should be done in time to inform the forthcoming negotiations on three-year settlements.
7.6 Council tax benefit should be recognised as a rebate rather than a benefit, and re-named 'council tax rebate', to properly reflect its main purpose: adjusting households' liability to council tax.
7.7 The Government should build on recent efforts to streamline delivery of council tax rebates by adapting IT systems so that the Pension Service can act as a portal to rebates for all callers, regardless of Pension Credit eligibility.
7.8 Further improvements to the claims process should be pursued to allow the Pension Service to liaise directly with local authorities in processing rebate claims.
7.9 Ministers should examine the scope for data sharing between agencies to proactively deliver council tax rebates to those who are entitled, with a view to achieving a step-change in the take-up of council tax benefit.
7.10 The Government should increase the savings limits on council tax rebate eligibility to £50,000 for pensioners.
7.11 The Government should, over time, abolish the savings limit in council tax benefit for pensioners, so aligning council tax rebate thresholds with the criteria for eligibility to the Pension Credit.
7.12 The powers to trade and charge conferred on 'best value' authorities in the Local Government Act 2003 should be extended to all local authorities.
7.13 The Government should carefully consider the wider framework of charging powers for statutory and discretionary services, including in the light of the Audit Commission's work when published later this year.
7.14 The Government should take new powers to allow local authorities to charge for domestic waste collection, developed in close consultation with residents and other key stakeholders.

CHAPTER 8 – BUSINESS TAXATION

8.1 The RPI cap on the national level of business rates should be retained.
8.2 The existing national arrangements for business rates should be retained at present, but a new local flexibility to set a supplement on the current national business rate should be introduced.
8.3 Local supplementary powers should be designed in a way which can gain credibility with business and the wider community. The key issues to be considered are:

- the appropriate scale of the supplement. At the upper end, some Business Improvement Districts have levied supplements as high as four pence. A lower limit would provide less revenue and less flexibility, but might enable confidence in new arrangements to develop more gradually. In that situation, there might be a case for allowing a higher limit in some cases, subject to more stringent approval mechanisms;
- retention of revenue, where I believe all revenues should be retained locally;
- the right form of accountability to business taxpayers. The most obvious options are some form of voted approval or a statutory consultation process. On balance, I propose that there should be a requirement to consult local businesses, and the wider community, before introducing a supplement, with a clear proposal and timetable. Revenues from a supplement should be hypothecated to the purposes agreed through consultation;
- how to ensure that supplements contribute to, rather than detract from, the local economy. I propose that authorities should be required to make an assessment of the impact of the supplement on the local economy, and the potential economic benefits of the spending they propose to finance from the revenues generated;
- the authority by which supplements should be levied. I recommend that supplements should be levied by unitary authorities and metropolitan districts, and in London and areas with two-tier local government, a single rate should be set through agreement between the relevant authorities, with a joint plan for the use of revenues. Where arrangements develop for collaborative working between authorities elsewhere in the country, this could usefully include cooperating around supplements. Powers to introduce Business Improvement Districts should remain with shire districts and the London boroughs;
- whether authorities should have a degree of further flexibility over which sizes of business pay the levy, which I would support; and
- whether there should be a threshold below which small businesses do not pay the supplement.

8.4 The Government should reform and reduce the empty property relief by:

- retaining the existing 100 per cent relief for short-term empty property (up to three months);
- reducing the rate of empty property relief thereafter; and
- providing factories and warehouses with the same level of relief as other properties.

8.5 The Government should develop proposals for the taxation of derelict property and brownfield land and consult on those with stakeholders.
8.6 The Government should conduct a review of exemptions and reliefs to consider the scope for removing inappropriate subsidies and distortions, and to simplify the system.

8.7 If the Planning-gain Supplement is introduced, the Government should:

- design it primarily as a local revenue source, with a regional share of an appropriate scale, not as a national source which may or may not be allocated to authorities. It is imperative that a transparent and predictable link between local development and local resourcing exists if development is to take place, or incentive effects are to be realised; and
- consider whether in two-tier areas, it could be managed through plans jointly developed and implemented by county and district councils.

8.8 The Government should consult on the costs and benefits of providing a permissive power for local authorities to levy taxes on tourism, including a possible tax on accommodation, and whether local authorities would use such a power. It should use the results of that consultation to examine the case for extension of such powers to local authorities.

APPENDIX 2: Criteria Identified by "A Fairer Way", 2006

Category	High Importance	Medium Importance	Lower Importance
Macro-economic	Economic effects		
Fairness	Relationship to benefits system	Comprehensibility; transparency	
Assessment / Collection	Ease of assessment, collection and payment	Cost of assessment and collection	
Yield-related	Stability and predictability		Buoyancy
Accountability	Size of tax base	Identifiability as local tax	Balance of funding
Implementation	Transitional issues		

Source: "A Fairer Way", Report by the Local Government Finance Review Committee, Edinburgh, 2006, p.68

APPENDIX 3: The Two Basic Single Stage Models considered by the 1981 Green Paper

Two basic, single-stage models were considered:

- **Model 1**: A single stage tax administered / collected in conjunction with VAT on behalf of local authorities. This would apply to all transactions subject to VAT, but local authorities would be given freedom to set the rate of tax (possibly within pre-defined limits).
- **Model 2**: A single stage tax with an entirely separate system of collection administered / set by local authorities themselves. The eligibility of goods / services might be decided either centrally or locally.