Increasing Taxes on Wealth. Lessons from the Welsh government reforms of Council Tax

Other

Increasing Taxes on Wealth

Lessons from the Welsh government reforms of Council Tax

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Introduction

Reducing wealth inequality is an important theme of the IPPR's Commission on Economic Justice. This report notes that: 'Wealth inequalities are worsening, and are a particular source of injustice, since wealth is often not earned, but instead either inherited or the result of rising asset values, unrelated to effort. Many of the causes of such inequalities, particularly rising house prices also serve to undermine prosperity'.[1] The IPPR Commission on Economic Justice highlights that wealth is much more unequally spread than income in the UK. For example, the median (mid-point) income of the richest 10% of the population is about seven times the median of the poorest 10% of the population. In contrast, the median wealth of the

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[1] IPPR Commission on Economic Justice (2018) *Prosperity and Justice. A Plan for the New Economy. The Final Report of the IPPR Commission on Economic Justice*, at p187. At https://www.ippr.org/files/2018-08/1535639099_prosperity-and-justice-ippr-2018.pdf, accessed 5/3/2019.

wealthiest 10% is 315 times greater than the poorest 10%. These statistics are echoed in other national and international research.[2]

There is much policy interest on the different ways of reducing this wealth gap. One strand of this focuses on spreading wealth throughout society through policies like the establishment of a Citizens' Wealth Fund.[3] Another strand, which can be combined with the above, concentrates on taxing wealth more heavily. Wealth can be taxed in many different ways. Taxes might be imposed on stocks of wealth (such as a land value tax), transfers of wealth (such as inheritance tax) or the gains to wealth (such as a capital gains tax).

There are lots of credible proposals for increasing the taxes on wealth.[4] The challenge is not so much adding to this vast array of ideas for taxing wealth but to turn rhetoric into reality.

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[2] For example, see Hills, J., Bastagli, F., Cowell, F., Glennerster, H., Karagiannaki, E. and McKnight, A. (2013) *Wealth in the UK. Distribution, Accumulation and Policy*, Oxford: Oxford University Press; Piketty, T. (2014) *Capital in the 21st century*, Harvard University Press: Cambridge, Mass; Intergenerational Commission (2018) *A New Generational Contract. The final report of the Intergenerational Commission*, at https://www.intergencommission.org/wp-content/uploads/2018/05/A-New-Generational-Contract-Full-PDF.pdf, accessed 10/5/2018.

[3] IPPR Commission on Economic Justice 2018; Intergenerational Commission 2018.

[4] For example, Mirrlees, J., Adam, S., Besley, T., Blundell, R., Bond, S., Chote, R., Gammie, M., Johnson, P., Myles, G. and Poterba, J. (eds.) (2011), *Tax by Design*, at https://www.ifs.org.uk/docs/taxbydesign.pdf, pp.368 - 405 accessed 25/3/2019; Boadway, R., Chamberlain, E. and Emmerson, C. (2011), *Taxation of Wealth and Wealth Transfers*, at

However, a commonplace in tax policy is that it is very difficult to increase taxes on wealth. There is a simple idea at the heart of this, namely that the 'losers' from any reform will campaign much more strongly against change than the 'winners' will lobby in favour of tax rises. Elected politicians are very reluctant to prompt a backlash so there is a bias to stick to the status quo.

Therefore, taxing wealth is not easy in the current political climate. However, this article suggests that there should not be a counsel of despair. Examples exist where politicians have seemingly prevailed against the odds. This paper examines one such case, that is the Welsh government revaluation of Council Tax in 2005.[5] The IPPR Commission on Economic Justice highlights rising property prices as a key factor behind widening wealth inequality in the UK. Examining the Welsh government example is therefore interesting because it concerns the taxation of property.

The Welsh government reform

Council Tax is the main tax on property in the UK and was introduced in 1993 and based on property values on 1st April 1991. Properties are placed in one of eight bands labelled A to H, depending on their value relative to other properties in the area, with A representing the lowest value, and H the highest. Council Tax bills are set as fixed multiples of the band D

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https://www.ifs.org.uk/uploads/mirrleesreview/dimensions/ch8.pdf, accessed 26/3/2019; IPPR Commission on Economic Justice 2018; Intergenerational Commission 2018.

[5] I have explored this Welsh government reform in greater detail elsewhere. See Prabhakar, R. (2016), 'How did the Welsh government manage to reform Council Tax in 2005?', *Public Money and Management*, 36(6), 417-424.

Council Tax bill. Central government fixes the ratios used in Council Tax bills and the local authority sets the band D Council Tax bill. For example, band A properties pay two thirds of the band D Council Tax bill and band H properties pay twice as much as a band D Council Tax bill. There is also a 25% discount on Council Tax bills for sole occupancy and discounts are also available for second homes.[6]

Council Tax has a number of well-known defects and repeated calls have been made for it to be reformed.[7] For example, it is based on property values that are around 30 years out of date. As a result, it is very regressive since tax bands do not match up with actual property values: Council Tax bills for band H properties are three times higher than band A properties despite the former being many more times the value of the latter. Furthermore, the 25% discount for sole occupancy provides incentives for the inefficient use of the existing housing stock.

In 2000, the Welsh government announced plans to reform local government finance. The Welsh government set up a Council Tax Revaluation Working Group to advise on the policy options and ran several public consultations on the different options. Following these consultations, the Welsh government introduced a new 'band I' for the highest value properties and revalued properties based on their value on 1st April 2003.[8]

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[6] Adam, S. and Brown, J. (2012), *Reforming Council Tax Benefit. IFS Commentary C123*, at https://www.ifs.org.uk/comms/comm123.pdf, at 7/3/2019.

[7] Mirrlees et al. 2011.

[8] Prabhakar 2016.

Tables 1 and 2 below show the effects of the 2005 revaluation on the numbers of properties in the different bands. Table 1 reports the Council Tax bands before and after the revaluation and Table 2 shows the numbers of properties in Wales in the different Council Tax bands before and after the revaluation. The second column of Table 2 shows the number of properties in each band following revaluation.[9]

Table 1: Council Tax bands in Wales

CT band	Property values £, Wales, (1993)	Property values £ Wales, (2005)
A	Under 30,000	Under 44,000
B	30,001 to 39,000	44,001 to 65,000
C	39,001 to 51,000	65,001 to 91,000
D	50,001 to 66,000	91,001 to 123,000
E	66,001 to 90,000	123,001 to 162,000
F	90,001 to 120,000	162,001 to 223,000
G	120,001 to 240,000	223,001 to 324,000
H	240,001 and above	324,001 to 424,001
I	N/A	424,001 and above

Table 2: Number of properties in different Council Tax bands in Wales

CT band	1993 list	2005 list
A	255,840	199,480
B	325,900	284,490
C	265,000	289,030
D	200,520	206,120
E	164,120	168,260
F	64,450	103,280
G	38,250	49,190
H	3,390	12,050
I	N/A	5,550

[9] Valuation Office Agency, (2015). *Council Tax Band changes due to 2005 revaluation in Wales*, at https://www.gov.uk/government/publications/properties-changing-council-tax-band-as-a-result-of-the-2005-revaluation-in-wales, accessed 7/3/2019.

The Welsh government predicted that 50% of properties would stay in the same band, 25% of properties would drop down the bands and 25% of properties would rise up the bands. However, four times as many properties moved up bands than fell down bands after the revaluation. A tax is usually understood to be progressive if the average tax rate increases as the tax base rises.[10] For Council Tax, the tax base refers to the value of the property. The Welsh revaluation made Council Tax less regressive, although there are important caveats. For example, Council Tax is paid by those people that own or rent a home. If a renter rather than a landlord pays the Council Tax, then the overall effect on progressive reforms may be ambiguous. The Welsh government introduced a three year transitional relief scheme to provide financial support for those properties that moved bands during the revaluation.[11]

The revaluation prompted a backlash among politicians and in the media who decried that the reforms created swathes of losers. A further revaluation in Wales planned for 2015 was called off and Westminster politicians cited the Welsh reforms as a reason for avoiding a revaluation in England. In 2010, the Secretary of State for Communities and Local Government for the Conservative Liberal Democrat coalition government Eric Pickles stated that: 'We've confirmed that English taxpayers will not face an unwanted council tax

[10] Mirrlees et al. 2011, p24.

[11] Welsh government (2018), Council Tax Revaluation letter, at https://gov.wales/sites/default/files/publications/2019-01/181102atisn12695lttr.pdf, accessed 26/3/2019.

revaluation hike … The [Welsh] 2005 revaluation showed how this tax exercise was used as an excuse to push up bills for hard-working families and pensioners'.[12]

Lessons from the reform

The Welsh government reforms of Council Tax in 2005 might be thought to be a strange example to cite when considering the feasibility of taxing wealth. Tax policy experts often prefer to abolish Council Tax altogether and replace it with an alternative tax.[13] The Welsh reforms were also modest and further progress seems to have stalled in Wales. Nevertheless, the Welsh example is instructive as it shows that policy reform is possible. The Welsh government did oversee a revaluation and introduce a new band to Council Tax. However, there are also grounds for building on or improving these reforms. Sir James Mirrlees chaired a high-profile review of the tax system that made a strong case for replacing Council Tax altogether with a Housing Services Tax.[14] A Housing Services Tax recognises that housing is a consumption good as well as an asset as householders consume housing services such as shelter and warmth. A Housing Services Tax is a type of Value Added Tax for housing. There is also a case for a Land Value Tax.

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[12] Prabhakar 2016; Department for Communities and Local Government, (2010) *Standing up for Local Taxpayers: Welsh Council Tax revaluation cancelled*, at , https://www.gov.uk/government/news/standing-up-for-local-taxpayers-welsh-council-tax-revaluation-cancelled, accessed 7/3/2019.

[13] Mirrlees et al. 2011.

[14] Mirrlees et. al 2011.

More recent developments are occurring elsewhere in the UK. In Scotland, the SNP leader Nicola Sturgeon has pressed for progressive reforms to Council Tax.[15] The Scottish government and Convention of Scottish Local Authorities convened a Commission on Local Tax Reform to inform political and policy debates prior to reforms.[16]

The Commission on Local Taxation's chief recommendation of ending Council Tax has yet to be implemented. Critics accuse the Scottish government of introducing only very modest reforms so far and have questioned whether the changes are progressive.[17] However, the current minority SNP administration has pledged further reform to win the backing of the Scottish Green party for their 2019/2020 budget. The 2019/2020 budget states that the Scottish government endorses the view that the present system of Council Tax must end. The agreement with the Scottish Green party means that the government is committed to publishing legislation by the end of the parliament (to be carried forward to the next parliament).[18]

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[15] Sturgeon, N. (2016), *Making local taxation fairer*, at http://www.snp.org/making_local_taxation_fairer, accessed 7/3/2019.

[16] https://news.gov.scot/news/commission-on-local-tax-reform, accessed 7/3/2019.

[17] Campbell, A. (2016), *Scottish Government proposals for Council Tax reform*, at http://www.parliament.scot/ResearchBriefingsAndFactsheets/S4/SB_16-28_Scottish_Government_proposals_for_Council_Tax_reform.pdf, accessed 7/3/2019.

[18] Scottish Government (2018), *Scottish Budget 2019-2020*, at https://www.gov.scot/publications/scottish-budget-2019-20/, accessed 7/3/2019.

Perhaps, two main lessons might be drawn from the above. First, it seems important for government to communicate the complexity of reform. The calculus of winners and losers has often been used to understand blocks to tax policy reforms. However, winners and losers may not be easily defined. In the Welsh government reforms, critics were quick to define or frame winners as those properties that moved down bands and losers that moved up bands. However, winners might also include those properties that remained in the same band following the revaluation. If any Council Tax changes are not supposed to raise extra revenue but are instead aimed at moving towards a more progressive payment system, then properties that stay in the same band after revaluation might also be deemed winners because their Council Tax bills may be lower than they would be without revaluation. The majority of properties remained in the same band following the 2005 revaluation.

Second, political will seems to be important for enacting reforms. Just relying on statistics or data to convey the complexity of winners and losers is unlikely to be enough to effect change. Political leadership and making a political case for reform will probably also be important. This would involve shifting the debate to consider why reforms are progressive rather than focusing narrowly on winners and losers. Of course, there are many complicating factors such as the constraints imposed by the party system. The Conservative party has traditionally presented itself as a party of home-owners and so is likely to oppose reforms. As can be seen in the press reaction to the Welsh government revaluation there is likely also to be opposition in the right-wing media. Any reforms rest on politics as well as claims about economic justice.