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# The Balance of Local Authority Funding in Wales A Consultation Paper from the Welsh Assembly Government – A Response

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## Abstract

The consultation paper *The Balance of Local Authority Funding in Wales* was prepared in the context of concerns over the current level of the council tax and the potential implications of existing trends for future council tax levels. This article examines the current debate on the alternative methods of funding local government in response to this document. Following an introduction to the issues it briefly looks at the short term before coverage of general principles of taxation against which longer term alternative methods of funding local government can be compared. It also presents an international picture in terms of funding local government in a number of countries to widen the potential debate for readers. After an examination in detail of each of the alternatives to the council tax seen as viable in the UK its conclusions attempt to assess the way forward in terms of funding local government expenditure. In these conclusions it is suggested that both the current structure of local government in Wales and the functions discharged by local authorities place burdens on the council tax which it is incapable of bearing. As such the role and functions of local government in Wales are in need of review as well as the financing of local government in Wales. Finally it takes the view that unless a solution to the current funding dilemma of local government is found this issue will not go away.

## Introduction

The consultation document, *The Balance of Local Authority Funding in Wales*, (National Assembly for Wales, 2004) was prepared in the context of concerns over the level of the council tax and the potential implications of existing trends for future council tax levels. This is consistent with the increased spending burdens which have fallen on local government and thus on council taxpayers. Nationally over the period 1998/99 to 2003/04 central government current expenditure rose by 32% with an increase in its total tax take of 26%. Over the same period local government current expenditure rose by 33% and the Council Tax by 51% (Travers, 2003, 22). In this context it is perhaps not the burden of council tax *per se* that is the problem but a general view that council tax is having to carry burdens for which it is simply incapable of bearing. These burdens are seen as falling on too narrow a base given central control over the business rate and the existing level of central government grant paid from national taxation. In Wales, however, council taxes are below those in England and the majority of properties fall into the lower bands B and C. It should be remembered that even a relatively small increase in council tax in the next budget year is based on a higher base figure than earlier years due to previous above inflation increases in the council tax. Thus it is the total amount that council taxpayers have to pay which tends to concentrate the mind and not whether the increase is set out in real terms or not or comparable or otherwise with England. This is seen as the cause of the problem as these increases are seen by council tax payers as being beyond their ability to pay and the tax is highly visible. This is especially true for those on fixed incomes. This view may well be emphasised in terms of the public perception of the general burden of UK taxation at present.

This article attempts to assess the implications of alternatives to council tax by commenting on the advantages and disadvantages of the potential alternative methods of financing local government. The response examines the alternatives to the present system and considers short and long term long timescales. It includes a brief examination of local government financing in a number of countries.

## The problem

Some of the key issues for any review of local authority finance are basically concerned with where money is being spent, how much is spent in those areas and, how to fund that expenditure. A potential problem for the review is that by concentrating on the balance of funding it is potentially ignoring issues over how and where money is being spent. In this context the structure of local government in Wales is important as one of the areas referred to by the consultation report is

'continuous improvement in service and efficiency' (National Assembly for Wales, 2004, 41). If at the macro level the structure of local government is inefficient, whatever is done in terms of funding is compromised. The current structure of local government in Wales was created prior to the Assembly coming into being and one wonders therefore whether this structure is consistent with the better government of Wales and reflects the continuing and future needs of Wales. While this maybe beyond the scope of the consultation it is an important issue. Twenty two local authorities is suggestive of inefficiency with considerable potential for the duplication of costs and an inability to take a truly strategic view for the benefit of the communities served. It is this structure with the revenue support grant accounting for a large proportion of local authority revenue expenditure that adds to the council tax burden as relatively small changes in the distribution of government grants have a major impact on the level of council tax in a particularly local authority through the gearing effect. This perhaps helps explain the debate over issues such as the deprivation grant and extra money provided for the elderly services recently announced by the Welsh Assembly Government. Larger local authorities (as with the old counties) have a greater ability to absorb changes in RSG where there is a loss of grant. This thus focuses attention on relatively marginal changes in the total grant available and its distribution when grant movements are announced. In addition certain initiatives by the Welsh Assembly Government, as with the recent report on community councils in Wales (National Assembly for Wales, 2003), are suggestive of greater powers for this tier of government. If these recommendations are adopted this will have a potential knock on effect on council tax as they are unlikely to be cost neutral as someone will have to pay unless equivalent efficiency gains can be found.

### Short term

In the short term it would appear that the avenues open to local government to limit council tax rises are those traditional tools of finance which are broadly to reduce expenditure, be more efficient, or, raise additional income from fees and charges. There is inevitably limited scope in these areas but they involve difficult choices as some services that may currently be free are provided to vulnerable groups or, where charges exist, these groups or individuals are unable to afford any increase. Other services such as leisure operate in a market place and as such increased charges may actually result in a loss of income to an authority as demand falls.

Under Section 76 of the Local Government Act 2003, a power exists where:

*'a person who is liable to pay council tax in respect of any chargeable dwelling and any day, the billing authority for the area in which the dwelling is situated may reduce the amount which he is liable to pay as respects the dwelling and the day to such an extent as it thinks fit'.*

This power appears to cover the ability to reduce to nil such a charge and possibly could be applied to a particular case or class of cases.

In Wales unitary authority status means that it as a local authority is the tax setting and billing authority this simplifies any complications that exist with two tier local government as in England. If such a power were exercised (to say, help individuals over 65) this would mean additional burdens falling on others since the authority must balance its budget. It is understood that legal opinion on this option has been sought in England and it may not be possible to use it to protect fixed income groups such as pensioners as any such decision could be subject to legal challenge by other groups who felt themselves in similar circumstances but ignored.

In addition the Local Government Act 2003 also extends powers in relation to charging and trading (Sec 93 to 98) and it may be possible for councils to consider potential sources of supplementary income. This ability to raise revenue must vary significantly by authority, and again in the Welsh context, will probably be related to size in terms of the ability to generate extra income.

Finally some of the alternatives to Council Tax (or sources of supplementary revenue alongside Council Tax) discussed later could also be implemented more quickly than others.

In the short term therefore options are limited. The exercise of capping powers may reduce expenditure but the Assembly would then be interfering directly in local decision making. This could be interpreted as not within the spirit of partnership and has obvious implications for democratic decision making at the local level although it remains an option.

### General Principles of Taxation

In assessing any method of financing local government that involves a potentially new tax, it is important to consider the key principles on which such a tax should be based.

Table 1 shows key principles that any tax should have. Other sources than those quoted by Tayib could be given but essentially similar principles would be expressed.

**Table 1 - General Principles of Taxation**

Principles	Attributed to	Context
Equity, Certainty, Convenience of payment and Economy in Collection	Adam Smith	Principles of a taxation system
Accountability, Fairness between individuals and areas, Efficiency, Stability, Flexibility and Comprehensibility, Local and paid directly	Layfield Report	Requirements of a financial system/tax system
Incentive and economic efficiency, distributional effect, International aspects, Simplicity and costs of administration and compliance, flexibility and stability, limit transitional problems, Fairness	Meade Report	Considerations in creating/revising a tax structure
Practicality, Fairness, Accountability, Cost of Administration, Fiscal dimension, Financial Control	HMSO (Green Paper), 1981	Features of a local tax system
Equity, Efficiency, Simplicity, Low Administration and Compliance Costs	O'Brien Report	Criteria for the tax system
Administratively feasible, Economic, Efficient, Equitable and Accountability	Ridge and Smith	Criteria for a local tax
Equity or fairness, Certainty, Convenience of payment, Economy in collection and compliance, Transparent and easy to understand, Minimise economic distortion	Jackson	Characteristics of an efficient tax system

(Source: adopted from Tayib, 1998, 140 )

In addition to the above points on individual taxes any tax also has to be affordable by the individual when viewed holistically in the complex picture that is UK taxation today. It also has to be capable of funding the expenditure required from it without that burden becoming excessive. Since the Municipal Corporations Act 1835 local authorities have had to balance their budgets and there is no scope for deficit financing (Coombs and Edwards, 1996, 30) This provision (with others on debt repayment) accounts for the financial stability of UK local government but compounds the problem of the burden on the council tax.

As stated in the introduction it could be argued that one of the key problems of council tax is that it has reached (or in some opinions exceeded) the maximum level tolerable when viewed in the totality of the tax burden. In this context and, again as indicated earlier, while the distribution of the tax burden is different from the old domestic rates system, it is likely that lower income households

(especially where that income is fixed) are now paying a larger proportion of their earnings than under that system.

### **An International Picture**

This section attempts to present some comparatives to compare the UK with other countries in terms of the funding of local authorities. Summary graphs are attached of the methods used to fund local government in the UK (Appendix A) and various countries for locally controlled resources (Appendix B). The countries were selected to show the range of methods used to fund local government around the world and are discussed later in this section in more detail in an attempt to inform the debate.

There are obviously considerable dangers in just making simple comparisons between countries as the range of services, for example, differs even if provided by seemingly comparable local authorities in different countries. There is also variation even within countries. In the UK, for example, in addition to single tier and two tier local government there are differences between the services provided between authorities in Wales and Northern Ireland. The City of Belfast, serving a population of approximately 300,000, spent £93,784,165 in 1999/2000 providing a much more limited range of services ([HYPERLINK "http://www.belfastcity.gov.uk" www.belfastcity.gov.uk](http://www.belfastcity.gov.uk)) than Cardiff which is broadly comparable in population terms. It is also the case that funding problems are not confined to the UK. In Germany many local governments are seen as in 'dire straits'. The German Federal government has therefore launched Agenda 2010 in an attempt to improve the financial situation of local authorities ([www.citymayors.com](http://www.citymayors.com)). Even where it appears that local government has its own tax raising powers (see Appendix C) the central government can step in to control what it considers to be the unacceptable macro economic consequences of local decisions. In Sweden during the 1990s the central government was forced to step in to control the local income tax raising powers of Swedish local authorities. In this context one of the alternatives presented in the consultation paper of local income tax, while superficially attractive may not stand up on closer scrutiny.

In this context the following summary is given to illustrate the funding of local government in the selected countries:

#### **Australia**

Property tax supplemented by fees and charges. There are specific grants although the majority of expenditure is financed locally.

#### **Denmark**

Counties and local authorities exist and share 10% and 41% of net public expenditure respectively. In principle both levels are free to determine their own standards of service and tax levels but discussions are held yearly with central government to fix 'voluntarily' expenditure and taxation levels. There appears general compliance with these guidelines although presumably if they were ignored the central government would be required to act.

#### **Canada**

Property taxes are the major source of revenue (58%) for local government within a balanced budget requirement. Non tax revenues are 26% and 16% from transfers from higher governments. There have been severe pressures on local government in Canada not to increase property taxes in recent years. This has been coupled with the downloading of responsibility from the central government and a consequent increase in fiscal pressure. Financial responsibility is seen as obscured.

### **Estonia**

Approximately 60% of local authority revenues comes from taking 56% of the central government revenue raised from income tax. The balance is local taxes (land, motor vehicles, boats and animals), non-tax revenues and government grants (23%). Sales taxes are a possibility but municipalities seem not to have imposed them.

### **France**

Finance is raised by the 'tax professionnelle' levied on businesses and liberal professions (50%), the 'foncier bati' levied on a building's owner (26%), the foncier non-bati levied on undeveloped urban land, agricultural land and forests (2%) and the taxe d'habitation levied on the rental value of dwellings (22%). A balanced budget is required by law with taxes collected and redistributed by the national tax office. Regions are also financed by indirect taxes on electricity consumption, vehicle registrations and property transfers. Departments are financed by motor vehicle taxes and land registration fees and taxes.

### **Germany**

On the surface local authorities appear to have the constitutional right to financial freedom. In practice they are regulated by the region (Land). Reliance at the local authority level on local taxes has diminished in favour of a share of income tax from the Federal government and motor vehicle taxes from the Land. Local authorities collect a business tax (40% to the Land) and land tax. There are also taxes or fees on dogs, hunting, public houses and entertainment. One third of local authority income comes from their own direct taxes, 20% from fees and charges and the rest by transfers from higher authorities. Bases for business and land taxes are decided locally and tax levels vary considerably between authorities.

### **Hungary**

Approximately 40% of the centrally collected personal income tax is transferred to local governments. Interestingly 38% goes to the place of income generation and 62% to take into account local tax raising potential. Local taxes have grown in importance since 1990 with the local business tax accounting for on average 84% of local tax revenues.

### **Malaysia**

Malaysia relies on property taxes, central government grants and charges for local services. The central government is attempting to make local authorities raise more funds locally but there is a major problem with the collection of income with some authorities having property tax arrears significantly in excess of annual revenue. Authorities are small scale in comparison to the UK.

### **Netherlands**

Considerably local freedom existed in the past but now revenues are raised centrally through a 'municipal fund' to spread the tax burden equitably due to the varying resources of local authorities. The principle direct local tax is on property based on market values reassessed every four years. This form of direct local taxation only accounts for about 8% of revenue. Approximately 50% comes in a block grant and 30% from the municipal fund established out of national taxation with the rest from fees and charges and minor taxes like on, for example, tourists and dogs.

### **Sweden**

Prior to 1990 rates of local tax were entirely set at the local level. The local tax is seen as regressive as its burden on local citizens is roughly twice the national income tax. It also includes a property element. Over 60% of county revenue comes from income tax and 40% of municipality income is from the same source. The balance of revenue comes from the State in a block grant or

reimbursement for State activities managed locally and from fees and charges. In the 1990s the state was forced to control local taxes because of the macro economic effects on government employment policies.

### **Switzerland**

Cantons and local authorities set their own rates of taxation but there are various mechanisms to redistribute funds from richer to poorer cantons and local authorities. Revenues are mostly from income and wealth taxes, estate duties and fees.

### **United States**

Local government in the US is a creature of each state and outside the control of the federal government. The majority of states limit levels of local property taxes and some also limit local sales, income and other taxes. Major sources of income are property taxes, sales taxes, alcohol and tobacco taxes, fuel taxes and income taxes. Nearly all local governments charge a property tax and most cities a sales tax. Other taxes are usually found only in large cities. Some counties have taxes on the extraction of natural resources where such resources exist. To take just one example, in Maine 44% of local authority income is from taxes on property, 30% on corporate and personal income tax and 26% from a sales tax.

In conclusion the general picture is broadly that the UK is unique in terms of its heavy dependence on a property tax to fund local authority expenditure although property taxes are important in other parts of the world.

### **The Alternatives**

While the following detail reviews the advantages and disadvantages of the alternative methods of financing local government expenditure, a combination of funding methods is possible.

#### **Local/Property Tax (Council Tax)**

In terms of arguments for council tax, the yield is easily calculated as it depends on the physical location of immovable property and the tax is easy to understand although the total funding package for local government is far from clear to the average individual and this affects the democratic deficit. In the UK there has been a long history of local property taxes in various forms (Cannan, 1927) and this creates legal precedent and administrative experience. Evasion is extremely difficult and property cannot be moved to cheaper tax areas for avoidance purposes and administrative costs are not excessive in relation to the yield. The council tax is certainly perceptible as is evidenced by the size of recent protests and the capital value of a property is equally part of an individual's total wealth as is income. This visibility aids to accountability. Unlike local income tax there are limited issues of confidentiality of the taxpayer's private affairs as there is no declaration of income unless council tax discount is claimed. The council tax banding brings in an element of progression as capital is as stated above equally a definition of wealth as income. To some extent it promotes 'economic efficiency' as householders could 'trade down' to cheaper property especially if they are single or children have left home. Bills can be reduced by discounts (e.g. one person occupancy), benefits (low income) and disability. Exemption is also available. Full council tax could be levied on second homes and, as has already happened in Wales, it is possible to increase the number of valuation bands. The revenue base is supported by the revenue support grant for burdens the tax cannot bear although the lack of buoyancy in council tax is a further advantage as it may force local councils to be efficient if the alternative is too high a council tax. A charge could be taken on a property for unpaid council tax. Finally the Local Government Committee of the Scottish Parliament in its report (2002) on Local Government Finance in Scotland felt that Council Tax is sound but recommended revaluation in Scotland's case.

Against this, however, the level of the tax is suggestive that it may have reached its limit in terms of affordability and ability to pay particularly for those on fixed incomes. The revaluation of property in Wales has already seen an increase of more than two council bands for many people living in property hot spots like Cardiff and indeed the Assembly government has had to protect these individuals against dramatic rises in bills further complicating accountability issues. It should also be remembered that the average bill per pound of property falls as the property value rises. As with arguments in the Layfield Committee the earning non householder who uses council services but does not directly contribute yet benefits. Commuters into a local authority area inevitably add costs to the area but do not pay for council services consumed. They do, however, add to general economic growth of an area with an impact on NNDR and pay national taxes an element of which is fed in to the revenue support grant. Social/qualitative factors contra the economic incentive to down trade housing. Capital tied up in property is not a liquid asset. The gearing adjustment given the high level of central support in Wales complicates accountability. The lack of buoyancy in the tax while it may prove an advantage in terms of encouraging efficiency is a disadvantage to councils.

### **Business Rate**

One possibility would be to return the business rate to local government control including the 'rating' of agricultural land. There seems general support from local authorities for the return of the business rate to local government and indeed this was recommended by the Scottish inquiry into local government finance. While the yield has apparently fallen over time it would provide an additional resource to the community where the industry is based. It would not be difficult to reintroduce in comparison with other alternatives such as Local Income Tax (discussed below) and would achieve a shift in the balance of funding of local government. It could establish/help the relationship between councils and business and in terms of relationships with private taxpayers has an impact on gearing as it provides an additional resource at the local level. Agriculture is a difficult issue but the economic case for exempting agricultural land should be examined and if the decision was that it should be rated it would provide an additional resource. A hybrid system is possible where there is some local impact on the rate level for a locally controlled element. Central government then sets the balance of the rate although this may complicate the system. Over time the level of central control could be reduced.

Against these arguments, however, is that an equalisation grant is needed as resources differ between local authorities. There may be resistance from local businesses to local control of the business rate but safeguards could be introduced. Different business rates could have an impact on investment location decisions. Its is less predictable than the current system and the return is linked with the impact of economic recession on potential yield. Certain types of businesses create extra costs which may not be reflected in the valuation or business rate paid. This includes, for example, takeaway food premises.

### **Local Income Tax (LIT)**

This would take the form of a locally variable income tax on all personal income and can thus potentially raise substantial sums of revenue for local authorities. It could enhance the accountability of local authorities by bearing on the inhabitants of the area concerned. By being related to the ability to pay it meets a fairness criteria and can feasibly be operated by the Inland Revenue making use of the PAYE system. Thus for some individuals it offers a potential reduction in the existing tax burden that council tax imposes. There could be possible efficiency savings if collected centrally by the Inland Revenue although this would have to be set against increased software, hardware and Inland Revenue staffing costs. It would also be possible to charge the tax at the point of residence and at a lower rate in the local authority in which the individual works although this could add major administrative complications.

As with all alternatives of funding local government there are disadvantages. It would add to the national tax burden for collection and assessment and the performance of the Inland Revenue over tax credits indicates that the Revenue might not be able to cope. The tax imposes a public and private compliance burden and raises issues over what is to be taxed as there are other tax schedules in addition to Schedule E. The tax should be broadly based to include income and salaries, pensions, fees, profits, dividends and interest. This would increase incentives to undertake avoidance which is particularly applicable to the self employed and the tax burden on so-called 'middle income' families would probably rise. In terms of accountability it would require special disclosure on pay slips if it was not to be hidden in the general tax burden to ensure accountability adding to set up costs. This would take time to implement and require new computer hardware and software and would be an extra overhead for employers. Such systems would be more complex where two tier government operates as it could create administrative and accountability difficulties. The resource base of local authorities would vary, requiring an equalisation scheme and general questions of hardship and welfare distribution could arise although as LIT is related to ability to pay at the lower income end, allowances would (could) protect individuals. This also raises issues over council tax benefits payable and currently managed by the Department of Social Security. The scheme could only go ahead if central government is willing to loosen control over one of its major economic levers, as LIT impacts on the central government's ability to undertake its macro economic management functions. Finally the income to the authority is probably not as predictable as with council tax.

### **Sales Tax**

This would consist of a locally variable sales tax that would be included in the price of goods. This tax, however, fails to meet the criteria of accountability and perceptibility. It would be part of VAT effectively and as this tax is seen as regressive it falls more heavily on poorer families. The growth of out of town shopping facilities would have a revenue impact as much shopping is no longer done locally (even increasingly through email). Large variations in the tax between authorities would distort economic decision making while a low tax rate would hardly be noticeable. There may be an EU regulatory issue in establishing such a tax.

To complete the picture a number of other possibilities are set out although they would probably raise relatively little income.

### **Congestion Charges**

Probably appropriate for consideration by cities where commuters come into that city in large numbers. It has potential environmental benefits but may distort business activity. Revenues have, apparently, been lower than anticipated in the case of London and businesses have claimed reduced takings over the previous year although there is a recognition that other factors were at play (Bell, 2003).

### **Motor Vehicle Duty**

Receipts retained locally either partially or fully. In effect the tax paid might be hidden in the price of the disc and not add to accountability. Non-motorists don't pay, and if it were possible to shop around motorists would buy a disc at the cheapest rate. Could provide an incentive to reduce tax evasion and abandon vehicles. Possible added burden on industry and commerce.

### **Pay Roll tax**

Cost to fall on employers but is a disincentive to employment and could vary by authority, acting as a disincentive to inward investment. Connection between employers and local authorities is provided by the business rate. This link would be strengthened if the business rate was within the control of local authorities.

## **Return to the Community Charge**

While it may have advantages as one tax within a package of taxes it has been tried and failed.

## **Low Yield Sources**

Includes tourist taxes, local lotteries, extending charging powers, local charges for Public Utilities Street Works and Environmental Taxes (e.g. plastic bag tax, fuel tax, green-field tax) While they may benefit local authorities, it would depend on the circumstances that each authority faced. Cardiff, for example, currently hosts numerous football finals but many will return to Wembley on completion of the new stadium and reduce demand for hotel beds. Yields are likely to be low and there would be administrative costs associated with each alternative. A fuel tax is likely to prove particularly unpopular given relatively recent events. Economic decisions may be distorted by such sources of income.

## **Service/Grant Changes**

It has been pointed out earlier in this article that a number of local authorities in Wales are relatively small and as such unable to absorb changes in the revenue support grant easily. While obviously a function of the last reorganisation of local government in Wales this comment is framed from a financial perspective rather than the political and community issues associated with this structure. In terms of population Merthyr with gross expenditure in 2002/03 of £147,688, 000 and revenue support grant of £52,081,000 (Merthyr Borough Council, 2003) is not significantly larger population wise than Barry Community Council (National Assembly for Wales, 2003). In addition increasingly major services such as education and social services are subject to the policies of central government but funded locally out of the revenue support grant allocation and other sources of funding and as such a case could be made to transfer these functions to central government. This would clearly reduce local authority expenditure (although the level of grants would fall) and hence have an impact on the Council Tax. This option was rejected in Scotland by the Committee of Inquiry. It would however potentially place accountability for local services at the local level and significantly reduce council tax.

A comparatively recent alternative has been suggested which aims to reduce the gearing effect but is only in the 'idea' stage. Essentially this would create a core grant to which an authority is entitled. On top of this there would be a variable element or 'top up' grant. This would, say, create a relationship such that a 5% increase in the councils budget would be met by a variable increase in the top up grant such that council tax rose by only 5% and not the geared effect as would exist currently. This is seen as improving accountability in that the spending decision is less opaque but against this the system generates uncertainty and it creates opportunity for authorities to spend more and drag in more of the variable element of the grant. This would not be popular with central government and may lead to strict capping (Freer, 2003). It is not seen as contributing to increased local accountability and adds to complexity.

## **Conclusions**

In the short term some relief for specific groups may be provided by the provisions of the Local Government Act 2003, but this needs time for the legal implications of that Act to become clearer. Also the present take up of council benefits is poor and encouragement could be given to relevant groups to claim their entitlement. A long term solution is however needed.

The early part of this article suggested that reform of the local government structure in Wales may provide savings to reduce the council tax burden. If central government also took on the burdens of national services like education and social services this would have the potential to significantly reduce local taxes, provide national and consistent standards of delivery, and be financed through national taxation which achieves equity through the progressive nature of mainly income tax. This

should enhance local accountability for locally provided services. There are obvious political issues to be addressed here but in term of funding would significantly reduce what was needed at the local level and thus potentially reduce council tax. As has been shown, it is the current level of council tax and the rate of increases therein which are the causes of the present debate and as such the problem could be significantly reduced or even eliminated by such a strategy.

The international comparison section of this article has shown that a variety of systems exist in different countries to fund local government. It would be dangerous to simply claim without detailed further analysis that one of these systems provides the answer to the UK's current dilemma. It was also shown that other countries have had problems with their funding structure. Table 1 shows that various 'cannons' of taxation exist and represent principles against which it is possible to measure the likely success or otherwise of a source of funding for local government. Local income tax meets many of these criteria but nevertheless its introduction would represent a significant political challenge to government as inevitably there would be gainers and losers, with the biggest losers probably being 'middle' income earners. It should also not be forgotten that council tax, by the measurement of property values, includes capital wealth which local income tax ignores. It seems, however, in the longer term that only LIT and council tax (in combination with the business rate) could realistically raise significant funds and at the same time achieve the majority, if not all of the taxation cannons outlined in this text. Indeed this was broadly the conclusion reached by the Scottish Inquiry into local government funding where Council Tax was seen as 'sound' but with a need for a new valuation (2002, para. x). Further work was suggested on LIT. In addition, that Report also recommended the return of the Business Rate to local government control (para., xii). This could be achieved relatively quickly and would mitigate the gearing effect of the current funding regime since currently councils are restricted to increasing the only source of revenue under their control. The revaluation of properties announced and to be implemented in Wales, however, has the potential to cloud accountability as a relief scheme to mitigate its effects from April 2005 has been announced.

In this article it is not council tax per se that is seen as the problem, it's the burden it is expected to carry. In the longer term it is felt, however, to be unrealistic to expect local authority services to expand or even remain at the present level and be funded locally. Thus council tax and local control of the business rate is seen as time limited. Either grants will continue to increase or another source of funding is needed. On the basis of the evidence, it is concluded that realistically the only alternative extra source is local income tax. This could either replace council tax or be part of a 'parcel' of local taxes potentially comprising council tax, local income tax and local control of the business rate. LIT in full or in part is not however a panacea and may complicate the central government's economic management of the economy. It thus needs further research. Local governments are not immune from funding crises where local income tax is a source of local revenue.

A sales tax is seen as having the potential to raise significant levels of new revenue but that potential is outweighed by its disadvantages particularly its regressive nature. Other alternatives such as tourist taxes provide the opportunity to raise revenues but not in sufficient volume to make a significant difference and the additional income potential would vary considerably between authorities. They may also distort taxpayer behaviour to an unacceptable extent and have associated administrative costs that would eat into any benefits. There would be variations between local authorities in their ability to raise such revenues and this could make the grant mechanism even more complex than it currently is. It is, however, recognised that a move to local income tax would have implications for the revenue support grant mechanisms in terms of unequal resources between authorities. This article and the Scottish Report is suggestive that the funding balance

between local and central government is insufficiently robust and that this adds to the democratic deficit. This is in part caused by the level of expenditure local authorities are required to incur rather than just deficiencies in the funding mechanisms.

Finally it is concluded that unless and until a solution to the council tax dilemma is found, the issue will not go away.

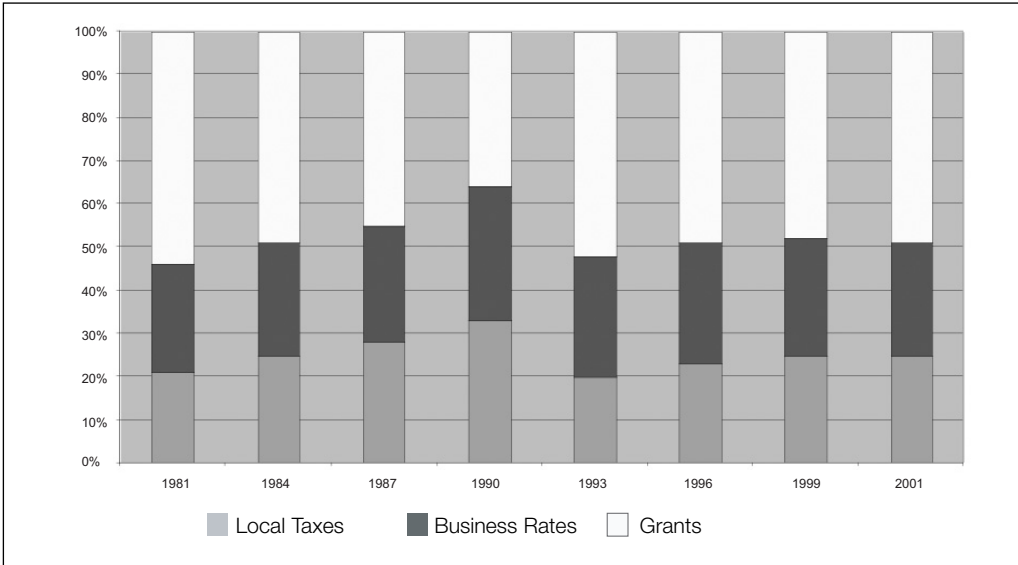
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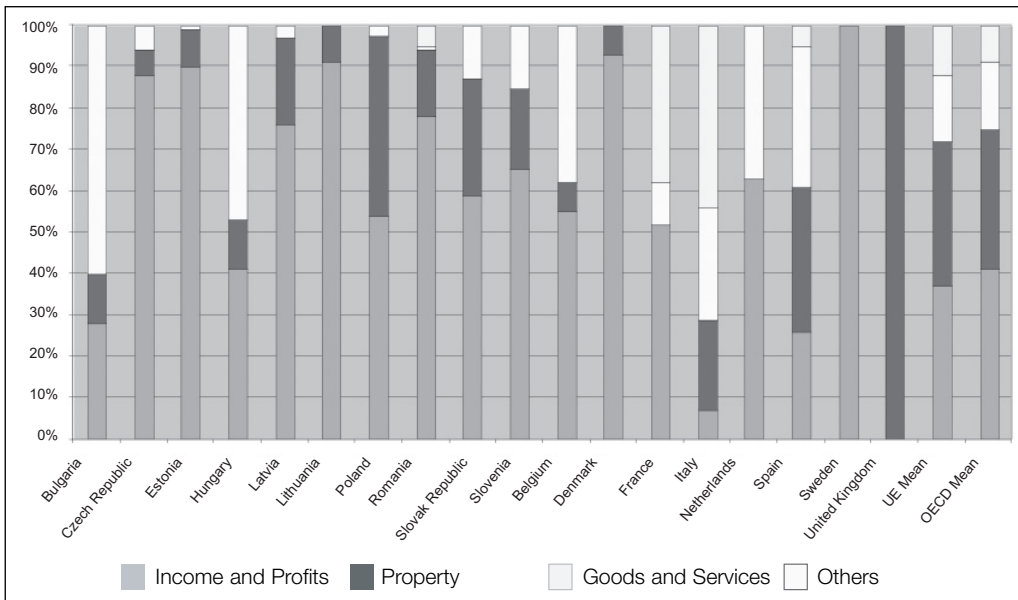
## Web sites

- HYPERLINK <http://www.belfastcity.gov.uk/corporateplan/profile.htm>
- <http://www.belfastcity.gov.uk/corporateplan/profile.htm>
- HYPERLINK [http://www.citymayors.com/news/german\\_tax1.html](http://www.citymayors.com/news/german_tax1.html)
- [http://www.citymayors.com/news/german\\_tax1.html](http://www.citymayors.com/news/german_tax1.html)
- HYPERLINK [http://www.oecd.org/document/37/0,2340,en\\_2649\\_34533\\_1907173\\_1\\_1\\_1\\_37427,00.html](http://www.oecd.org/document/37/0,2340,en_2649_34533_1907173_1_1_1_37427,00.html)

**Appendix A: Sources of Local Authority Finance 1981 to 2001 - Source: Wood (Adpted) 2003**



**Appendix B: Sources of Sub National Revenues - Source: www.OECD**



**Appendix C: The Local v Central Funding Balance - Source.OECD 1999 and 2001**

Level	Sub-national government taxes as % of total tax	SNG sets tax rate and base	SNG sets tax rate only	SNG sets tax base only	Revenue sharing where the CG;SNG revenue split...				CG sets both rate and tax base of SNG tax	Total
					...is set by SNG	...can be changed only if SNG agree	...is set in legislation and may be changed unilaterally by CG	...is set annually by CG as part of the budget		
		(a)	(b)	(c)	(d1)	(d2)	(d3)	(d4)	(e)	
Bulgaria (2000)	Local	10.0	-	-	-	-	39.0	61.0	-	100.0
Czech Republic (1999)	Local	11.1	5.6	-	-	-	91.7	-	-	100.0
Estonia (1999)	Local	16.2	9.2	-	-	-	90.8	-	-	100.0
Hungary (1999)	Local	10.4	49.2	-	-	-	-	50.8	-	100.0
Latvia (1999)	Local	17.1	-	-	-	-	-	-	100.0	100.0
Lithuania (1999)	Local	22.0	-	-	-	-	-	-	100.0	100.0
Poland (1999)	Local	8.3	-	41.9	0.6	-	57.6	-	-	100.0
Romania (2000)	Local	10.5	-	6.0	0.6	-	-	75.0	18.4	100.0
Slovak Republic (2000)	Local	4.0	7.0	28.2	-	-	-	64.8	-	100.0
Slovenia (2000)	Local	7.9	16.7	0.6	0.4	-	82.3	-	-	100.0
Mean (by country)	-	11.8	7.6	9.2	0.2	0.0	36.1	25.2	21.8	100.0
Belgium (1995)	Local	6.0	13.0	84.0	-	-	2.0	1.0	-	100.0
Communities		13.0	-	3.0	-	97.0	-	-	-	100.0
Regional		10.0	8.0	92.0	-	-	-	-	-	100.0
Denmark (1995)	Municipalities	22.0	-	96.0	-	-	4.0	-	-	100.0
Counties		9.0	-	93.0	-	-	-	-	7.0	100.0
Netherlands (1995)	Municipalities	1.0	-	100.0	-	-	-	-	-	100.0
Polder boards		1.0	-	100.0	-	-	-	-	-	100.0
Spain (1995)	Local	9.0	33.0	51.0	-	16.0	-	-	-	100.0
Regions		5.0	15.0	7.0	-	78.0	-	-	-	100.0
Sweden (1995)	Municipalities	22.0	4.0	96.0	-	-	-	-	-	100.0
Counties		11.0	-	100.0	-	-	-	-	-	100.0
United Kingdom (1995)	Local	4.0	-	100.0	-	-	-	-	-	100.0
Mean (by tier)	-	9.4	6.1	76.8	0.0	15.9	0.5	0.1	0.6	100.0