

Council Tax, Local Income Tax and The Myth of the Fireman and the Nurse **A Scottish Action Against Council Tax Report**

Over the past two years or so, there has been much talk, by those political parties opposed to the concept of local authority funding by local taxation under the principle of ability to pay, of Local Income Tax (LIT) being unfair to many households.

If memory serves, these scare tactics first received prominence when Charles Kennedy, the then leader of the Liberal Democrats and advocate of LIT, was confronted by the fact that the Council Tax/LIT “break-even-point” for a two adult household, in a band D property was that they each earned around £20,000 per annum. This imaginary couple were subsequently dubbed the **Fireman and Nurse**; the intended strong implication being that these household circumstances constitute some kind of average or norm, and consequently, normal households with a bit more income would be unfairly treated by LIT.

Things have moved on little in the past two years, and since we have more reliable published data for household income for 2005, our analysis is more exact for that period. Also, none of the basic principles has changed since then. Therefore, unless specifically stated otherwise, all calculations refer to 2004/05 data.

Let's now look at Scottish household income from two aspects:

1. How does the imaginary couple's income compare with that of other Scottish household incomes and can their income be regarded as some kind of norm? Or, if their income can't be regarded as typical of Scottish household incomes, what income level would be fairer to use as a benchmark figure?
2. How does this typical or benchmark household income stack up with a comparison of the relative impact of Council Tax and LIT?

Source of the Data on Scottish Household Net Incomes.

The statistical data used in this short study are taken from “Scotland's people”, Results from the **2005 Scottish Household Survey** (which is a Scottish Executive National Statistics Publication) – Tables 6.42/6.43 of which are to be found on Page 130 of:

<http://www.scotland.gov.uk/Resource/Doc/140387/0034518.pdf>

From the glossary of terms contained in Appendix 1 of the above, it would appear that the income bands quoted in the above referenced tables represent net annual household income. This, in terms of the survey data means the income, which might normally be called the combined “take home pay” of the main householder and partner (if any), but which excludes the income of any other household adults, except in so far as they may contribute “dig money” to the main householder. The first 2 columns of Table 1. have been extracted from the above referenced data.

Imaginary Couple's Net Annual Household Income.

In order to compare the imaginary couple's income with the statistical data, we have reduced gross incomes by amounts which we consider to be credible employee standard deductions. The applied deductions are income tax, employee national insurance contributions and a 5% gross pay, tax free pension contribution. In this way, the couple's £40,000 combined gross pay converted to net household annual income is calculated as £28,856. - see Table 2.

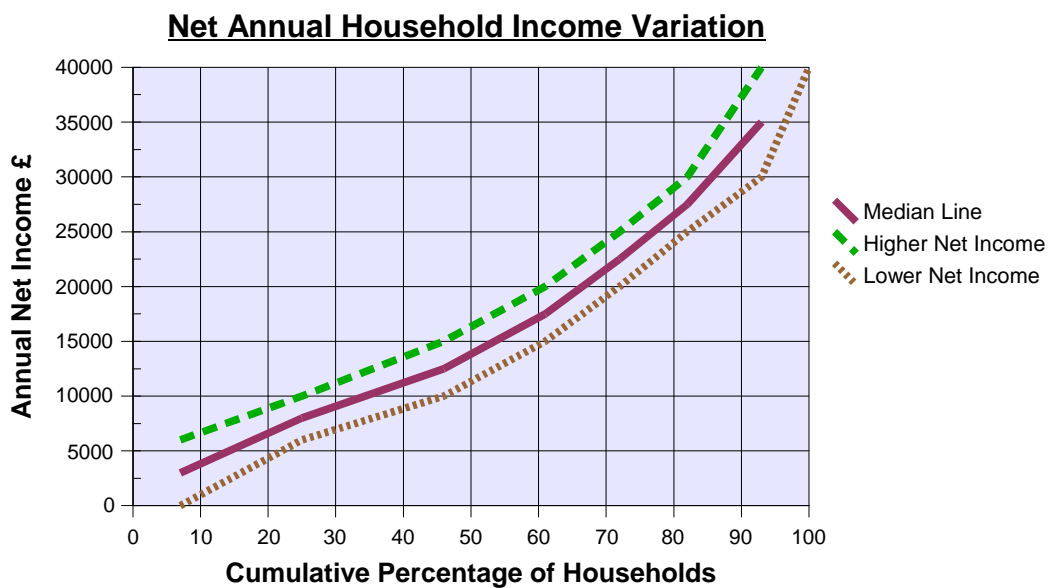
Table 1. Percentage of Households in Each Net Income Band

From 2005 Scottish Household Survey.

Net Income Band £	Percentage of All Households	Cumulative % of All Households
0 – 6,000	7	7
6,001 – 10,000	18	25
10,001 – 15,000	21	46
15,001 – 20,000	15	61
20,001 – 25,000	11	72
25,001 – 30,000	10	82
30,001 – 40,000	11	93
Over 40,000	7	100
Total	100	

Chart 1. - From Table 1. Data

The chart has been drawn to illustrate the upper and lower values of each net income band and also a median line. The upper and median net incomes are indeterminate for the over £40,000 band.



Observations from Statistical Data.

Reading from the median line on Chart 1, an income of £28,857 represents approximately 84%, indicating that about 16% of households have a higher net income.

Again, from the median line, 50% of all households appear to have a net annual income of approximately £13,500.

Clearly, we must recognise that the £40,000 gross annual household income of our imaginary couple in no way typifies Scottish household income, since they are in the top 16% of all households.

If we are to postulate that a net annual household income of £13,500 is typical, we would have difficulty in determining the tax liabilities without making assumptions as to the type of household and whether there are one or two wage earners. Since the widely quoted fireman and nurse scenario assumes a two adult household with no dependants and no savings, then we will do the same here. We will consider (see Table 2.) that the £13,500 may be made up of one wage earner with a gross income of £18,530 or two wage earners, each with a gross income of £7,833, both households contributing 5% of gross income towards a retirement pension. It is noted that £7,833 in 2004/2005 was fairly close to the minimum wage for full time employment.

Table 2. Household Income and Deductions - £

The table assumes income tax personal allowance, thresholds and tax rates for tax year 2004/2005.

Gross Annual Household Income	Tax Free Pension Payment	Taxable Pay	Starting Rate Tax	Standard Rate Tax	National Insurance	Net Annual Household Income
2 x 20,000	2,000	28,510.00	404.00	5,383.40	3,356.10	28,856.50
18,530.00	926.50	12,858.50	202.00	2,384.47	1,516.35	13,500.68
2 x 7,833	783.30	5,392.70	404.00	297.60	799.36	13,501.74

Table 3. Local Taxation Rates – LIT Applied to Basic and Higher Rate - £

Gross Annual Household Income	Taxable Pay	LIT at 3%	LIT at 4%	LIT at 4.5%	LIT at 5.35%	LIT at 6.5%
2 x 20,000	28,510.00	734	979	1101	1309	1590
18,530.00	12,858.50	325	434	488	580	705
2 x 7,833	5,392.70	41	54	61	72	88

Table 4. Council Tax for Glasgow 2004/2005. - £

Band A	Band B	Band C	Band D	Band E	Band F	Band G	Band H
790	922	1,053	1,185	1,448	1,712	1,975	2,370

Discussion

Burt (Ref. 1 – Section 10, para's. 46 & 47) uses, as an example when discussing LIT, modelling work carried out by Stirling University. This work estimates the amount of LIT required, under various scenarios, to remit the total council tax receipts in Scotland, including the Council Tax Benefits granted by Westminster. Of these, the most commonly quoted scenario by Scottish Labour is “6.5% applied to earned income subject to income tax at basic and higher rates”, payable in 2006/07.

Burt goes on to estimate, again presumably using 2006/07 tax data, the LIT payment for our notional couple (2 x £20,000 gross income) as £1,670 under 6.5% LIT. This figure is arrived at apparently without taking account of tax allowances beyond personal allowance. Is this notional, relatively well-off couple really contributing nothing towards their retirement pensions?

Table 3

The same incomes as in Table 2 are used in Table 3 to calculate LIT liabilities applied to earned income subject to income tax at basic and higher rates.

Of particular interest is the 5.35% rate as it represents approximately the same total remittance as the 6.5% rate, but assumes that Westminster would continue to contribute a grant roughly equal to the Council Tax Rebate grant which it pays at present.

Scottish Labour politicians, including the Finance Minister, are adamant that this would not be the case and that Westminster would cease to pay the 3% of total council funding that the Council Tax Rebate represents. If this punitive measure were indeed taken, it could be seen as vindictive in the extreme. An analogy exists here with recent statements regarding the Welsh Assembly which apparently is to be given additional legislative powers. Westminster would be required to approve any new or changed legislation. The Welsh Secretary, Peter Hain, when asked about a Westminster possible veto, said it would be very unlikely to be used as “we (Westminster) would be likely to reap a bitter harvest”.

Comparison of LIT and Council Tax.

Glasgow has been chosen for this comparison as it has one of the highest Council Tax rates, and it also contains some of the most deprived areas, in Scotland.

At the 5.35% LIT rate, the imaginary couple with the relatively high net household income of £28,856 would pay about £1,309 as opposed to Council Tax of £1,185 if in band D or £1,448 if in band E.

The much more representative couples with a net household income of £13,500 would pay, under all LIT scenarios in Table 3, less than Council Tax – even in band A.

Council Tax Rebate.

Neither couple with a net household income of £13,500 would qualify for Council Tax Rebate if occupying a property below band G.

Conclusions

1. The legendary fireman and nurse, having a net household income in the top 16% are in no way representative or typical of Scottish households. Any attempt to portray them as such, either implicitly, as has been widely done, or explicitly is a distortion of the truth. Even so, their income would correspond approximately to the break even point between 5.35% (6.5%) LIT and the Glasgow set Council Tax between band D and band E properties.
2. Approximately 50% of all Scottish households have a net household income of around £13,500. At this income, all Glasgow households would pay less under all rates of LIT considered in Table 3 than with Council Tax of any property value band.
3. Table 3 illustrates that LIT, being progressive, would much more closely reflect ability to pay than does Council Tax, which is regressive and as such discriminates against those on low incomes by subsidising the higher income households.
4. LIT automatically compensates for changes in income. For example, if the fireman or nurse were to stop earning for any reason, their reduced earnings would automatically be reflected by a proportionate reduction in LIT, whereas they would be required to pay exactly the same as before under Council Tax.

Ref. 1 – Sir Peter Burt and others. “A Fairer Way” 2006 Report by the Scottish Local Government Finance Review Committee.