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The third rail of British politics [1]

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The SNP government in Scotland has decided [3] it wants to replace council tax with a local income tax.

The problem is, their local income tax is not a local tax at all. Although its proceeds would be used to pay for local services, it would not be set or collected locally. Basically, three percent on income over the personal allowance would be added to a person?s usual tax bill. Aside from higher income taxes being precisely what nobody needs, this is hardly a recipe for increased local government accountability.

The problem with local government finance is that councils themselves raise less than 30 percent of the money they spend. Being so reliant on central government for funding makes local councils merely the agents of the centre. This means that there is no meaningful link between taxation, representation and spending. There is little incentive for efficiency, little accountability to voters, and little policy choice come election time. The reliance on central government funding has another nasty side effect: if a council needs more money, it has to raise council tax quite substantially to make a real difference to its budget. The SNP?s proposed reform addresses none of these issues.

There is another problem. Based on broad assumptions, the Scottish government says any household with an income of less than £58,000 would be better off. They may be right. But that means households earning more than £58,000 a year will end up paying more. This is the problem the Lib Dems encountered in the 2005 when they campaigned for a local income tax. A middle class couple, say a teacher married to a nurse, could easily end up worse off. That?s always bad politics.

What?s the solution? By happy coincidence, VAT raises almost the same amount of money as central government distributes to councils in grants. Replacing VAT with a local sales tax (set and collected locally) would be the simplest way of making councils self-financing, as Douglas Carswell argued in this [4] ASI paper. Of course, competition in policy is the essence of true localism, so we shouldn?t be too prescriptive. I?d tell local government they had three permissible sources of revenue - property taxes, sales taxes and service charges - and leave the rest up to them. If people started moving out, they would know they?d got something wrong.

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