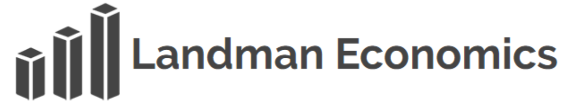

Raising taxes to deliver for Scotland

A report by Howard Reed, Landman Economics, commissioned by STUC

November 2023

Acknowledgements

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1. Introduction and Background

Landman Economics has been commissioned by the Scottish Trades Union Congress (STUC) to produce a new report exploring the options for increasing taxes in Scotland to fund investment in public services.

This is an update to the previous report in 2022, *Options for increasing tax in Scotland to fund investment in public services* (Reed 2022), which helped shape the debate around the 2023/24 Scottish Budget and led to a rise in the top rate of tax.

The 2023/24 Scottish Budget, which is due to be delivered in December 2023, and further Scottish Government legislation, provide an opportunity to introduce a package of progressive tax measures and begin a process of property and land valuations to kickstart a replacement for the Council Tax, and to reform business taxes.

With public services being stretched to breaking point, the need for investment has never been greater.

The structure of this report is as follows. Chapter 2 discusses potential increases in income tax over and above those announced in last year's Scottish Budget, including reductions in the top rate threshold and the introduction of a new tax band in between the current higher rate and top rate bands. Chapter 3 looks in detail at the flaws and inequities in the current Council Tax system and outlines an updated proposal to replace Council Tax with a tax based on an annual percentage levy on the value of each residential dwelling – the Proportional Property Tax. Chapter 4 makes the case for introducing taxes on wealth – specifically an annual wealth tax and land value tax (LVT). Chapter 5 discusses other potential taxes on businesses, land and property, and consumers with significant revenue-raising potential. Chapter 6 outlines a costed package of tax increases to raise more money for investment in public services, and Chapter 7 looks at the distributional and potential macroeconomic impacts of the tax package. Chapter 8 offers conclusions.

2 Income Tax

This chapter discusses the distributional effects of potential increases in income tax over and above those announced in the December 2022 Scottish Budget. This report models a range of reforms to income tax rates and thresholds, including reductions in the higher rate threshold and the introduction of a new tax band in between the current higher rate and top rate bands, as well as increasing the higher and top rates. Section 2.1 presents estimates of the revenue yield from these income tax increases, while Section 2.2 shows the distributional effects by household net income decile.

2.1 Estimated yield of selected income tax reforms

This report provides updated modelling of three reforms to the income tax system that were recommended in last year's report:

a) Reducing the higher rate threshold (HRT) for income tax from its current value of £43,662 to £40,000.
b) Increasing the higher rate and top rate of income tax by one penny. This means that the higher rate becomes 43% and the top rate (above £125,140) becomes 48%.
c) Introducing a new income tax band of 45% (i.e. 2 percentage points more than the higher rate) between the current higher rate and top rate thresholds (between £75,000 and £125,140 of taxable income).

In addition we also model one further reform:

d) Extending the new 45% band downwards so that income between £58,000 and £75,000 is taxed at 45% (as well as income above £75,000). This has been proposed by IPPR Scotland, Poverty Alliance, Oxfam Scotland and a number of other organisations[1].

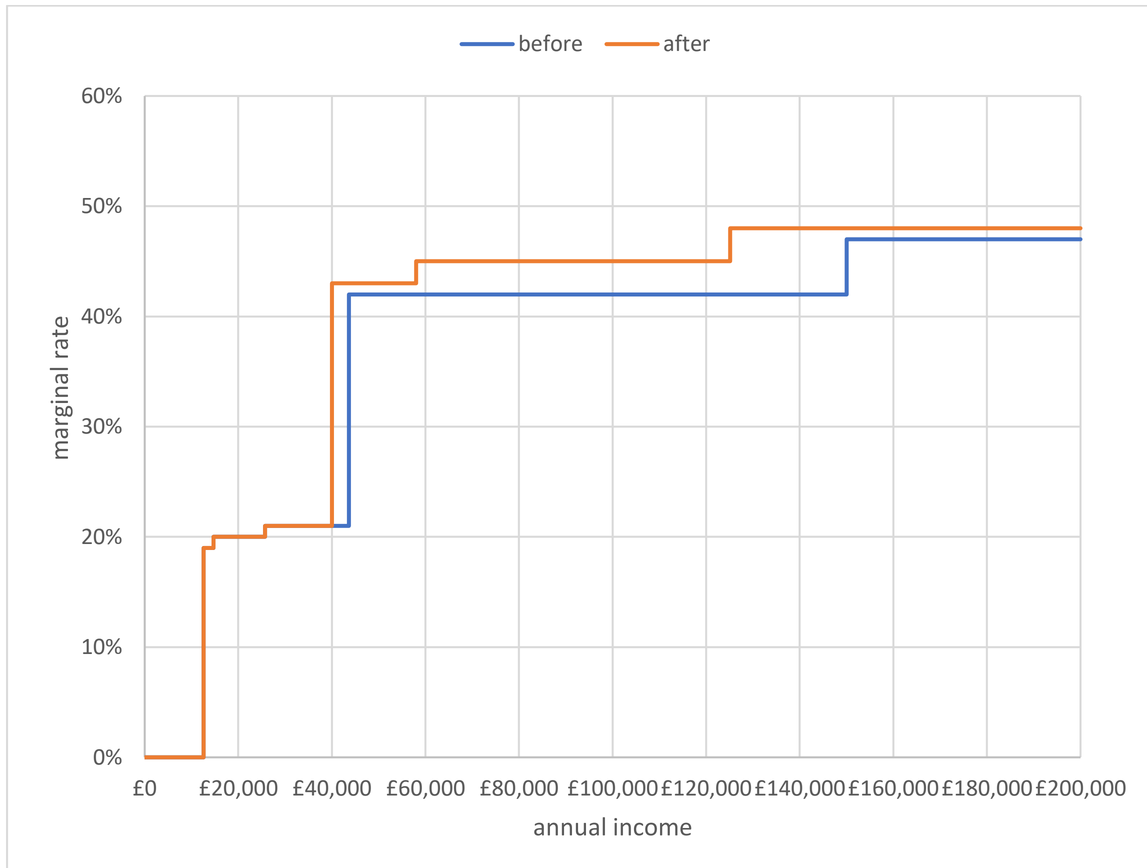
Note that these tax rates only apply to earned income and other income which is not from savings and dividends. Savings income in Scotland is taxed at rates that are set at the UK level.

Figure 2.1 below shows the proposed marginal rate schedule for income tax after these reforms (the red line), compared to the existing (2023/24) Scottish income tax marginal schedule (the blue line). For easy comparison, the reforms are modelled as if they had been introduced at the start of the current tax year (i.e. April 2023).

[1] See IPPR Scotland *et al* (2023).

The proposed reforms do not affect any Scottish taxpayer with income (excluding savings and dividend income) below £40,000[2].

Figure 2.1. Income tax marginal rate schedule before and after proposed reforms, using 2023/24 baseline



Source: author's calculations

Table 2.1 shows the estimated additional revenue arising from the proposed package of reforms to income tax, broken down by component. The estimates are produced using the Landman Economics tax-transfer model, with revenue yield forecasts from the Scottish government for changes to higher and top rate income tax (Scottish Government, 2023a) used to calibrate the model results to make them consistent with official estimates, which include adjustments for potential behavioural effects of tax increases, particularly at the top end of the distribution (for example,

[2] It is important to note that the marginal rate schedule in Figure 2.1 does not include employee (or self-employed) National Insurance contributions (NICs). Because the Upper Earnings Limit for NICs is set by the UK Government rather than the Scottish Government, there is currently a marginal rate of 54% (42% income tax plus 12% NICs) for employees in Scotland earning between £43,662 and £50,270, dropping to 44% (42% income tax plus 2% NICs) above the UEL. The recently announced cut in employee NICs to 10% reduces the combined marginal rate to 52% over this range. The reforms in this report would take the combined marginal rate back up to 53% over a slightly wider range (£40,000 to £50,270).

increased tax avoidance, and potential outward migration from Scotland)[3]. The size of these effects is inherently uncertain[4], but we have used the Scottish Government's own estimates of the behavioural effects of tax increases in the higher rate and top rates as a benchmark and estimated a potential behavioural response for our proposed new 45% income tax band between £75,000 and £125,140 by interpolation.

Table 2.1. Estimated additional annual revenue from increases to income tax

Reform	Additional revenue (£m)
Reduce higher rate threshold to £40,000	502
1p increase in higher rate (£40,000 to £125,140)	112
1p increase in top rate (above £125,140)	5
Introduce 45% band for incomes between £75,000 and £125,140	92
Widen 45% band so that it applies to incomes between £58,000 and £75,000	68
Total	779

Source: estimates from modelling using Landman Economics tax-transfer model, calibrated to estimates from Scottish Government (2023a).

Table 2.1 shows that the combined package of reforms raises just under £780 million annually. The largest revenue-raising measure is the reduction in the higher rate threshold, which raises just over £500 million. The increase in the higher rate of income tax raises just over £110 million, while the introduction of a 45% income tax band for incomes between £58,000 and £125,140 raises £160 million (£92 million plus £68 million). The annual revenue yield from the increase in the top rate of tax is relatively small, at £5 million. This is for two reasons: first, the number of Scottish taxpayers with incomes above £125,140 is relatively low, and second, the assumptions that the Scottish Government uses on "taxable income elasticity (TIE)" – the extent to which taxable income adjusts in response to an increase in tax rates – are that top incomes are relatively sensitive to increases in tax rates, and hence increases in rates on top incomes will raise relatively little.

[3] For a detailed discussion of the potential behavioural responses to Scottish tax policy diverging further from England, see the recent report by the Poverty and Inequality Commission (2023), in particular pages 16-17.
[4] As Scottish Deputy First Minister Shona Robison pointed out in a recent session of the Scottish Finance and Public Administration Committee, "there is quite a lot of uncertainty when it comes to estimating taxpayers' behavioural responses" (Scottish Finance and Public Administration Committee, 2023)

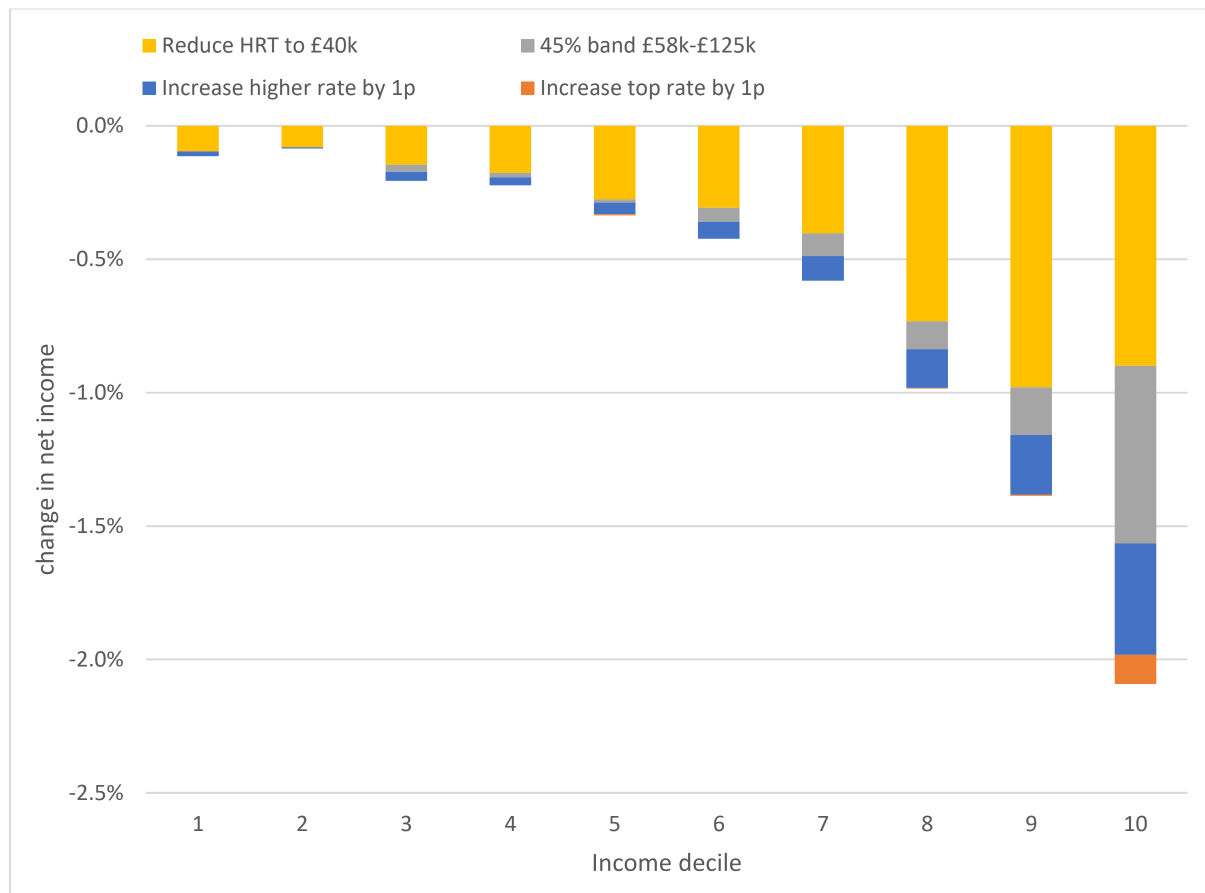
To some extent, these pessimistic assumptions reflect the limits on the devolved Scottish Government's powers to legislate on income tax within the UK. There are obvious loopholes in the existing system which reduce the yield on increases in top tax rates due to avoidance – for example, the fact that tax on dividends and capital gains is lower than income tax means that taxpayers who can relatively easily reclassify income as dividends or capital gains pay lower rates of tax. However, the Scottish Government does not have powers to set the rates of tax on dividends, savings or capital gains paid in Scotland – this is done at a UK-wide level by the UK Government. Devolution and alignment of these taxes would tend to reduce taxable income elasticity and increase the yields from increases in marginal rates at the top end of the income distribution. Devolution of the power to set rates and bands of income tax for savings and dividend income for Scottish taxpayers is one of the recommendations from the recent Poverty and Inequality Commission report *How better tax policy can reduce poverty and inequality* (Poverty and Inequality Commission, 2023).

3.2 Distributional impacts of increases in income tax rates

Figure 2.2 shows the distributional impact of the package of reforms to income tax presented in Table 2.1. The Figure is a "stacked bar chart"; that is, the overall distributional impact of the tax package is shown by the stacked sum of all the bars. The horizontal axis of the Figure shows deciles of equivalised household income (from the poorest households in decile 1 to the richest households in decile 10). Changes in annual net income are shown in percentage terms on the vertical axis.

The package is very progressive overall across most of the income distribution, with the richest decile of households paying an average of just over 2 per cent of net income in increased income tax and the second richest decile paying around 1.4%, while households in the middle of the distribution pay an average of around 0.35 to 0.45 per cent of net income and the poorest two deciles pay only around 0.1 percent of net income. The most progressive components of the tax package are the increase in the higher rate band and top rate bands and the new 45% income tax band for incomes between £58,000 and the top rate threshold. It is worth noting that this analysis does not account for how the revenue is used – for example through increased spending on public services. There is a strong body of evidence that investment in public services is progressive (for example Horton and Reed 2010; Reed and Portes 2018; Ogden and Phillips 2023).

Figure 2.2. Distributional impacts of package of income tax reforms



Source: Landman Economics modelling using Tax-Transfer Model running on Scotland subsample of 2019/20, 2020/21 and 2021/22 Family Resources Survey data

2.3 Using income taxes to fund investment in public services

As a source of tax revenues to fund investment in public services, the income tax system has the advantages that increases in tax rates above the higher rate threshold are distributionally progressive and administratively easy to implement, with the necessary tax infrastructure already in place and the Scottish Government having clearly defined powers to implement these increases. The package of reforms shown in Table 2.1 and Figure 2.2, which includes reductions in thresholds and a new tax band between £75,000 and the top rate threshold, as well as increases in rates, results in over £700 million per year which the Scottish Government can allocate towards investment in public services. This is after behavioural changes and tax avoidance is accounted for.

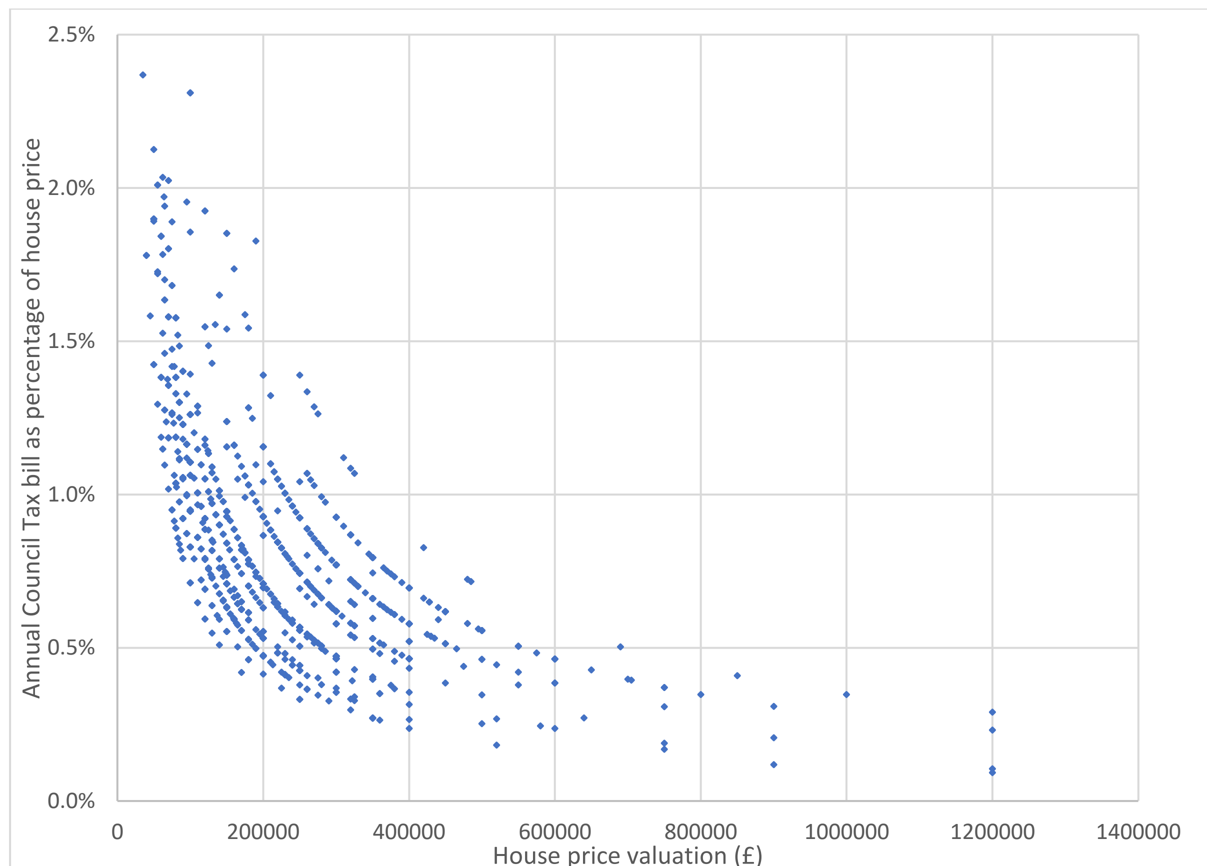
3 Reforming Council Tax

3.1 Problems with the Council Tax system

The Scottish Government's tax-setting powers include control over the organisation and parameters of the local tax system. Currently, the main local tax system in Scotland (as in England and Wales) is Council Tax, which has serious weaknesses.

There are three main weaknesses of the Council Tax system in Scotland. Firstly, the system is regressive, with households living in high-value houses paying far less as a proportion of their property wealth than households living in lower-value houses. This is illustrated in Figure 3.1, which uses data on Council Tax bills and house price valuations for households in Scotland from the most recent wave of the Understanding Society survey and plots house price valuation in 2020-21 (on the horizontal axis) against Council Tax as a proportion of house price value (on the vertical axis). Figure 3.1 shows that Council Tax as a proportion of house price is much higher for low-valued houses than for high-valued houses.

Figure 3.1. Council Tax bill as percentage of house price valuation, homeowners, Understanding Society Wave 12 (2020-21), Scotland



Source: Landman Economics analysis of Scotland subsample of Understanding Society Wave 12 data

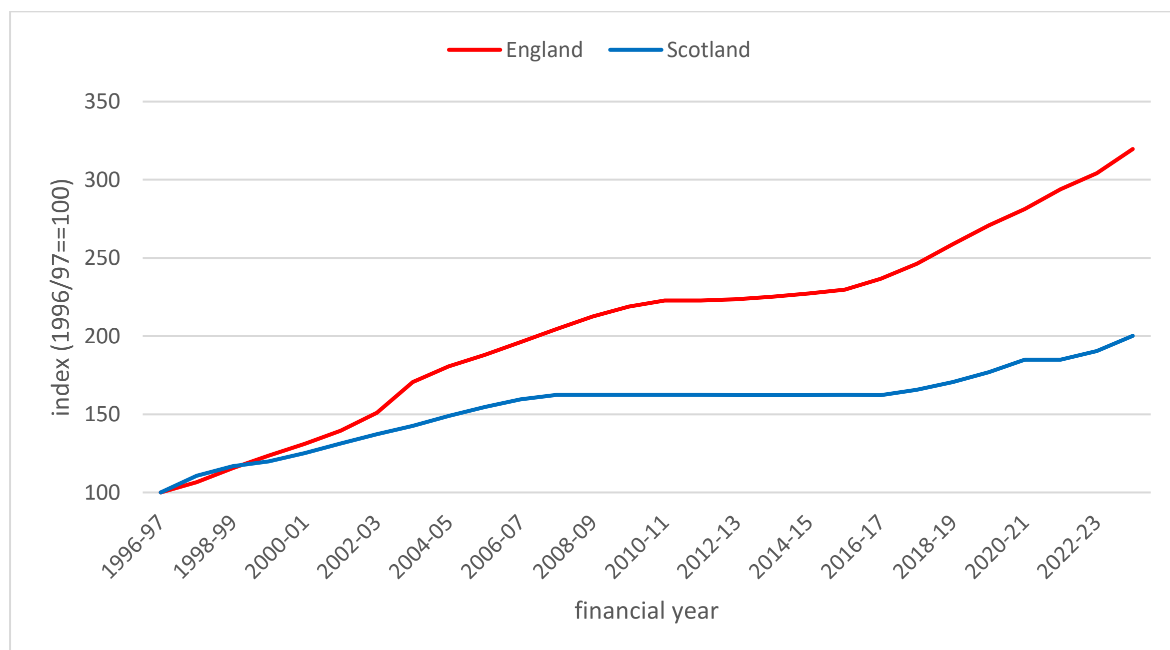
The second major weakness is that there is substantial variation in Council Tax as a proportion of average house prices across local authorities in Scotland. In Inverclyde, the average Council Tax bill for 2023/24 is £1,158 which is 0.87% of the average house price in mid-2023. By comparison, in the City of Edinburgh the average Council tax bill of £1,484 is 0.44% of the average house price – only half as much as in Inverclyde.

Thirdly, the bandings used for the Council Tax system in Scotland are still mainly based on house valuations from 1991, which are now over three decades out of date. The 2015 Commission on Local Tax Reform showed that 57% of properties in areas they modelled would change band if revaluation had been conducted in 2014. Around half of those were currently in a higher band than they would be after revaluation (and so would pay less Council Tax if such a revaluation was conducted), and around half would pay more as a consequence of revaluation (Commission on Local Tax Reform, 2015).

In addition to this, since the late 1990s Council Tax increases (in percentage terms) have been lower in Scotland than in England. Figure 3.2 shows average Council Tax bills for Scotland (in blue) compared to England (in red) since 1996/97, indexed to 100 in 1996/97. While average Council Tax bills doubled in Scotland between 1996/97 and 2022/23, bills more than trebled in England over the same period. The increase in Council Tax in Scotland was 120 percentage points lower than in England over the period 1996/97 to 2022/23.

Over the last 15 years since the Council Tax freeze was introduced in 2007/08, average Council Tax bills have grown by 60 percent in England but only 23 per cent in Scotland.

Figure 3.2. Average Council Tax bills in Scotland and England, 1996/97 to 2022/23: indexed, 1996/97=100



Source: Landman Economics analysis of Scotland and England Council Tax data from Scottish Government (2023b) and DLUHC (2023)

Looking at the last 15 years since the Scottish Government originally introduced a Council Tax freeze, Scottish Councils would have had an extra £800 million to spend on services if Council Tax in Scotland had risen at the same rate as in England since 2007/08. For comparison, the total amount of Council Tax billed by councils in Scotland in 2023/24 was just under £3 billion (Scottish Government, 2023c). This "Council Tax gap" presents significant challenges for funding local authority-provided services in Scotland. In the remainder of this chapter, we look at reforms which would help close this gap and raise substantial additional revenue through property taxation in a progressive manner.

3.2 Progressive changes to the current Council Tax system

There are several changes to the Council Tax system that could be made immediately to make Council Tax more progressive without undertaking a fundamental reform of local taxation. These include:

- Scrapping the Council Tax reductions for purpose-built holiday homes and second homes[5].
- Adding further discretion to the empty homes surcharge – an additional 50% after two years of the property being empty and a further 50% after three years. This would allow for a maximum of 300% Council Tax on long-term empty properties, similar to how the charge for empty homes in Wales operates (Welsh Government, 2023).
- Increasing Council Tax for bands E, F, G and H. In recent months the Scottish Government was consulting on increases to Council Tax of between 7.5% and 22.5% for those living in bands E to H. Based on 2023-24 Council Tax rates, the average annual increases would be £139 for households in Band E, £288 for households in Band F, £485 for households in Band G and £781 for households in Band H, potentially raising an additional £176 million, with around 28% of all properties being impacted (Scottish Government 2023d, p7). However, in October 2023 Scottish First Minister Humza Yousaf announced that Council Tax would be frozen for the 2023/24 tax year (Scottish Government, 2023e), "to support people struggling with the effects of high inflation". This is a retrograde step which will further widen the Council Tax gap between Scotland and England, making it harder to fund Scottish public services effectively. Furthermore, as the IPPR has shown, freezing Council Tax makes virtually no difference to households in poverty, and so cannot be defended on the grounds of distributional equity (Hawkey, 2023).

[5] The Scottish Government recently laid regulations before the Scottish Parliament giving local authorities the power to increase council tax on second homes and empty homes (Scottish Government 2023i).

3.3 Replacing Council Tax with a Proportional Property Tax

The progressive changes to the Council Tax system outlined in Section 3.2 above would resolve some, but not all, of the current problems with the Council Tax system. In particular, the banding structure of Council Tax only crudely reflects property values, and the banding is still based on valuations from over thirty years ago.

In response to the problems with the current Council Tax system, the campaigning group Fairer Share has proposed a more fundamental reform: replacing Council Tax with a Proportional Property Tax (PPT) where households pay a percentage of the value of the property each year (Fairer Share, 2020). The PPT reform was originally proposed for England, where Fairer Share estimated that a tax rate of 0.48% of house value per year for properties in England would raise the same amount as current Council Tax levels (with a double rate of 0.96% for second homes). As the structure of the Council Tax systems in England and Scotland is similar[6], it is relatively straightforward to apply a similar distributional analysis to Scotland.

3.3.1 Revenue yield of a PPT

Table 3.1 shows the revenues from the introduction of a PPT for Scotland at various rates for the annual payment on a primary residence, ranging from 0.5% per year to 0.9% per year. The analysis makes the following additional assumptions[7]:

- Two-thirds of the PPT is passed through to tenants in the private rented sector and one-quarter is passed through to social tenants[8].
- In the private sector, buy-to-let landlords pay the remaining proportion of the PPT liability for private sector tenancies (one-third).
- Second homes pay a double rate of PPT.
- any household currently claiming Council Tax Reduction (CTR) pays no more under the PPT than they would have done under the Council Tax for 2023/24 (we investigate the impact of this assumption in more detail in Section 3.3.3 below).

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[6] There are some minor differences; for example, the band multipliers used in Scotland for Bands E, F, G and H are more progressive than the equivalent bands in England.
[7] These assumptions are the same as those used by WPI Economics in its analysis of the revenue yield from a PPT (WPI Economics, 2021).
[8] Note that the Scottish Government recently committed to a 3% cap in rent increases and are considering introducing rent controls by the end of the current parliament. Rent controls would prevent PPT costs being passed to tenants, and would tend to make the distributional results of a PPT more progressive than those shown in Figure 3.3 (because tenants have lower incomes on average than owner-occupiers).

Table 3.1. Revenues from the replacement of Council Tax with a Proportional Property Tax

Annual percentage charge on property value	Average annual household bill (if introduced in 2023/24)	Yield (£m)	Additional revenue compared to Council Tax (£m)
0.5%	£1,190	2,853	-131
0.6%	£1,414	3,390	406
0.7%	£1,634	3,918	934
0.8%	£1,851	4,438	1,454
0.9%	£2,067	4,956	1,972

Source: Landman Economics analysis of Understanding Society Wave 12 and Wealth and Assets Survey Round 7 data.

The results in Table 3.1 show that a PPT of 0.6% raises just over £400 million compared to the current Council Tax yield of £2.98 billion in 2023/24. This accounts for just over a quarter of the current “Council Tax gap” of £1.7 billion. A PPT of somewhere between 0.8 % and 0.9% would raise enough to completely close the funding gap between Scotland and England.

A comparison with the results from last year’s tax report shows that a higher percentage charge on property values is required to achieve an equivalent yield to Council Tax, compared to 12 months ago. This is because average property prices were approximately unchanged in nominal terms in July 2023 (the most recent available data at the time of publication[9] compared to 12 months before, whereas Council Tax bills for 2023/24 increased by an average of just over 5 per cent compared to the previous year.

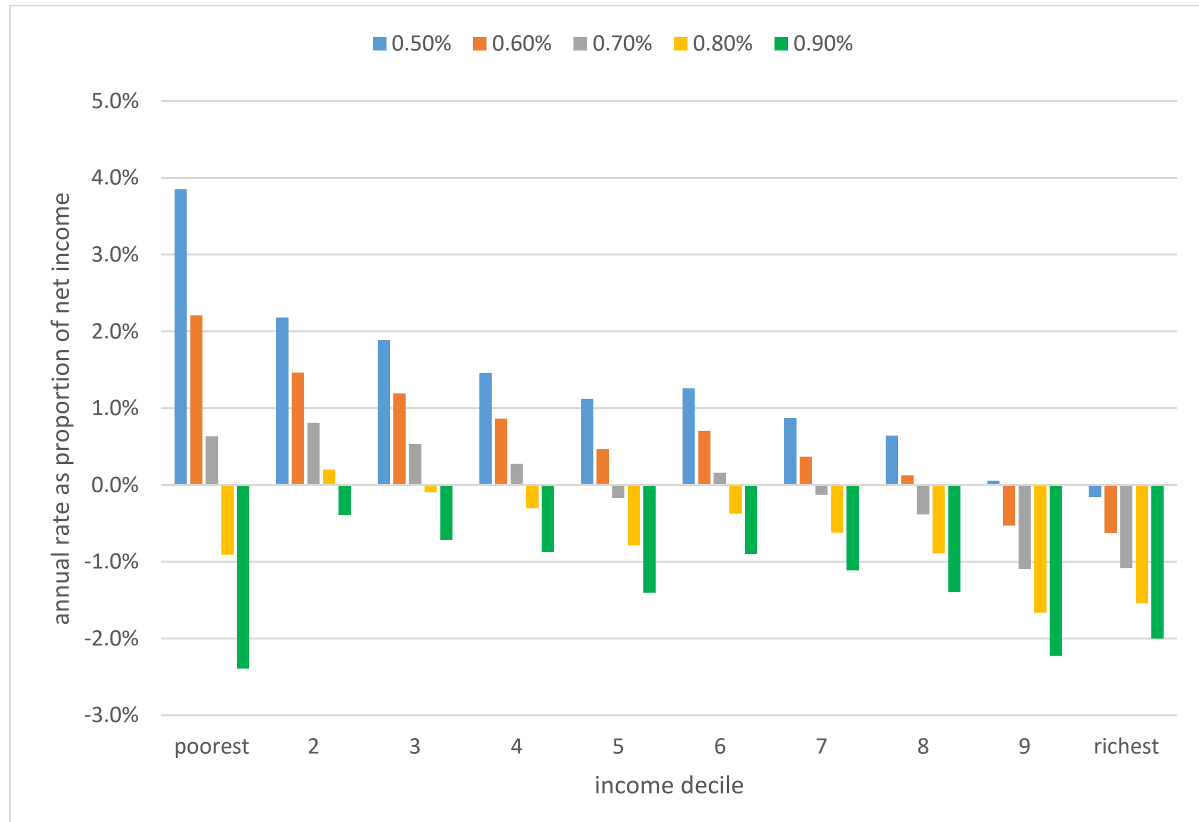
3.3.2 Distributional impacts

Figure 3.3 below shows the distributional effects of the Proportional Property Tax by income decile at the five rates shown in Table 4.1 above. When the PPT is set at 0.5%, the distributional effects are progressive across the household income distribution, with average gains in deciles 1 through 9, and average losses in decile 10. Thus, a PPT set at 0.5% is an (approximately) revenue-neutral with progressive distributional impacts. If the PPT is set at 0.6% the results are still progressive across most of the distribution although the percentage gain in decile 6 is slighty higher than decile 5. At rates of 0.7% per year the impacts in decile 5 and deciles 7 through 10 are negative on average. Rates of 0.9% per year produce negative impacts across the whole income distribution and a substantial average negative impact of over 2% of net income in the lowest income decile. These results suggest that while a PPT set at 0.7% or below can produce progressive distributional effects

[9] House price data for Scotland are provided by the UK Land Registry: https://landregistry.data.gov.uk/app/ukhpi

while raising revenue, setting a rate above this level point would require a more extensive replacement for the Council Tax Reduction scheme to compensate low-income households who lose out from the replacement of Council Tax by PPT.

Figure 3.3. Distributional effects of a Proportional Property Tax at five different rates, by household income decile



Source: Landman Economics calculations using Understanding Society Wave 12 and Wealth and Assets Survey Round 7 data.

3.3.3 Compensating low-income families when introducing a PPT at 0.7%

This subsection looks in more detail at the cost of compensating low-income households who lose out from the switch from Council Tax to a Proportional Property Tax. The analysis assumes that PPT is introduced at an annual rate of 0.7% of property values, on the grounds that setting the tax at this level has progressive impacts and raises substantial additional revenue. We model the gross yield from the PPT and two different compensation packages for low-income households:

- **Package 1:** any household currently claiming Council Tax Reduction (CTR) pays no more under the PPT than they would have done under the Council Tax for 2023/24. This is the compensation package used for the PPT options modelled in Table 3.1 and Figure 3.3 above.

- **Package 2:** any household currently claiming CTR and/or in the lowest 30 per cent of the equivalised household net income distribution pays no more under the PPT than they would have done under the Council Tax for 2023/24. This is a more generous package than Package 1 because it also compensates households who are not currently claiming CTR, but who are on low incomes. This could be implemented (for example) by integrating the compensation package for PPT much more closely with Universal Credit than is currently the case for CTR, although this would require collaboration with DWP to be easily implementable.

Table 3.2 shows the revenue yield from a 0.7% PPT without any compensation package and with each of the packages outlined above in place. Table 3.2 shows that without a compensation package in place, almost 7 in 10 households in each of the lowest three deciles lose out from a PPT set at 0.7%. With compensation Package 1 in place (at a cost of around £740 million), the number of households losing out falls significantly, to around a quarter of households in the lowest three deciles. Package 2 reduces the number of low-income households losing out from the PPT to zero (by definition), at an additional cost of around £150 million on top of the cost of Package 1.

Table 3.2. The cost and distributional effects of PPT compensation packages

Compensation package	None	Package 1	Package 2
Gross yield (£m)	4,658	4,658	4,658
Cost of package (£m)	0	741	892
Net yield (£m)	4,658	3,918	3,767
Increase in yield compared to 2023/24 Council Tax	1,674	934	783
Proportion of households losing out in lower deciles of income distribution:			
Decile 1	68%	25%	0%
Decile 2	67%	22%	0%
Decile 3	69%	28%	0%

Source: Landman Economics calculations using Understanding Society Wave 12 and Wealth and Assets Survey Round 7 data

3.3.4 Rebalancing yields across Scottish local authorities

As noted in Section 3.1 above, there is a discrepancy across Scottish local authorities in terms of average Council Tax bills as a share of current average house prices – ranging from 0.44% in the City of Edinburgh to 0.87% in Inverclyde. As a consequence, the introduction of a uniform PPT rate across all Scottish local authorities is likely to leave authorities in areas where house prices are low relative to current Council Tax bills with a revenue shortfall compared to local authorities where revenues are higher.

One potential way of addressing this discrepancy would be for local authorities to set a higher percentage rate of PPT in areas with lower house prices. However, this could leave some lower-income households worse off unless the PPT compensation package was made correspondingly more generous. Alternatively, a more equitable solution would be to revalue block grants to compensate local authorities with relatively low yields from PPT compared to their needs for public service funding.

3.3.5 The case for a Proportional Property Tax, revisited

Overall, replacing Council Tax with a Proportional Property Tax at a rate of 0.7% (with an accompanying compensation package) could raise £783-934m to fund additional investment in public services provided by local authorities, closing much of the "Council Tax gap" in revenues between Scotland and England. In addition, the PPT would fix many of the most glaring drawbacks and inequities of the current Council Tax system, and has progressive impacts across most of the household income distribution. The main barrier to the immediate introduction of the PPT is that it requires updates to property valuations before being introduced (although there is a strong argument for updating the 1991 valuations anyway, even if Council Tax were to be retained). Based on the original timescale for Council Tax, which was introduced for the 1993/94 tax year following a valuation exercise in 1991, it seems reasonable that a PPT could be introduced in Scotland for the 2026/27 tax year using property valuations undertaken in 2024[10].

It is also important that a substantial compensation package should be in place to protect low-income households who would otherwise lose out from the shift from Council Tax to a PPT which yields more revenue. Based on the results from Table 3.2, around 15 to 20 per cent of the gross yield from a PPT needs to be recycled into an enhanced rebate or reduction scheme to ensure that low-income households pay no more than they would have done under the current Council Tax system.

[10] The recent Poverty and Inequality Commission report recommends that "As a priority, domestic property revaluation is needed in relation to Council Tax. Work on this should start now to be in place no later than 2026 (with a 2024 or 2025 date of valuation)." (Poverty and Inequality Commission 2023, p5)

4 Wealth taxes

In addition to replacing Council Tax with a more progressive local tax system (such as the Proportional Property Tax modelled above), the Scottish Government has the power to introduce a tax on wealth, provided this is implemented as part of the local tax system rather than a national tax. This chapter provides updated estimates for the potential yield from a wealth tax if introduced in Scotland.

4.1 Modelling a tax on wealth

4.1.1 Methodology

This report models the introduction of a locally administered tax on wealth in Scotland using data from the Scottish component of the UK Wealth and Assets Survey, which is a survey dataset collected on a biannual basis with high levels of detail on the assets owned by households in the survey. The definition of property wealth here includes:

- Net property wealth (including primary residences plus other domestic properties such as second homes or buy-to-let, but excluding commercial properties);
- Pension wealth;
- Net financial wealth (assets minus debts);
- Physical wealth (the value of household contents, possessions and valuables owned, such as antiques, artworks, collections and any vehicles owned by individuals).

The modelling assumes that wealth is taxed on a household, rather than an individual basis[11]. In line with other recent research on wealth tax, we assume that a proportion of revenues from the wealth tax is avoided. Because property is immobile, the avoidance rate on property wealth tax is assumed to be low – we assume 5% avoidance. (Some of this may be due to a decline in property values after the introduction of the tax). We assume a higher rate of avoidance of 40% for financial assets and physical wealth as these are more mobile, with a rate of 20% for pension wealth (which is usually more “tied up” than other financial assets due to the UK Government’s rules regarding the age at which pensions can be accessed)[12]. This is consistent with recent modelling of the revenues from an annual wealth tax by Tippet

[11] This is the approach taken by Tippet et al (2021) in recent modelling work. The LSE Wealth Tax Commission (Advani *et* al, 2020) decided on an individual assessment basis for wealth in its recommendations but said that a household assessment unit was a credible alternative.

[12] These avoidance rates have been revised slightly compared to last year’s tax report (Reed, 2022) in response to feedback and discussion regarding the wealth tax modelling in that report.

et al (2021) who assume that avoidance reduces revenues by between 15% and 50%[13].

The wealth tax modelled here would operate on an annual basis, rather than being a one-off tax as recommended by Advani *et al* (2020). This is because a key objective of the tax measures outlined in this report is to provide stable funding for investment in public services on an ongoing basis, and it makes more sense to use a recurring annual tax than a one-off tax to achieve this objective. Additionally, one of the Scottish Government's National Outcomes in its National Performance Framework is to share wealth more evenly and an annual wealth tax would enable ongoing progress in achieving this objective (Scottish Government, 2023f).

4.1.2 Revenue yield

Table 4.1 presents updated estimates for the revenue yield from an annual wealth tax charged at the following marginal rates on wealth above £1m per household:

- 0.5% per year for wealth between £1 million and £2 million;
- 1% per year for wealth between £2 million and £5 million;
- 2% per year for wealth above £5 million.

The results show that an annual wealth tax at the rates suggested could raise just over £1.4 billion per year. Most of this yield is from households with wealth between £1 million and £5 million. Overall, the wealth tax would affect just over one in eight Scottish households (13.2%).

Table 4.1. Estimated yields from proposed wealth tax for Scotland by marginal wealth band

Wealth Threshold	Percentage of households with wealth in band	Total value of taxable wealth in band (£bn)	Marginal rate	Illustrative yield of annual wealth tax in band, £m
£1m - £2m	13.2%	158.8	0.5%	794
£2m - £5m	2.7%	56.6	1%	566
£5m and above	0.2%	2.8	2%	56
Total yield				**1,416**

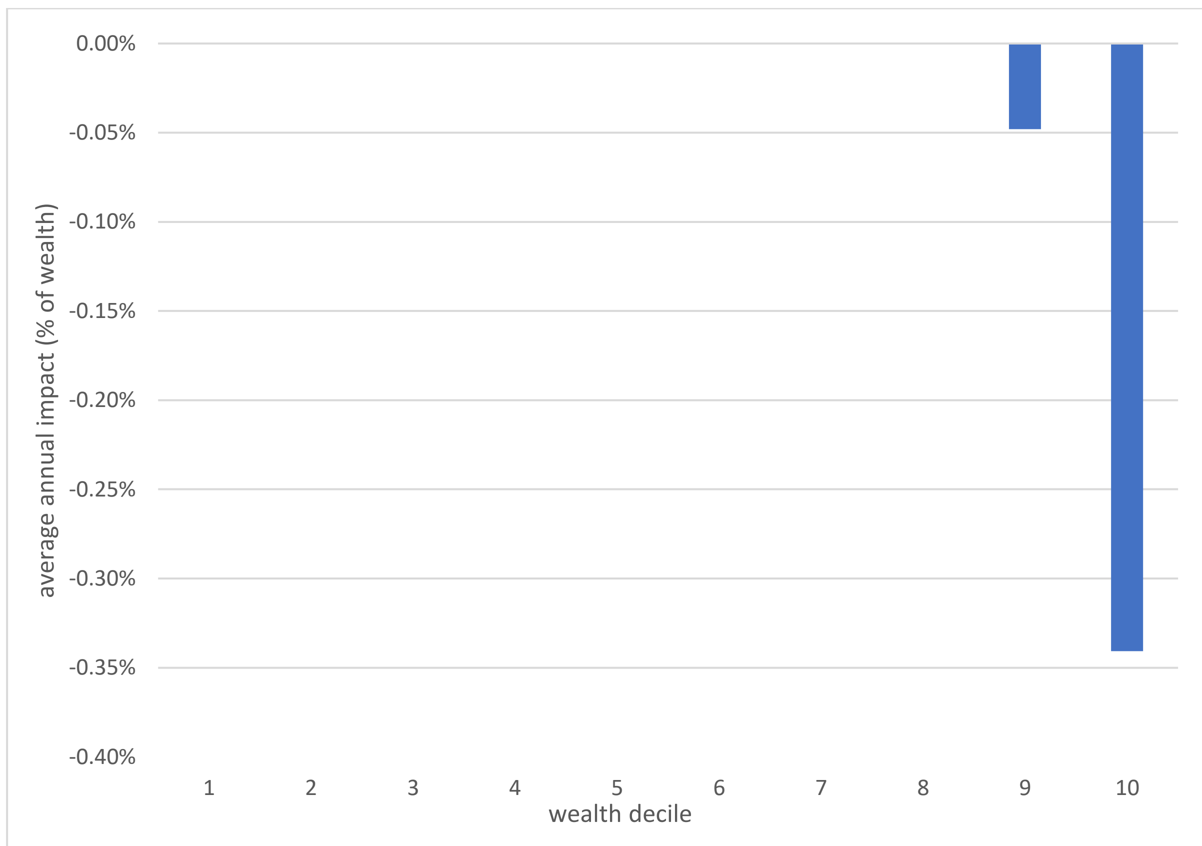
Source: Landman Economics estimates using Scotland subsample of Wealth and Assets Survey Round 7 data. Avoidance rate assumed to be 5% for property wealth, 20% for pension wealth, 40% for other forms of wealth.

[13] The 40% avoidance figure is chosen to take account of the risk that avoidance of the wealth tax might be higher if it were introduced for Scotland only, rather than on a UK-wide basis, because high-wealth individuals might move across the border into England to avoid the tax. This is an increase from last year's report where we assumed a 35% avoidance rate.

4.1.3 Distributional impacts

The distributional impacts of the wealth tax at the marginal rates indicated above by deciles of household wealth are shown in Figure 4.1 below. Given that the wealth tax only applies to households with net wealth above £1 million, it is not surprising that the tax only has an impact in the 9th and 10th deciles of the wealth distribution. Most of the impact is on households in the top wealth decile (average losses of just under 0.3 per cent of total wealth).

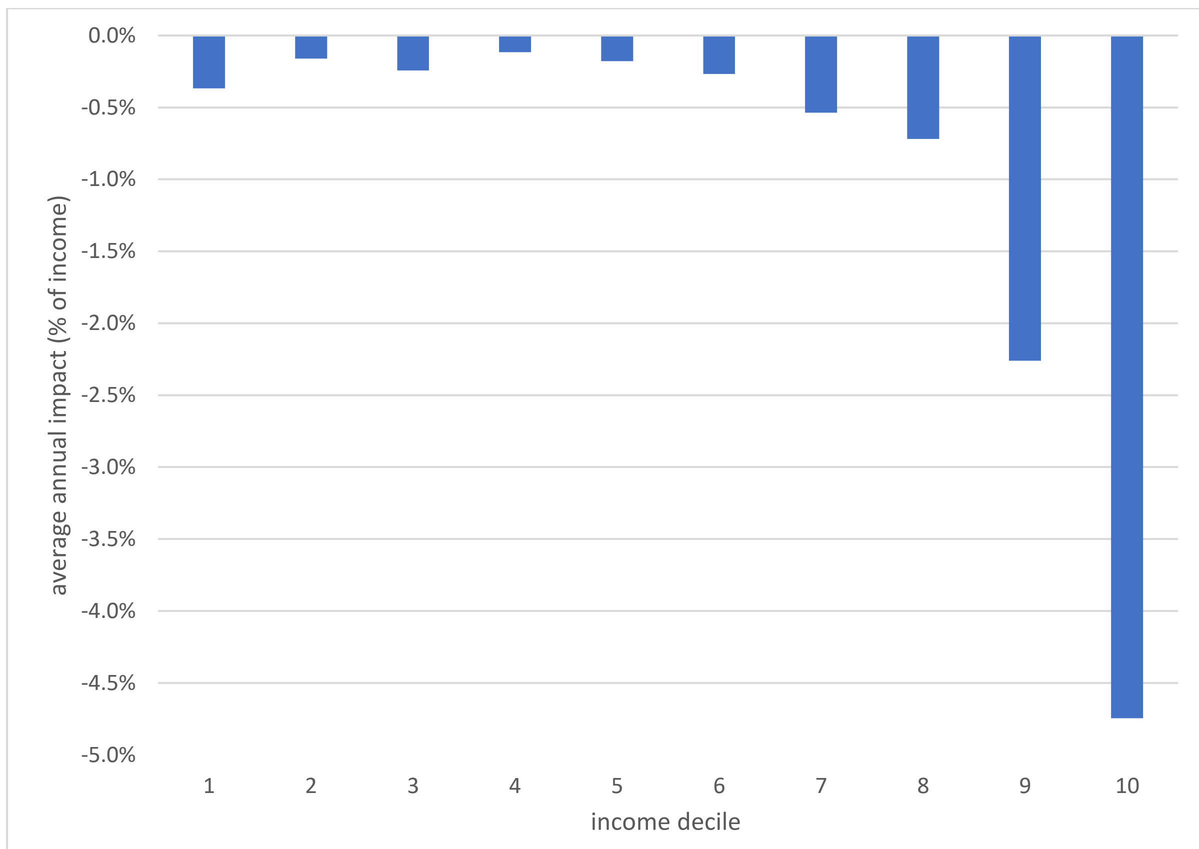
Figure 4.1. Distributional impact of wealth tax by household wealth decile



Source: Landman Economics modelling using Wealth and Assets Survey Round 7 data

The distributional impacts of the wealth tax by household income decile (represented as a percentage of annual household income rather than annual household wealth) are also progressive, as shown in Figure 4.2 below. Average losses for the top income decile are just under 5% of net income, and around 2.3% of net income for the 9th decile. In the bottom 60 per cent of the income distribution, the average impact of the wealth tax is less than 0.5 per cent of net income per year.

Figure 4.2. Distributional impact of wealth tax by as a percentage of net income by household income decile



Source: Landman Economics modelling using Wealth and Assets Survey Round 7 data

4.1.4 Pros and cons of a wealth tax

The wealth tax has the advantage of good revenue raising potential and being progressive with respect to both wealth and incomes. The main drawback is that it requires updated valuations of property and also valuations of other forms of wealth (including pension funds and physical wealth). The LSE Wealth Tax Commission (Advani *et al*, 2020) estimated that the administration costs of a wealth tax would be equal to a maximum of 1 per cent of the total revenue raised by the tax, and this report uses that assumption in Chapter 6 where the recommended package of tax measures includes a wealth tax. There is also the technical difficulty of estimating the yield for a wealth tax given the uncertainties regarding the level of avoidance and the low response rate for super-wealthy households in the Wealth and Assets Survey.

The requirement for a new administrative system for valuing wealth means that there would be an inevitable delay before a wealth tax could be introduced in Scotland. A timeline from initial proposals in early 2024 to introduction in the late 2020s seems reasonable.

4.2 Land Value Tax

A land value tax (LVT) is a type of asset-based taxation that has received a lot of attention in Scotland recently[14]. Rather than a tax on property values, a LVT taxes the value of land (excluding buildings or other improvements to the land. Land values vary according to location and permitted use of the land (e.g. residential, commercial, agricultural).

The precise yield and distributional effects of a LVT in Scotland cannot be estimated without more research to impute land values for residential (and indeed commercial) land[15]. Therefore, this report does not present revenue yield estimates or distributional results for an LVT. However, the distributional effects of replacing the current Council Tax system with a tax on residential land values are likely to look fairly similar to the distributional effects of the Proportional Property Tax modelled in Section 4.1, if the LVT is levied as an annual percentage of land values. If the LVT is levied as a percentage of land values *above a threshold* (i.e. with an exemption for households below a certain value of land), then the effects are likely to look more similar to the progressive wealth tax shown in Section 4.2 above.

LVT has the advantage of being a relatively efficient tax in economic terms because it taxes the locational rents arising from the location of land (and its designated purpose under the current planning system) rather than taxing improvements to land. It has good revenue-raising potential, and is likely to look progressive with respect to incomes and wealth (if the impacts look anything like the property and wealth taxes modelled earlier in this chapter. It could supplement (or replace) current domestic property taxation and could also apply to land used for business purposes (thus supplementing or replacing current business taxation).

A pre-requisite for the introduction of a LVT is that it requires valuation of all land in Scotland (or at least all land used for domestic purposes, if the tax were for domestic land only), as well as a complete register of all land in Scotland (the current Scottish land registry is not a fully complete record of all land ownership in Scotland, although considerable progress has been made towards completion in recent years)[16]. As with the wealth tax discussed above, LVT presents technical implementation challenges which mean that the earliest it could be introduced in Scotland would probably be the 2027/28 or 2028/29 tax year[17].

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[14] See for example Scottish Land Commission (2018, 2022); Wightman (2009)
[15] For Wales, researchers at the University of Bangor for the Welsh Government (ap Gwilym, Jones and Rogers, 2019) found that around 48% of residential property value in Wales was land value. A similar analysis would be possible for Scotland.
[16] See Registers of Scotland, "Delivering the benefits of a complete land register", October 2022. https://www.ros.gov.uk/performance/land-register-completion
[17] The recent Poverty and Inequality Commission report recommends that "the Scottish Government should set an aim to be in the position to bring forward a package of proposals to tax wealth by the end of the current Scottish Parliament session in 2026" (Poverty and Inequality Commission 2023, p7).

5 Other potential taxes

This chapter looks at other potential sources for raising tax revenue to fund an investment in public services more widely.

Section 5.1 assesses the potential for increases paid by businesses and the non-domestic sector, while Section 5.2 looks at property and land taxes (in addition to those already considered in Chapter 4) and Section 5.3 looks at consumption-based taxes, including taxes on flying.

5.1 Increased tax revenue from businesses and the non-domestic sector

5.1.1 Landfill Tax

Scottish Landfill Tax currently raises around £100m per year and is devolved to the Scottish Parliament (Revenue Scotland, 2023a). The rate it is levied at has remained at the UK level but it could be raised by the Scottish Government – for example, a 30% increase would raise approximately £30m of extra revenue.

5.1.2 Scottish Aggregates Levy

The Scotland Act 2016 provides the Scottish Parliament with the power to introduce a devolved tax on the commercial exploitation of aggregates in Scotland, to replace the UK Aggregates Levy. The Scottish Government's programme for government published in September proposes an Aggregates Tax Bill – "The Bill will deliver on powers devolved in the Scotland Act 2016 by setting out the key arrangements for a devolved tax on the commercial exploitation of aggregates in Scotland" (Scottish Government 2023g, p57). The Scottish share of the UK aggregates levy is around £60 million. Increasing the Scottish Aggregates Levy by 30 per cent, could raise in the region of £18 million.

5.1.3 Reforms to Non-Domestic Rates (NDRs)

Non-Domestic Rates (NDRs) are the main form of local business taxation in Scotland. Current NDR statistics (Scottish Government 2023h) show that total reliefs for NDRs for 2022-23 were just under £800m.

There are a number of possible reforms which could increase net revenue from NDRs. Most obviously, last year's tax report (Reed 2022) recommended changes to the Small Business Bonus Scheme (SBBS), the largest single component of NDR

reliefs, to streamline the system and reduce costs. Scrapping the SBBS would save around £280 million per year (Scottish Government, 2023h) which could be used to fund a relief for employers providing “fair work” as defined by the Scottish Government: “fair work means secure employment with fair pay and conditions, where workers are heard and represented, treated with respect and have opportunities to progress” (Scottish Government 2023i).

Other savings that could be made to the current NDRs system include:

- Revisiting the Public Health Supplement which was in force from 2012 to 2015 – a levy on large retailers selling alcohol and tobacco.
- Incrementally reducing reliefs for empty industrial ground.

5.2 Property and land taxes

5.2.1 Land and Buildings Transaction Tax (LBTT)

The current combined revenue from both residential and non-residential LBTT is around £800m (Revenue Scotland, 2023b). This is a relatively small tax take given that the value of the residential sales market alone was £22.2 billion in 2021-22 (Registers of Scotland, 2022). Options to raise more money from LBTT include:

- Splitting the £750,000+ residential property band into two, covering £750,000-£1 million and £1 million+, with a higher rate of 15% for properties valued at over £1 million
- Increasing the £325,000-£750,000 residential rate from 10% to 12%
- Splitting the £250,000+ non-residential band into two, covering £250,000-£500,000 at 5% and £500,000+ at 10%
- Introducing a 15% surcharge for overseas entities/non-UK residents buying property, similar to what is applied to Stamp Duty in England (currently at 5%).

Overall we estimate that these measures would raise £240 million per year.

5.2.2 Additional Dwelling Supplement (ADS)

ADS is LBBT charged on second or third buy-to-let homes. It is currently levied at a rate of 6%, up from 4% previously. UNISON Scotland estimate that increasing ADS by a further 2% would raise an extra £56 million (UNISON Scotland, 2022).

5.2.3 A Land Value Tax for commercial land

A Land Value Tax for domestic properties has already been discussed as a policy option in Section 4.3 of this report. By extending LVT to commercial land, it would be possible to supplement or replace the current Non-Domestic Rates system with LVT. The current total forecast yield of NDRs for the 2023/24 tax year is £3.08bn (Scottish Government, 2023h). By replacing this with a LVT with a slight extra yield (say, between 3 and 5 per cent of the total yield – up to £150 million per year) it would be possible to deliver additional funding for public services while enhancing the efficiency of the business tax system.

5.2.4 Carbon Emissions Land Tax

The John Muir Trust has published initial proposals to introduce a local carbon emissions land tax on landholdings exceeding 1,000 hectares in the upcoming Land Reform Bill. They estimate that a notional average tax of £3 per hectare could raise up to £12.5m per year (John Muir Trust, 2023) while incentivising the active management of land to reduce emissions.

5.3 Consumption taxes

5.3.1 Online sales tax

In February 2022 the UK Government published the results of a consultation exploring the arguments for and against an online sales tax (OST) (HM Treasury, 2023). Shortly afterwards, the Scottish Government and COSLA (the umbrella organisation for local authorities in Scotland) published a report *The New Future for Scotland's Towns* outlining actions to better embed a 'town centre first' approach to support high streets in Scottish towns. In November 2022 the UK Government announced that it would not introduce an OST due to concerns raised about an OST's complexity and the risk of creating unintended distortion or unfair outcomes between different business models. A subsequent response by the Scottish Government (Scottish Government, 2023j) noted that the Scottish Government would "review the responses to the UK Government's consultation and carefully consider the implications for our own commitment to explore a Digital Sales Tax in Scotland". The document also noted that "the availability of data on the reserved matters of corporate/business taxation and on the composition of Scottish retail businesses presents a significant challenge to the consideration of a devolved Digital Sales Tax". In addition, an attempt by the Scottish Government to introduce a digital sales tax would likely be subject to legal challenge by the Westminster Government due to its impacts on the UK market for online goods and services. Because of the potential legal problems surrounding the introduction of an OST we have not

included it in the overall package of recommended tax reforms in Chapter 6 of this report.

5.3.2 Tourist Tax/ Local Visitor Levy

The Scottish Government introduced the Visitor Levy (Scotland) Bill to the Scottish Parliament in May 2023. While this is aimed at enabling Local Authorities to levy a tourist tax or local visitor levy, it could be expanded to include National Parks. While the Scotland-wide revenue yield from a local visitor levy would depend on how many local authorities implement the scheme, there have been some estimates of revenue raising potential at the local level. For example, the City of Edinburgh Council has estimated that a tourist tax in Edinburgh could raise between £5 million and £35 million a year depending on the model used (City of Edinburgh Council, 2022; Swanson, 2023).

5.3.3 A Frequent Flyer Levy

Air Departure Tax was devolved to the Scottish Government in 2016 but is not yet in operation because the Scottish Government cannot reach an agreement with the UK Government on how to stop Highlands and Islands airports being impacted.

There were 28.9 million air terminal passengers in Scotland in 2019 and only 5% of these travelled to or from other Scottish airports. The vast bulk of passengers go from Glasgow (GLA) or Edinburgh (EDI).

With an exemptive or no detriment policy for the Highlands and Islands, a progressive extension of this tax, such as a frequent flyer levy or fixed penalties for airlines that fail to adopt time-sensitive plans for transition to green fuel sources, could increase revenue while helping meet net zero targets.

Based on an analysis of proposals by the New Economics Foundation (2021) for a frequent flyer levy combined with an estimate of the proportion of flights in the UK originating in Scotland, we estimate that a frequent flyer levy for Scotland could raise around £50 million per year.

5.3.4 Tax on private jets

Oxfam (2023) have modelled the potential revenue gains at the UK level from a tax tax on private jets using a new, higher rate of Air Passenger Duty (APD). In 2022, an estimated 90,000 to 100,000 private planes took off in the UK, causing just over 500,000 tonnes of CO_2 emissions (European Business Aviation Association, 2023). There are currently three rates of APD, one of which is a “higher rate” for heavy aircraft that are equipped to carry fewer than 19 passengers. Chartering a private jet

to fly from Glasgow can cost upwards of £6,400 (Campaign for Better Transport, 2022) while the higher rate of APD raises only £78 per (domestic) flight – around 1% of the total cost of the charter flight.

The Campaign for Better Transport has previously argued for a new ‘super rate’ of APD for all private flights, at 10 times the current highest rate for domestic flights: £780. Based on survey evidence suggesting that the average number of passengers on a plane is 4.7, Oxfam (2023) estimates that additional revenues from this increased rate of APD for private jets would be just over £320 million at the UK level.

For this report we have estimated the potential yield from applying an APD rate of £780 *for private flights originating from Scotland*. Analysis of Transport Scotland’s statistics on private jets departing from airports in Scotland[18] suggest that approximately 8% of private jet flights from the UK depart from Scotland. Using this statistic as a proxy for the share of UK-wide revenue that a super rate of APD could raise if applied to Scotland only, produces an estimate of (£320m x 8%) = approximately £25 million.

The Scottish Green Party has suggested a higher rate of APD for private jet passengers, of £1,000 per flight, suggesting that this measure could raise £50 million to £100 million per year (Scottish Green Party, 2023).

[18] Transport Scotland (2023), Table 8.9

6 Tax recommendations

This chapter outlines an updated and costed package of tax increases to fund increased investment in public services, in Scotland. The reforms are divided into short-term reforms (which involve changes to rates and thresholds of existing taxes and could be implemented at the next Budget with the increases taking effect in April 2024) and longer-term reforms (which require more substantial changes to the tax system such as revaluation of properties, or the setting up of new tax collecting apparatus). The full longer-term package of tax reforms could be in place by 2027 or 2028 if implementation of the reforms started in 2024.

6.1 Short term reforms

The short-term reforms comprise the following:

i) **Changes to income tax:** the package of reforms outlined in Chapter 2.
ii) **Increases to Land and Buildings Transactions Tax** along the lines specified in Section 5.2.1. The target for increased LBTT revenue suggested here is £240 million, which would be a 30% increase in revenue yields from current levels.
iii) **An increase in Additional Dwelling Supplement** from its current level of 6% to 8%.
iv) **Increasing Scottish Landfill Tax** by 30 per cent.

Table 6.1 shows estimates of the revenue yield from the short-run reforms (at 2023/24 prices). The overall amount raised by the short term package is just over £1.1 billion. Based on the average Scottish public sector salary, and accounting for national insurance contributions and pension costs, £1.1 billion would fund 24,000 public sector workers in Scotland[19].

Table 6.1. Estimated revenue raised from short-term package of reforms

Reform	Revenue
Income tax reforms	779
LBBT increases	240
ADS: increase by 2%	56
Scottish Landfill Tax: increase by 30%	30
Total revenue raised per year (£m)	**1,105**

Source: income tax reforms – as in Chapter 2. Other taxes: author's calculations based on Chapter 5

[19] Calculations based on mean public sector salary in Scotland of £34,816, taken from Annual Survey of Hours and Earnings (2023) https://www.ons.gov.uk/employmentandlabourmarket/peopleinwork/earningsandworkinghours/datasets/regionbypublicandprivatesectorashetable25

6.2 Longer term reforms

The longer-term package of reforms comprises the following:

i) **Replacing Council Tax with a Proportional Property Tax at a rate of 0.7% for primary residences and 1.4% for second homes**. The overall increase in gross revenue from PPT is £1,674m. £892m of this extra revenue should be used to fund an enhanced rebate/reduction scheme for low-income households, to ensure that no low-income households lose out from the switch to PPT (compensation package 2 in Table 3.2). This leaves a remaining net revenue gain of £783m.

ii) A progressive **annual wealth tax** on household assets above £1 million at the following rates:

- £1 million - £2 million: 0.5%
- £2 million - £5 million: 1%
- £5 million and above: 2%

This tax would operate through the local tax system[20].

ii) **Scrapping the Small Business Bonus Scheme for Non-Domestic Rates** and replacing it with a relief for employers providing "fair work". Combined with other smaller changes to the NDRs system as outlined in Section 5.1, we estimate that this could initially save around £200 million a year, although the revenue yield would fall if a greater proportion of employers introduced fair work practices.

iii) **Replacing or supplement Non-Domestic Rates in Scotland with a Land Value Tax on commercial land** which raises a small amount of extra revenue (£100m, or around 3 per cent) compared to current revenue yields.

iv) **A frequent flyer levy** which we estimate will raise an additional £50 million per year.

v) **A super tax on private jets** which is estimated to raise £25 million per year (based on the calculations in Section 5.3.4).

vi) introduce a **local carbon emissions land tax** on landholdings exceeding 1,000 hectares (as outlined in Section 5.2.4. above).

vii) **Increasing the Scottish Aggregates Levy** by 30 per cent, raising £18 million.

[20] Calculations for revenue yield assume that the administrative cost of collecting the tax is equal to 1% of total revenues.

Table 6.2 shows estimates of the revenue yield from the longer-term reforms (at 2022/23 prices). The overall amount raised by the longer-term tax reforms is just over £2.6 billion. When combined with the short-term measures discussed in Section 6.1 above (the full package of short-term and long-term reforms raises just over £3.7 billion in 2023/24 prices. Based on the average Scottish public sector salary, and accounting for national insurance contributions and pension costs, £3.7 billion would fund 82,000 public sector workers in Scotland[21].

Table 6.2. Estimated revenue raised from longer-term package of reforms

Reform	**Revenue (to nearest £m)**
Wealth tax: 0.5% per year on assets £1-£2m, 1% on assets £2-£5m, 2% on £5m plus	1,416
Scrapping Small Business Bonus Scheme	200
PPT at 0.7% of property values combined with expanded rebate system	783
LVT on commercial property	100
Frequent flyer levy	50
Super tax on private jets	25
Carbon emissions land tax	13
Increase Aggregates Levy by 30%	18
Total revenue raised per year (£m)	2,605
Total revenue raised per year: short-term and long-term packages combined	3,710

Sources: Wealth Tax: as in Section 4.1. PPT: as in Section 3.3. Other taxes as specified in Chapter 5.

[21] Calculations based on mean public sector salary in Scotland of £34,816, taken from Annual Survey of Hours and Earnings (2023) https://www.ons.gov.uk/employmentandlabourmarket/peopleinwork/earningsandworkinghours/datasets/regionbypublicandprivatesectorashetable25

7 Economic impacts of the tax

This chapter looks at three aspects of the economic impact of increases in spending on public services (alongside the tax rises implemented to fund the increase: the distributional impacts (by income, wealth and gender), effects on the Scottish economy (macroeconomic impacts) and the environmental impacts.

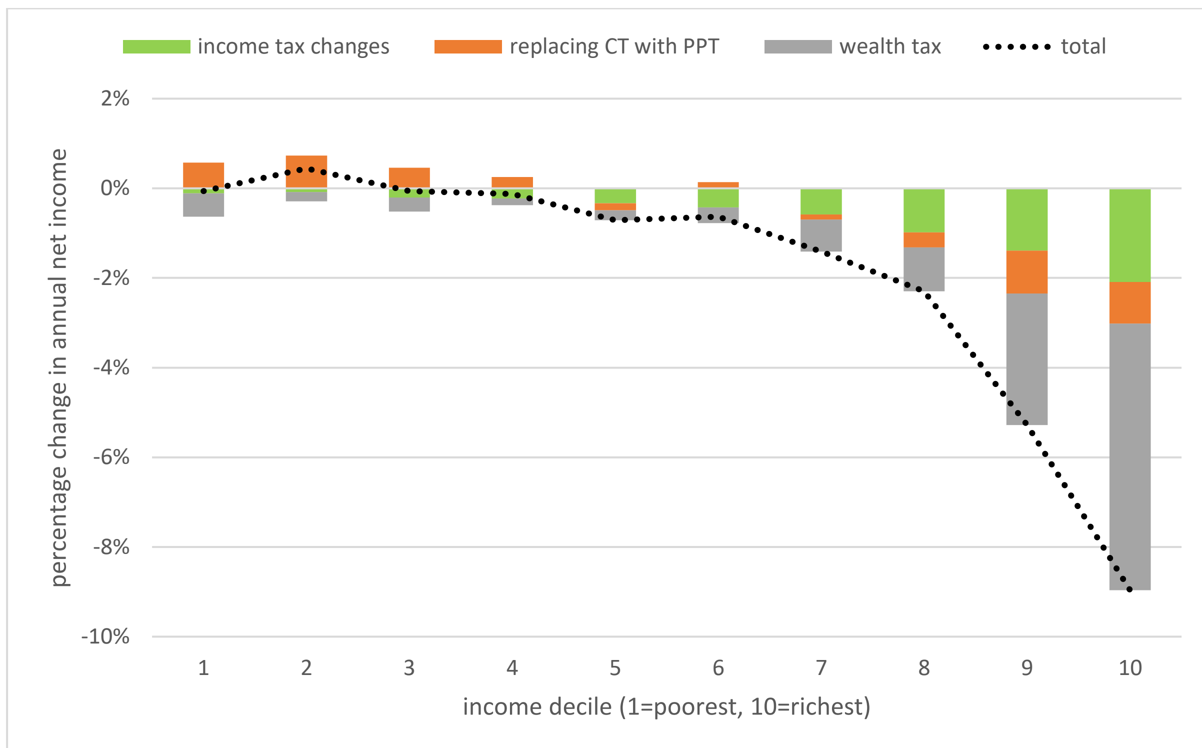
7.1 Distributional impacts

7.1.1 Impacts by income decile

Figure 7.1 shows the combined impact of the package of increases in income tax and the Proportional Property Tax and wealth taxes outlined in Chapter 6. The distributional effects for PPT show the change in net household incomes arising from the replacement of Council Tax by the PPT. The distributional impact of changes to business taxation (such as the reduction in expenditure on the Small Business Bonus Scheme, the replacement of Non-Domestic Rates with a Land Value Tax on commercial land, and the increases in landfill tax and the Scottish Aggregates Levy) are not shown as it is not possible to show the impacts of changes to business taxation on household incomes using any existing robust methodology. Similarly, increases in property transactions taxes (the LBBT and ADS) are not shown as the sample of Scottish households buying property in datasets such as the FRS or Understanding Society is not large enough to derive robust distributional results.

The distributional effects in Figure 7.1 are shown as a percentage of household net income, by household income decile.

Figure 7.1. Distributional income tax changes, PPT and wealth tax by household income decile



Source: Landman Economics analysis of Scotland subsample of Family Resources Survey and Wealth and Assets Survey data

Figure 7.1 shows that the changes to income tax are very progressive (as shown in Chapter 2), with the top two household deciles paying substantially more of the extra income tax as a percentage of income (on average) than households lower down the income distribution.

The introduction of a PPT has a progressive impact on the income distribution, with average gains for households in the bottom four deciles and losses for households in the top four deciles (with the top two deciles losing an average of 1% of their net incomes). The introduction of a wealth tax has an especially progressive impact at the very top of the household income distribution, with losses of around 6 per cent of net incomes on average. It should be noted that percentage losses are so high for the top income decile because average wealth for this decile (around £2.6 million) is much higher than average net income (just under £100,000), meaning that a 3 per cent annual charge on all household wealth above £2 million represents a large sum compared to average net income. However, households in the top decile would not necessarily need to fund their annual wealth tax payments out of current income; they could sell assets to fund the tax, or – in the case of property wealth – the wealth tax could be deferred until the property was sold or transferred after death[22].

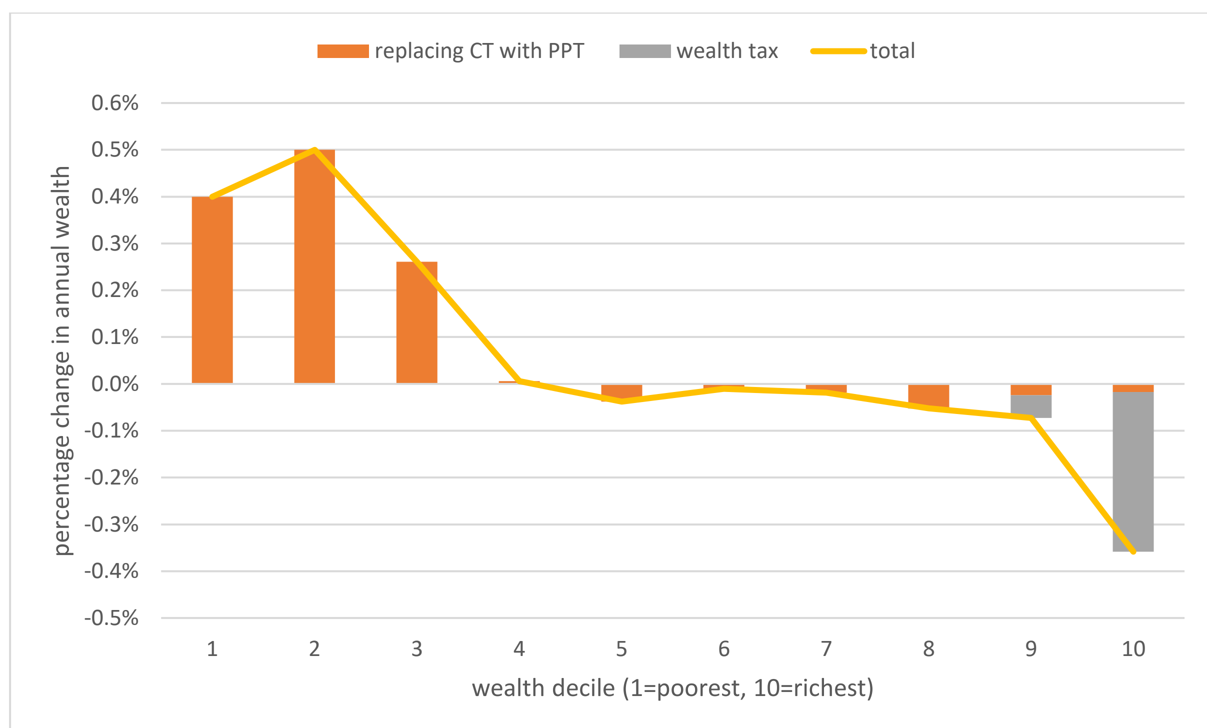
[22] Fairer Share (2020) gives details of how a deferral system for property taxation could be operated. This would reduce the yield from the wealth tax in the short-to-medium term but would increase it in the longer term.

Overall, the combined income tax, PPT and wealth tax package has a roughly zero average impact across deciles 1 to 4, and increasingly negative impacts in the top six income deciles, rising 9 per cent in the top income decile.

7.1.1 Impacts by wealth decile

Figure 7.2 shows the combined impact of the PPT and wealth tax by household wealth decile[23].

Figure 7.2. Distributional impacts of reforms to property and wealth taxation by household wealth decile



Source: Landman Economics analysis of Scotland subsample of Wealth and Assets Survey data

Figure 7.2 shows that the replacement of Council Tax with a Proportional Property Tax has a progressive impact across most of the wealth distribution. For low-wealth households the tax burden of PPT is lower, on average, than Council Tax (after taking account of the enhanced reduction scheme for PPT compared to Council Tax). For households in the top six wealth deciles, there is a slight negative impact from the introduction of PPT due to the increased revenue yields from PPT

[23] it is not possible to show the impact of the income tax package by wealth decile because the Landman Economics tax-transfer model is not currently configured to model income tax changes on the Round 7 Wealth and Assets Survey data.

compared to Council Tax. For households in the top wealth decile, the wealth tax plus the extra yield from PPT results in a combined tax payment of around 0.35 per cent of total wealth per year on average. Thus, the combined impact of the tax package is strongly progressive with respect to wealth.

7.1.3 Other distributional impacts

As explained in last year's report (Reed 2022) a package of progressive tax reforms along the lines presented here helps reduce inequalities in net incomes by gender, particularly if combined with a boost to public sector pay and additional investment in public services[24].

7.2 Macroeconomic impacts

The macroeconomic impacts of an increase in spending on public services fully funded by a tax increase (which is necessary in this case, given the Scottish Government's lack of borrowing powers and hence the need to balance its budget) is likely to have an expansionary macroeconomic effect for four reasons:

- First, the "balanced budget multiplier", which implies that overall spending in the economy will increase because the increase in government spending is likely to be higher than the reduction in private sector consumption due to the increase in tax (because the "marginal propensity to consume" out of private sector income is less than 100%, due to saving by private sector households).
- Second, any increases in the public sector pay bill arising from the increase in public spending (either due to hiring new public sector workers or pay increases for existing public sector workers) are likely to increase net income in the middle of the income distribution (deciles 5 through 9, where most public sector workers are located) while the tax increases reduce income in the top decile (10). The marginal propensity to consume is likely to be higher for households in the middle of the income distribution compared to households at the top of the income distribution, and the combined package of pay increases and tax increases could therefore lead to a rise in economic activity through increased consumption and multiplier effects.
- Third, because the bulk of the combined (short-term and longer-term) tax package consists of taxes on wealth and property rather than taxes on incomes, it is likely that the wealthiest households will sell assets to fund their annual wealth tax payments rather than making the payments out of current

[24] Research on the distributional impact of public spending shows that spending on most services (such as health, social care, schooling, early years and social housing provision) is strongly redistributive with respect to household income. By the same token, real-terms spending cuts since 2010 have been regressive (see Horton and Reed, 2010; Reed and Portes, 2018).

income. This is likely to mean that the increase in current consumption from increased pay for public sector workers will be larger than the reduction in consumption due to wealth tax payments for the wealthiest households, even though the pay and tax package is designed to be revenue-neutral overall.

- Finally, to the extent that increased public spending leads to improved functioning for public services that are currently cash-strapped (such as Councils and the NHS), it should lead to productivity improvements by enabling a healthier society and healthier workforce. For example, across the UK as a whole, the Office for National Statistics suggests that long COVID has increased economic inactivity rates (ONS, 2022). If additional funding for the NHS in Scotland results in better diagnosis and treatment for long COVID sufferers, this could result in an increase in the number of healthy workers in Scotland which would deliver productivity benefits.

7.3 Environmental impacts

The package of additional investment in public services (and the associated tax increases) includes a number of measures which have been suggested by climate advocacy groups to facilitate transition of the Scottish economy to net zero and shift the costs of carbon emissions on to polluters. Most obviously, the Oxfam (2023) report *Payment Overdue: fair ways to make polluters across the UK pay for climate justice* recommends a super tax on private jets, and a frequent flyer levy, both of which are covered in Section 5.3 of this report. Also, a recent report published by Stop Climate Chaos Scotland (Dixon, 2022) suggests replacing Council Tax and other local taxes with a land, property or local wealth tax. The John Muir Trust's recommendation for a tax on carbon emissions from land is recommended in Section 5.2 of this report.

8 Conclusions

The updated results in this report show that there is potential to fund increased investment in public services in Scotland using a progressive and costed package of tax increases. In the short run, the report recommends a number of reforms to the tax system which could be introduced as early as April 2024, raising just over £1.1 billion of additional revenue per year as follows:

- £779 million from a series of income tax reforms
- £240 million from increases to Land and Buildings Transactions Tax
- £56 million from increasing the Additional Dwellings Supplement
- £30 million from increasing Scottish landfill tax.

In the longer run, the report recommends raising almost an extra £2.6 billion per year from a series of more complex reforms to the tax system including:

- £1,416 million from a wealth tax
- £783 million by replacing Council Tax with a Proportional Property Tax
- £200 million from scrapping the Small Business Bonus Scheme for Non-Domestic Rates and replacing it with a better targeted scheme of relief for Fair Work employers
- £100 million from the introduction of a Land Value Tax for commercial land
- £50 million from a frequent flyer levy
- £25 million from a super tax on private jets
- £13 million from a carbon emissions land tax
- £18 million from increasing the Scottish Aggregates Levy.

This package of reforms could be fully in place by 2028 if legislated for in 2024.

In combination, the short-run and longer-run packages could raise an extra £3.7 billion per year used to fund substantial additional investment in Scotland's public services. £3.7 billion could fund 82,000 public sector workers in Scotland. The elements of the package of tax increases which can be modelled are distributionally progressive whether measured by household wealth or household income.

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