



TOWARDS A FAIRER TAX IN SCOTLAND:

The Scottish Pensioner Perspective

Submission to the Scottish Government consultation on a Local Income Tax

June 2008

Submission to the Scottish Government's Consultation – *A Fairer Tax for Scotland*

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June 2008

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1.0 INTRODUCTION

Age Concern Scotland, in conjunction with the School of Accounting, Economics and Statistics at Napier University, has prepared this report in response to the Scottish Government's consultation on the proposal to replace Council Tax with a Local Income Tax. Its purpose is to provide impartial comment on this proposal and to examine some of the basic premises upon which it is based. This report also makes some radical suggestions on Council Tax reform for older people in Scotland with the intention of encouraging innovative thinking, stimulating debate and widening discussion about other ways of addressing the inequities of Council Tax.

At face value, the Local Income Tax appears to be more popular with older people than Council Tax. While many older people will be better off under the Scottish Government's proposals 33 per cent of single pensioners and 12 per cent of pensioner couples will be no better off. Not all of the questions relating to the introduction of the Local Income Tax have been satisfactorily explored or answered which means that the full extent of its benefit to older people is difficult to assess accurately.

Age Concern Scotland has been consistent in its view of local government tax reform systems irrespective of whether these are property or earnings related. We have historically upheld three key principles on local government tax systems:

- They must be fair (based on the ability to pay)
- Easy to understand (practicable in their application)
- Sustainable (they raise enough money to pay for services)

The current Council Tax system, based on property banding, is relatively easy to understand and enables older people to budget with a degree of certainty. It has, more or less, shown itself to be economically sustainable in that it has continued to support local government service delivery. It is not however deemed by older people to be a fair tax because it does not take into account their ability to pay. It does therefore continue, by default, to penalise some of the most vulnerable and economically disadvantaged older people in society, despite the availability of means tested benefits such as Council Tax benefit. The principles outlined above underpinned our submission to the *Council Tax Abolition and Service Tax Introduction (Scotland) Bill* as proposed by the former MSP, Tommy Sheridan, as we believe they are a good and simple measure of any system.

We have confined ourselves very much to the impact of changes in the tax system on the pensioner population and have not entered into the wider economic debate about the potential impact of different taxation regimes on the Scottish economy. Nor have we entered into the 'constitutional' dimension to the debate concerning the continuation of Council Tax benefit under any proposed alternative charging system to the Council Tax. We

believe this approach to be entirely appropriate for an older people's charity. Council Tax and Local Income Tax are highly-charged subject areas and it is important that charities engage in this debate with sensitivity while retaining objectivity and maintaining a non-political stance.

2.0 THE CONTEXT

2.1 Pensioner Income in Scotland

In 2007 the average gross household income in Scotland was £23,075 (High Level Statistics, Scotland, May 2008). This contrasts sharply with the average pensioner household income for the same period which was £12,579 and which is primarily made up of the state pension and occupational pensions. The sources of pensioner income in Scotland are not significantly different from the rest of the UK.

The average pensioner household income however varies substantially across Local Authority areas. For example, the two local authorities with the lowest average pensioner household income were Glasgow City and Eilean Siar at approximately £11,500. The two local authorities with the highest were East Renfrewshire and East Dumbartonshire with an approximate average income of £14,500. This is a gap of 26 per cent. On the other hand, there are local authority areas where pensioner household income reached nearly £40,000, albeit the number of pensioner households in this category is extremely small.

The definition used for low income households is less than 60 per cent of the average figure which in 2007 was £13,845. Of the 1.15 million Scottish households below this income level, pensioner households constitute approximately 44 per cent.

There are only three Local Authorities where the average pensioner household income is marginally above 60 per cent of the Scottish average income level – these include East Dumbartonshire, East Renfrewshire and Argyll & Bute. All the other twenty-nine Local Authorities have average pensioner household incomes below the 60 per cent threshold.

Table 1: UK Retired Household Income 2005/06 by Quintile Group

	BOTTOM				TOP
Income Source	1st	2nd	3rd	4th	5th
Earnings (1)	1770	3160	4320	7970	25240
Pension	5250	6520	6250	6520	6520
Non-Cont Benefits	1220	1810	2710	2880	2010
Gross Cash Income	8240	11490	13280	17370	33770
Disposable Cash Income	7340	10500	12170	15480	28260

Source: ONS, 2006, Note: (1) Earnings are from occupational pensions and investment income. In each quintile the share in earnings from investment income is very small.

An interesting feature of this data is that the share of earned income from wages is less than 10 per cent in every quintile. This means that those pensioners in some of these quintile groups will now pay more in tax as a result of the removal of the 10p band. This further explains why some pensioners will either pay the same or more under a Local Income Tax since income from occupational pensions is not excluded (see *A Fairer Local Tax for Scotland, 2008*). In fact the latter makes it clear that 33 per cent of single pensioner households and 12 per cent of pensioner household couples will be no better off under the proposed Local Income Tax.

2.2 Pensioner Contributions to the Council Tax

In 2007 Scottish pensioner households paid a total of £456m (see Chart 3, page 16) in Council Tax which represents, on average, 6.3 per cent of their income and just under 20 per cent of the total Council Tax paid. The reason for this is that there are significantly more single pensioner households living alone. 76 per cent of pensioner households pay either the full Council Tax or are paying a contribution towards their Council Tax (*net Council Tax greater than zero*).

To put this into perspective it means that just under 104,000 single pensioner households in Scotland in 2008 will continue to pay the same (in Local Income Tax) as they currently do in Council Tax. It is projected that by 2024 the number of pensioner households affected will rise to nearly 138,000, 70 per cent of whom will be single female pensioners.

In 2007, pensioner households paid on average £792 in Council Tax, this is net of the 25 per cent single person household entitlement. When correlated by Local Authority area, the relation between the proportion of pensioner households aged 65 and over and those receiving the 25 per cent single person household entitlement and/or Council Tax benefit is over 83 per cent. This suggests that it is the 25 per cent single person household entitlement that dominates the reduction received by pensioner households. When we compare the proportion of pensioner households receiving the 25 per cent single person reduction and/or Council Tax benefit with earned income by these households per Local Authority area the correlation is 63 per cent. This is surprising since we would expect to see a negative correlation between Council Tax benefit and earned income unless all or almost all of such is income that is disregarded for Council Tax benefit.

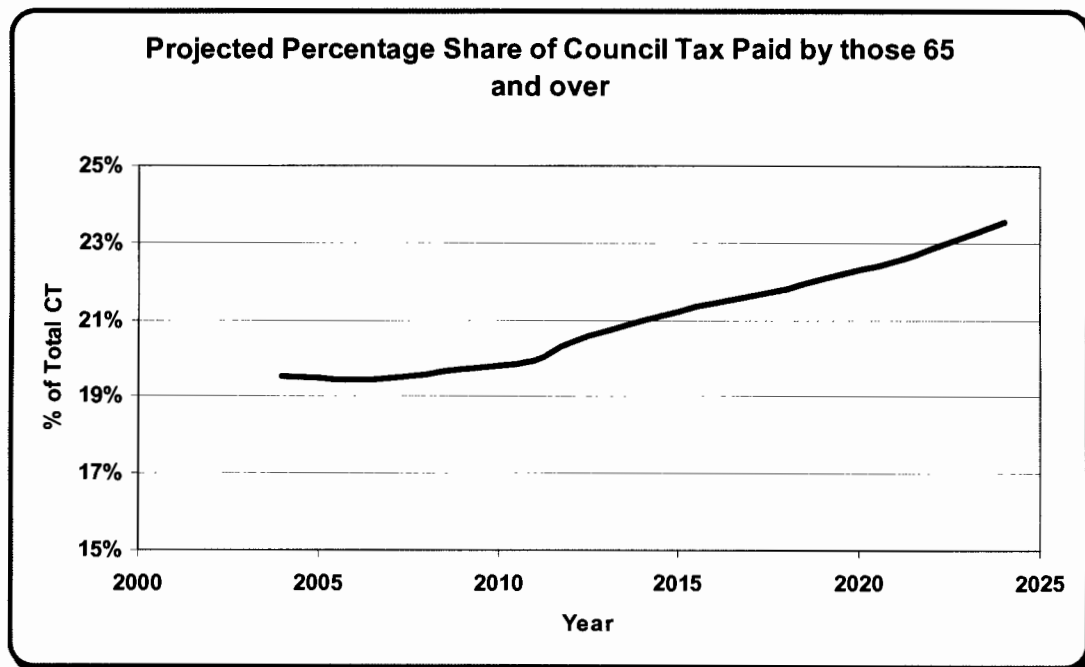
In West Dunbartonshire for example, pensioner household earned income averaged £252 in 2006/07 with 79 per cent of pensioner households having received Council Tax benefit. In Clackmannanshire, on the other hand, the pensioner household earned income averaged £775 with the same 79 per cent of these households having also received Council Tax benefit (including the 25 per cent single person household entitlement). It would seem that even a threefold difference in earnings makes little difference to the

proportion of pensioner households who receive Council Tax benefit inclusive of the 25 per cent single person household entitlement.

This can only be the case if it is the 25 per cent single person household entitlement that dominates the distribution. Of course this does not indicate the amount of actual Council Tax benefit received in the two Local Authority areas. The average net of entitlement Council Tax in Clackmannanshire was £744 in 2006/07 and £700 in West Dumbartonshire. It is not possible to determine how much of these two sums were actually paid by pensioners since the data simply does not allow this. Basically, other than the 25 per cent single person household entitlement, there appears to be no readily available data that will detail the actual *cash amount* paid by pensioner households.

Given that Scotland has an ageing Scottish population, if no change is made to the current Council Tax system the percentage of total Council Tax contributed by pensioner households will increase from just under 20 per cent in 2008 to 24 per cent in 2024.

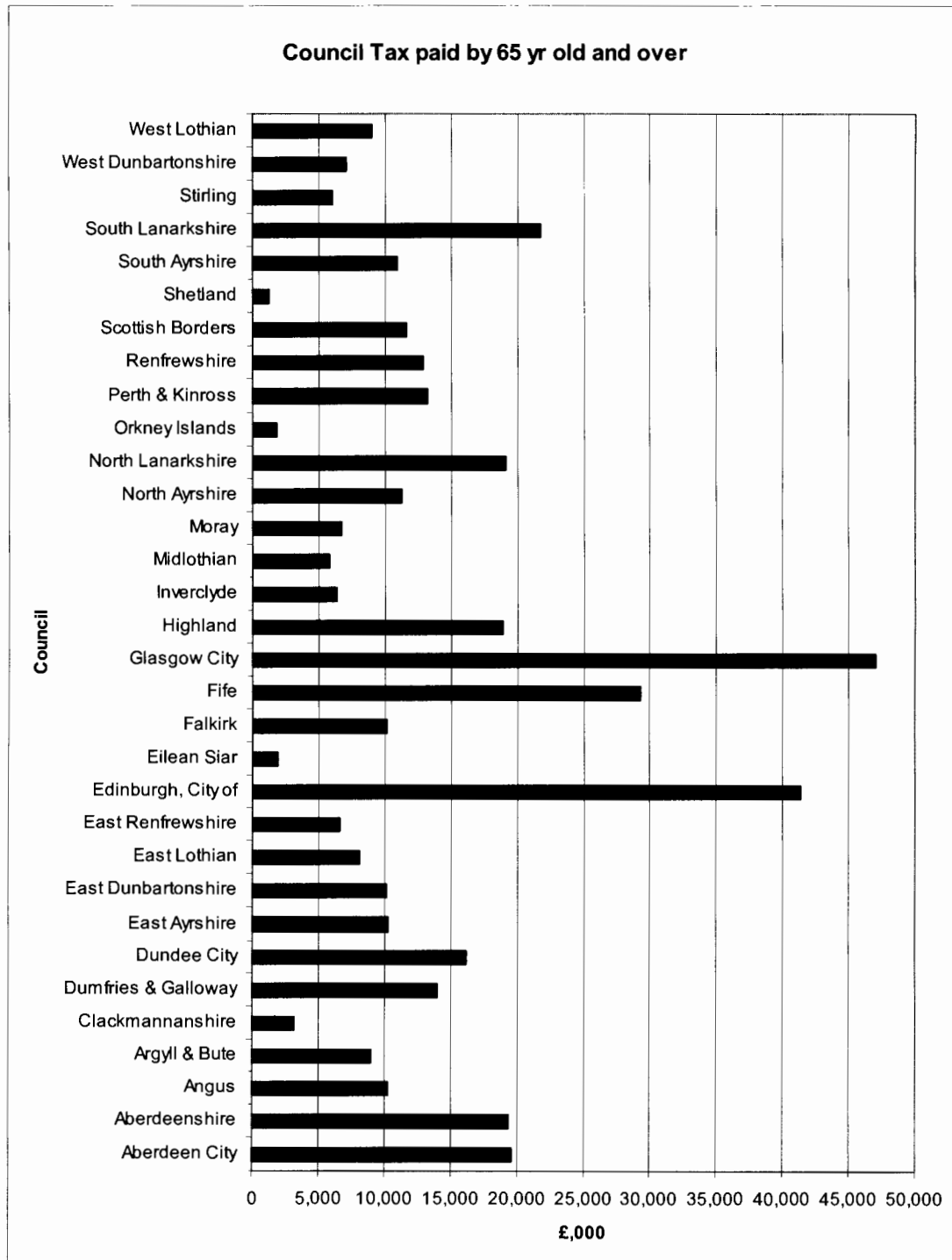
Chart 1: Pensioner Contribution to Scottish Council Tax



In figures, this means a growth from £456m in 2008 to about £620m in 2024 (see Chart 3 page 16). If we consider all quintile groups of pensioner households, except the top quintile, then average gross cash income is only 45 per cent of average gross cash income for the UK as a whole. Even the top quintile of pensioner households only manages an annual gross cash income marginally above that for the UK as a whole. In other words, if there are 'rich' pensioner households then they must be few and far between. In any case such pensioner households are most often asset rich (home ownership) and certainly not cash rich. This is a very small proportion of the pensioner household population and to include them in a complete Council

Tax abolition would have little effect on the financing of Council Tax in Scotland. The breakdown by Local Authority area in pensioner household Council Tax payments in 2006/7 is given in Chart 2 below.

Chart 2: Council Tax payments by Pensioner Households in 2006/7



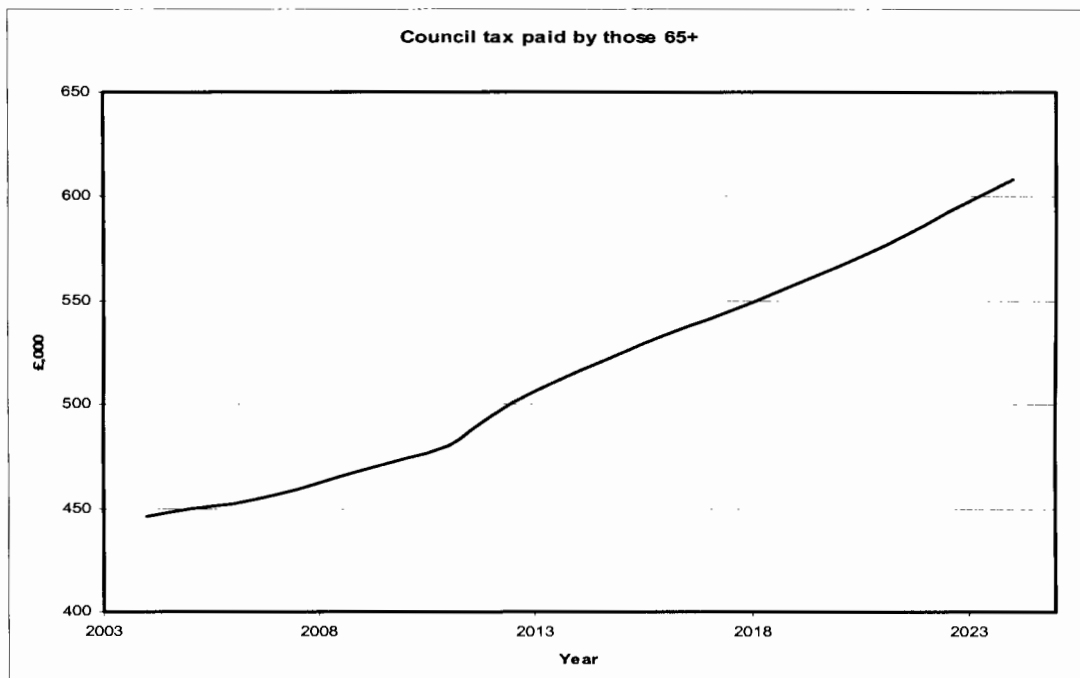
The contribution towards Council Tax by pensioner households varies substantially according to pensioner household distribution across Scotland's local authority areas. This should be dependent on the size of the pensioner population per Local Authority area but it is also related to the proportion of such households per Local Authority area. This is because the distribution of pensioner households is not even across the Local Authority areas of Scotland. Therefore the relationship between the proportion of pensioner households and their contribution to the Council Tax per Local Authority area is in fact extremely tenuous resulting in some Local Authority areas receiving greater amounts of Council Tax benefits from the Department of Work & Pensions than others.

As discussed earlier, the proportion of pensioner households in receipt of Council Tax benefit (inclusive of the 25 per cent single person household entitlement) varies between Local Authority areas - from over 83 per cent in Glasgow City to a mere 54 per cent in Moray. In Glasgow about 94 per cent of pensioner households do not have an earned income while in Moray the figure is 84 per cent. This seems strange given the massive difference in Council Tax benefits take-up between the two Local Authority areas and it is extremely difficult to explain but clearly there is a low take up in Moray. There appear to be considerable differences in pensioner household incomes, Council Tax benefit receipts and almost no correlation between the two across the Local Authority areas. This would suggest that a significant degree of spatial inequality already exists for pensioner households in spite of the Council Tax benefit system.

While targeted or means tested benefits are claimed to be fairer, in that wealthier people are not in receipt of such benefits, the reality is that the proportion of relatively wealthy pensioners in Scotland is so small as to make targeting almost unnecessary. Furthermore, as the evidence indicates, the availability of advice and information about how to claim benefits (arguably the real difference between Moray and Glasgow) may be a decisive factor in claim rates, and hence the impact on poorer pensioners.

The pensioner household contributions are projected to grow substantially from just over £456m in 2006/07 to over £620m in 2024, a 50 per cent increase in the contribution by pensioners to Scottish Council Tax. This will be reflected across every Local Authority area in Scotland. The amount of increase is shown in the Chart below:

Chart 3: Growth in Pensioner Household Contribution to Council Tax in Scotland to 2024

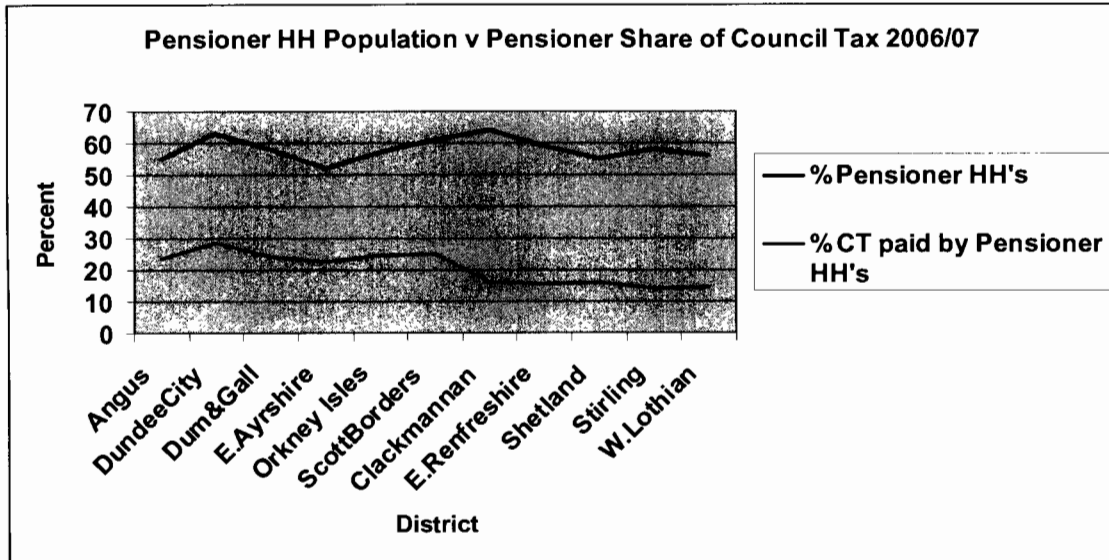


In practice the Department of Work & Pensions will be paying a substantial part of this through Council Tax benefits but only if the current system of entitlements and benefits is retained. However any deviation from the latter could result in pensioner households becoming significantly worse off purely in relation to the incidence of Council Tax. The amount of Council Tax benefit, including the 25 per cent single person household entitlement varies between local authority areas. For example in Angus, Dundee City, Dumfries & Galloway, East Ayrshire, the Orkney Islands and the Scottish Borders the amount received by pensioner households was *less* one standard deviation below the average. In other words the contribution by pensioners to the total Council Tax in these Local Authority areas is significantly higher than the average for Scotland as a whole. And yet the amount received in Clackmannanshire, East Renfrewshire, Shetland, Stirling and West Lothian was *greater* than one standard deviation above the average. This means the pensioner contribution to the total Council Tax in these Local Authority areas was significantly less than the national average. This distribution is surprising for two reasons.

Firstly, we would expect the second category to include Local Authority areas with the greatest problems, (for example in terms of the Multiple Deprivation Index) such as Glasgow, Inverclyde, South Lanarkshire and so on, yet these are not represented in this category. This suggests that the take up of Council Tax benefit in these Local Authority areas is not as high as it should be. Similarly, for those Local Authority areas where the benefit is significantly below the average it suggests that either pensioners are very well off or, more likely, the take up of Council Tax benefit is extremely low. When we

compare the proportion of pensioner households in these Local Authority areas with their share of the Local Authority area Council Tax we find almost no association – this is clear given in the Chart below:

Chart 4 Association of Pensioner Households and Council Tax Paid by Pensioner Households



In fact the correlation coefficient between these two proportions is a mere 11.24 per cent. In other words, there is almost no association between the proportion of pensioner households in a Local Authority area and their contribution to that area's Council Tax. This is not what we would expect. What this analysis suggests is that the impact of Council Tax on pensioner households is significantly different for different types of households and for pensioner households located in different Local Authority areas in Scotland.

In other words, there appear to be three types of inequality in the impact of Council Tax on pensioners – in terms of *where a pensioner lives* (spatial), *gender* and *single status*. In effect it means that a single female pensioner living in a Local Authority area such as Dundee is likely to be in the very worst position regarding the impact of the Council Tax. Such inequalities in Scotland between the pensioner population and the population as a whole, and within the pensioner population, are unacceptable for a socially cohesive Scotland.

We believe that although a Local Income Tax will go some way towards correcting these it cannot possibly do so universally. An alternative is that Council Tax benefit could be given the same status as other universal benefits i.e given as of right in order to sweep away, in one policy, these significant inequalities. This is a policy that could be phased-in over time.

2.2 Single Female Pensioner Households

According to a report by the Office of National Statistics (ONS) – ‘*The Effects of Taxes and Benefits on Household Income (2005/2006)*’ a total of 59% of pensioner households with two or more adults are in the lowest 40 per cent of the UK income distribution. However in the case of single female pensioner households 67% are in the lowest 40 per cent of the income band. In other words, the majority of pensioner households are represented by single females and two thirds are in the lowest income groups in society. The office of National Statistics (ONS) also report that this situation has hardly changed in the past decade. This pattern is reflected across all component countries of the UK.

When compared to non-retired households the proportion of income paid by pensioners in Council Tax is higher and this is particularly the case for single female pensioner households. Given that in Scotland the latter make up nearly 75 per cent of all single pensioner households and that this proportion is projected to increase, then a key issue raised in this report is one of gender inequality amongst our older population.

We also know from the most recent Office of National Statistics (ONS) report (*op cit*) that this group, on average, have an income which is only 69 per cent of that received by *single male* pensioner households. This means that within the pensioner population as a whole the impact of the Council Tax is highly skewed against the most vulnerable and economically disadvantaged pensioner households.

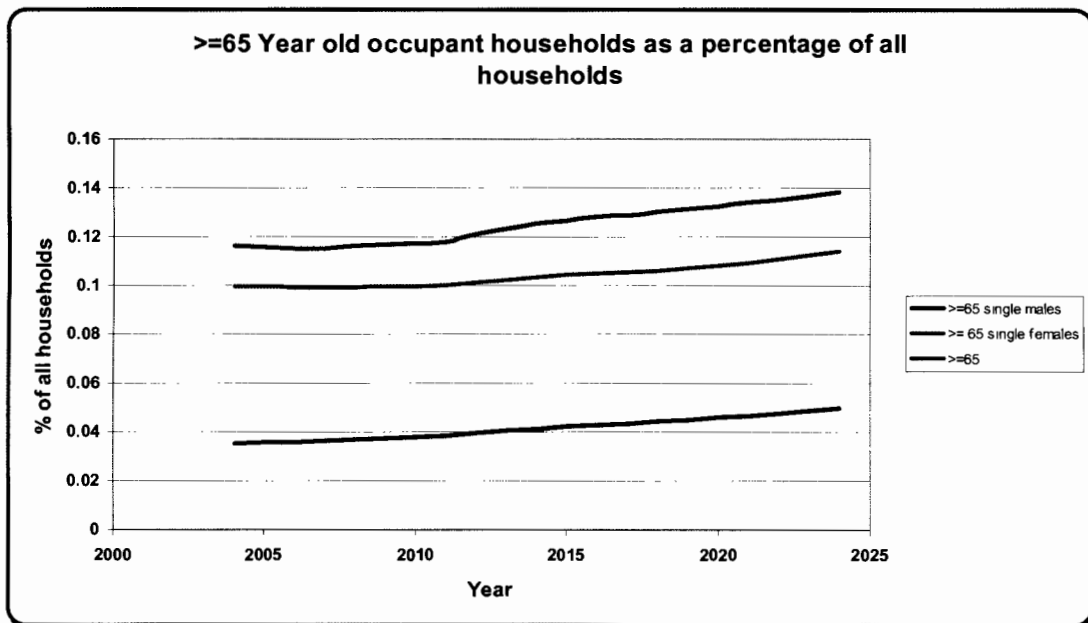
In 2004/05 the total number of pensioners in Scotland living in relative low income was estimated at 170,000 which was 30 per cent of all pensioner households (in 2007 this rose to 44 per cent). Of these, 110,000 were female and 60,000 were male (see *High Level Statistics Scotland, 2008*). The majority of these female pensioners will be in single person households. As the definition of relative low income is 60% or less of the GB average income we already know that female pensioners receive, on average, only 69 per cent of the male pensioner income and, although it is not possible to provide an exact calculation, this would suggest that the majority of our single female pensioners are existing considerably below the 60 per cent average income definition of relative low income. When we consider that this particular group represents nearly 40 per cent of all pensioner households there is clearly a major gender issue here. Even by 2024 the percentage they occupy amongst all pensioner households will fall only marginally. The projections are given in the table below.

Table 2: Structure of Pensioner Households

Year	All 65+ HH's	%Single Pensioner HH's	%SFPH	%SMPH	SF as % of all SPHH's
2007	576,120	54	39.5	14.5	73
2024	768,000	54.2	37.7	16.5	69.5

As we move up the age scale (to 85 or over) we find that the percentage of females living alone is projected to increase from 59 per cent in 2007 to 70 per cent in 2024. Between 2006 and 2031 the growth of the pensioner population aged 75 and above will be 81 per cent and for those aged 60 to 74 it will be 40 per cent. These astonishing growth rates however hide the fact that the considerable majority will be single female pensioners as illustrated in Chart 5 below.

Chart 5 - 65 Year old occupant households as a percentage of all households



In other words gender inequality can become more serious with increasing age and the question must therefore be asked about whether this is fair. This will be substantially more relevant for the single female pensioner than for any other group in society. It could further be argued that since this group, more than any other, receives maximum benefit towards Council Tax (if they take this up) then a complete abolition of the Council Tax for this group will make no significant difference to public finances. The same argument also applies to the 60,000 single male pensioners in Scotland who live below 60 per cent of the average GB income.

The above analysis clearly demonstrates that the current Council Tax system produces several types of unintended inequalities, not least gender inequality. Removing these using a Local Income Tax, property tax or hybrid tax will not necessarily work unless it is fully funded. Similarly, changing Council Tax to one of the above will still leave many pensioners, especially single pensioners, having to pay a substantial proportion towards Local Authority funding in the future.

In summary, if a Local Income Tax is introduced without full funding or at a level which makes it impossible to retain it at a 3p in the £ level, it may fail a sustainability test and end-up costing some older people more than originally envisaged in *'Towards a fairer tax in Scotland'*. Income taxes are less predictable and less easy to budget for than property based taxes, albeit they are fairer. Similarly, tinkering with Council Tax bandings will not address many of the inequalities of the present system.

Age Concern Scotland believes there is value in examining the case for very significant discounts for pensioner households under the present system as a potential alternative to the Local Income Tax as proposed.

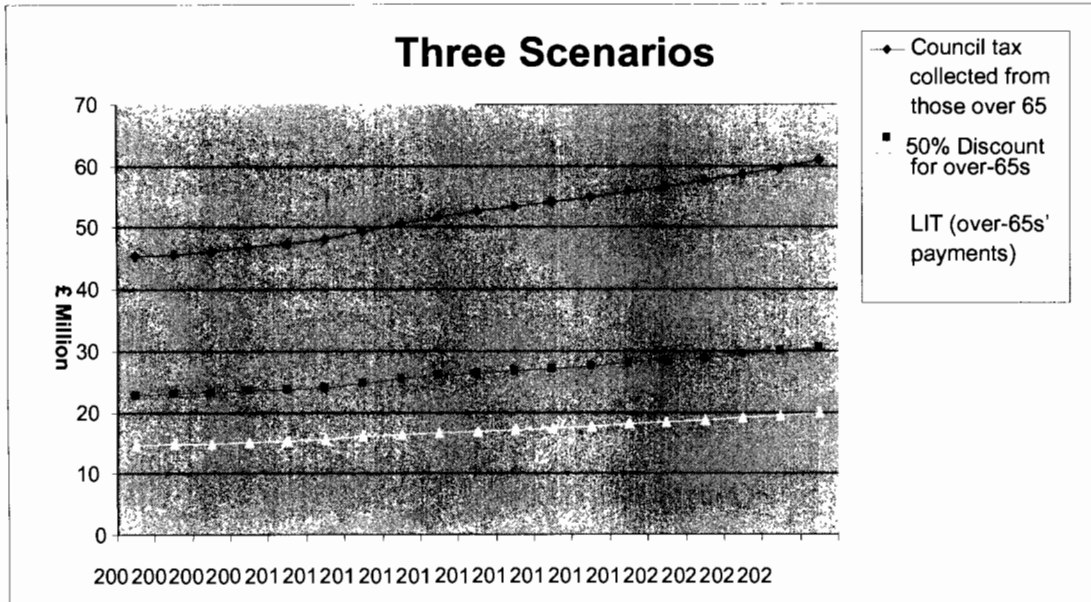
3.0 THE ARGUMENT FOR A DISCOUNTED RATE OF COUNCIL TAX

3.1 FINANCING

Over the next three years the Department of Work & Pensions is forecast to provide £1.1bn in Council Tax benefit to Scottish local authorities. Our forecast of the total contribution (including Council Tax benefit) from the pensioner population to 2024 is given in Chart 3. If we compare this over the next three years with two proposed alternative systems, Local Income Tax and a 50 per cent discount for all pensioners on Council Tax we can see the impact each will have on how much tax the pensioner population pays, shown in chart 6 below.

Under the three scenarios in the period 2007 to 2012, that is – Top Line – no change; Middle Line – 50% discount and Bottom line – Local Income Tax pensioners will still contribute substantially to the funding of local authority services.

Chart 6: Three Scenarios



If, for example, the Local Income Tax had been in force in 2007, Scotland's pensioners would still have paid a total of £148m. They actually paid £466m in 2007, net of the 25 per cent single person entitlement and Council Tax benefit.

Those who will be expected to pay a contribution under Local Income Tax still represent about one-third of all pensioners, yet the equivalised income for these pensioners is by no means significant in terms of the UK average. Even though the Local Income Tax and to a lesser extent a 50 per cent discount proposals help many pensioners they cannot help all pensioners, particularly that significant group who rely heavily on an occupational pension and for whom the actual sum is actually quite small.

Table 3: Pensioner Contributions Forecast 2007-2102

YEAR	2007	2008	2009	2010	2011	2012
No Change	456.32	461.99	468.28	473.71	480.17	494.74
50% Discount	228.16	230.99	234.14	236.85	240.08	247.37
LIT	147.94	149.68	151.67	153.46	155.58	159.94

As can be seen from this table, on the face of it, pensioners as a whole would contribute less under a Local Income Tax system than a substantially reformed Council Tax system with a 50% discount. However, this assumes that all the existing Council Tax benefit is available for use in the Local Income Tax system. The sum involved is approximately £400m. Additionally, the savings that are estimated in 'Towards a fairer tax in Scotland' of £60-80m of the new system of Local Income Tax are just that –

'estimated'. If these two elements are not presented in the calculation of the overall funding package for Local Income Tax, the funding will need to be found from elsewhere which will have significant implications for the rate at which the Local Income Tax is set, or the level of public expenditure on local government services.

Council Tax raises approximately £2.1bn. A Local Income Tax will not raise as much and is therefore to a degree reliant on use of Council Tax Benefit to 'square the circle.' Under the Local Income Tax the top 10 per cent of income earners will pay (approximately) an additional £60.40 a month as part of the equation of making a Local Income Tax 'stack-up' financially. If, for example, a 50 per cent discount were given to pensioner households, the equivalent sum to be found from top earners would be £24.68 or at a 100 per cent discount £49.36 a month.

In short, even top earners would be paying less because it can be proposed that by giving a discount to pensioner households the Scottish Government would be able to argue that the £400m in Council Tax benefit should still be available. Giving a 50 per cent discount to all pensioners, assuming all other factors remain the same, would require about £231 million of Council Tax to be replaced. A discount of 100 per cent to all pensioner households would require about £462 million. This can be raised by increasing the tax on the employed population, who would at least be clear that their increased taxes were going directly to the pensioner population.

3.2 Balance of Benefit

It is arguable that a Local Income Tax will directly benefit two-thirds of pensioner households, if Council Tax benefit and potential savings are taken into account.

It is equally arguable that a council tax discount policy for pensioners would benefit even more pensioner households because a discount policy would continue to attract Council Tax Benefit.

What it comes down to is the willingness of the population that is earning to pay a higher level of tax to pay for a lesser rate of tax for pensioners.

Under a Local Income Tax there are many more households which stand to gain who would certainly not gain under a discounted council tax system, but at least these households would be receiving other forms of state benefit and would still be protected.

A discounted system will therefore very likely offer a greater measure of protection to the financially most vulnerable among the pensioner population than a Local Income Tax.

Taking this argument further, if Council Tax Benefit were paid as an *entitlement* rather than a benefit to be claimed, something that all pensioners

would receive automatically then considerable savings would accrue from a simpler system.

There are some who would argue that the Local Income Tax policy leaves the very wealthy pensioner untouched. As it is acknowledged in the Scottish Government's own consultation paper this is a very small group of people and should not be considered material in balancing the cost and benefits of the proposed new discounted council tax system.

3.3 Is a discount scheme practical?

The technology or system required to generate a significant discount on the basis of age already exists in the Department of Work and Pensions and Local Authority systems. There is little effort required to load such an instruction into the software. To do so is relatively simple and it is this which makes our proposal worthy of further consideration. The other element which adds to the practicability is that no action is required on behalf of the pensioner to 'trigger' the discounted Council Tax as the data on residence, age, and date of birth is already in the systems.

4.0 LOCAL INCOME TAX – QUESTIONS TO BE ANSWERED

Age Concern Scotland fully accepts that the Local Income Tax could benefit approximately two-thirds of the pensioner households in Scotland. However, this may leave some pensioners no better off and, in some cases they could be worse off depending on how occupational pension income and other sources of income are treated. There are however a number of questions that Age Concern Scotland believes need to be answered in order to remove some of the doubt over the viability of the Local Income Tax.

- *If the Department of Work & Pensions do not transfer Council Tax benefits in the future it is unlikely the 3p in the £ Local Income Tax will be sufficient to sustain Local Authority funding. Will the Scottish Parliament have the legislative competence to raise the tax beyond the proposed level of 3p in the £.?*
- *How will water and sewerage charges be treated under the Local Income Tax? For example, will water metering become compulsory? If so, who will pay for the installation of water meters? If it is to be the householder, then the potential cost of installing meters which may range from £200 - £300 per single meter may potentially wipe out the benefit of the winter fuel allowance in a single year for pensioner households, for example.*
- *What consideration has been given to the fact that Local Income Tax would leave some 'higher' income households substantially worse off? This could, for example, have a serious impact on skilled labour supply in the future thereby constraining Scotland's development as a 'knowledge' economy and lead to fiscal flight by many employed within essential occupation sectors such as health, for example.*

- *Every person earning income above the basic tax allowances will incur a Local Income Tax? What impact will this have for those on relatively low income households. For example, a sole earner could be faced with a liability greater than their current Council Tax charge.*

5.0 CONCLUSION

Age Concern Scotland has sought to demonstrate that there may be other alternatives to a Local Income Tax in order to address the issue that has given rise to the debate about Council Tax, in particular its obvious unfairness to pensioners.

If, as we have argued, a policy of a substantial discount is phased in over time, it will most probably be more effective in protecting the most vulnerable and economically disadvantaged pensioners than a Local Income Tax. This option is then surely worthy of more detailed examination.

88 per cent of our pensioner population have an annual income of less than 60 per cent of the average income for the country as a whole. There is no other section of Scottish society in this position. To attempt to address this through a Local Income Tax is a brave and laudable effort to address true unfairness inherent in the system. However, the same issues might equally be addressed through substantial discounts to pensioner households without the inherent disruption that introducing a new system will entail.

6.0 METHODOLOGY

1. All council tax receipts and band D rates by council were obtained from Scottish Government Local authority Statistics for 2006-2007.
2. Then from the General Register of Scotland estimates of all occupied dwellings, small 65 yr old and over dwellings and single occupancy 65 yr old and over dwellings were obtained.
3. Then from the Scottish Household Survey 2005-2006 using the random adult 65 yr old and over the percentage obtaining benefit were computed for small adult households and single pensioner household. The mean level of council tax benefit was then computed.
4. Finally the amount of council tax paid by 65 yr olds and over was calculated using the following procedure:

Total council tax paid by 65 yr olds and over =

Number of 65 yr olds and over households * tax on band D – % small adult households * number of 65 yr old and over households * mean benefit given to small adult households – % of single pensioner households * number of 65 yr olds and over households * Tax on band D * 0.25 – % of single pensioner households * number of 65 yr olds and over households * mean benefit given to single pension households

7.0 DATA SOURCES

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Scottish Government, **A Fairer Local Tax for Scotland**, 2008. Consultation Paper.