National Tax Journal, Vol. 44, no. 4, (December, 1991), pp. 421-36

LESSONS FROM THE BRITISH POLL TAX DISASTER**

PETER SMITH*

ABSTRACT

As a means of financing British local government, the attempt to replace the residential property tax with a community charge, or poll tax, has proved disastrous. Yet underlying the reform was the intellectually appealing notion of seeking to enhance accountability in local government affairs. This paper traces the origins of the poll tax, describes how it was intended to operate, documents the implementation difficulties, and analyzes the reasons for its failure. It concludes that the notion of accountability underlying the poll tax is flawed, and that mistakes were made in implementation. Many of the lessons learned are of general applicability.

UNTIL 1989, British local government had available only one source of local taxation: the local property tax, known as the rates. This tax was levied on both residential and non-residential (business) property, the tax base being the notional rental of the property at some point in time.[1] The property tax had withstood the test of time—indeed it is possible to trace its origins to the Poor Law Relief Act of 1601 (Topham, 1983). However, there always existed a tension between its role as an onerous tax (related to ability to pay) and a beneficial tax (related to benefits received). In addition, the large variations in tax bases between different parts of the country gave rise to apparent inequities. It was these considerations that encouraged Margaret Thatcher[2] to pledge in the election campaign of October, 1974 that a future Conservative government would abolish the rates within the lifetime of a Parliament. However, that election was won by the Labour Party, and the commitment to abolition was dropped by the Conservative Party. There were subsequent reviews of the rates, the latest of which was in 1981 (United Kingdom Government, 1981). None of these persuaded the central government to implement reforms.

Nevertheless, the local property tax continued to be a source of discontent within the Conservative Party. A combination of events in 1985 gave added impetus to the search for an alternative. A revaluation of the tax base in Scotland gave rise to large increases in local property taxes for many natural Conservative supporters. In addition, the Thatcher government was becoming increasingly exasperated at its failure to control local government. It had sought to use the system of grants-in-aid to local government to secure expenditure control, but this policy failed, and led to many unanticipated problems which were criticized in a series of official reports (Audit Commission, 1984, National Audit Office, 1985). Moreover, Mrs. Thatcher's 1974 pledge to "do something" about the rates made her sympathetic to reform.

As a result, in 1986 the national government produced a consultation document entitled *Paying for Local Government* (Department of the Environment, 1986). This proposed three major reforms to local government finance: a revision of the system of central government grants-in-aid; the replacement of the local non-residential property tax by a national business property tax, unrelated to local government expenditure; and the replacement of the residential property tax by a flat rate community charge—or poll tax—to be levied on all adults living in a jurisdiction. These policies were included in the 1978 Conservative national election manifesto, and, after the election was won, Mrs. Thatcher claimed it was to be the "flagship" of her new administration. The proposals were enacted virtually intact (UK Government, 1988), and were implemented first in Scotland in 1989, and then in England and Wales in 1990.

In the event, the poll tax proved to be one of the most disastrous domestic policies enacted by a British government since

*University of York, York, United Kingdom.

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the Second World War, leading to widespread protests, civil unrest, and extensive non-payment. Its introduction in England was associated with a sharp decline in the Conservative Party support in opinion polls, and it was almost certainly the principal reason for the challenge to Margaret Thatcher's leadership of the party in November, 1990 and her replacement by John Major (Gibson, 1990). All United Kingdom political parties are now committed to the abolition of the tax.

There are numerous lessons to be learned from the failure of the poll tax. The purpose of this paper is therefore to describe the origins of the tax, to explain how it operates, and to analyze the reasons for its failure. The paper starts with a description of the background to local government finance in the United Kingdom. The details of the poll tax are then described, and the underlying rationale for the reform summarized. The next section describes the implementation of the reforms, which played a key part in their subsequent failure. The paper ends with an analysis of the reasons for the failure and the lessons to be learned. The simultaneous reforms to central government grants-in-aid and non-residential property taxation are referred to when necessary. However, the main focus of attention throughout is on the residential tax reforms—the switch from property tax to poll tax.

United Kingdom Local Government

Local government is a major segment of the United Kingdom economy, accounting for 12 percent of gross domestic product. Although the power of local governments is circumscribed by the national government, they have until recently enjoyed the freedom to set their own spending levels and local rates of taxation. A cycle of local democratic elections every four years is the principal mechanism for controlling local politicians and bureaucrats (Foster, Jackman and Perlman, 1980). However, the first Thatcher government, elected in 1979, viewed local government with some hostility, and saw the containment of local government expenditure as an important policy objective. The downward pressure on expenditure was to serve two purposes: to enhance the efficiency with which local services were delivered, and to reduce the volume of aggregate local government expenditure. Scrutiny of ministerial pronouncements at that time confirms that macroeconomic objectives were of "paramount importance" (Heseltine, 1981).

Using the direct controls already in place, the central government was quickly able to reduce the volume of local government capital expenditure. However, the control of the considerably larger volume of current expenditure proved more difficult, and was to preoccupy much of the central government's legislative energy throughout the 1980s. Details of the legislation enacted are given by Travers (1986). Some of the most important policies were the implementation of a new system of central government grants-in-aid (1981); the imposition of grant penalties for high spending (1982); granting the central government power to limit tax rates (and therefore expenditure) in selected jurisdictions (1984); the abolition of seven strategic urban local governments, including the Greater London Council (1985); the imposition of compulsory competitive tendering (1988); and a range of initiatives in specific service areas designed to reduce the power of local government and reduce spending levels. Nevertheless, these measures failed to arrest the inexorable rise in current expenditure during the 1980s, which was in real terms between 1 percent and 2 percent per annum (Chartered Institute of Public Finance and Accountancy, 1981 to 1989).

Until the 1990 reforms, local government expenditure (net of user charges) was funded from two sources: the local property taxes and central government grants. The property taxes in a locality were levied at the same rate on both residential and non-residential property.[3] Bennett (1982, Chapter 2) gives details of the various grant mechanisms employed since 1974. Between 1981 and 1989 the bulk of the central government grant-in-aid in England was in the form of what was known as the block grant. This terminol-

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ogy is confusing, as the grant was in fact a general grant with a mixture of lump sum and matching elements. Although Bennett lists 12 possible objectives associated with central government grants-in-aid, the stated purpose of the block grant was simply to equalize for both differences in spending needs and resource base between jurisdictions. In the terminology of King (1984), it was an unconditional power equalizing grant. Implicitly, however, the government sought to use the grant for macroeconomic purposes. To that end, throughout the decade it steadily reduced the average proportion of expenditure funded by the grant (from 59.1 percent to 43.3 percent) and decreased the rate at which the matching grant was paid (Association of County Councils, 1989).

Central to the operation of the block grant system were estimates by the central government of the costs in each local government of providing a standard level of services (Bramley, 1990). These estimates were often referred to as needs assessments, and were derived using a complex methodology involving over 100 indicators of need (Society of County Treasurers, 1989). If a local government then spent at this needs assessment, the block grant was set so that it was able to levy the national rate of taxation. Algebraically, if BG_i^* was the entitlement to block grant in jurisdiction i when spending at the same level as its needs assessment NA_i, then

$$BG_i^* = NA_i - g^*.RB_i \quad (1)$$

where g^* was the standard national rate of taxation when spending at needs assessment, and RB_i was the jurisdiction's property resource base.[4] Then, if expenditure varied from the needs assessment, the block grant was altered so that, for equal per capita variations in expenditure away from the needs assessment, equal changes occurred to the local tax rate, regardless of the resource base of the locality. In general, therefore, block grant entitlement BG_i when spending was at a level EXP_i could be written as:

$$BG_i = EXP_i - \left\{\left[\frac{EXP_i - NA_i}{POP_i}\right].\alpha + g^*\right\}.RB_i \quad (2)$$

where POP_i was the population in locality i and α was the national parameter determining the rate at which rates of local taxation varied as per capita spending diverged from NA_i.[5] Note that there was a matching element of block grant implicit in equation (2) equal to $\partial(BG)/\partial(EXP) = 1 - \alpha.RB/POP$.

Thus, in principle, for a given level of service provision, a resident (or business) would experience the same rate of local government taxation regardless of the local level of needs or resource base. Of course the actual tax bill incurred by a household would then depend on the valuation placed on its residence for local tax purposes. Although disputes about the valuation placed on individual residential properties were rare, occasional general revaluations were necessary when the tax base became outdated, and were often politically embarrassing. Indeed, it was the effects of the 1985 Scottish revaluation which are said to have precipitated the decision to abolish the residential property tax (Gibson, 1990).

The Thatcher Government's Critique of the Property Tax

The shortcomings of the local property tax were well-rehearsed, and had been addressed in previous official investigations (United Kingdom Government, 1981). However, the critique in the 1986 proposals *Paying for Local Government* marked a new departure in adopting an economic perspective on the problems of local government finance. In particular, it introduced the notion of accountability, and examined the extent to which the prevailing system of finance failed to promote accountability in local government. Full accountability would be achieved by ensuring that all those who vote for local government services make some contribution to the cost of the services for which they vote, and by establishing a clear link

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between changes in local expenditure and changes in local tax bills. The document claimed that a system of local government finance which promoted accountability would give clear price signals to the electorate and would therefore help to secure an economically efficient allocation of resources in local government.

From an accountability perspective the property tax had a number of defects. Firstly, the residential tax was levied only on heads of household or (in the private rented sector) landlords. As a result, many adults, such as non-heads of household and private sector tenants, did not pay the tax directly and—it was claimed—could therefore vote for local government services without having to bear any direct financial consequences. In addition, at the time of publication of *Paying for Local Government,* many welfare claimants made no contribution to local government finance. Secondly, and conversely, the business sector and the central government made marginal contributions to local government finance—through the non-residential property tax and the block grant—without having any direct control over expenditure. The residential sector (the electorate) could therefore in some sense "free ride" on the non-residential sector and on the central government, and did not bear the full cost of marginal spending decisions made through the ballot box. This analysis implies the effective price of marginal local government expenditure to many local residents was too low. Much of the electorate would therefore be encouraged to vote for high levels of expenditure, and it is clear that the Conservative government presumed that a result of these shortcomings was that the aggregate level of local government expenditure was higher than was economically efficient.

In addition to these efficiency arguments there were equity arguments put forward to justify the proposals. These were set out most clearly in a ministerial statement (Department of the Environment, 1987a):

"Rates are unfair It is unfair that so many people make no financial contribution to their local authority. And rates are also unfair because they bear little relation to the use people make of local services. Why should a widow living alone pay the same rates bill as four wage-earners living next door in an identical house? Why should someone pay more for the same local services just because they [sic] live in an area where property values are higher?"

This analysis suggests that the perceived inequity arose because the property tax was not well matched to the consumption of services. The benefit principle, rather than the principle of ability to pay, therefore appears to have been uppermost in the Thatcher government's mind. The ministerial statement also highlights an associated equity argument which surrounded the large geographical variations in property values (and therefore in valuations for the purposes of local taxation) found in the United Kingdom. Recall that the equalization principle implicit in equation (2) sought to secure equal *rates* of taxation for comparable levels of service. Because of the large geographical variations in residential property values across the country, this system gave rise to large variations in local tax *bills.* The Conservative government clearly considered these to be arbitrary and unfair.

The proposals for reform flowed directly from this analysis. The local business property tax would be abolished, to be replaced by a national uniform rate of taxation, independent of local expenditure levels. The revenue from this national tax would be redistributed to local governments in proportion to their adult populations, and so would in effect become a lump sum grant-in-aid to local governments. The business property tax would therefore no longer finance marginal local government expenditure. Similarly, the matching element of central government grant noted in the previous section was to be abolished, to be replaced by a pure lump sum grant. In this way, local governments would receive no matching subsidy from either the business sector or central government.

As a result, all marginal expenditure would have to be financed by the residential sector. Clearly it was possible to retain the local property tax. However, the accountability argument implied that the burden of the local residential tax should

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be borne to some extent by all adults. It was this logic that gave rise to the proposals for the personal community charge, or poll tax. Moreover, it was proposed that, apart from the poorest members of the community, all adults in a locality should pay the same poll tax. Those with very low incomes would receive welfare support of up to 80 percent of the local poll tax, but would nevertheless still bear some of the liability associated with extra local government expenditure.

Various arguments were deployed to defend the flat rate nature of the poll tax, perhaps the most controversial of the proposals. The architects of the system used standard economic models to argue that distributional aspects of taxation should be left to the national level, and that local taxes should be neutral in this respect (Foster, 1986). The ministerial statement quoted above noted that—because half of local services are funded from national taxation (in the form of grants-in-aid)—under the poll tax

> "the richest households in fact would pay 20 times more than the poorest for the full cost of local services. The redistribution of income is the job of the [national government] and not the 400 local authorities" (Department of the Environment, 1987a).

As well as confirming the wish to leave redistribution to national taxes, this argument also sought to dispose of the claim that the poll tax would contradict the ability-to-pay principle. However, the principal equity argument for the flat rate poll tax put forward by the government reflected the benefit principle. The official name of the new tax—the community charge—indicated that it was seen as a charge for services received, and the ministerial statement argued that

> "the community charge will spread the burden of paying for local services fairly among all adults, and it will be more closely related to the use people make of local services."

The distributional effects of the reforms were profound, both among geographical areas and among income groups. At a territorial level, the new basis of equalization resulted in large swings in central government grant support, and therefore in local residential taxation. The equalization principles outlined above meant that—under the property tax system—jurisdiction i imposed the following local residential taxation LRT_i:

$$LRT_i = \left\{\left[\frac{EXP_i - NA_i}{POP_i}\right].\alpha + g^*\right\} .RB_i.PR_i \qquad (3)$$

where PR_i was the proportion of the local property resource base in the residential sector.

The poll tax grant mechanism is by comparison simple. Central government grants are set so that, if a jurisdiction spends at its needs assessment, then it should be able to impose the national standard community charge c*, so ensuring that some notion of needs equalization is secured. However, because the tax base becomes population (albeit excluding those under the age of 18), it was decided that there was no need for any resource equalization of the sort employed under the property-based taxation system. Therefore, under the reforms, the local residential taxation in local government i—the community charge—is given by the equation

$$LRT_i = EXP_i - NA_i + c^*AP_i \qquad (4)$$

where AP_i is the adult population in locality i and c* is the national standard community charge for spending at NA_i. Clearly the values for LRT in individual areas given by equations (3) and (4) can differ considerably, even if the national parameters α, g* and c* were chosen to ensure the same aggregate level of central government grant support to local government as a whole.

Moreover, the marginal increase in local taxation for additional expenditure differs under the two systems. Under the property tax, equation (3) implies that $\partial(LRT)/\partial(EXP) = \alpha.RB_i.PR_i/POP_i$. That is, the cost to the local residential sector of additional spending depended on the per capita residential sector resource base. Under the community charge, the entire burden of any spending above NA is borne

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by the local adult population in the form of an increased community charge bill. The remaining financing requirement in the local government is made up by lump sum central government grant support and the locality's entitlement to non-residential property tax. As a result, under the poll tax the value for $\partial(LRT)/\partial(EXP)$ in all localities becomes one. In practice, because of the chosen level of α, this revised marginal price is for most local governments considerably higher than the price under the property tax system. Note that this analysis suggests that localities with low per capita residential resource bases under the property tax suffer most in respect of increases in marginal price. In general, therefore, although most areas gain increased lump sum grant from the reforms (largely because of the change in non-residential property taxation from a matching to a lump sum basis), most areas suffer a considerable increase in the marginal price to the residential sector of increases in local expenditure.

The proposed reforms also have profound redistributional consequences between individual households. These effects were examined in *Paying for Local Government*. The principal determinants of gains and losses are the number of adults in a household and the valuation of the family home under the property tax system. The greatest losses would accrue to families with large numbers of adults living in low valued property. With no welfare support, this analysis would imply a large swing in local tax liability from high income to low income groups (*Paying for Local Government*, Annex F). However, as Smith (1991) shows, few income groups *as a whole* gained or lost significantly from the poll tax reforms after welfare payments had been taken into account. The one exception was the top 10 percentile, which gained substantially. However, the change from a property to personal basis of taxation resulted in swings in liability *within* income groups, and there were a large number of households which gained or lost considerably from the proposed reforms.

Implementation of the Poll Tax

At an early stage, the central government, the public sector accountancy body, and several commentators produced estimates of the average residential tax bill arising from the change, assuming invariance in expenditure levels, needs assessments, and aggregate levels of grants-in-aid (Department of the Environment, 1987b, Chartered Institute of Public Finance and Accountancy, 1987, Gibson, 1986). These exercises alerted politicians and the electorate to the large geographical swings in tax liability arising from the reforms. However, the methods employed ignored the possibility that the reforms might induce behavioural responses on the part of local government in the form of expenditure changes. The assumption of unchanged expenditure was curious because one of the principal objectives of the reforms was to drive down expenditure levels, and econometric studies did indeed predict large reductions in expenditure arising from the increased price of marginal expenditure to the electorate (Barnett, Levaggi and Smith, 1991a).

Moreover, by focusing on *average* tax bills, the calculations ignored the profound changes in liability among households noted above. This aspect of the reforms was more resistant to presentation. The national government produced some rudimentary analysis, indicating that 58 percent of households would gain from the reforms (Department of the Environment, 1988). Such analyses disguised the fact that the households enjoying the largest gains contained only one adult, while households with more than two adults usually lost from the reforms. As a result, the number of *persons* gaining from the reforms was much smaller than superficial analysis suggested. Electorally, therefore, the poll tax proposals were far less attractive than much of the central government's presentation would suggest. Not until the reforms had been implemented was a satisfactory analysis of their distributional impact published (Smith, 1991). Gibson (1989) gives a description of the presentation by the gov-

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ernment of the poll tax, and concludes that it was defective in not alerting elected representatives to the full implications of the reforms.

Indeed, the proposals were the subject of surprisingly little public debate at the time of their publication. They were duly incorporated into the Conservative Party's 1987 election manifesto, but were barely mentioned in that year's national election campaign. To some extent this was because the proposals envisaged a period of ten years over which the residential property tax would be phased out, with a concomitant gradual phasing in of the poll tax. A further factor contributing to the low level of public debate was the failure of the opposition parties to develop credible alternative proposals.

After the 1987 election was won and the poll tax became Mrs. Thatcher's flagship, events began to move quickly. Legislation was rapidly enacted to implement the reforms in Scotland in 1989. These measures provoked relatively little public debate outside Scotland, not least because there were few areas of Scotland on which the Conservative Party depended for votes in national elections. John (1989) gives details of the Scottish experience. However, the legislation for England and Wales, to secure implementation a year later—in 1990—did not receive such an easy passage.

It was clear that the major winners from the poll tax proposals would be areas with high property values in the southeast of England—the areas with highest Conservative Party support—which would see their local tax bills reduced to a national average level as a result of the reforms. Once this became known, a euphoric Conservative Party conference in 1987 persuaded the national government to abandon ideas of phasing in the new tax. This decision was reinforced by the reservations of many in local government about the feasibility of running two systems of local taxation side by side. Instead the poll tax was to be introduced wholesale, and the property tax abolished forthwith, first in Scotland, in 1989, and then in England and Wales in 1990.

Given the decision to implement immediately, the consequent large gains and losses between localities noted above were deemed by the central government to be unsupportable in the short run, so a system of "area safety nets" was devised. These were lump sum transfers from areas that gained (in terms of grant) to areas that lost from the reforms, assuming no changes in expenditure levels in individual local governments or aggregate grant-in-aid. The magnitude of an area's safety net contribution (or receipt) was equal to the gain (or loss) in grant arising from the reforms.[6] This was to be financed by a uniform increase (or reduction) in the poll tax in the area. The attraction to the central government of this scheme was that it was self-financing—under the chosen assumptions, the sum of the gains equalled the sum of the losses—so no extra grant-in-aid was required. The notion underlying safety nets was that these lump sum transfers between localities would protect individuals from the reforms. The safety nets were to be abated by 25 percent per year, so that after four years the reforms would be allowed to operate in their unadulterated form (Department of the Environment, 1988).

Although retained in the first year of implementation, this scheme on its own proved to be unacceptable for two reasons. Firstly, as implementation approached, elected representatives became increasingly aware of the swings in liability among households as well as swings among areas. Even if local governments passed on the entire local safety net to residents in the form of reduced (or increased) poll taxes, all adults would receive the same subsidy (or supplement) to their tax bill. There was, therefore, an implicit assumption that all residents in a locality suffered (or benefited) to an equal extent from the reforms. In practice, even in a single locality, there were large variations in the losses and gains among households, arising from variations in property values and in household composition. The government argued that the changes due to household composition were intrinsic to the poll tax, and could not be protected. However, protection was eventually introduced for households living in

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properties with especially low valuations under the property tax, regardless of their ability to pay (Department of the Environment, 1989). Further political pressure resulted in this protection being increased substantially in the second year of the poll tax, indicating that the central government had underestimated the importance of considering the circumstances of individual households (Department of the Environment, 1991a).

The second failure of the safety net scheme was that it led to high poll tax levels in areas that would eventually gain from the reforms. These areas had previously experienced relatively high residential taxation because of their high resource bases. However, because of the safety net transfers to losing areas, local governments in these gaining areas were required to levy some of the highest poll taxes in the first year of the new system, and so the long run gains of the reforms were not immediately apparent. Residents in high resource, low needs areas—predominantly controlled by Conservative local governments—could not understand why their poll tax bills were very much higher than many low resource, high needs areas, which were often Labour-controlled, and perceived to be relatively high spending. The safety net, therefore, antagonized the very constituency that the poll tax was expected to benefit. Although the central government took over funding of the safety net in the second year of the reforms, the damage it caused to the credibility of the poll tax in its first year of operation was severe.

The 1988 Local Government Finance Act enabled the national government to proceed with the implementation of the new taxes. The legislation was strongly opposed by most representatives of local government (see, for example, Association of Metropolitan Authorities, 1986). Apart from the political objections to the poll tax, the principal technical objection was the administrative difficulty associated with the collection of the tax, most importantly relating to registration of taxpayers and collection of the tax. In spite of their reservations, however, local governments began to compile poll tax registers of all adults living in their localities, and make arrangements for sending out poll tax bills. The debate outlined above led to many last minute changes, so that only three months before implementation local governments were still uncertain about important details relating to issues such as exemptions, welfare payments, and safety nets. The complexities of the regulations gave rise to many difficulties with computer software, and there was considerable uncertainty in many areas about the ability to implement the poll tax on time. In the event, however, most jurisdictions managed to keep to the required timetable, and the first poll tax bills were sent out in April, 1990. Thus, although generally hostile to the tax, local government took all reasonable steps to ensure that it would operate as required by the central government.

Another preoccupation of local government in the months leading up to the introduction of the poll tax was the choice of expenditure levels (and therefore of poll tax levels) in the first year of the new arrangements. As noted above, econometric analysis suggested that, in the long run, the increased marginal price of local expenditure was likely to drive down budgets. However there were, in the short run, additional political considerations. It was clear as implementation approached that the principles underlying the new tax were attracting widespread hostility. It was, therefore, likely that it would be the architects of the tax—the Thatcher government—and not local government that would be blamed for poll tax levels. Some commentators, therefore, judge that many local governments did not respond to all the economic incentives implicit in the new system; indeed those antagonistic to the new tax had an incentive to set high levels of the tax in order to discredit it further (Hughes, 1989).

The central government estimated that the average poll tax figure would be £278 per adult. However, this calculation was based on an assumed inflation rate of 4.76 percent, when the actual rate was more likely to have been 8.5 percent (Ridge and Smith, 1990). The purpose of this unrealistic assumption was to maintain down-

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ward pressure on local government expenditure, in the belief that electorates would blame local governments for poll taxes in excess of the central government estimate. However, as Barnett, Levaggi, and Smith (1991b) show, there was in the event a real increase in local government spending in 1990 of 3.9 percent, only part of which can be explained by increased responsibilities (such as collection of the poll tax). This tends to confirm Hughes' theory that local government took advantage of the new tax to secure modest expenditure growth, and judged that the blame for high poll tax levels would be deflected onto the central government.

Moreover, unlike previous years, when the business sector met roughly 50 percent of such "overspends," the residential sector had to bear the entire cost of spending in excess of needs assessments. The "nationalization" of the business property tax gave rise to the so-called "gearing" effect, whereby, as the percentage of local government expenditure financed by local taxation diminishes, so the sensitivity of local tax bills to expenditure decisions increases.[7] This combination of factors led to an average poll tax of £363 in England, 30 percent higher than that predicted by the government. It is noteworthy that, when the first estimates were produced by the central government in 1987, a basic community charge of £178 was proposed.

As soon as the first bills were sent out in England the hostility to the new tax became evident. There were public demonstrations throughout the country, and a widely reported riot in central London. A campaign of non-payment, begun in Scotland, spread south of the border. The introduction of the tax was associated with a prolonged drop in the opinion polls for the national government, and increasing unease amongst Conservative Members of Parliament. In November, 1990 Michael Heseltine deemed the time was right to challenge Margaret Thatcher for the leadership of the Conservative Party. Although the ostensible occasion for his challenge was policy towards the European Community, he was quick to assert his consistent opposition to the poll tax and made its abolition a central plank of his campaign. The outcome of the leadership challenge was victory for John Major, who had also promised a review of local government finance. This resulted in April, 1991 in the proposals to abandon the ill-fated tax and to return to a property-based residential tax, albeit with a 25 percent discount for one-person households, the last vestige of the poll tax (Department of the Environment, 1991c).

Analysis

Most textbooks on public sector finance make reference to poll taxes. From an economic perspective, under certain restrictive circumstances, a poll tax will lead to fewer market distortions than any other form of local taxation (King, 1984, Chapter 6). However, until the 1986 United Kingdom proposals, the poll tax had in modern times remained an intellectual abstraction, most useful as a benchmark against which to assess the merits of other, more practical taxes. The UK reforms were, therefore, a major departure from accepted taxation wisdom, and it is instructive to analyze the factors contributing to its failure. Discussion of matters of principle comes first, followed by an analysis of implementation issues.

The Principles of the Poll Tax

Clearly, it is unlikely that the reforms described above would have made much progress unless they had answered immediate political needs. However, they were unusual in UK taxation history, in that—unlike the conventional pragmatic response to taxation problems—the entire package was informed by a unifying and coherent principle, namely accountability. The failure of the poll tax therefore suggests that the axioms underlying the proposals were either faulty or incomplete.

The notion of accountability is closely linked to the economist's view of allocative efficiency. The architects of the poll tax took the view that, if consumers of local government services faced the "correct" tax price for the services for which

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they voted, then an efficient allocation of services would result. Matching subsidies from the business sector and central government, it was claimed, meant that such tax prices were too low under the previous property tax system. This analysis is, therefore, based on standard economic views of the desirability of non-distortionary taxes.

Unfortunately, the extension of such simple economic principles to goods and services provided collectively—as in local government—is far from straightforward (Mueller, 1989). In particular, "consumers" of local government services lack an efficient and complete market in which to make their preferences felt. The only mechanisms for exercising choice are migration—a costly and often infeasible option—and the ballot box, which is a very imperfect control mechanism. The shortcomings inherent in electoral systems are particularly marked in the United Kingdom for two reasons. First, most candidates in local government elections are nominated and supported by national political parties. As a result, the electoral choices of voters often reflect their judgement on the national government rather than the performance of the local jurisdiction. And second, there is a tradition of "first past the post" elections, in which each electoral district of a local government selects only one representative—the candidate gaining the highest number of votes. With usually at least three candidates standing in all such districts, and no form of proportional representation, the political composition of local governments often bears little relation to the proportion of votes cast for each political party.

In addition, there are market imperfections implicit in the delivery of many of the services provided by local government. Most of the services are, to a greater or lesser extent, public goods, and so the usual problems of securing an efficient level of production are encountered. Indeed, as King (1984, Chapter 4) shows, there are strong arguments for providing matching subsidies to local governments to correct for spillover effects. In this sense, therefore, the effective abolition of matching subsidies implicit in the 1990 reforms appears to contradict received public finance wisdom. The crude electoral system and the public good problem imply that provision of clear tax prices may be neither a necessary nor a sufficient condition for allocative efficiency.

Barnett, Barrow, and Smith (1991) undertook a study of accountability in English local government using data from 1985, the year in which the poll tax proposals were developed. They sought to measure the extent to which various forms of subsidy—such as business taxes, grants-in-aid, and welfare payments—distorted spending patterns in 410 local governments. Measures of these subsidies were regressed against the variation in spending from the central government's needs assessments, a measure of "overspending." It was found that the magnitude of matching subsidies from the business sector and grants-in-aid were indeed associated with increased spending in the expected way, and that therefore the reforms to business property taxes and central government grants could be justified within the context of the accountability argument. However, no such association could be found between overspending and the level of welfare payments, or the prevalence of non-heads of household, or the number of private rented tenancies in an area. As a result, the authors concluded that the extent to which individual adults could free-ride appeared to have no relationship with overspending, and they therefore could find no *ex ante* evidence to support the accountability arguments underlying the introduction of the poll tax. It is noteworthy that, although the data existed to undertake studies of this sort at the time of publication of the poll tax proposals, no empirical work was commissioned to test the assertions on which the reforms were based.

Subsequently, Barnett, Levaggi, and Smith (1991b) have attempted to determine whether the putative changes in residential sector accountability brought about by the 1990 reforms have affected local government spending levels. Again the results are negative, casting doubt *ex post* on the accountability principle. Of

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course, such empirical tests may be too insensitive to detect the impact of changes in accountability, or spending may already be at efficient levels. However, it is more likely that the accountability principle is flawed, and that—without simultaneous reforms to electoral systems and methods of providing local public goods—the enhancement of tax price accountability has an insignificant impact on local government behaviour.

The reforms reflected the preoccupations of contemporary economics, in that the underlying efficiency arguments were more coherent than the equity arguments. The crucial equity consideration that underpinned the proposal for a flat rate community charge was the benefit principle—the notion that the poll tax would be a closer approximation to benefits received than the property tax. Again this assertion was testable before the proposals were developed, and again such an opportunity was spurned. Subsequent research by Bramley, Le Grand, and Low (1989) has in fact indicated that higher income groups tend to consume a higher volume of local public goods than lower income groups. Moreover, some of the services provided by local government—such as housing, fire services, and refuse collection—are better considered a service for households than for individuals. As a result, they concluded that the property tax yielded tax bills closer to benefits received than does the poll tax. Far from being enhanced, therefore, the benefit principle was actually compromised by the reforms.

Another widely held notion of equity is that taxes should bear some relationship to ability to pay. The residential property tax reflected this principle, albeit imperfectly, by relating tax liabilities to some measure of market value of the residence occupied. It could be argued, albeit somewhat perversely, that the community charge did reflect ability to pay, in the sense that local household tax bills would reflect the number of adults in the household, which might be construed as a better measure of ability to pay than the notional rental value of their home. Few took this argument seriously, however, and the ostensible failure of the poll tax to reflect ability to pay was a major reason for its failure to attract widespread public acceptability.

Its severely regressive nature is of course the main reason why public finance textbooks usually refer to a poll tax as an intellectual curiosity rather than a feasible option as a local tax. As noted above, some apologists for the tax were prepared to argue that distributional issues should be left to national taxation. However, no effort was made to amend the national tax system to correct the redistributional effects of the poll tax. Moreover, no serious attempt was made to present poll tax figures net of welfare benefit, so that the perception amongst many was that all adults would be liable to the full poll tax. In fact, welfare benefit claimants—those on very low incomes—received a subsidy of up to 80 percent of the poll tax. To finance the remaining 20 percent their welfare payments were augmented, but only by 20 percent of the government's unrealistically low prediction of the national average poll tax. The inevitable overspending that occurred in most localities resulted in higher poll taxes than allowed for in welfare payments. Many claimants, who had no effective control over this additional expenditure, had to find the extra liability from an already tight budget. There was a widespread perception, therefore, that the poll tax was a severe burden for members of low income households, and this ran counter to many citizens' concept of fairness.

A final consideration for any tax is its administrative complexity. The British property tax had been established for many years, and had become easy for local government to administer. The technical complexities of deriving valuations were of course considerable (Hepworth, 1984). However, a clear (though arbitrary) methodology for valuation had been developed over time, and valuations were rarely challenged. The most serious disputes occurred in the non-residential sector, and were relatively small in number. In addition, registration of property was straightforward, compliance costs negligible, and evasion very difficult. The ma-

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jor administrative shortcoming of the property tax was the need periodically to revalue property, although the consequent difficulties were usually of a political rather than an administrative nature.

The inevitable problems of administration that the community charge would give rise to were dismissed as "not insuperable" in *Paying for Local Government*. They were, however, an important reason for the very strong opposition to the proposals amongst local governments, even those under Conservative control. In the event, the worst fears of opponents of the tax were realized. Registration of residents was an intrinsic problem because, unlike property, residents exhibit a high degree of mobility. The Audit Commission (1991) found that, even in rural areas, 36 percent of entries on the community charge register changed in the first year of the tax. The figure in inner London was 55 percent. Furthermore, the high degree of resistance to the poll tax led to a reluctance amongst many citizens to register, in spite of the threat of heavy fines. The extent of non-registration is unknowable, but almost certainly important. It is instructive to note, for example, that the 1991 Census of Population indicates the first drop in population in the United Kingdom since 1801 (Office of Population, Censuses and Surveys, 1991). The census office had unprecedented difficulties in obtaining responses, particularly in inner cities, and most commentators attribute this directly to widespread fear of being identified for poll tax purposes.

Moreover, the extent of non-payment has been considerable. Most local governments budgeted for a certain amount of non-compliance and unrecoverable tax bills. However, by the end of the first year, only 90 percent of the poll tax had been collected in England, indicating a much larger prevalence of non-payment than local government had anticipated (Department of the Environment, 1991d). The Audit Commission (1991) estimates that 21 percent of poll tax payers require a summons before making a payment, a sevenfold increase over the volume of summonses issued under the residential property tax, and the courts have been overwhelmed by actions from local governments to recover unpaid debts. A further complication is that the costs of recovering unpaid taxes are often in excess of the debt, particularly when the individual involved is a low income welfare claimant. In narrow accounting terms, collection of these debts cannot be justified, and pursuit of such creditors is therefore prosecuted principally in order to discourage others from defaulting.

In the first year of operation of the poll tax, the administrative costs of collecting local taxes rose from £200 million to £605 million in England (Chartered Institute of Public Finance and Accountancy, 1990). This excludes the increased costs of court actions and debt recovery, and the shortfall in revenue arising from non-payment. John Major's stated reason for abandoning the poll tax was that it had become "uncollectable," and so the administrative difficulties associated with the tax were intrinsic to its failure. The problems of administration were in fact insuperable, and the lack of consideration of this issue at the design stage was therefore clearly a major shortcoming.

To summarize, the 1990 reforms were based on an economic concept—accountability—which has been shown to be flawed, and which is clearly in need of further research and intellectual development before it can be applied to local taxation systems. The poll tax contravened the benefit principle it was intended to promote, and little attempt was made to address another important equity issue—ability to pay. No account was taken of the administrative difficulties the tax would give rise to. In short, the principles on which the poll tax was predicated were faulty and incomplete.

The Implementation of the Poll Tax

The poll tax, like its predecessor, is a highly visible tax. Indeed, such visibility is intrinsic to its objective of enhancing accountability if citizens are to recognize the full costs of their electoral choices. Yet, visibility was a mixed blessing at the implementation stage of the reforms. Ridge

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and Smith (1990) estimate that 49 percent of adults were not heads of household in 1984, so on the introduction of the poll tax many voters became directly liable for a local tax for the first time. Such a large segment of the population is clearly a powerful electoral force. In addition, many households, particularly in areas with low property values, lost heavily from the reforms. As a result, the introduction of the poll tax was always likely to be an electorally risky undertaking, and it was imperative that special care was exercised in the implementation strategy.

The initial, sensible approach at implementation was to propose a gradual phasing in of the poll tax, so that it would operate alongside the property tax for a number of years. Once this gradualist philosophy had been jettisoned, implementation became more complex. The first attempt to protect losers from the full rigours of the new tax was the area safety net scheme. As indicated above, this scheme was attractive to the national government because it was self-financing. However, it was ineffective for a number of reasons. In particular, it failed to protect many individual households, and it alienated many gaining areas. A baroque system of protection for individual households was, therefore, hastily superimposed on this original scheme in an attempt to cushion individual losers more effectively. This new scheme was difficult to administer and required additional central government funds, which was presumably why it had originally been resisted.

At the same time as introducing the poll tax, the central government was intent on maintaining its downward pressure on local government expenditure by adopting low expenditure targets and keeping the level of grant-in-aid unchanged from previous years. Local government's inability (or reluctance) to meet the unrealistically low spending targets then led to poll tax levels greatly in excess of those predicted by the central government. This meant that many more households than originally envisaged were paying a higher level of local tax than under the property tax, contributing to the perception that the reforms generated many more losers than gainers. With the benefit of hindsight, it is apparent that the central government should have temporarily relegated its objective of containing expenditure to secondary importance during the delicate implementation phase. The primary objective should have been securing acceptance of the new tax, which may have required an increase in the level of grant-in-aid to encourage low poll tax levels in the first year of implementation.

It is interesting to note that the central government did have the power to limit expenditure in most local governments if it felt that their expenditure was "excessive," and so could have moderated poll tax levels even after budgets had been set. In the event, it chose to invoke such powers in only 21 jurisdictions in the first year of the poll tax, and even in those areas the consequent reduction in poll tax levels was modest (Patten, 1990a).

Many of the errors made in the first year of the reforms were highlighted by changes of policy made in the second year (1991/92). Measures such as the increased provision for transitional relief, and the scrapping of contributions to the area safety net by gaining localities, have been mentioned already. In addition, the central government decided to implement severe universal expenditure limitation in the second year of the poll tax (Patten, 1990b). Of course this measure represented a considerable strengthening of central government power, and severely compromises most notions of local democratic government. However, it did succeed in moderating local government expenditure rises (Chartered Institute of Public Finance and Accountancy, 1991). Furthermore, and most fundamentally, after poll tax levels had been set in the second year, the national government—now under the leadership of John Major—announced a large increase in grant-in-aid, resulting in a universal per capita reduction of £140 in poll tax levels. Average poll tax levels fell from £392 to £252, indicating that the government realized that poll tax levels had been too high (£363) in the first year of the reforms (Department of the Environment, 1991b).

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On their own, the shortcomings in implementation may not have been fatal to the poll tax if there had been a widespread perception that the reforms led to a fair system of local government finance. Yet, as Gibson (1989) shows, no serious attempt was made to convince the public of the supposed virtues of the poll tax, and many of the documents produced by the central government to explain the new tax were inadequate or misleading. Once the poll tax was implemented, the disparity between central government predictions and actual poll tax levels became apparent, and the credibility of the reforms suffered irretrievable damage. The presentational failures allowed local government to deflect hostility to poll tax levels onto the central government, and to secure a modest but significant rise in expenditure. In addition, by failing to abate public hostility, the presentational shortcomings are unlikely to have helped local governments overcome the difficulty of compiling poll tax registers, and collecting the tax.

So the combination of the natural gains and losses arising from the reforms, the original crass safety net scheme, the unrealistic spending assumptions, and the presentational failures led to a very high proportion of the population perceiving that they had lost in the first year of the reforms. It is therefore highly likely that the subsequent dramatic drop in Conservative support in opinion polls was a direct result of the local tax reforms, and mistakes in implementation almost certainly played an important part in their failure.

Conclusion

Several lessons of general applicability can be learned from the United Kingdom poll tax debacle. Underlying the tax was the elegant and theoretically persuasive concept of accountability—the idea that consumers of local public goods should bear the full financial consequences of the choices they make on local services through the ballot box. The architects of the poll tax believed that the enhancement of accountability would lead to increased allocative efficiency in local government. Yet this proposition was not tested before implementation, even though such tests could have been undertaken. Even if one views such *ex ante* tests with suspicion, at the very least it would have been prudent to have exposed the electorate gently to the full rigours of an accountable tax system, by means of pilot schemes and gradual phasing in of the reforms. It might then have been possible to test whether the accountability arguments were sustained. The evidence that does exist suggests that they would not have been. In any case, wholesale experimentation with a major source of tax revenue is not to be recommended. However, impatience and reforming zeal got the better of prudence so far as the Thatcher government was concerned, and it plunged on with the reforms even when their impracticality and adverse electoral consequences were becoming apparent.

The implementation of the tax has been shown to be inept. Any reform on such a scale is likely to create a large number of winners and losers. Diminishing marginal utility of income implies that there is almost certainly an asymmetry of passion between winners and losers, particularly when the losers are in the lower income groups. As a result, an astute administration would have ensured that losers were comprehensively and obviously protected from the immediate effects of the reforms. This could only have been achieved by a large injection of central government grants-in-aid and welfare payments, and possibly by reforms to the national taxation system. However, such measures were anathema to the Thatcher government. And, as we have shown, the measures that were taken to protect losers only succeeded in antagonizing the gainers.

Finally, it is important not to forget the administrative difficulties associated with the poll tax. If the tax had enjoyed widespread support, then the problem of securing a reliable and comprehensive register of taxpayers may not have been insurmountable. However, the government made no serious attempt to convince doubters of the virtues of the poll

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tax. As a result there was widespread failure to register and default on payment. The tax had become uncollectable.

The legacy of the tax's failure is serious. It has brought into question the legitimacy of local taxation in the United Kingdom. There is serious doubt about the amount of poll tax revenue that can be collected before the replacement is in place in 1993. The extra grant-in-aid injected into local government in the second year of the poll tax means that only 14.9 percent of local government expenditure is met from local taxation. This has two important consequences. First, it exacerbates the gearing effect, and so makes local poll taxes unduly sensitive to expenditure changes. Secondly, the increase in grants-in-aid encourages increased expenditure in local government. Because of the flypaper effect of grants-in-aid, it is unlikely that local governments will pass on all the increased grant to local residents in the form of reductions in poll taxes (Barnett, Levaggi, and Smith, 1991c). Therefore, so long as the central government is committed to containing local government expenditure, it is likely to impose severe expenditure limits on local government for the foreseeable future. In short, the failure of the poll tax is a potent threat to local democracy in the United Kingdom. The episode is a salutary lesson in the importance of designing tax schemes that enjoy widespread acceptance and that are simple to administer.

ENDNOTES

**Thanks are due to Richard Barnett, Rosella Levaggi, and three referees.

[1]The last valuation of residential property in England relates to 1973.

[2]She was then in opposition, in the shadow cabinet of Edward Heath.

[3]There was a small subsidy to residential property tax payers, known as domestic rate relief, paid at a fixed rate in the pound.

[4]The formal term used by the central government for NA_i was grant-related expenditure assessment (GREA), and g^* was known as the grant-related poundage for spending at GREA.

[5]This representation omits some of the more arcane aspects of local government finance, such as various adjustments made to the effective resource base by the central government, various lump sum transfers made between localities in the Greater London area, and the domestic rate relief. Also, the parameter α increased by 25 percent for expenditure in excess of a central-government specified spending threshold, about 10 percent higher than the needs assessment.

[6]There were some amendments to this "pure" safety net arrangement as political pressures became acute. These were mainly to place an upper limit on the contributions made by gaining localities.

[7]Much was made of the gearing effect by some commentators on the tax. If local expenditure X is funded by a lump sum element M and a local tax T, then clearly X = M + T, and any change in X, say ΔX, must be equal to the change in T, ΔT. As a result, the proportionate increase in tax brought about by a change in X is given by

$$\Delta T/T = \Delta X/T = \Delta X/(X - M).$$

Clearly this ratio increases as M increases. The increase in the gearing effect brought about by the reforms was particularly severe, first because local government lost the matching subsidy from the business sector and central government grant, and second because the business sector property tax became lump sum, thereby effectively increasing M.

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