

## A Fairer Local Tax for Scotland

### July 2008

#### Introduction

The Federation of Small Businesses is Scotland's largest direct-member business organisation, representing almost 20,000 members. The FSB campaigns for an economic and social environment which allows small businesses to grow and prosper.

Small businesses are key users of local services and also contribute significantly to the funding of local authorities.

The FSB is pleased to submit our comments to this consultation as we have a number of general comments to make on this proposal.

#### Impact on Small Businesses

Small businesses are the back-bone of the Scottish economy, with 98% of Scottish businesses employing fewer than 50 employees. Between 2006/2007, Scotland's small businesses created 26,000 new jobs. It is important for the Scottish Government to consider the impact on this vital component of the Scottish economy when introducing any significant pieces of legislation.

The partial Regulatory Impact Assessment (RIA) contained within the consultation document made little effort to analyse the potential impact on small businesses, nor did it consider the potential deterrent effect on future business start-ups. Small businesses need an indication of the expected financial and time implications of this scheme, as businesses will be expected to implement it. The small business test is an important aspect of the RIA process and we are disappointed that it has not been more effectively used as a tool to help develop legislative proposals.

The administrative burden on small businesses of this new proposal could be considerable. While payment of the Council Tax is undertaken by the individual, under the proposed Local Income Tax (LIT) this responsibility would transfer to the employer, who would have to calculate each employee's LIT liability. This additional burden would fall particularly hard on small business owners; as they have neither payroll departments nor the spare time to undertake this task.

The FSB represents thousands of businesses in sectors of the economy where there is a seasonal element to the business and thus a higher turnover of staff. Businesses in the hospitality sector, for example, will find this proposal difficult

to deal with. The FSB is concerned that the LIT could present our members with an additional administrative burden, which many small businesses could find hard to comply with. The increased levels of bureaucracy which the LIT would inevitably bring would leave small business owners with less time to devote to their businesses. This is unlikely to be in line with the Government's key aim of sustainable economic growth.

This proposal could also have a number of consequences for small companies with cross-border staff. For example, an employee who lives in Gretna, but works in Carlisle would have to pay the LIT, but the English based employer would have to administer it. The additional administrative costs will apply not only to Scottish small businesses, but to other UK small businesses that may have staff based in Scotland.

While small businesses do not engage to the same extent in the wage negotiations of larger companies, there is a possibility that the higher wages demanded by employees in larger companies in Scotland, could impact on smaller businesses. This could also lead to increased competition for staff in larger companies with many smaller businesses finding it hard to compete – particularly in the current challenging economic climate. This proposal is potentially a tax on labour in Scotland and could send out a message that Scotland's effective basic and higher rates of taxation are the highest in the UK. The perception could be created that with the highest rates of direct taxation, Scotland would be a poor investment opportunity.

The FSB is also concerned that if the funds raised by this proposed new tax result in a funding gap for local authorities, the delivery of non-statutory schemes, such as economic development, could be diminished as a cost saving measure. FSB Scotland welcomed with recent return of this responsibility to local authority control however we would be concerned about any potential threat to the success of this move at such an early stage.

## Conclusion

FSB Scotland understands the Government's wish to reform local taxation however, the proposal for a Local Income Tax risks adding an unnecessary burden on Scotland's small businesses. Not only will this detract from achieving economic growth but it risks sending out the wrong message to businesses at a time when small firms are looking to government to help mitigate rising costs.

FSB Scotland believes that there are a number of problems to resolve and questions to answer in relation to this proposal. We also have a number of reservations as outlined in our submission above. We see potential for increasing costs to small businesses, as well as an increasing administrative burden, which would fall most heavily on those businesses that are least able to absorb the costs and implement the changes.

It is clear from the consultation document that more thought needs to be given to this scheme – particularly looking at the practicalities and costs of implementation. A more detailed RIA should be compiled and published, outlining a more complete assessment of the costs and time involved in changing the system. This must be done before the Scottish Government publishes its legislative proposals.

For further information on any of the points raised in this submission, please contact Martyn McIntyre, Policy Officer, on [martyn.mcintyre@fsb.org.uk](mailto:martyn.mcintyre@fsb.org.uk) or 0141 221 0775.