

Local Government and Public Services Committee

LGPS(2)-05-06(p7)

Date of meeting: Wednesday 15 March 2006

Venue: Committee Room 3 & 4, National Assembly for Wales

Title: Note of Ministerial visit to Denmark

Purpose

1. To receive a note giving details of the ministerial visit to Denmark in May 2005.

Recommendations

2. That the committee notes the issues and findings during the visit to Denmark.

Background

3. The note of this meeting was planned to be circulated to Members at the same time as the submission to the Lyons Inquiry. When it was decided to delay the submission the note of my visit to Denmark was not circulated. This is now attached.

Compliance

There are no issues of propriety or regularity.

Action

The Committee is invited to note the contents of this paper.

Sue Essex

Minister for Local Government and Public Services

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Note Of Visit To Denmark 19-21 May 2005

Objectives of Visit

- To determine the nature and extent of the local taxation system in Denmark within the context of the relationship between local and central government.
- To assess whether any lessons can be learnt from the Danish system of local taxation, which includes an element of local income tax.
- To provide evidence for the Welsh Assembly Government's submission to the Independent Inquiry into Local Government Finance in England (the Lyons Inquiry).

Background Rational for Visit

- The Danish model of local government has some differences to the Welsh system but some similarities exist in terms of the tiers and functions of local and central government. One of its most interesting facets is that some of local government's expenditure is financed by a local income tax.
- There has been much debate in the recent past at, both a UK and a Welsh level, as to the appropriate form of local taxation and whilst a local income tax has been ruled out as a complete replacement for the Council Tax it has not been ruled out as a supplement to it.
- Some research was undertaken by the Chartered Institute of Public Finance and Accountancy (CIPFA) for the Office of the Deputy Prime Minister (ODPM)-led Balance of Funding Steering Group on the issues and costs associated with the introduction of a local income tax on this basis. However, this has left many questions unanswered in terms of the detailed working of the system at the practical, cultural and perception level. The opportunity to learn about and better understand these issues in a country already operating such a system would be invaluable.

Meetings

- In order to meet these objectives the following meetings were arranged with parties in Denmark:
- Leif Jeppesen, Director of Local Taxation, Copenhagen Municipality
- Jann Larsen (Legal Counselor) and Ib Kok Hansen (Head of Section) Ministry of the Interior and Health
- Asger Munk, National Secretariat for Urban Regeneration, Ministry for Refugees, Immigrants and Integration
- Peter Gorm Hensen (CEO) and Jens Bjorn Christiansen (Head of Department) Local Government

Note of Discussions by Topic

Local Government Finance

Income Tax

- It was noted that as part of the reorganisation of local government in Denmark (wef 1 January 2007) that all tax assessment would be taken over by central government (currently the State collects and redistributes local income tax). The representative from Copenhagen Municipality felt that there had been little public or media interest in these changes to arrangements. This is despite the fact that the changes affect 12,000 public service employees. One of the reasons is that the public would still be able to have queries answered locally and it would not affect service delivery. This would mean that the annual tax assessment/return which all Danes complete for their local and national taxes would be handled by the State. It was hoped that these changes would realise savings.
- These new arrangements would not affect the ability of the new municipalities to set their own level of local income tax. It was noted that whilst the municipalities are free to set their own level of local income tax the current arrangements relating to financial penalties for those setting the level of their local income tax above a certain amount would be likely to continue after the reorganisation.
- Local income tax is proportionate to income and not progressive i.e. every citizen in the municipality pays the same flat rate percentage of their income regardless of how much they earn. The rate paid is based on residency as of 5th September.

Current levels of local income tax are as follows:

	2000	2001	2002	2003	2004	2005
	%	%	%	%	%	%
Av. Municipal LIT	20.57	20.71	20.75	20.75	20.76	20.78
Av. County LIT	11.55	11.84	11.88	11.9	11.9	11.9
Av. Total LIT	32.04	32.48	32.55	32.58	32.58	32.6

- These averages mask a wide variation in the amount of LIT paid, for example in 2004 the range

was 28.5 to 35.6%. The LIT payable is added to the national income tax payable which is collected on a progressive basis with the lowest band being 5.5%, the medium band being 6% and the higher rate being 15%. The amount of tax due is based on similar calculations in the UK with a basic tax free allowance of DKK 36,800 in 2004 with various allowable deductions against tax available. The tax payable is charged against all income, including capital income and income from personally owned businesses, with a tax ceiling which ensures that personal contributions (LIT and national IT) do not exceed 59% of total income. This does however not include Labour Market Contribution (LMC) of 8% and some other minor taxes and contributions.

- This split in the level of income tax collected between local government and the State reflects a different distribution in responsibility for service delivery from the UK (see below). The State and social funds currently accounts for 46% of public sector expenditure in Denmark and local government accounts for 54%. However in terms of total tax revenues (all taxes including VAT) the State collects 68% and local government collects 32%.

Property Tax

- As well as the local income tax the municipalities (and at the moment the regions) levy a property tax on both domestic and non-domestic properties. The amount which can be raised per property as a flat rate percentage of the land value is determined by the local authority with bands set by central government. For example, the present bands are 0.6-2.4% for municipalities (these will be increased by 1% at the bottom and the top end on reorganisation so that the municipalities will have access to the current level of property taxes set by the regions).
- Both domestic and non domestic properties are subject to bi-annual revaluations (domestic one year, non-domestic the next). The valuations are undertaken by the central government and there are special arrangements for older people to access loans from the government to defer payment until they move or repay the loan from their estate. There is a mechanism for appeals but the representative from Copenhagen municipality felt that appeals are few in number which could possibly be a function of the frequency of revaluations.
- Corporation tax is levied by the State at a rate of 30% but local government receives a proportion of the tax levied from the businesses in its area. This is currently 13.41% of the amount levied. However, it was noted that central government is considering making corporation tax part of the equalisation system post 1 January 2007 but no decision has yet been made on this.
- Overall levels of both local and central taxation are high but there seemed to be little issue in terms of collection rates. There also seems to be a strong culture of citizens paying their taxes on the understanding that the welfare system would be superior to that found elsewhere and that public services would be of a high standard.
- Local taxation accounts for 57.8% of local government income and another source of local

income includes fees and direct charges for some of the services delivered (20.4%). The remainder of local government's expenditure is financed as follows: 12.1% reimbursements, 5.8% grants and VAT equalisation and 1.7% other financing. This results in a significantly different balance of funding to the UK.

Central Government funding

- Central government does provide an element of grant funding to local government which is intended to equalise on both tax base and need. This is part of the annual negotiations which take place between central and local government which appear to be undertaken along similar lines to that in Wales with LGDK representing the municipalities at the discussions.
- In terms of capital expenditure the amounts which local authorities may borrow are determined annually by central government with no equivalent to the prudential borrowing system.
- Finally it was noted that local authorities must calculate their budgets for the relevant budget year and provide three-year forecasts of their expenditure i.e. produce a four-year budget.

Local Government Structures, Reorganisation and Service Delivery

- Over the last four years there has been much discussion and consultation on the reorganisation of local government in Denmark. The arrangements have now been finalised and this will result in a reduction in the number of municipalities from 271 (average population 16,000) to 98 (average population 52,000 with a minimum of 20,000) and a reduction in the number of regions from 14 to 5. This will result in a reduction in the number of elected members from approximately 5,000 to 2,000. It was noted by LGDK that there was a belief amongst local politicians that democracy will suffer as a result of this reduction in elected members and it will be interesting to see whether the current turnout rates at elections of around 75% are affected post reorganisation. It was also noted that the local elected members receive an allowance but none (apart from mayors) receive a salary.
- The principles behind the reform relate to ensuring that there is coherence in service delivery for citizens and to realise improvements in efficiency. It is hoped that the larger units created by the reorganisation will lead to professional sustainability and be able to utilise economies of scale.
- The Ministry of the Interior anticipated that there would be savings from the mergers of perhaps 2-3% and maybe 5% for the smallest municipalities but that research had indicated that there was a U-shaped curve as regards savings so that a point might come where costs would increase. It was also noted that there would be some 'up front' costs attached to the merger process.
- The process of reform is also worthy of note, whereby central government has set very broad parameters for the new authorities, for example specifying a minimum population of 20,000 and

where this is not possible that binding agreements for service delivery must be entered into. However, for the most part it would appear that the mergers have taken place on a mutual basis between municipalities. In some cases there have been 6-7 municipalities involved and in others only 2 or three. There has been a role for LGDK in brokering some of these mergers and there has been consultation with the public. It would seem that the public is not too attached to their particular municipalities but are concerned that public services will continue to be of a high standard post reform.

- It was noted that there had been one forced marriage between a municipality with a poor record in financial management and its neighbours which was the last merger agreed. In this instance the central government had been required to become involved in the negotiations and in the provision of a financial incentive.
- No requirement to consult local populations was imposed by the central government but some municipalities had held local referenda to help inform their decision making.
- The regions will still be elected bodies but will lose their tax raising powers on reorganisation and be funded by block grant from the central government and some charged based on volume levied on the municipalities. Some of their current tasks such as secondary education (age 16 years and above) will be transferred to central government and some of their tasks (such as culture) will be transferred to the municipalities. The focus for the new regions will be the provision of health services and health insurance and some regional co-ordination functions such as regional development plans, specialised social institutions and highly specialised environmental tasks.
- It was noted that citizens in Denmark are becoming less tolerant in differences in service delivery standards and that central government sets minimum service standards for many services on a legislative basis. This point was noted by both LGDK and the Ministry of the Interior and health. The later in respect of the delivery of health services and was noted as one of the drivers to the reduction in the numbers of regions.
- Central government is starting to publish key performance statistics for local government and has also started to introduce a system of financial incentives to stimulate performance delivery in some areas such as care for older people. The amount of central government involvement with local service delivery is on the increase and the Ministry of the Interior gave the example of primary education where a recent OECD report had been critical of the service delivery especially in the area of mathematics.
- It was also noted that post merger the equalisation system operated by central government would not recognise populations of less than 20,000, there was thus a financial incentive to ensure mergers resulted in a minimum population of this size. It was also noted that LIT rates will be frozen during the transition so that the mergers cannot be used as a motivation for increasing LIT

rates.

- It was noted by LGDK that Denmark is at the leading edge of e-government so that for many citizens there would be a seamless transition during the merger process as many conduct their business with both local and central government through a public sector portal. It was noted that LGDK felt that 'back office' functions and administration were good and efficient already because of the progress made with e-government.
- It was also noted that there is much emphasis being placed on citizen focused service delivery now whereas the previous driver to e-government had been the attainment of efficiencies and economies of scale.

Deprivation

- A meeting was held with the Ministry for Refugees, Immigrants and Integration to learn about the area based initiatives being undertaken to tackle deprivation in the form of urban regeneration.
- The schemes discussed related to 12 areas and covered approximately 120,000 inhabitants mostly in and around Copenhagen over a period of 5-7 years. The funding was based on the local communities submitting a plan for consideration by the Ministry and the plan was required to include an exit or anchorage strategy.
- The plans were developed by local citizens and institutions and it was felt that this was extremely important to develop ownership at a local level for the scheme. Each group was also required to make a yearly statement of affairs and the groups exchanged experiences on a bi-monthly basis. It was also noted that a critical success factor was the involvement of experienced project managers with the groups. The schemes ranged from relatively simple schemes such as a 'walk and talk' scheme to more complex capital schemes involving infrastructure improvements.
- The way in which local interest and support for the schemes was discussed and some groups had made innovative use of technology such as the provision of videos as opposed to the more traditional means of communication and dissemination of information in the form of meetings.
- It was noted that one of the difficulties which the groups encountered in engaging with local authorities in their area was the way in which local authorities are divided into departments and the nature of the 'silo mentality'. It was identified that the way to overcome this was to have buy in to the project by the Chief Executive of the relevant local authority.