Llywodraeth Cymru
Welsh Government

Reforming Local Government Finance in Wales: An Update

October 2018

Mae'r ddogfen yma hefyd ar gael yn Gymraeg.
This document is also available in Welsh.

 WG36165 Digital ISBN 978 1 78964 292 6

Reforming Local Government Finance in Wales: 2018 update

Introduction

In October 2017, the Welsh Government provided an update about our phased programme of reforms to local taxes and the wider local government finance framework[1]. This document outlines progress over the past year and an update about our progress towards meeting the aims and objectives set out in our National Strategy, *Prosperity for All*.

Our priorities in developing a system of local taxation, which meets future needs are fairness for citizens and businesses while sustaining funding for vital local services. A key feature of this work is to strengthen the financial resilience of local authorities, so that they are better able to meet the financial challenges local services face, including those posed by the UK's exit from the European Union. We have consulted, and will continue to consult, on specific proposals as they develop but welcome all comments and contributions to the debate as it progresses.

Background and work programme

1. *Taking Wales Forward* and *Prosperity for All* outline the priorities for the Welsh Government for this term and beyond. Many of these will only be achieved with the help from other public bodies. Welsh Ministers invest functions in local authorities to deliver the national priorities at a local level and local authorities have freedom to set priorities about the services they believe will benefit communities.

2. There is a significant body of research into how local services should be funded in Wales; in the rest of the UK and internationally[2,3,4]. Much of the discussion has focused on local taxation as a means of raising revenue but also as a lever to meet various economic and social aims. Evolving council tax and non-domestic rates policy is an integral part of a phased reform of the wider funding framework for local government in Wales.

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[1] Reforming Local Government Finance in Wales: An Update, October 2017. https://gov.wales/docs/dsjlg/publications/localgov/171010-finance-reform-update-en.pdf

[2] Systems of Local Government Finance, Local Taxation and Resource Allocation. (Bennett, Allen and Grace, 2016). http://gov.wales/statistics-and-research/evidence-review-systems-local-government-finance-local-taxation-resources-allocation/?lang=en

[3] Scottish Commission on Local Tax Reform, December 2015. http://localtaxcommission.scot/download-our-final-report/

[4] Independent Commission on Local Government Finance Wales, March 2016. http://www.cipfa.org/partners/independent-commission-on-local-government-finance-wales/final-report

3. Our *Tax Policy Report*[5], which was published alongside the draft Budget 2019-20 on 2 October 2018, sets out progress in considering tax policy in Wales in a strategic way. The law requires that local tax revenue be used to fund local services. This creates some opportunity to consider how local taxes sit alongside the newly-devolved taxes and UK taxes which people, organisations and businesses will continue to pay. Where we make changes to local tax policy, we will make them in accordance with our tax principles – Welsh taxes should:

   - Raise revenue to fund public services as fairly as possible;
   - Deliver Welsh Government policy objectives, in particular supporting jobs and growth;
   - Be clear, stable and simple;
   - Be developed through collaboration and involvement;
   - Contribute directly to the Wellbeing of Future Generations Act goal of creating a more equal Wales.

4. Figure one outlines the objectives of the Welsh Government's programme of reforms and the anticipated timeframes associated with each element. As this is an evolving programme of work, some of the items have been amended since our 2017 update and some new items have been added where matters and opportunities have arisen. The remainder of this document provides further detail about each of these areas, grouped into the short, medium and longer term.

5. The work programme requires input from a wide range of stakeholders. Our expert-led Local Government Finance Reform Working Group was established in 2016 to test the possibilities in an applied and practical way. The Finance Sub Group of the Partnership Council for Wales provides the main forum for local government members and public sector partners to engage in the broader discussion. We are also engaging regularly about detailed matters with the Welsh Revenues and Benefits Group and the Distribution Sub Group. These engage key professionals from all 22 local authorities and wider local government about proposals relating to the finance system, in particular, their role as guardians of the effective use of public money.

[5] Welsh Government Tax Policy Report 2018, October 2018.
https://gov.wales/docs/caecd/publications/181003-welsh-tax-policy-report-en.pdf

Figure one: Objectives for local taxes and indicative timeline

Fair, progressive and better targeted local taxes

- new Small Business Rates Relief scheme that supports WG priorities (achieved April 2018 and ongoing development)
- lower non-domestic rates bills by switching the annual uprating from RPI to CPI (achieved April 2018)
- consult on changes to rates relief for independent schools and hospitals (2019)
- fair and progressive council tax (initial improvements in 2018)
- improve consistency in the treatment of care leavers and Severely Mentally Impaired people (from 2019)
- improved Council Tax Reduction Scheme taking account of UK welfare reforms (from 2019)
- ***explore*** different approaches to local taxes, eg. fundamental changes to council tax banding, land value taxes, local income taxes (from 2018)

Effective and proportionate local tax administration

- non-domestic rates 2017 revaluation and transition (achieved)
- improve council tax arrears management and enforcement (from 2017)
- reconsider the imprisonment sanction for council tax (from 2018)
- next non-domestic rates revaluation for 2021 (from 2018)
- tackle non-domestic rates avoidance (from 2018)
- non-domestic rates appeals reform (from 2018)
- improve information sharing and capability (part achieved and ongoing)
- ***explore*** modernised and more frequent property valuation resets (from 2017)

Supporting the wider local government finance framework

- support for city & growth deals (from 2018)
- provide new capital financing flexibilities (achieved)
- develop the settlement formula in response to changing spending patterns (annually) and local tax changes (from 2019)
- develop a funding framework to enable reform and service transformation (through Local Government Bill)
- ***explore*** the balance of funding between locally raised and centrally provided (from 2019)

Sound financial governance and strengthened local accountability

- supporting the role of the Chief Finance Officer in a changing environment (continuous)
- engaging citizens in decisions about spending priorities (continuous)
- develop accounting and audit framework (from 2019)
- continuous improvement to financial governance as a result of other changes described

Short-term reforms

6. These comprise changes which are within the existing powers of the Welsh Ministers and have been, or are being, implemented relatively quickly.

Fair and progressive council tax

7. *Taking Wales Forward* includes a commitment to **work with local government to review council tax to make it fairer**. Our published update in October 2017 outlined the work we have undertaken to define what we mean by fairness; what our objectives are and the range of possible improvements. We have examined a number of options to improve progressiveness, including changes to the tax relativities charged between the nine council tax bands; the property valuation basis; ways to improve the Council Tax Reduction Scheme (CTRS) and ways to improve the treatment of households in debt or those less able to contribute.

8. A key feature of the evidence we gathered in autumn 2017 suggested that many households are not always aware of the various forms of support they are entitled to or that they do not take up support for a number of complex reasons. When we looked at take-up rates of core welfare benefits we found a considerable variation of between 56% and 84%[6] for the UK overall. Our assessment of eligibility suggested take-up of the CTRS could be between 55% and 65%[7], although this will vary between local authority areas.

9. While take-up of the CTRS in Wales is difficult to measure, we know the number of households receiving support has fallen in all local authority areas since 2013-14, yet there is little evidence to suggest household finances have significantly improved. With the administration of Housing Benefit, in particular, being removed from local authority control as it is migrated into Universal Credit, dual applications for CTRS are expected to diminish further.

<u>Awareness campaign</u>

10. Responding to the evidence of potentially low take-up rates for council tax support, the Welsh Government launched a national awareness campaign as households received their annual council tax bills in March 2018. The campaign aimed to promote the CTRS and provide advice and support to thousands of households across Wales. The campaign activity includes:

[6] Department for Work and Pensions estimates of take-up (2015-16): Job Seekers Allowance 56%, Pension Credit 61%, Housing Benefit 77%, Income Support / Employment and Support Allowance 84% https://www.gov.uk/government/statistics/income-related-benefits-estimates-of-take-up-financial-year-201516
[7] Analysis of the Office for National Statistics' Family Resources Survey.

- New and easier-to-understand advice on the Welsh Government website, which received more than 20,000 unique hits between March and September 2018;
- 150,000 slips containing advice about council tax support and debt management included with reminder notices for households which have missed a payment between May and October 2018;
- 10,000 posters and flyers sent to local authorities, community hubs, advice centres, housing associations, third sector organisations and elected members;
- Targeted social media advertisements;
- Engaging with advice services, including MoneySavingExpert.com and Citizens Advice, to improve guidance and help promote available support, which has resulted in national coverage; and
- Establishing a data group with local authorities to use information to proactively identify eligible households which are not receiving support.

Support for mentally impaired people

11. Research by Money Saving Expert in September 2017[8] highlighted concerns about inconsistent advice about council tax, which was being given out throughout the UK to mentally impaired people. Drawing on our more general awareness campaign for CTRS, we have worked with Money Saving Expert to focus on this issue in Wales. The Welsh Government, Money Saving Expert and local authorities have worked together to develop clear and consistent advice and a guide[9] to be used as a tool to raise awareness of the specific council tax arrangements for people who are, or who live with someone who is severely mentally impaired (SMI).

12. A joint campaign was launched on 26 September 2018 by the Cabinet Secretary for Finance and Money Saving Expert, which featured in national media and MSE's email alerts, which regularly reach up to nine million people. Thousands of copies of the guide have been distributed to local authority contact centres, Citizens Advice centres and charities to aid practitioner handling of SMI cases. The next stage of the campaign will comprise Welsh Government working with local authorities and MSE to develop a consistent application form for the SMI discount. We will also review the procedures in local communities to ensure access to forms, and review training needs for practitioners, drawing on the expertise of organisations such as Age Cymru.

[8] Money Saving Expert "The Disregarded Discount", September 2017. https://images6.moneysavingexpert.com/images/documents/SMI_report-2017_final-interactive.pdf
[9] Are you eligible to pay less council tax? https://beta.gov.wales/sites/default/files/publications/2018-08/council-tax-discount-reduction-leaflet_0.pdf

Support for care leavers

13. Care leavers are young people who were in the care of a local authority for at least 13 weeks since the age of 14. Care leavers can be some of the most vulnerable young people in society with no family support network during important events in their lives, such as moving into their first home after leaving care. The Welsh Government has encouraged local authorities to exempt care leavers from paying council tax until they reach the age of 25.

14. The numbers of care leavers requiring a council tax exemption are small, as many already receive support through other means, such as the Council Tax Reduction Scheme (CTRS) and single adult discount. We do not believe there should be any barriers to local authorities applying this discretion. At the time of publication, nine local authorities in Wales are voluntarily delivering a care leaver exemption. The Welsh Local Government Association is exploring how this practice can be adopted across Wales to ensure consistent treatment.

15. The Welsh Government will consult on creating a mandatory exemption to ensure all care leavers across Wales are treated equally with regards to council tax and are exempt from paying council tax under the age of 25. Subject to the outcome of a consultation we will consider what legislation is required to create a mandatory exemption from 1 April 2019.

Non-Domestic Rates: supporting businesses to thrive

Changes to the annual uprating for non-domestic rates

16. Non-domestic rates raise more than £1bn every year in payments non-domestic property owners and occupiers as a contribution to the cost of local government and police services. There are approximately 110,000 ratepayers in Wales, whose bills are calculated using two variables – the 'rateable value' of each property, which is set by the independent Valuation Office Agency (VOA) and the 'multiplier' set annually by the Welsh Government, which reflects official measures of inflation.

17. In December 2017, the Welsh Government decided to change the annual uprating procedures to reflect movements in the Consumer Prices Index (CPI) rather than the Retail Prices Index (RPI)[10]. This change in approach means non-domestic property owners received lower rates bills for 2018-19 than expected and will continue to do so in the future. The annual saving to ratepayers across Wales is approximately £9m and is fully-funded by the Welsh

[10] Cabinet written statement, December 2017. https://gov.wales/newsroom/localgovernment/2017/171213-small-business-rates/?lang=en

Government. This decision demonstrates our commitment to reducing the burden on ratepayers while ensuring vital funding for local services remains sustainable.

Better targeted support for small businesses

18. *Taking Wales Forward* includes a commitment to **deliver a tax cut by supporting small businesses with their non-domestic rates bills**. Our published update in October 2017 outlined the initial steps we took to extend our temporary small business rates relief (SBRR) scheme in 2017-18; to put it on a permanent footing from April 2018 and to explore further improvements for 2018 and beyond.

19. Our review of the scheme highlighted additional features which could help to foster the conditions needed to ensure businesses and communities continue to thrive. Following a period of consultation[11], the Cabinet Secretary for Finance announced new proposals[12,13] for an improved scheme from April 2018. These new features included:

- Enhanced relief for childcare premises to support our flagship commitment to offer 30 hours of free childcare for working-age parents of three and four year-olds;
- Targeted support for community energy projects;
- An extension to the high street rates relief scheme for 2018-19;
- An extra £1.3m for local authorities in 2018-19 to provide discretionary relief to local businesses and other ratepayers, which would benefit from locally-determined assistance.

20. These enhancements were funded by limiting the number of properties eligible for relief to two per business in each local authority. This policy releases an estimated £7m per year by preventing larger businesses and national chains from benefiting from a scheme, which is designed to help small businesses. As we evaluate the success of the enhancements delivered in April 2018 we are continuing to explore ideas, which require a longer lead time to develop. More information about these wider ambitions for SBRR is provided in the section about medium-term reforms.

[11] Delivering a tax cut for small businesses: A new SBRR scheme for Wales, July 2017. https://beta.gov.wales/sites/default/files/consultations/2018-02/consultation_doc-en.pdf
[12] Cabinet written statement, December 2017. https://gov.wales/about/cabinet/cabinetstatements/2017/smallbusinesratesrelief/?lang=en
[13] Summary of responses, December 2017. https://beta.gov.wales/sites/default/files/consultations/2018-02/171213-tax-cut-responses-en.pdf

21. The Welsh Government will consult on proposals, in the next 12 months, to change the eligibility of independent schools and private hospitals to receive rates relief, bringing them into line with state-funded schools and NHS hospitals, which are liable for non-domestic rates.

Effective and proportionate local tax administration

Council tax debt management and enforcement

22. Our commitment to improve fairness also extends to reviewing the procedures through which council tax is collected and managed. We undertook research in autumn 2017 to consider what can be done to improve collection and arrears management[14]. The Welsh Government is working with local authorities to develop a proportionate and citizen-centred approach to council tax enforcement, ensuring local authorities have a clear policy for how they will treat vulnerable households and reduce the use of bailiffs. The Welsh Local Government Association has partnered with the 22 local authorities to develop a protocol (the *Council Tax Protocol for Wales: Good Practice in the Collection of Council Tax*), which we hope all stakeholders will sign up to, to improve consistency in how we treat households in arrears or at risk of arrears.

23. There is a great deal of further work to do before we can be assured that organisations are doing all they can to prevent council tax debt from escalating. The Welsh Government firmly believes that finding it difficult to get out of an escalating civil debt should not be treated like a crime. We have consulted on a proposal to remove the sanction of imprisonment for non-payment of council tax[15]. The Welsh Government will shortly announce its decision on the way forward.

Improving information sharing and data capability

24. Over the course of 2018, we have reviewed and enhanced our data-sharing arrangements with the Valuation Office Agency (VOA) to ensure we receive more frequent and detailed valuation data to support council tax and non-domestic rates policy development. This accompanies the existing sharing of information between local authorities and the Welsh Government, which provides vital information about the cost and effectiveness of reliefs and exemptions. Using powers under the Enterprise Act 2016, we established a

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[14] Government Social Research ‘Research into local authorities’ approach to council tax collection in Wales’, published 28 September 2017. https://gov.wales/statistics-and-research/local-authorities-approaches-council-tax-debt-recovery/?lang=en

[15] Removal of the sanction of imprisonment for the non payment of council tax, June 2018. https://beta.gov.wales/sites/default/files/consultations/2018-06/180611-removal-of-sanction-of-imprisonment-non-payment-council-tax.pdf

data-sharing gateway between the VOA and local authorities to help authorities manage their administration of non-domestic rates. We will continue to improve our data capability in the future so that it supports better-informed policy making.

Forecasting non-domestic rates revenue

25. Effective local tax administration also encompasses the capability to forecast non-domestic rates revenue so that we can manage the fluctuations in the funding available for local services, which would otherwise occur. Bangor Business School published its assessment of the forecasts for Welsh taxes alongside the outline draft Budget[16]. Its report includes the Welsh Government's forecast for the ‘distributable amount’ of non-domestic rates for the years up to 2022-23. Bangor Business School concluded that the non-domestic rates forecast was an established process that has been operated for many years by knowledgeable and experienced staff and, in recent years, the divergence of actual figures from the forecast has been small, suggesting this is a well-understood procedure.

26. We are working with the Valuation Office Agency to determine what appeals information could be made available to improve our forecast.

Funding flexibility for local government

27. The multi-billion pound finance framework that underpins the delivery of local services is a complex and interconnected system of different components. In April 2018, we extended local government’s flexibility to use capital receipts to fund investment in transformational activities for a further three years to 2021. We have also introduced changes to the capital finance and accounting regime by relaxing the constraints around loan capital transactions, specific share capital transactions and bonds. This places local authorities in Wales on an equivalent footing to local authorities in England. Capital spending decisions have revenue consequences which have implications for other funding, including the amount of revenue raised from local taxes.

28. We have also begun to explore the scope for share-gain approaches to local taxes where authorities could retain part of additional revenue which they raise through their own efforts. This includes looking at the potential for some form of non-domestic rates retention on a regional basis in connection with the current city deals – and potentially with the growth deals in the future – where the actions of the authorities working together result in a net growth in rates

[16] *Independent Scrutiny and Assurance of Devolved Tax Forecasts for Wales*, Bangor University https://beta.gov.wales/sites/default/files/publications/2018-10/bangor-report-2018.pdf

revenue. Local authorities have also been invited to suggest other areas where their efforts to improve the collection of local taxes results in better yield. This links to work to tackle fraud and avoidance in the rates system, which is covered later in this document.

Medium-term reforms

30. This phase comprises the changes to meet our aims and commitments which require a longer time period to consider and introduce and may require new legislative provision. The implementation of such changes will extend over more than one Assembly term.

Fair and progressive council tax

Assessing the impact of welfare reform

31. In addition to raising awareness of support for households in meeting their council tax liability, we are undertaking an extensive assessment of the impact of the UK Government's welfare reforms on household eligibility for the Council Tax Reduction Scheme (CTRS). It cannot be right that decisions taken in the UK context about welfare can have an impact on local taxation in Wales; an area of responsibility that has been devolved for decades. Yet, due to the way aspects of council tax policy mirror eligibility criteria for UK benefits, we are beginning to see an adverse impact across Wales as Universal Credit (UC) is being rolled out.

32. The Welsh Government will commission a detailed assessment of the impact of Universal Credit on CTRS. We suspect the impact is being felt in a number of ways:

- By directly reducing the number of automatically-passported cases, making it more difficult to proactively contact households and making the application process more complicated for eligible households;
- Through a loss of information held by local authorities as the administration of Housing Benefit is removed from local authority control;
- The switch to UC is having a negative shock to households, which may be causing or aggravating debt issues;
- Advice services are being over-burdened by UC cases and do not have the right information to signpost households to council tax support.

33. The detailed assessment will draw on data held by local authorities and related bodies to find and target households which are missing out on the support they should be receiving or were previously receiving. As it is a household-level assessment, the research will span a year, which means we can capture several stages of the UC rollout in new parts of Wales and identify how different households are affected. We will report on the findings of this exercise later in 2019.

Developing the Council Tax Reduction Scheme

34. The Council Tax Reduction Scheme (CTRS) is a priority for this government as it provides direct support to vulnerable and low-income households. We will continue to maintain full entitlements to the scheme in 2019-20, despite a reduction in the funding passed to Wales by the UK Government when it abolished Council Tax Benefit in 2013. This ensures almost 300,000 households in Wales – one in five – receive help with council tax. Of these, 220,000 households pay no council tax at all.

35. The findings from the research into the impact of Universal Credit (UC) will inform our development of CTRS from 2020-21 onwards to ensure parity of treatment between UC and non-UC households. We will also use the findings to consider whether a more fundamental rethink of the scheme is required in the medium term to mitigate the impact of welfare reform and to make council tax fairer and more progressive. The possibilities include amending the 'taper' (the rate of contributions to council tax for those who receive partial support); amending the means-test; considering income thresholds and the treatment of certain categories of household within the scheme, such as deductions for non-dependents.

36. As part of our longer term exploration (outlined in paragraphs 61-77) we will consider whether any new approach to local taxation in the future requires a separate support scheme or whether support could be more directly integrated into the design of the tax.

Council tax property valuation

37. Properties liable for council tax are placed in one of nine council tax bands based on property values assessed by the independent Valuation Office Agency (VOA). The purpose of this is to enable a system where the different bands can attract smaller to larger tax liabilities. Council tax bands in Wales are based on values as at 1 April 2003. Having undergone a revaluation exercise since its inception, Wales is in a better position than England and Scotland where council tax is charged on the basis of property values from 1991.

38. We will evaluate the success of our shorter-term measures to meet our commitment to make council tax fairer, such as the national awareness campaign, improvements to debt enforcement, mitigating the impact of UC and better treatment of care leavers and the severely mentally impaired. If we conclude there is more to be done to meet our commitment, there are further possibilities to explore in the medium term. This could include reconsidering the tax relativities charged between the nine council tax bands.

39. Without a revaluation exercise of the 1.4 million domestic properties in Wales, we are constrained in our ability to make fundamental changes that would help to make the system fairer – for example, adding bands to increase progressiveness and modernising the thresholds to fit present market conditions. We will commission an assessment of the likely impact a revaluation exercise would have on Wales' domestic tax-base if it were carried out. This will comprise an independent statistical exercise taking into account the latest available information on market values, transactions and physical changes to properties. The findings will be available later in 2019.

40. Revaluation exercises for council tax are costly and challenging to deliver. Therefore, in addition to this, and given advances in technology and data availability since 2003, we are exploring the viability of modernised methods of valuation which could ensure the council tax base can be more frequently updated in the future in a timelier and more cost-effective manner.

Supporting businesses to thrive

Rates relief beyond 2018

41. The enhancements we made to SBRR in 2017 and 2018 were designed to improve the scheme in a short timeframe. However, we have broader aims for how the scheme could operate in the future. The Cabinet Secretary for Finance and the Minister for Children, Older People and Social Care announced in September[17] 100% rates relief will be available for all childcare premises from April 2019, regardless of the size of the property. The scheme will provide an extra £7.5m support to all childcare providers for a three-year period. This decision supports our flagship pledge to offer 30 hours free childcare for working parents of three and four-year-olds, which is being rolled out across Wales. Rates relief will support the childcare sector as it grows capacity to deliver the offer, creating new jobs and childcare places.

Time-limited relief

42. A question posed by the Welsh Government in 2017 was whether small businesses should receive relief on a permanent basis or whether, in certain circumstances, the relief should be time-limited. For example, relief could be provided to start-ups as new ratepayers establish and grow, with support being gradually withdrawn as businesses become self-sustaining. Views from ratepayers and industry representatives suggested this was a more fundamental debate that required dedicated thought and consultation with

[17] Welsh Government statement, September 2018.
https://gov.wales/newsroom/people-and-communities/2018/100-per-cent-rates-relief-for-childcare-providers-in-wales/?lang=en

sectors in the future. There was some support for a time-limited element to rates relief, though some expressed concerns about any new framework creating opportunities for fraudulent behaviour. The Welsh Government is drawing together evidence of the advantages and disadvantages of such an approach and will consult further.

Alignment with *Economic Action Plan*

43. Providing rates relief is an important financial investment by the Welsh Government in our support for small businesses – we provide more than £200m of support to ratepayers across Wales every year. It is essential we target this investment to support priorities which are of social, economic or environmental benefit to Wales. The Welsh Government's *Economic Action Plan*[18] provides a framework for doing this and there may be opportunities to align rates relief to support the plan's broader ambitions. The Economic Contract requires businesses seeking direct financial support from the Welsh Government to demonstrate the following:

    - Growth potential;
    - Fair work (as defined by the Fair Work Commission);
    - Promotion of health, including mental health, skills and learning; and
    - Progress in reducing carbon footprint.

44. While direct financial support excludes non-domestic rates policy, we posed similar questions in the consultation about the future of SBRR in 2017. There was support for targeting rates relief to sectors such as renewable energy, tourism, public houses and businesses in rural communities. We have discussed how we are providing rates relief to childcare premises; a priority sector outlined in the *Economic Action Plan*.

45. The Welsh Government is considering whether rates relief should be targeted at those ratepayers, which support the government's wider objectives, such as those in the *Economic Action Plan*, or carry out activities which do not cause social or environmental harm. Under such a focus, rates relief could be withdrawn from businesses associated with payday lending, tanning salons and fast-food outlets.

46. As the approach to implementing the Economic Action Plan is worked up we are reviewing opportunities to align rates relief policy with Wales' wider economic ambitions. However, we must weigh the possible future enhancements against creating complexity for ratepayers and for local

[18] Welsh Government Economic Action Plan
https://gov.wales/topics/businessandeconomy/economic-action-plan/?lang=en

authorities when administering relief. This will determine whether future enhancements would be integrated into the rates system, delivered as part of the SBRR scheme, as separate schemes or through specific grant funding.

47. Our future ability to target rates relief to wider priorities depends in part on the information about businesses held by local authorities as administrators of non-domestic rates and by Welsh Government as policy-makers. For example, local authorities do not currently hold information about when new businesses come into existence, whether businesses pay the living wage (or other Fair Work measures), or information about employees. It will be necessary to consider whether it is appropriate and feasible for local authorities or the Welsh Government to hold more detailed information for the purposes of non-domestic rates.

48. It will be necessary to consult further on the range of ideas posed to align non-domestic rates policy to wider priorities and the requirements of the *Economic Action Plan*.

Improving non-domestic rates administration and compliance

<u>Non-domestic rates revaluation for 2021</u>

49. A revaluation exercise is a periodic review of the rateable values of all non-domestic properties in Wales. It is carried out to maintain fairness and accuracy of the system by redistributing the tax liability amongst ratepayers to reflect changes in the property market and to capture any changes that have been made to properties. On 11 July 2018 the Welsh Government announced it would bring the next revaluation exercise for non-domestic rates forward by a year from 2022, to 2021. This announcement means the rateable values on which non-domestic rates bills are based will reflect the latest market conditions and enable ratepayers to plan ahead for changes in liability. The exercise is not designed to raise additional revenue.

50. The independent Valuation Office Agency (VOA) is responsible for carrying out revaluation exercises. It will compile the next rating list to be used by local authorities for billing and collection purposes. The exercise has already begun and a new list will take effect from 1 April 2021. There is a great deal of activity required to implement a revaluation exercise, by the VOA but also by local authorities, the Welsh Government, the National Assembly for Wales and by ratepayers themselves.

51. The UK Government has announced it will adopt a three-yearly revaluation cycle in England after 2021. In light of the broader programme of work outlined in this update paper, and our ambitions to explore alternative approaches to

local taxes over the longer term, it would be premature to commit to the same three-yearly cycle. This is further discussed at paragraph 67.

Tackle non-domestic rates avoidance

52. Since 2015, the Welsh Government has been designing new measures to target and deter rates avoidance, alongside work being taken forward in Scotland[19], England[20] and Northern Ireland[21]. To develop our evidence base, in 2017 we asked local authorities to analyse billing systems to identify the scale of known or suspected rates avoidance in Wales. On the basis of that exercise, we believe avoidance amounts to at least 1% to 2% of the total yield – or between £10m and £20m annually, with some commentators suggesting it could be much higher.

53. All the funding raised from non-domestic rates is pooled and allocated to local authorities to help fund local services. Any avoidance therefore represents a loss in the funding available to those services. The evidence collated confirms the suspected methods of avoidance and supports various reviews undertaken by other administrations. These were primarily non-reporting of changes in circumstances; artificial occupation of empty properties to claim cycles of relief; bogus or dormant 'charities' occupying unsuitable or empty premises and phoenix trading or abuse of insolvency law.

54. The Welsh Government consulted[22] between April and June 2018 about an extensive set of measures to ensure the opportunities for those that wish to avoid contributing to the cost of local services are minimised. These included:

- Duties on ratepayers to report a change in their circumstances that would affect their rates liability;
- Powers for local authorities to request information from ratepayers and interested third parties;
- Powers for local authorities to enter and inspect non-domestic properties to verify information that would aid billing and collection;
- Changes to empty property relief arrangements;

[19] Report of the Barclay Review of Non-Domestic Rates, August 2017. https://www.gov.scot/Resource/0052/00523643.pdf
[20] Ministry of Housing, Communities and Local Government and HM Treasury discussion paper, December 2014, and summary of responses, July 2015. https://www.gov.uk/government/consultations/business-rates-avoidance-discussion-paper#history
[21] Review of Northern Ireland's non-domestic rating system, October 2015: https://www.finance-ni.gov.uk/sites/default/files/consultations/dfp/Review%20of%20Non-Domestic%20Rating%20System%20-%20Consultation%20Paper%20-%201%20December.pdf
[22] Welsh Government consultation, closed June 2018. https://beta.gov.wales/tackling-avoidance-non-domestic-rates-wales

- Potentially asking local authorities to publish a list of ratepayers in receipt of reliefs to aid transparency;
- Minimising abuse of charitable relief to ensure only genuine charities are supported;
- Future consideration of a General Anti-Avoidance Rule (GAAR) for local taxes in Wales (noting that the Welsh Government already has a general and targeted anti-avoidance rules for land transaction tax);
- Improving collaboration between organisations, sharing best practice amongst local authorities and improving our guidance for ratepayers.

55. Some of the proposals require new primary legislation and will be included in the proposed Local Government and Elections (Wales) Bill 2019 scheduled for introduction in February 2019. Other proposals require amendments to subordinate legislation or working with relevant agencies to improve practices. As the measures proposed for inclusion in a the Local Government Bill will not be enacted until 2020 at the earliest, and we will wish to provide sufficient time for ratepayers, local authorities and other organisations to prepare for the changes, we are considering implementing all changes together on 1 April 2021. This would coincide with the introduction of a new rating list following the next revaluation.

56. The Cabinet Secretary for Finance announced a series of measures to tackle avoidance on 16 October[23]. The package of measures set out by the Cabinet Secretary cannot be developed without the input and support of the business community, the majority of which pays the rates which are due. As we develop the finer details of proposals in 2019, we will continue to work collaboratively with ratepayers, industry representatives, local authorities, the VOA, the Charity Commission and relevant UK Government departments.

Non-domestic rates appeals reform

57. Earlier this year we consulted[24] on ways to improve the appeals system for non-domestic rates in Wales. We sought views on all aspects of the existing framework and gave stakeholders the opportunity to comment on a number of proposed changes. The views and evidence gathered are informing possible future legislative and administrative changes. The Welsh Government is working with ratepayers, the VOA and the Valuation Tribunal for Wales to explore in detail the potential implications of any changes. Our objective in

[23] Tackling Fraud and Avoidance of Non-Domestic Rates in Wales
https://gov.wales/about/cabinet/cabinetstatements/2018/tacklingfraudandavoidancendrwales/?lang=en

[24] Welsh Government consultation, closed January 2018.
https://beta.gov.wales/reforming-non-domestic-rates-appeals-system-wales

doing so remains to create an appeals framework that is more efficient and effective without putting unnecessary burden on ratepayers.

Long-term reforms to local taxes

58. This section outlines our progress towards an applied and practical exploration of different approaches to local government finance. Delivering fundamental reforms would require substantial new primary legislation and would need to be implemented over more than one Assembly term.

Explore different approaches to local taxes

59. Our update in October 2017 described the evolution of a conversation that has been happening in Wales, in the UK and around the world about funding mechanisms for local services and in particular, how local taxes are designed and raised. We set out our intention to move this conversation forward by exploring different approaches to raising local taxes in an applied and practical way, to assess whether there would be any real benefits for Wales.

60. Over the course of 2018, the Welsh Government has undertaken literature reviews and held discussions with the Local Government Finance Reform Working Group about land value taxes, local income taxes and modernised versions of the existing property-based taxes. The Working Group brings together expertise from economists, valuation experts, data and statistics, local government officers, experts in public service and those with the perspective of taxpayers, fairness and equality.

Themes for applied and practical assessment

61. The Working Group considered what our 'themes for assessment' of the alternative approaches for local taxes might be:

    - **People and taxpayers** – Can an alternative approach demonstrate local accountability; what would be the public acceptability of change; does it meet broader policy outcomes; what is the interface between the future approach and other taxes people and businesses will continue to pay; would taxpayers recognise an alternative approach as a local rather than a national tax; what is the social impact of an alternative approach.

    - **Sustainability of local services** – Does an alternative approach raise the same, less or more revenue for local services; what is the degree of future buoyancy; where should the tax liability fall, for example, on owners, on occupiers or someone else; what is the wider economic impact of an alternative approach; what is the optimal level of stability of a new tax design, for example, responsive yet not vulnerable to economic shocks or cycles.

- **Fairness** – Would an alternative approach be more or less progressive than the existing arrangements, ensuring those that are able to, contribute more than those who cannot; who would be the likely winners and losers compared to the existing approach; what would be the Welsh Government's policy on reliefs and exemptions in order to provide support where it is needed; would there be a future requirement to redistribute the revenue raised amongst areas of Wales to ensure equity.

- **Practical implementation** – How would we go about registering and valuing the entity that is to be taxed (both initially and periodically); what upfront costs would be incurred in developing the required infrastructure and capability; would collection and administration be more or less efficient than the existing arrangements, is the future approach affordable to maintain; does the alternative approach encourage adverse behaviours that do not currently exist; what are the legislative requirements for developing and implementing an alternative approach, are there any constitutional or devolution constraints.

62. The group proposed a number of areas for technical research during 2019. It was generally of the view that the literature provided good conceptual reasons to replace non-domestic rates with a local tax based on the value of land, and that this would be a sensible basis for consideration in Wales. There would need to be an assessment of the impact of its introduction on land prices and future distortion of the property market. Raising local taxes according to the value of land may not eliminate the need for a mechanism that redistributed the resources raised amongst local authority areas in Wales.

63. To develop a land value tax, the group considered a likely requirement would be a robust and accurate register of land in Wales. HM Land Registry estimates up to 15% of land in England and Wales may be unregistered but aims to achieve comprehensive registration by 2030[25]. It would be important to examine in more detail the scale and characteristics of unregistered land in Wales. The group considered whether moving from one approach to the other could be a gradual process. This would require an ability to separate the value of land from the value of property so that each element can be changed gradually.

64. In relation to local income tax, it was considered this concept was most suitable in the domestic context. The group considered there would be greater revenue risks and volatility and these effects can be more pronounced than other

[25] HM Land Registry blog 'Searching for unregistered land', February 2018. https://hmlandregistry.blog.gov.uk/2018/02/05/search-owner-unregistered-land/

approaches to local taxation, for example, during periods of recession and lower employment. However, some Scandinavian countries administer a form of local income tax effectively and this would be an area to focus further research on.

65. A local income tax as a replacement for council tax would also display a higher degree of mobility. The Holtham Commission[26] found in 2008, 50% of the Welsh population lived within 25 miles of the border with England, compared to only 3.5% of the Scottish population living within 25 miles of the border with England. This also raises questions about mobility within Wales, if it were so designed that a local income tax would need to encompass 22 local authority borders. While a local income tax has the potential to be more progressive than other approaches by relating more directly to disposable household income, it is likely that very high earners would also be highly mobile if the difference in local tax rates were too great. This risk may mean that revenue stability is favoured over progressivity. The costs of administration would also be an important consideration.

66. The Scottish Government has asked the Scottish Land Commission[27] to assess the potential for land value based taxes in Scotland. We have met the Scottish Land Commission to understand how it is approaching this question. The Commission's initial work considers the potential of land value taxation to contribute to more productive, accountable and diverse use of land. We will continue to meet the Commission periodically to learn about their findings and recommendations.

<u>Timeline for technical work</u>

67. The discussions this year have helped formulate the phases of the work programme for 2019, where the focus will be on empirical and technical work to assess the magnitude and nature of the practical challenges. The Welsh Government will undertake a series of distinct but linked pieces of research throughout 2019:

- We will explore the feasibility of a land value tax as a possible replacement for non-domestic rates. This would be an initial step with a view to further work, assessing land value tax as a replacement for council tax;

- We will conduct a hypothetical revaluation and re-banding exercise for council tax to assess whether modernising council tax is a viable option to be compared with any alternative approaches;

[26] Independent Commission on Funding & Finance for Wales (the 'Holtham Commission') Final Report, July 2010. https://gov.wales/docs/icffw/report/100705fundingsettlementfullen.pdf
[27] Scottish Land Commission website https://landcommission.gov.scot/

- We will explore better and more frequent ways to value non-domestic property within the existing framework for non-domestic rates, if the Welsh Government concludes alternative forms of tax are not viable; and

- We will explore the feasibility of a local income tax or local turnover tax as possible alternative approaches to domestic and non-domestic taxation.

68. These priorities will be reflected in the Welsh Government's tax policy workplan, which is due to be published in early 2019.

69. Further research about local income tax has not yet been scoped but will be considered in due course. The findings from the technical work will be brought together in early 2020. The Welsh Government will outline the possibilities ahead of the National Assembly elections in 2021.

70. The Welsh Government continues to be clear any alternative method of raising local taxes must raise funds for local government in a stable and predictable way, as this is the legislative and constitutional basis on which local taxes exist within the current devolved settlement. Once the outcomes of the technical work are available, we will use these to further consider how the other elements of the finance system for local government should be changed, such as grant funding and the balance between locally raised and centrally provided revenue.

71. Within Welsh Government there will need to be a broader consideration of the development of a local land value tax alongside our other proposals to consider a national vacant land tax on stalled sites. While these proposals are designed to meet a different policy aim (to help meet housing and development needs by bringing land into productive use rather than to raise revenue for local services) there will be common considerations and interdependencies. We will wish to consider these issues in more detail over the coming year, and alongside the analysis put forward in various academic report, such as the Wales Centre for Public Policy report on risks and opportunities for the Welsh tax base[28].

72. Throughout 2019, our intention is to develop more detailed and formalised discussions with organisations such as HM Land Registry and the Valuation Office Agency, which may have views on alternative approaches and may have practical information to share.

[28] Wales Centre for Public Policy, July 2018
https://www.wcpp.org.uk/wp-content/uploads/2018/07/The-Welsh-Tax-Base-_WCPP-Final-180627.pdf