Llywodraeth Cymru
Welsh Government

Welsh Government

Welsh Tax Policy Report 2021

March 2021

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Foreword

This report summarises the progress made against the latest Tax Policy Work Plan, which I published in September 2020. It describes the programme of research, development, reviews, and communications activity which we have been undertaking to strengthen our understanding of the operation of Welsh taxes, and of the opportunities to use taxes to help deliver our ambitions for Wales.

This work follows the principles described in our Tax Policy Framework, including our aim to develop taxes which are fair, and are aligned with the Welsh Government's wider policy priorities.

The topics are presented under three themes:

A. Develop tax policy as fairly as possible, aligned with Welsh Government policy priorities, and in collaboration with stakeholders.
B. Operate and develop Welsh taxes within a UK context.
C. Increase knowledge and understanding about taxes in Wales.

In addition, the findings from more detailed analytical research of Welsh taxes are provided in the annexes. These examine the impact of recent changes to Land Transaction Tax, evaluate previous forecasting of Land Transaction Tax and Landfill Disposals Tax, and take a close look at Welsh Rates of Income Tax by studying the tax base, and considering what would be the effects of changing the tax rates.

I hope you find this report useful. If you have any questions or comments, or would like to learn more about any of the subjects discussed, please contact the Welsh Treasury through one of the channels listed at the end of the document.

Rebecca Evans.

Rebecca Evans MS
Minister for Finance and Trefnydd
March 2021

Background

1. The way public services are funded in Wales has changed, following the introduction of three devolved Welsh taxes – Land Transaction Tax (LTT), Landfill Disposals Tax (LDT), and Welsh Rates of Income Tax (WRIT).

2. In return for the tax revenue generated by the Welsh taxes, the UK Government has reduced the block grant funding it provides to Wales by an equivalent amount.

3. It is essential that Welsh taxes are operated efficiently and effectively, to generate the revenue needed to fund Wales' vital public services – such as health, social services, education, and transport infrastructure.

4. The devolution of tax powers allows the Welsh Government to develop a more strategic approach to central and local taxation in Wales, ensuring it is better able to tackle the needs and priorities of citizens and businesses. The Welsh Government set out its approach in 2017, in the Tax Policy Framework[1]. This includes five principles to shape Welsh taxes:

   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; and
   - Contribute directly to the Well-Being of Future Generations Act goal of creating a more equal Wales.

5. The Welsh Government has operated a tax policy cycle, involving publication of a work plan, followed by research, analyses and engagement, before reporting on the emerging findings and conclusions.

6. Publication of the work plan is intended to raise awareness among stakeholders and other interested people and organisations about what the Welsh Government is investigating, enabling them to ask questions, and contribute views, knowledge and experiences. To support this, the Welsh Government has held tax conferences in 2018, 2019, and 2020, to provide opportunity to explore some of the work streams and other tax issues in more detail.

[1] Welsh Government Tax Policy Framework: https://gov.wales/sites/default/files/publications/2018-10/tax-policy-framework.pdf

Welsh tax rates

Background

7. Land Transaction Tax (LTT) and Landfill Disposals Tax (LDT) were introduced on 1 April 2018, and are collected and managed by the Welsh Revenue Authority (WRA). Welsh Rates of Income Tax (WRIT) were introduced on 6 April 2019, and are collected and managed by HMRC.

Welsh Rates of Income Tax

8. Income tax is partially devolved to Wales, which means that while the Welsh Government is able to vary the three income tax rates (basic, higher and additional) for Welsh taxpayers[2], all other aspects of the tax remain the responsibility of the UK Government, and HMRC continues to administer income tax in Wales.

9. The process involves the UK Government reducing each of the three income tax rates for Welsh taxpayers by 10p, and making a corresponding reduction to the Welsh block grant, which funds devolved public services in Wales. The Welsh Government decides whether to set the Welsh rates at 10p, thereby reinstating the funding for services (and retaining parity between Welsh and English taxpayers) or to set different rates.

10. In line with its commitment not to increase WRIT during this Senedd term, the Welsh Government intends to set the Welsh Rates of Income Tax for 2021-22 at 10p. This proposal must be confirmed by the Senedd, through a motion prior to the agreement of the final Budget.

11. Figure one shows the rates and thresholds, based on the 2021-22 Income Tax thresholds and personal allowance which were announced in the UK Government's Spending Review, November 2020, and which are due to be confirmed in the UK Spring Budget[3].

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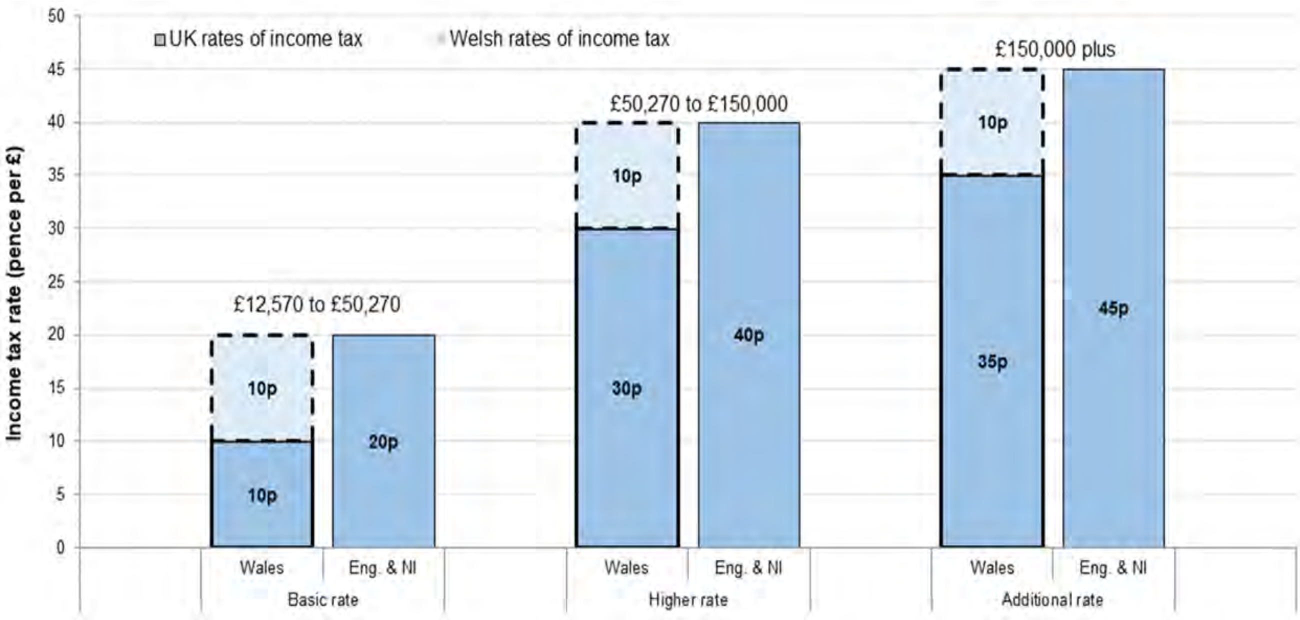
[2] In most cases, Welsh taxpayers are defined as people who live in Wales, however a full definition is provided under s.8 of the Wales Act 2014:
http://www.legislation.gov.uk/ukpga/2014/29/section/8/enacted

[3] Spending Review 2020, 2.8 National Living Wage and personal tax thresholds, "Further, the government will increase the 2021-22 Income Tax Personal Allowance and Higher Rate Threshold in line with the September CPI figure":
https://www.gov.uk/government/publications/spending-review-2020-documents/spending-review-2020

Figure one: Income tax rates in Wales, 2021-22*



* Income tax rates for 2021-22 announced in the UK Government's Spending Review, November 2020, and due to be confirmed in the UK Spring Budget 2021.

Land Transaction Tax

Rate changes during 2020-21, and rates for 2021-22

12. The 2020-21 LTT rates initially remained unchanged from earlier years. This retained the approach of maintaining consistency and stability for the property markets in Wales.

Main Residential Rates: Tax Rates and Tax Bands

13. As part of the Welsh Government's COVID-19 response on 27 July 2020, the rates and bands for the main rates of LTT were changed for a time-limited period. The rates and bands for the temporary tax reduction period apply from 27 July 2020 to 31 March 2021. The Welsh Government made a decision not to provide tax reductions in this period to taxpayers liable to the higher residential rates.

14. The changes to the main residential rates were made by made affirmative regulations on 22 July 2020, and came into force on 27 July 2020. The rates applicable to the higher residential rates were not changed. The explanatory memorandum[4] that accompanied the regulations included a statement of the policy intent that the changes would have a "positive effect on the housing market and the economy more generally this year". The regulations, and therefore the rate changes, were approved by the Senedd on 29 September 2020.

[4] 'Explanatory Memorandum to The Land Transaction Tax (Temporary Variation of Rates and Bands for Residential Property Transactions) (Wales) Regulations 2020': https://senedd.wales/laid%20documents/sub-ld13367-em/sub-ld13367-em%20-e.pdf

15. On 3 March 2021 the Minister for Finance and Trefnydd made further regulations to extend the temporary tax reduction period so that it will end on 30 June 2021[5]. The Senedd vote to approve these regulations is to be held on 23 March 2021.

Table one: LTT residential main rates (before 27 July 2020 and from 1 July 2021)

Price threshold	LTT rate
£0 to £180,000	0%
More than £180,000 to £250,000	3.5%
More than £250,000 to £400,000	5%
More than £400,000 to £750,000	7.5%
More than £750,000 to £1,500,000	10%
£1.5m-plus	12%

Table two: LTT residential main rates (from 27 July 2020, and before 1 July 2021)

Price threshold	LTT rate
£0 to £250,000	0%
More than £250,000 to £400,000	5%
More than £400,000 to £750,000	7.5%
More than £750,000 to £1,500,000	10%
£1.5m-plus	12%

Higher Residential Rates: Tax Rates and Tax Bands

16. The Welsh Government made the decision not to provide any temporary tax reductions to taxpayers liable to the higher residential rates. The tax rates and bands therefore remained the same as initially chargeable from 1 April 2018, when LTT came into force. These are set out in table three, below.

17. However, as part of the draft Welsh budget announced on 21 December 2020, the higher residential rates were increased by 1 percentage point each. This change came into effect on 22 December 2020, and provided transitional rules for those taxpayers who had exchanged contracts on, or before, 21 December. A Written Statement by the Minister for Finance and Trefnydd described the policy changes in relation to the devolved and partially devolved taxes[6]. The regulations making the change received Senedd approval on 2 February 2021.

18. The rates and bands that applied for the period up to and including 21 December 2020 are provided in table three, and the rates that apply from 22 December are set out in table four, below.

[5] Written Statement by the Minister for Finance and Trefnydd - 3 March 2021 regulations: https://gov.wales/written-statement-land-transaction-tax-extension-temporary-tax-reduction-period and 'Explanatory Memorandum to The Land Transaction Tax (Temporary Variation of Rates and Bands for Residential Property Transactions) (Wales) (Amendment) Regulations 2021': https://senedd.wales/media/l2nozj1k/sub-ld14189-em-e.pdf

[6] Written Statement by the Minister for Finance and Trefnydd about Welsh Devolved Taxes and Welsh Rates of Income Tax, 21 December 2020: https://gov.wales/written-statement-welsh-devolved-taxes-and-welsh-rates-income-tax-draft-budget-2021-22

Table three: LTT residential higher rates (before 22 December 2020)

Price threshold	LTT rate
£0 to £180,000	3%
More than £180,000 to £250,000	6.5%
More than £250,000 to £400,000	8%
More than £400,000 to £750,000	10.5%
More than £750,000 to £1,500,000	13%
£1.5m-plus	15%

Table four: LTT residential higher rates (from 22 December 2020)

Price threshold	LTT rate
£0 to £180,000	4%
More than £180,000 to £250,000	7.5%
More than £250,000 to £400,000	9%
More than £400,000 to £750,000	11.5%
More than £750,000 to £1,500,000	14%
£1.5m-plus	16%

Non-residential Rates: Tax Rates and Tax Bands

19. As part of the Welsh Government's draft Budget for 2021-22, published on 21 December 2020, the zero rate tax bands which apply to non-residential property transactions were increased from up to £150,000 to up to £225,000. The changes apply to both the non-residential main rates and the non-residential lease rent rates. These changes came into effect on 22 December 2020, and provide reductions for transactions which complete on or after 22 December 2020.

20. The regulations making the change received Senedd approval on 2 February 2021.

21. The draft Budget for 2021-22 also included a change to the specified amount of relevant rent, increasing the amount by 50% from £9,000 to £13,500. The relevant rent amount is used to apply an anti-avoidance rule. Increasing the amount by the same percentage as the non-residential zero rate bands ensures it will operate in the same manner, and to the same extent, as before the changes were made. The new amount of relevant rent applies from 4 February 2021, following approval by the Senedd.

22. The rates and bands which applied in the period up to, and including, 21 December 2020 are set out in tables five and six. The rates which apply from 22 December are shown in table seven and eight below.

Table five: LTT non-residential main rates (before 22 December 2020)

Price threshold	LTT rate
£0 to £150,000	0%
More than £150,000 to £250,000	1%
More than £250,000 to £1,000,000	5%
£1m-plus	6%

Table six: LTT non-residential main rates (from 22 December 2020)

Price threshold	LTT rate
£0 to £225,000	0%
More than £225,000 to £250,000	1%
More than £250,000 to £1,000,000	5%
£1m-plus	6%

Table seven: LTT non-residential lease rent rates (before 22 December 2020)

Price threshold	LTT rate
£0 to £150,000	0%
More than £150,000 to £2,000,000	1%
£2m-plus	2%

Table eight: LTT non-residential lease rent rates (from 22 December 2020)

Price threshold	LTT rate
£0 to £225,000	0%
More than £225,000 to £2,000,000	1%
£2m-plus	2%

Landfill Disposals Tax

23. The rates for 2021-22 were approved by the Senedd on 2 February, and will increase with inflation from 1 April 2021. This continues the policy of maintaining consistency with the UK Government's approach to landfill tax rates.

Table nine: LDT rates (rate per tonne) 2020-21 and 2021-22

Rate	2020-21	2021-22
Standard	£94.15	£96.70
Lower	£3.00	£3.10
Unauthorised	£141.20	£145.05

A. Develop tax policy as fairly as possible, aligned with Welsh Government policy priorities, and in collaboration with stakeholders

1. Strengthen the Welsh tax base.

Continue to take action to support growth in the Welsh tax base, and develop the means to monitor progress.

Background

24. The spread of COVID-19, and the actions to contain it, have had a dramatic impact on Wales and many countries around the world. The deterioration in labour market conditions, associated with the pandemic and the UK's departure from the European Union, is likely to have persistent, adverse effects on people's long-term socio-economic outcomes. Evidence shows that even short spells of unemployment can harm people's future employment and wage prospects, with subsequent negative impacts on the Welsh tax base.

Evidence and Analysis

25. The full impact of the current economic circumstances on the Welsh tax base will only manifest itself over the coming years. The Welsh Government will continue to undertake research to provide a better understanding of the Welsh tax base. As part of this on-going research, a detailed analysis of the tax base for Welsh Rates of Income Tax (WRIT) is provided at Annex two. This includes analysis of the characteristics of the income tax base in Wales, past and projected performance of employment and earnings, and the possible current differential impact of the COVID-19 pandemic on Wales and on England and Northern Ireland.

Outcome and next steps

26. Recognising the risks posed to the Welsh Tax base by the current economic environment, the Welsh Government continues to take unprecedented actions to support individuals and businesses in Wales.

Supporting Businesses

27. Our £2bn business support package means companies in Wales have access to the most generous offer of support anywhere in the UK. This is in addition to the wage support schemes available from the UK Government during the pandemic.

28. Our support builds on the foundations laid by the Economic Action Plan, published in 2017, which sets out our vision for inclusive growth and productive regions. More than 13,000 businesses have benefited from £300m of support from our Economic Resilience Fund, protecting 100,000 jobs which might otherwise have been lost. In October 2020, we provided a further £300m of support in the fund's third phase.

29. The Development Bank of Wales was launched in 2017 and has played a crucial role in helping firms grow, survive and thrive across the term. The Bank reported a record 457 investments totalling £103.3m in 2019-20, creating or safeguarding almost 4,000 jobs across Wales. To help grow firms and provide jobs faster, the Bank also launched an updated fast track loan this year – loans of up to £25,000 are now available with a

decision made in two working days. Including the Help to Buy Wales scheme, the Development Bank of Wales currently manages over £1.2b of Welsh Government funds.

30. Business Wales has maintained its crucial support to Welsh businesses. Business Wales' schemes have created 12,700 jobs since January 2016, helping to create 3,805 new enterprises, and generating more than £33.7m of exports. This success has continued this year: the Accelerated Growth Programme created more than 1,660 jobs between October 2019 and August 2020. We provide more than £230m of non-domestic rates relief to businesses and other ratepayers through our range of rates relief schemes. Since 2017-18 we have provided additional relief for retailers and businesses on the high street. Our rates relief schemes mean that three-quarters of all ratepayers across Wales have received rates relief this year, with more than 70,000 businesses paying no rates at all.

31. The pandemic has had a particular impact on the hospitality sector, and we have taken quick action to support this important part of our economy. We have provided a total £450m of support for the sector – the most generous support package in the UK. The package includes 100% rates relief for retail, leisure and hospitality businesses with a rateable value of £500,000 or less, and a sector-specific £180m fund as part of the Economic Resilience Fund.

International Strategy

32. One of the ambitions of our International Strategy is to grow the resilience of the Welsh economy by increasing exports and attracting inward investment. Successfully delivering on this ambition will create jobs and opportunities for people in Wales and help support our tax base. In December 2020, we published our Export Action Plan[7] which sets out the practical steps the Welsh Government is taking to support Welsh exporters – both in terms of leaving the EU and aiding recovery from the COVID-19 pandemic, including:

- Delivering a series of measures to support businesses to export during, and in the immediate aftermath of, COVID-19 to support them to **recover** and **rebuild**;
- Ensuring our exporters are prepared for any new trading environment (requirements) with the EU, after the ending of the **transition** phase following the UK's exit from the EU, and any other new free trade agreements;
- **Reinventing** our export support programmes to adapt to the 'new normal' post COVID-19; and
- Driving the **growth** of Welsh exports in the longer term, increasing the contribution that exports make to the Welsh economy, including by broadening our exporter base.

33. Furthermore, the International Strategy outlines how we will ensure Wales is recognised for being the best place in the UK for graduate start-ups, which will encourage those who study in Wales to stay in Wales.

[7] Export Action Plan: https://gov.wales/sites/default/files/publications/2020-12/export-action-plan.pdf

Supporting People

Employability and Skills

34. Helping people to build the human capital they need to secure fair, rewarding work is central to our approach to strengthening our tax base. In July 2020, we invested £40m to boost our Jobs and Skills Package and our COVID Commitment to ensure anyone over 16 in Wales can access advice and support to find work, pursue self-employment, or find a place in education or training.

35. Our Community Employability Programmes, delivered in collaboration with local authorities and the Department for Work and Pensions, have supported more than 54,000 people since 2015 with training, essential skills and work placements, with more than 20,000 gaining employment. We have adapted the programmes to provide continued outreach in our most deprived and vulnerable communities.

36. Since April 2020, 6,620 people have been supported to improve their skills with nearly 3,000 entering employment. Working Wales has helped more than 20,000 people since April 2020 with advice, guidance and support across various programmes, including free online learning for workers on furlough.

37. We have achieved our target of creating 100,000 high-quality apprenticeships in this Senedd term, enabling people to develop skills while earning a wage. We continue to offer incentives of up to £3,000 to support apprenticeship recruitment.

38. We have also piloted Degree Apprenticeships, focusing on skills gaps in Digital/ICT and Advanced Engineering. Over this Senedd term, we will have allocated £575m for apprenticeships and traineeships. Since 2014, we have helped 26,700 people into work and supported 112,800 qualifications through £861m investment from the EU structural fund programme. The Employability Support Programme, first launched in 2016, reached more than 1,800 participants over the same period, with 745 of those entering employment. The national rollout of the Personal Learning Account Programme, which launched in September 2019, helps workers access retraining and find new employment in areas of skills demand.

39. Our progressive and equitable student support system, which is unique in Europe for financing full and part time undergraduates and postgraduates with living costs grants and loans, has helped underpin a 51% increase in first year, full-time postgraduates from Wales, and a 20% increase in part-time postgraduates from Wales since the 2015/16 academic year. Our two new Seren Programmes have contributed to record numbers of students from disadvantaged and non-traditional backgrounds in Wales going on to higher education.

40. Our ReAct scheme helps people who have been made redundant, or have become unemployed for another reason, through subsidised wages and job-related training. This year we expanded the scheme, and since April 2020, ReAct has provided nearly 2,000 vocational training grants for learners and awarded wage subsidies to almost 300 employers.

41. In November 2020, we celebrated 20 years of the Wales Union Learning Fund, which has supported more than 5,000 people with accredited and non-accredited learning, advice, and guidance on essentials skills and career progression since April 2020. The Flexible Skills Programme has delivered priority training to more than 2,000 employees to increase the digital talent base and support workforce skills in key sectors such as advanced engineering. This programme complements our £12m investment in the world's first compound semi-conductor cluster in Newport, putting us at the forefront of world-leading technology and employing 1,500 people.

42. Our In Work Support Service has been pivotal in supporting people to stay in work through physiotherapy, psychological therapy and occupational therapy. Since September 2015, the Service has supported 7,200 people, including 3,800 with musculoskeletal issues and 3,400 with mental health conditions. Our Out of Work Service has also worked with more than 13,000 people, helping some 2,700 to achieve a work-related certificate or qualification and 1,000-plus people into employment.

Migration policy

43. We are determined that people from other countries who have chosen to make their home in Wales feel welcomed and valued members of our communities, contributing as they do in many ways, not least to the economic wealth and tax base of our country. We continue to urge the UK Government to engage with us on all migration issues which have cross-cutting implications for many aspects of the public policies and services that we are responsible for delivering.

44. Given the strength of Wales' interests in relation to migration, we want to have a meaningful engagement with the UK Government in this respect of its policy, the changes to the immigration system that came into effect in January 2021, and the implications these have on needs and priorities of businesses and essential front line services in Wales.

Supporting EU citizens to stay in Wales

45. The last few years have been unsettling for many, but particularly so for those citizens who came originally from elsewhere in Europe and have made their home in Wales. We will use every opportunity to ensure the rights and status of EU citizens in Wales are protected. We continue to support EU nationals in applying for the EU Settlement Scheme (EUSS) to secure their entitlements by making free help and advice available to them, noting the Scheme deadline of 30 June 2021.

46. Alongside funding Newfields Law and Citizens Advice Cymru to deliver advice and support services, we work closely with the EUSS Wales Coordination Group, which includes a number of other organisations in Wales (including funding from the Home Office), and works to deliver their services across Wales in a planned, focussed and coordinated manner.

47. We remain concerned about the number of vulnerable EU citizens in Wales who may not secure their settled or pre-settled status for a number of different reasons and could find themselves with uncertain status in the UK, with corresponding impacts on access to public services in Wales.

Fair Work

48. We are delivering our priorities and ambitions for a fair work nation, using every lever we have to help realise fair work outcomes and improve working lives for the better. We are exercising the power of the public purse and our social partnership approach to promote fair work practices across the public and private sectors. We have made good progress in establishing the Social Care Forum, which is considering measures to improve working conditions and pay in social care. We have set up a national Health and Safety Forum, which is bringing social partners, enforcement agencies and others together to improve Health and Safety outcomes. We have also successfully launched a campaign targeted at providing workers and employers with the knowledge, tools and support to make workplaces better, fairer and more secure.

49. Our support for fair work is not limited to social value and moral and ethical arguments – we see fair work as fundamental to a prosperous economy. This reflects the strong relationship between fair treatment of employees, their well-being and engagement with increased commitment, productivity, lower absenteeism, better recruitment and retention, and other aspects of business and economic performance. International evidence from the OECD and others suggests that far from undermining competitiveness, high labour standards and smaller inequalities in the distribution of income and wealth can support economic success.

50. We will step up our work with social partners to champion the benefits of employers and Trade Unions, working as partners in a spirit of collaboration, shared commitment and mutual respect to make the workplace a better place for all – improving access to Trade Unions is key to this. The best employers provide fair work and recognise the business benefits of doing so, and we will continue to advocate the economic as well as ethical case for fair work as we take this agenda forward.

The National Development Framework: Future Wales – The national plan 2040

51. Future Wales, as the National Development Framework will be known, will support the growth in the tax base by identifying where housing and employment, and the services and infrastructure which support them, will be located.[8]

52. The Welsh Government published Future Wales: The National Plan 2040 in February 2021. Future Wales will cover the 20 year period up to 2040, and will be reviewed every five years.

53. Future Wales identifies three national growth areas – Wrexham and Deeside, Swansea Bay and Llanelli, and Cardiff, Newport and the Valleys. The Welsh Government wishes to see national growth focussed in these areas over the next 20 years. Future Wales will inform Welsh Government decisions on spending and investment to support growth in the areas

54. There are clear links between housing and the economy, both in terms of the immediate economic benefits associated with house building, and the importance of the availability of good quality housing in helping to attract and retain a workforce to support the tax base. Future Wales identifies that around 110,000 new homes are needed in Wales by 2039, and these will extend the tax base for residential properties.

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[8] Future Wales: The National Plan 2040:
https://gov.wales/future-wales-national-plan-2040-0

We have committed to delivering 20,000 affordable homes during this government term. Good progress is being made towards achieving the target. We are confident we will deliver on this commitment, due in no small part to our record investment of £2bn in housing this Senedd term.

2a. Continue to keep Land Transaction Tax under review

Ensure the devolved taxes are operating as intended, and consider opportunities for the taxes as levers to support wider policy objectives. This includes considering the impact of the temporary changes to the Land Transaction Tax residential rates in response to the effects of the COVID-19 pandemic.

Background

55. Residential property in Wales is subject to Land Transaction Tax (LTT) when it is purchased, and to council tax on a recurring basis.

56. LTT higher rates are charged on additional residential properties bought by individuals who already own a residential property – for example second homes, buy-to-let properties – and on the purchase of any residential property where the buyer is not an individual, such as a company.

57. The higher rate of tax on additional properties was introduced for stamp duty land tax (SDLT) in April 2016. In replacing SDLT with LTT in Wales, the higher rates were replicated both because stakeholders stressed the importance of consistency across the taxes and the revenue raised by this aspect of the tax. If the higher rates had not been replicated, there would have been a need to raise this revenue from other taxpayers to maintain the funding available for public services in Wales. The net amount of money raised from the December 2020 changes (estimated by the OBR to be £14 million for 2021-22) will be used to fund social housing initiatives.

58. During scrutiny of the Land Transaction Tax and Anti-avoidance of Devolved Taxes (Wales) Act 2017, it was suggested local authorities should be able to make representations to Welsh Ministers about the higher rate surcharge, to help to meet the needs of different communities in Wales. Local authorities may make representations to Welsh Ministers, and the then Cabinet Secretary for Finance and Local Government wrote to the leaders of all local authorities in Wales inviting their engagement about the operation of the higher rate surcharge in their area, once sufficient data are available to inform these discussions.

59. The Welsh Revenue Authority (WRA) and the Welsh Treasury are fully engaged in the Welsh Government's work in relation to the pressure on housing in certain areas, particularly tourist hotspots, as a result of purchases of homes to be used as holiday homes, as part of a furnished holiday letting business, or as both. The policy areas relevant to this issue are wide ranging. The rate of LTT charged when buying such homes is part of the Welsh Government's consideration.

Evidence and analysis

60. The WRA regularly publishes monthly and quarterly LTT data. It also publishes annual data, with the second annual statistical release for LTT covering the second year of operation (2019-20), providing a range of information about residential property transactions[9].

[9] Land Transaction Tax statistics: April 2019 to March 2020:
https://gov.wales/land-transaction-tax-statistics-april-2019-march-2020

61. As previously, the WRA analysed LTT data in relation to the higher rates for additional properties on a local authority basis. The data show a wide variation between local authorities in the level of higher rate residential transactions as a percentage of all residential transactions.

<u>Outcome and next steps</u>

62. We will continue to consider the evidence on taxation of residential property, including non-primary residences. This includes engaging with local authorities to understand their experience of the impact of LTT in their particular areas. As indicated earlier, these considerations around local impact has been given increased focus, as the issue of second home ownership has increased in profile over the last year (including a debate in the Senedd on the impact of second home ownership[10]). The Welsh Treasury, along with the WRA, has started considering some of the interactions within the legislation in relation to non-primary residences.

63. The Welsh Government will also seek to evidence the success of the reductions in the non-residential property transaction taxes, to see if the action has supported small and medium businesses as they move towards recovery following the actions necessitated by the COVID-19 pandemic. It may be difficult to identify significant changes effected by the tax changes given the size of the changes and the wider economic impacts caused by the pandemic, but the changes should support businesses looking to expand, or start-up, and also those that need to dispose of property in order to survive into the future or to close.

64. More broadly, we will consider the scope and arrangements for an independent review of the Land Transaction Tax. The review will meet a commitment in the legislation to carry out a review of LTT within six years of the bill receiving Royal Assent (i.e. by May 2023).

[10] Senedd debate on second home ownership, 23 September 2020: https://record.assembly.wales/Plenary/6566#A60408

2b. Continue to keep Landfill Disposals Tax under review

Ensure the devolved taxes are operating as intended, and consider opportunities for the taxes as levers to support wider policy objectives.

Background

65. The Landfill Disposals Act establishes and sets out the framework and operational arrangements for Landfill Disposals Tax (LDT). It was the first of the environmental taxes to be introduced in the UK as landfill tax in 1996, and was devolved to Wales in April 2018. The Welsh Revenue Authority (WRA) has been collecting and managing the tax successfully for the last three years.

66. The first LDT regulations setting the rates were made in 2018, and they have since been set annually in subsequent regulations for approval by the Senedd. To date, our LDT rates have matched the UK landfill tax rates, following a commitment to maintain consistency with the UK Government's approach to landfill tax rates for the lower and standard rate of tax in the first two years.

67. By setting rates that are consistent with UK landfill tax, public services in Wales will continue to benefit from tax revenue, while ensuring the risk of the movement of waste across borders is reduced. Furthermore, stability over rates may benefit businesses given the current economic uncertainty generated by the pandemic and the UK's departure from the European Union.

Evidence and analysis

68. LDT revenues in 2019-20 were £37 million.

69. The OBR's LDT forecasts published with the draft Budget are £28m in 2020-21, and then £33m in 2021-22. The large reduction in 2020-21 occurs due to lockdowns in response to COVID-19. This will also impact on revenues in 2021-22. Forecasts for the rest of the UK are similarly affected.

70. The uncertainties around the revenue forecasts are particularly acute in the short run as a result of COVID-19. However, the underlying model undergoes a robust quality assurance process involving the Welsh Government and the OBR, and is based on the most up to date and relevant information available at the time.

71. As we move towards our ambitious goal of a zero waste Wales, the amount of waste sent to landfill will continue to fall. Smaller revenues from landfill taxes are expected across all UK countries in future.

72. The unauthorised disposals rate is primarily aimed at deterring unauthorised waste disposal, rather than raising tax revenue. The WRA is developing its approach to using these new tax powers, to identify where they may be used most effectively to support partners across Wales in tackling unauthorised waste disposals. During this developmental phase, levels of non-compliance are not known, therefore it is not possible to quantify the level of potential revenue.

Outcome and next steps

73. The rates for 2021-22 were approved by the Senedd in February, and will increase with inflation from 1 April 2021. This continues the policy of maintaining consistency with the UK Government's approach to landfill tax rates (see table ten).

Table ten: LDT rates (rate per tonne) 2018-19 to 2021-22

Rate	**2018-19**	**2019-20**	**2020-21**	**2021-22**
Standard	£88.95	£91.35	£94.15	£96.70
Lower	£2.80	£2.90	£3	£3.10
Unauthorised	£133.45	£137.00	£141.20	£145.05

74. Looking ahead, we will be considering the scope and arrangements for an independent review of LDT. The Review will meet a commitment to carry out a review of the tax within six years of the legislation being agreed (i.e. by September 2023).

3. Progress a Vacant Land Tax

Continue to seek powers for a Vacant Land Tax, to allow the Welsh Government to consider tax options to support the policy objective of bringing idle land back into productive use.

Background

75. As announced in 2018, the Welsh Government is seeking new tax powers for a potential Vacant Land Tax. This would support the policy objective of bringing idle land back into productive use, including land which already has permissions associated with it or is within the local development plan, but is not currently being developed. In pursuing these new tax powers, we are both aiming to acquire powers which could provide an additional lever with which to achieve our housing and regeneration ambitions for Wales, and testing the Wales Act mechanism by which new tax powers can be devolved.

76. In March 2020, following agreement at a Joint Exchequer Committee that Welsh Government proposals for a Vacant Land Tax were sufficiently developed to move to the next stage of the process, the Welsh Government submitted a formal request to the UK Government for devolution of the legislative competence in this area. This formal request was in keeping with the process agreed between UK and Welsh Ministers for the devolution of new tax powers to Wales, as provided by the Wales Act 2014. On the 19 August 2020, the Financial Secretary to the Treasury responded that yet more detail would be required from Welsh Government before the formal request could be taken forward.

Evidence and Analysis

77. In 2019, the Welsh Government commissioned research into stalled sites in Wales to help inform the policy development and design of a potential vacant land tax. The specification for this research was produced by a cross-policy team, including the Welsh Treasury, and the departments leading on planning, housing, regeneration, the economy and local government, as well as the Welsh Revenue Authority (WRA). We have also worked with external stakeholders, including house builders, commercial developers, landowners, planning authorities, surveyors, housing associations and the third sector.

78. Arcadis Consulting (UK) Limited was appointed by the Welsh Government to undertake this research, which builds upon previous work looking at stalled development sites in Wales, and looks more broadly at the extent and nature of stalled sites in their entirety. The purpose of the research is to establish a robust evidence base which can be used as part of ongoing discussions around a Vacant Land Tax in Wales, considering taxation as a policy lever to bring forward development to support housing need and regeneration.[11]

79. Once competence for a Vacant Land Tax has been devolved, we will take forward a significant programme of work to develop the detailed policy, engage with businesses and the wider public, as well as issuing a formal public consultation.

[11] *Research into stalled sites in Wales* final report, Arcadis, March 2020: https://gov.wales/sites/default/files/publications/2020-03/stalled-sites-research.pdf

Outcome and next steps

80. The Welsh Government's experience of moving through the agreed process to seek new tax powers has been protracted and challenging. It has become apparent there are serious flaws in the agreed process for devolution of further tax competence, and it is difficult to envision a scenario whereby the Welsh Government could successfully make the case for further tax competence under existing arrangements.

81. While we will continue to seek powers for a Vacant Land Tax, we will also make the case to the UK Government for the urgent review and reform of the process for agreeing the devolution of new tax powers.

4. Identify options for paying for social care in the future

Consider how taxation may be used to pay for social care in Wales. This includes developing an understanding of the collection, administration, distribution and implementation considerations associated with any proposals.

Background

82. The Paying for Social Care Inter-Ministerial Group (IMG) was set up to consider how we respond to the increasing need and cost for social care. The IMG has focused on considering the possibility of raising additional funding for a social care 'promise' in the context of Professor Holtham's proposal[12] for a hypothecated levy to create a social care fund.

83. As set out in the 2019 Tax Policy Report[13], the IMG has framed its approach to exploring options within the context of the commitment to person-centred services and prevention established by the Social Services and Well-being (Wales) Act 2014, and continued with the Welsh Government's long-term plan for health and social care, A Healthier Wales, and the vision for a seamless service for citizens.

84. On 4 February 2020, the Minister for Health and Social Services, provided an update on the work of the IMG[14] including planned work for 2020. A key element of this work was to undertake a 'listening period' of engagement designed to start a national conversation about social care and the challenges the sector faces, especially related to paying for social care. It would also reflect learning from the work already undertaken to promote a positive case for taxation in Wales.

85. Due to the COVID-19 pandemic, the listening period was cancelled, as many stakeholders who the Welsh Government wanted to engage with on these challenging issues were heavily involved in the front-line response to the pandemic. However, while the COVID-19 pandemic has inevitably had an impact, progress has been made in other aspects of the IMG's work. This includes: developing knowledge, gathering and analysing evidence to understand how any funds could be raised to support a social care promise, and the cost of potential options for a social care promise.

Evidence and Analysis

86. In considering how a social care promise could be funded the IMG has drawn on the four key principles set out in Professor Holtham's independent report. These principles are:
    - Exploring the importance of hypothecation in the context of public acceptability for any new proposal;
    - The importance of inter-generational fairness and progressivity;
    - Whether benefits should be linked to financial contributions; and

[12] *Paying for Social Care*, Professor Holtham Independent Report, June 2018:
https://gov.wales/paying-social-care
[13] Welsh Tax Policy Report 2019:
https://gov.wales/welsh-tax-policy-report-2019
[14] Update to the Senedd on the work of the IMG, by the Minister for Health and Social Services, 4 February 2020:
https://record.assembly.wales/Plenary/6079#A56122

- Whether the approach to generating resources should be in the mould of traditional 'pay-as-you-go' to meet immediate costs or based on a 'funded' approach so at least some of the resources generated would be invested to meet future care costs.

87. In addition, the IMG has considered international examples and drawn on the knowledge and expertise within the Welsh Revenue Authority (WRA).

88. In the context of the principles set out above, the IMG has considered:

- The *funding requirement* on an annual and recurring basis;
- The value of *hypothecation* compared with retaining flexibility for future needs;
- The *contributory principle* (the idea that the benefit would only be available based on a contribution, such as through an insurance-type scheme, rather than from general taxation);
- Opportunities to address *inter-generational fairness* by varying tax rates by age;
- The importance of *progressivity for the whole programme* – balancing a progressive tax with a promise that may include a less progressive component, such as a more generous charging regime;
- *Collection and administration considerations and* costs – more bespoke and complex revenue options are likely to increase the costs of administration;
- The appetite of the UK Government for further tax devolution based on current lack of progress for devolving powers for a straightforward Vacant Land Tax; and
- Explored the possibility and potential effectiveness and limitations of how a Welsh tax would work in practise if introduced without a UK wide solution.

89. In exploring the issue of inter-generational fairness, independent legal advice on the merits of an age related component to an income tax has been obtained and informed further thinking. In addition, separate legal advice on the parameters for establishing and operating an investment fund in Wales, such as that suggested by Professor Holtham is currently being procured.

90. Further, tax design expertise has been provided by the WRA to understand the practical considerations and implications related to collection, data, administration, distribution and implementation of a new tax. This is integral to developing knowledge and capability in designing new tax related ideas. The WRA has played an important role in helping to assess ideas from a practical implementation prospective.

91. The IMG has emphasised the importance of ensuring any funding model or solution, where this comprises a tax related option, must be progressive and fair to taxpayers and transparent as to how any additional revenue raised is spent.

<u>Outcome and next steps</u>

92. The spread of COVID-19, and the actions to contain it, have led to a sharp increase in government borrowing and debt[15]. The outlook for economic activity and the public

[15] The Office for National Statistics estimated that UK Public sector net borrowing is estimated to have been £8.8 billion in January 2021, £18.4 billion more than in January 2020, which is both the highest January borrowing since monthly records began in 1993 and the first January deficit for 10 years. Public sector net debt rose by £316.4 billion over the first 10 months of this financial year to reach £2,114.6 billion at the end of January 2021, or around 97.9% of GDP; maintaining a level not seen since the early sixties.

sector finances in Wales, and other countries, remains highly uncertain. With the progressively challenging and uncertain fiscal environment, a UK wide solution to funding social care has become increasingly more favourable, but it remains highly uncertain what will happen in the future. However, the Office for Budget Responsibility's most recent Fiscal Sustainability Report concluded that "in almost any conceivable world there would be a need, at some point, to raise tax revenues and/or reduce spending (as a share of national income) to put the public finances on a sustainable path".[16]

93. Any decision about whether, how and when to use tax policy levers in Wales would need to consider:
    - The possibility of the UK Government implementing other fiscal measures that would have an impact in Wales; and
    - The need to support economic recovery in Wales to generate the tax revenues to pay for Welsh public services. Independent organisations such as the Organisation for Economic Cooperation and Development (OECD) have warned of the dangers of tightening fiscal policy too early and hampering the economic recovery from the COVID-19 crisis.

94. The potential likely fall in tax revenue from the sharp reduction in economic activity means that additional tax revenue may be needed to support existing public spending. Raising extra tax to support further improvements or new investments, in that context, may be challenging.

95. The IMG has focused on building consensus around this agenda and the fundamental challenges within the sector by providing a series of statements to the Senedd, as well as some specific technical briefings on the work of the IMG to the Health, Social Care and Sport Committee, the Equality, Local Government and Communities Committee, and the Finance Committee, in November 2020. The purpose of these technical briefings was to share knowledge developed of the scale of the challenges of paying for social care and to inform thinking of how to respond to this challenge across the Senedd.

96. With this Senedd term drawing to a close, the programme of work will provide future governments with useful analysis and policy development for support with the on-going funding pressures within the social care sector.

https://www.ons.gov.uk/economy/governmentpublicsectorandtaxes/publicsectorfinance/bulletins/publicsectorfinances/january2021

[16] *Fiscal Sustainability Report*, Office for Budget Responsibility, July 2020, page 18: https://obr.uk/fsr/fiscal-sustainability-report-july-2020/

5. Consider the case for developing new environmental taxes for Wales, working where appropriate with the UK Government

Continue to work with the UK Government on the development and implementation of a UK wide Plastic Packaging Tax, and develop an evidence base to better understand the impact of other environmental related taxes.

Background

Plastic packaging

97. The Welsh Government is continuing to engage with the UK Government in examining the options for tackling unnecessary plastic use and waste, recognising the advantages of adopting a consistent approach across the UK. This has included supporting consultations on a UK plastic packaging tax, extended producer responsibility (EPR) for packaging, and a deposit return scheme (DRS) for drinks containers.

98. The UK Government announced a further consultation on the detailed design of the plastic packaging tax as part the UK Budget in March 2020, and the summary of findings was published in November 2020, alongside the draft primary legislation for technical consultation. The technical consultation closed in January 2021.

Single-use plastic cups

99. The Welsh Government has committed to exploring the potential for a tax or charge on single-use plastic cups. The Welsh Government's 'Beyond Recycling' consultation, which closed in April 2020, sought views on proposals for a tax or charge on single-use plastic cups and food containers in Wales. A summary of responses was published in September 2020 (see paragraph 107, below).

100. The Welsh Government has been working with the UK Government to secure new powers for Welsh Ministers under the UK Environment Bill, including the power to set charges on single-use plastic products, which could be used in relation to single-use plastic cups made wholly or partly of plastic.

Aggregates Levy

101. The UK Government concluded its review of the UK Aggregates Levy (UKAL), and a summary of findings was published in July 2020 (see paragraph 108, below).

102. As part of the review findings, the UK Government confirmed its commitment to keep devolution of UKAL to Wales under review, citing cross-border impacts as a particular concern.

Evidence and analysis

Plastic packaging

103. The Welsh Government has been facilitating engagement with key stakeholders in Wales in relation to the recent UK Government consultations. In May 2020, Welsh stakeholders were encouraged to attend an information sharing event on the plastic

packaging tax, led by the UK Government. In August, the Welsh Government, alongside WRAP Cymru and the UK Government, led an engagement event specifically for Welsh stakeholders in the plastic packaging industry. Throughout 2020, opportunities were taken to engage with local authorities and the food and drink industry in Wales on the EPR measures.

Single-use plastic cups

104. The Welsh Government is currently building an evidence base to assess the merits of introducing a Welsh tax or charge on single-use plastic cups. Data on single-use cup usage is poor, however, it is estimated that approximately 2.5 billion single-use coffee cups are used in the UK each year[17], although some estimates suggest the figure could now be nearer 5 billion[18], and as high as 10 billion when all single-use cups are included. Assuming 5 billion single-use coffee cups are used in the UK each year, it is estimated that approximately 237 million could be used in Wales[19].

105. Another factor to take into account is the growth in reusable cups. Research estimates suggest that 44% of Welsh consumers used a reusable cup at least once during 2020, with estimates that growth in reusable cups was up to 8% across the board to the end of 2019[20].

106. Voluntary recycling schemes have been positive in helping to support the market, however, they will only go so far, with current schemes likely to cover only a proportion of the market.

107. The 'Beyond Recycling' consultation summary report summarises the views of 200 written responses as well as around 800 additional responses from those who contributed their thoughts at engagement events. Of the small portion of responses which directly discussed taxes or charges on single-use cups, some were in favour, some were against, and some were interested in receiving further information. More specifically, responses expressed interest in how best to make use of our fiscal powers to support the transition to a circular economy[21]. For example, responses discussed the benefits of taxes or charges on single-use plastics, such as carrier bags or cups/cutlery, but also highlighted the importance of supplementing taxes or charges with initiatives that encourage the re-use of materials and products, rather than switching from one single-use resource to another.

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[17] 'Where will your coffee cup end up? Not in the recycling': https://conversation.which.co.uk/food-drink/recycling-disposable-coffee-cups-starbucks/

[18] Disposable Packaging: Coffee Cups and Plastic Bottles inquiry, Environmental Audit Committee. Written evidence submitted by Eunomia: http://data.parliament.uk/WrittenEvidence/CommitteeEvidence.svc/EvidenceDocument/Environmental%20Audit/Packaging/written/70645.html

[19] Options for extended producer responsibility: food and drink packaging waste, research report by Eunomia: https://gov.wales/options-extended-producer-responsibility-food-and-drink-packaging-waste

[20] 'Review of the Welsh Out-of-home coffee market', by Brookdale and Category-Insight Consulting, January 2021: https://gov.wales/review-of-the-welsh-out-of-home-coffee-market

[21] Responses to the 'Beyond Recycling' consultation, September 2020: https://gov.wales/sites/default/files/consultations/2020-09/beyond-recycling-summary-of-responses_1.pdf

Aggregates Levy

108. During the Review of the aggregates levy[22], several stakeholders expressed concerns about the implications of there being different levies on aggregates in Scotland and the rest of the UK in the future, and about potential devolution to Wales.

109. Stakeholders referred to existing issues around compliance and competition which businesses in Northern Ireland face because of the border with the Republic of Ireland. Those stakeholders who expressed a view were consistent in their desire for the structure of UKAL and the Scottish levy on aggregates to remain closely aligned, calling for maximum consistency of the design and rate of the taxes following devolution.

Outcome and next steps

Plastic packaging

110. In recognition of the response from Welsh industry that any tax policy interventions be consistently applied across the UK, it will be important to maintain a collaborative approach across governments. The Welsh Government will continue to work with the UK Government on the implementation arrangements for the plastic packaging tax.

111. An industry working group for the plastic packaging tax has been established, with representation from trade organisations across a range of sectors and with business interests across the UK nations. The group is considering the details of the tax, in particular in areas highlighted by the summary of responses to the policy design consultation.

112. Following its consultation on the primary legislation for the tax, the UK Government will introduce legislation in a future Finance Bill. This will be followed by publication of the secondary legislation and guidance giving more detail, which will be essential for businesses to prepare properly for the introduction of the tax, and to meet the new requirements from April 2022.

113. Further consultations on EPR and DRS are expected in the spring 2021.

Single-use plastic cups

114. Given the lack of data on single-use cups, better evidence is needed on single-use cups placed on the market (POM) and recycled in Wales. We are working with the UK Government to gather more evidence from industry on single-use cups, including POM data, market trends and recycling rates across the UK.

115. Within the proposed EPR schemes for packaging, waste producers of commonly littered packaging, such as fast food packaging and single-use cups, will be made responsible for the costs of end of life management of these products. This will place a strong incentive on these producers to prevent littering. In addition, sellers of drinks in single-use cups will be required to provide in-store takeback of single-use cups and ensure they are recycled. In the longer term, targets will be set and this will help

[22] UK Government Review of the Aggregates Levy: https://www.gov.uk/government/publications/review-of-the-aggregates-levy

facilitate increased 'on the go' recycling of single-use cups, in places such as transport hubs.

116. Given the environmental impact of single-use cup production and disposal upon the environment, there is a case for looking at prevention measures to help reduce their use more rapidly at a consumer level, through imposing a charge or tax at point of purchase, and to help encourage the use of less environmentally damaging alternatives, such as reusable cups.

117. There are a number of options available for pursuing Welsh taxes or charges on single-use plastic cups. For new Welsh taxes to be introduced, the mechanism available is provided for by the Wales Act 2014 (noting the current issues with the process and need for its review and reform). For charges, the UK Environment Bill provisions for charges on single-use plastic items are being explored. Both options are running on different timescales and require further consideration of a number of factors including any assessment of potential impact and unintended consequences. The Welsh Government will continue to work closely with the UK Government on the development of both processes.

118. The 'Beyond Recycling' strategy was published in February 2021[23]. It sets out a position on single-use cups to develop options for a tax or charge on single-use plastic cups and food containers in Wales. The Strategy also sets out action to remove unnecessary single-use items from events and other showcase activities in Wales. In the first instance, this will involve engaging on banning single-use cups from many stadia in Wales.

119. Any potential tax or charge measure on single-use drinks cups would need to be carefully coordinated with the respective initiatives for EPR, DRS, and bans on specific single-use plastic items. It will also be important that any potential social and economic impacts are considered and factored into policy design to ensure a proportionate impact across different social groups. Central to the approach we take in Wales will be to ensure the right steps are taken to build on Wales' world leading waste agenda.

Aggregates Levy

120. As part of the next steps, the UK Government has confirmed plans to conduct further consultation and engagement on the issues raised during the review, as well as committed to explore new ways of collecting data. The Welsh Government will continue to work with the UK Government on future consultation and engagement exercises, and help galvanise input from Welsh stakeholders.

121. The Welsh Government will also continue to work with the Scottish Government, as it progresses work to devolve the levy to better understand the potential implications of devolution. This will be done alongside a review of the aggregates market and flow in Wales.

[23] 'Beyond Recycling' strategy, published February 2021:
https://gov.wales/beyond-recycling

6. Examine the case for enabling local authorities to introduce a Tourism Tax

Continue to gather evidence and to discuss and assess with a range of stakeholders and experts whether there is a case for providing permissive powers to local authorities to implement a tourism tax (this would not be for this Senedd term). This will include consideration of the ongoing implications of COVID-19 on the tourism industry.

<u>Background</u>

122. Tourism taxes can take many forms but one of the most common is a tax on overnight accommodation. We have monitored tourism tax developments in the UK and internationally since 2018, and previously intended to publish a call for evidence on a tourism tax in 2020. However, this work was paused in spring 2020 in light of the uncertainty and continued impact of COVID-19 on hospitality.

<u>Evidence and analysis</u>

123. We continue to monitor progress and consider examples, both internationally and within the UK, of how tourism taxes work in practice. It will be important to continue to do this in 2021 as we consider what the implications of COVID-19 might be on tourism taxes internationally, as the industry seeks to recover from the impact of the pandemic. A number of policy issues require further exploration and consideration, including Value Added Tax (VAT) rates on tourist accommodation, particularly now that the UK has exited the EU, and how local tourism taxes would intersect with other key policy areas such as local taxes and existing regulatory pressures, and the potential need for statutory registration.

<u>Outcome and next steps</u>

124. Work exploring the potential for a Tourism Tax in Wales was paused in 2020, due to the impact of COVID-19. The Welsh Government is in the early stages of resuming this work, initially focusing on consideration of the revenue raising potential, with a view to enabling the next Welsh Government to take this forward if it wished. This work will continue within the context of the need to support the tourism, hospitality and events sector during the recovery.

7. Complete the published programme of short and medium-term improvements to the local taxes

The update on Reforming Local Government Finance in Wales, published in November 2019, sets out the actions to be taken over the next year [2020] to complete the work to improve council tax and non-domestic rates in line with the commitments in our Programme for Government.

Background

125. In our 2016 programme for government, we committed to making council tax fairer, and providing support to small businesses, as well as supporting the future sustainability of local government. We subsequently embarked upon a phased programme of action. Many of the improvements identified for shorter and medium-term delivery have since been achieved as a result of significant effort and collaboration between local government, the Welsh Government, the Welsh Local Government Association and a range of other organisations.

126. Further detail about the agreed programme of work and our accomplishments to date have been reported on an annual basis since 2017[24]. More recently, the Welsh Government has outlined the possibilities for longer term reform, summarising the findings from the programme of work completed over this Senedd term to inform the debate ahead of the next Senedd term.

Outcome and next steps

Council Tax

127. Our achievements over the course of this Senedd term include exempting young care leavers from council tax until the age of 25, removing the sanction of imprisonment for the non-payment of council tax, improving access to discounts for people with severe mental impairments, implementing a citizen-focused protocol for managing council tax collection and arrears, and encouraging take-up of our Council Tax Reduction Scheme and other council tax support.

128. We have continued to deliver our Council Tax Reduction Scheme (CTRS) to help people make ends meet. Each year, we have given £244m to local authorities to fund council tax reductions under the scheme. This has resulted in annual council tax bills being reduced for around 280,000 households. Most of these households – around 220,000 – pay no council tax at all[25].

129. The CTRS has been a priority for this government, both in terms of ensuring it supports vulnerable and low-income households in the fairest way possible, and in terms of extending its reach. This is one reason why we commissioned detailed research by Policy in Practice, in January 2019, to shed light on the impact of Universal Credit on our national council tax support scheme, council tax debt, and rent arrears in Wales.

[24] Reforming local government finance: annual updates: https://gov.wales/reforming-local-government-finance-annual-updates
[25] Council Tax Reduction Scheme: annual reports: https://gov.wales/council-tax-reduction-scheme-annual-reports

A final report was published in July 2020[26], and we will now need to reflect carefully on whether a more fundamental rethink of the scheme is required to mitigate the impact of welfare reform.

130. We have also provided additional financial support to local authorities to cover an increase in CTRS caseload as a result of COVID-19. Since the beginning of the pandemic, we have provided an additional £10.9m to local authorities to support those who have sought assistance as a result of the financial impact on household incomes. We will continue to monitor take-up of CTRS in the face of a global pandemic, and are committed to responding where appropriate.

131. We have also extended the flexibilities available to local authorities in relation to council tax. From 1 April 2017, councils have been able to apply a council tax premium of up to 100% on long-term empty homes (unfurnished and empty for over 12 months) and second homes (dwellings which are not a person's sole or main home and which are substantially furnished). Certain properties are excepted from the premiums. These are discretionary powers and it is up to each local authority to decide whether to apply any premium, and at what level. The powers were introduced in response to calls from some local authorities. They form part of a package of tools to help authorities tackle issues affecting local housing supply: they were not introduced as a revenue-raising measure.

Non-domestic rates

132. On non-domestic rates, we have invested significant sums of public money in targeted relief for small businesses, high streets, hospitality and childcare premises; we have implemented a revaluation exercise to maintain the integrity of the tax base, including transitional protection; and we are putting in train measures to tackle non-domestic rates avoidance.

133. We are currently providing over £230m of non-domestic rates relief to businesses and other ratepayers through our range of permanent relief schemes which, as well as Small Business Rates Relief, include Charitable Relief and Empty Property Relief. Since 2017-18, we have also provided additional relief for retailers and businesses on the high street. We have allocated an additional £350m of funding for 2020-21 to provide 100% rates relief for all retail, leisure and hospitality businesses with a rateable value of £500,000 or less, ensuring these sectors received additional support in these difficult times.

134. In total, the Welsh Government is providing over £580m of reliefs to ratepayers in Wales this year. The rates relief schemes provided by the Welsh Government result in three-quarters of all ratepayers across Wales receiving rates relief, and more than 70,000 businesses will pay no rates at all.

135. For 2021-22, we are also freezing the non-domestic rates multiplier, ensuring that, prior to applying reliefs, no ratepayers will see an increase in their rates bills. We continue to examine options for further support in the next tax year.

[26] Universal Credit, Council Tax Reduction scheme and rent arrears in Wales: https://gov.wales/universal-credit-council-tax-reduction-scheme-and-rent-arrears-wales-0

Longer term reform

136. We have achieved all of the above within the constraints of our existing systems and frameworks, but we recognise there are other ideas to consider. We have therefore explored whether more fundamental reform of the system is possible over the longer term. We want to make local taxes more progressive and more aligned to our wider policy ambitions, while maintaining vital revenue for local services. Where possible, we want to use all the levers available to us to tackle poverty and share wealth.

137. With these aims in mind, we commissioned a range of in-depth research to inform our thinking and published a summary of this work in February 2021. We also held our first Local Taxes Conference on the research in November 2020. This proved a successful engagement exercise with many of our key stakeholders in attendance, and allowed us to gather further insights into perceptions and future possibilities.

138. *Reforming Local Government Finance: Summary of Findings*[27] focusses on the future of local taxes – council tax and non-domestic rates – beyond the current Senedd term. It reflects on research studies conducted by the Institute for Fiscal Studies and Sheffield University about council tax revaluation in Wales, and the possibilities this may offer to make the system more progressive; on Bangor University's initial assessment of whether a local land value tax could replace council tax or non-domestic rates; and on the work of Jennie Bunt from Cardiff University, who explored whether local taxes could be based on assessments of income. Brought together, our suite of research provides important analysis and helpfully outlines the further work that would be required were the Government to decide to take forward more radical reform.

139. Overall, we continue to recognise vital local services like education and social care rely on a fair funding system that is fit-for-purpose as services evolve. We are using every lever we have to make Wales a more equal, prosperous and green society. Local government must be enabled to go on delivering better public services for everyone, to provide the best foundation in early life, to help those who need it most, and to tackle poverty by creating a thriving economy which benefits everyone fairly.

[27] Reforming Local Government Finance: Summary of Findings: https://gov.wales/reforming-local-government-finance-wales-summary-findings

B. Operate and develop Welsh taxes within a UK context

8. Examine how the Welsh Government could respond if there is a need to make changes to the Welsh Tax Acts

Consider the responses to the consultation: 'Tax Devolution in Wales: Enabling changes to the Welsh Tax Acts' which explores a range of scenarios for the two fully-devolved taxes, Land Transaction Tax and Landfill Disposals Tax, including the impact of adjustments to the block grant as a result of measures introduced by the UK Budget to the UK predecessor taxes (stamp duty land tax and landfill tax).

<u>Background</u>

140. The ability to ensure Welsh Ministers can make changes, subject to Senedd approval, to the 'Welsh Tax Acts' at short notice is considered necessary in number of circumstances:
    i. To stop avoidance or evasion of the devolved Welsh taxes;
    ii. To comply with international obligations;
    iii. In situations of exceptional need, such as in response to a tribunal or higher courts decision, or in response to national emergencies such as COVID-19; and
    iv. In specific circumstances where Welsh Ministers consider it expedient in the public interest to do so. In particular, in response to tax policy changes made by the UK Government to 'predecessor' taxes (that is, one where we have an equivalent devolved tax).

141. It is important to protect the tax revenues that fund our essential public services. At the moment, every time there is a UK budget cycle there is a risk that there may be a change which impacts on a devolved tax. Such changes could have implications for businesses, the property market and a direct budgetary impact on resources. This may now be more likely, as recovery measures start to be implemented. For example, immediate changes to SDLT which result in an increase to UK Government tax revenues will increase the block grant adjustment and reduce the Welsh Government's resources. In this scenario, the Welsh Government would either need to operate with a reduced budget or find alternative ways of raising such revenues to maintain existing resource levels.

142. Conversely, where the UK Government makes changes which reduce UK tax revenues from SDLT, the block grant adjustment will decrease and the Welsh Government's budget will increase. In these types of scenarios when tax reductions are made to UK predecessor taxes there may be a need to act quickly to reduce potentially undesirable distortions to markets which could harm businesses in Wales.

<u>Evidence and Analysis</u>

143. A review of the issues that may impact on the Welsh Government, taxpayers and businesses led to the development of proposals to provide the Welsh Ministers with new powers to enable changes to the Welsh Tax Acts in specific circumstances. Following informal engagement events, a Welsh Government consultation: *'Tax Devolution in Wales – Enabling changes to the Welsh Tax Acts'*[28] was published on 16

[28] *Enabling changes to the Welsh Tax Acts* consultation: https://gov.wales/enabling-changes-to-welsh-tax-legislation

July 2020 and closed on 15 October. A number of virtual engagement events were held with key stakeholders. The consultation sought views on the conferring of regulation making powers on the Welsh Ministers to ensure they could make changes, subject to Senedd approval, to the Welsh Tax Acts at short notice in a number of circumstances.

144. A summary of consultation responses[29] was published on 21 December 2020. The consultation responses were, broadly, supportive of the Welsh Government's proposals as set out in the consultation document.

Outcome and next steps

145. Following the outcome of the consultation, policy and legal instructions have been developed that incorporate key reflections from a small number of professional representative bodies. Work will now commence on drafting legislation, and it is intended a bill will be ready to introduce early in the next Senedd term, should the next Welsh Government choose to introduce a bill.

[29] *Enabling changes to the Welsh Tax Acts* consultation – summary of responses: https://gov.wales/sites/default/files/consultations/2020-12/enabling-changes-to-the-welsh-tax-acts-summary-of-response.pdf

9. Develop a more strategic approach to the ways taxes operate in Wales

Engage with partners to co-produce a collective agreement about the expectations for how existing and future taxes should operate from the perspective of people and businesses.

Background

146. The Tax Policy Framework[30], published in 2017, provides the wider strategic context and vision for taxes in Wales. This Framework recognises that fiscal devolution provides for new areas of work and therefore, new opportunities to develop and strengthen direct engagement and relationships with citizens, businesses, partners and other stakeholders. In the area of tax administration and implementation, the initial focus has centred on considering and testing with partners the case for developing a more strategic approach to the way taxes operate in Wales.

Evidence and Analysis

147. The three nationally collected Welsh taxes – Welsh Rates of Income Tax (WRIT), Land Transaction Tax (LTT), and Landfill Disposals Tax (LDT) – together with the two locally collected taxes – council tax and non-domestic rates – provide the basis for considering whether and how to bring a coherent, whole-systems approach to underpin the different administrative arrangements governing the implementation of these taxes. However, the landscape is complex – WRIT is collected and administered by HMRC, LTT and LDT by the Welsh Revenue Authority (WRA), and the locally-collected taxes are the responsibility of the 22 local authorities in Wales.

148. Each of the different tax authorities and the individual taxes bring with them different structures, processes, requirements and, therefore, ways of operating. Added to this mix is the relationship with the administration of UK reserved taxes and benefits. Looking to the future, there are other taxes which could potentially be devolved to Wales, and any new Welsh taxes which could be implemented in the future.

149. We began identifying and exploring some of these issues with partners prior to the COVID-19 pandemic, although focus then shifted to more immediate priorities, including the need to establish and administer essential financial support to citizens and businesses. Our initial engagement indicated that – given the interdependencies and challenges of navigating, governing and administering what is becoming an increasingly complicated landscape for taxpayers, tax authorities, and tax policymakers – it is important to better understand this landscape in order to determine where tangible outcomes can be sought to deliver efficiencies, greater clarity and improvements for all. Our ability to deliver efficiencies and simplification will also depend on our future policy ambitions, and the choices we make about how these are reflected in tax policy.

150. The response to the COVID-19 pandemic necessitated action and administration at a pace and level rarely seen outside of wartime. This together with how society in general and the wider economy has moved to greater digitalisation has highlighted the ability

[30] Tax Policy Framework:
https://gov.wales/tax-policy-framework

on the part of governments to mobilise and drive forward reform. This has seen the UK Government step-up its 'Making Tax Digital' programme, with publication of its 10 year strategy to fully modernise tax administration in the UK in July 2020[31]. The OECD's Forum on Tax Administration[32] provides another avenue through which to gain knowledge of how different tax administrations around the world are also taking account of both the challenges and opportunities presented by the pandemic to establish new models of tax implementation and management.

151. Delivering quality services for both tax administrators and taxpayers requires a good understanding of the range of issues and challenges which taxpayers and citizens – particularly vulnerable groups with limited knowledge and experience of different taxes – face when interacting with tax authorities and systems. Here our work with our partners and stakeholders, including the Wales Council for Voluntary Action (WCVA) and the Low Income Tax Reform Group (LITRG), is fundamental as we continue to consider and identify opportunities to ensure citizens' voices are brought to bear on this work.

Outcome and next steps

152. As is evident from the above, there is significant activity underway in the area of tax administration and implementation. It is important that we take account of this work, engaging appropriately with our partners and stakeholders, taking every opportunity to learn from good practice within Wales, and international practice to shape the development of a strategic approach to tax administration in Wales.

153. Tax administrations and systems develop differently, shaped by different governing and legislative structures, policy ambitions, as well as history and culture. Standardisation of implementation processes across all of the different taxes is unlikely to be practical or even desirable, as the different taxes exist for different purposes and to achieve different outcomes. However, we will continue to build on our experiences of operating taxes in Wales, taking the opportunity to collectively establish common principles to underpin quality tax administration and implementation practice in Wales.

[31] *Building a trusted, modern tax administration system*, UK Government, July 2020: https://www.gov.uk/government/publications/tax-administration-strategy/building-a-trusted-modern-tax-administration-system#our-10-year-strategy
[32] OECD Forum on Tax Administration: https://www.oecd.org/tax/forum-on-tax-administration/

10. Assess the case for further tax devolution to Wales

As the conditions and implications of both the UK's departure from the EU and COVID-19 become clearer, identify new and existing UK taxes which should be considered for devolution to Wales, and make the case to the UK Government.

Background

154. Taxation can be a powerful lever for influencing behaviour change, as well as generating revenue to support public spending to meet the needs of Wales, and enabling the Welsh Government to develop more progressive taxes. Earlier sections have commented on a Vacant Land Tax, and noted the challenges encountered with navigating the agreed process between the UK Government and the Welsh Government for the devolution legislative competence for new taxes. The failure of this mechanism significantly impacts the ability of this government and future governments to undertake further tax devolution to Wales, and we will make the case to the UK Government for the urgent review and reform of the process.

155. The catastrophic impact of COVID-19 on the aviation industry makes more urgent our continuing call to the UK Government for the devolution of Air Passenger Duty (APD) to Wales.

Evidence and Analysis

156. In November 2017, the Welsh Government published the findings of research by Northpoint Consultants into the potential market, competition and economic implications of devolving APD to Wales.

157. While the UK Government has stated it "*remains concerned about the competitive impact of introducing tax competition within a single aviation market. We consider Cardiff and Bristol airports to serve the same market*." The peer-reviewed analysis showed Cardiff and Bristol airports operate in largely distinct catchment areas. In its final report, after carefully considering the evidence, the Welsh Affairs Committee concluded: *"We understand the arguments made by Bristol Airport, but as it is already a strong performer with far more passengers than Cardiff Airport, we are not persuaded that its successful business would suffer significant and lasting damage, even if APD were abolished entirely*."

158. There is unanimous support for the devolution of APD to Wales from aviation, tourism and business sectors in Wales, and compelling evidence for the economic benefits it could bring, enabling growth in the aviation sector and wider economy.

Outcome and next steps

159. We will make the case to the UK Government for urgent review and reform of the process to devolve further tax competence to Wales.

160. The UK Government remains unwilling to accept the mounting evidence that APD should be devolved to Wales. We will continue to raise this issue with UK Ministers, and to press the UK Government to review its untenable position. Furthermore, we continue to build the evidence base on the benefits devolution of APD would bring to Wales, for example enabling growth in the aviation sector and wider economy.

C. Increase knowledge and understanding about taxes in Wales

11. Examine how potential changes to Welsh Rates of Income Tax could impact on Welsh taxpayers

Examine the financial impacts on income tax payers of increases and decreases in Welsh Rates of Income Tax, according to their income, gender, age group, industry, and where they live in Wales.

Background

161. The Welsh Government has produced two extensive pieces of analysis on income tax, which are published in the annexes to this report – a Welsh Rates of Income Tax ready reckoner (Annex one) and an analysis of the income tax base (Annex two).

162. The ready reckoner provides estimates of the potential revenue impact from changes to each of the three Welsh Rates of Income Tax. Some of the technical work in producing these estimates builds on the evidence the Welsh Government presented to the Senedd's Finance Committee, for its inquiry into the impact of variations in national and sub-national income tax[33]. The estimates reflect work on the behavioural impacts from tax divergence within the UK, as mentioned in the Welsh Government's response to the inquiry recommendations[34].

163. The analysis of the income tax base provides insight into the structure of the income tax base in Wales relative to England and Northern Ireland. It also shows who pays WRIT by the basic, higher and additional rates according to gender, age and income. From this analysis, the impact of potential changes to WRIT can be observed.

Evidence and Analysis

164. The table below shows the ready reckoner estimates for WRIT, described in detail in Annex one. These include all of the expected behavioural effects which may have a material effect on revenues. They cover the possible impact on decisions about whether to work or not, how much to work, the extent to which individuals engage in tax planning and avoidance, where to live, and whether to incorporate.

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[33] Senedd Finance Committee inquiry into the impact of variations in national and sub-national income tax: https://business.senedd.wales/mgIssueHistoryHome.aspx?IId=26476

[34] The Welsh Government's response to the Finance Committee's inquiry into the impact of variations in national and sub-national income tax: https://senedd.wales/laid%20documents/gen-ld13468/gen-ld13468-e.pdf

Table eleven: Ready-reckoner estimates for the Welsh Rates of Income Tax (£ million)

		2021-22	2022-23
Basic rate	Current rates	1,779	1,854
	+1p	*177*	*185*
	-1p	*-177*	*-185*
Higher rate	Current rates	241	248
	+1p	*23*	*24*
	-1p	*-23*	*-24*
Additional rate	Current rates	44	49
	+1p	*3*	*3*
	-1p	*-3*	*-3*

Estimates based on OBR's Economic and Fiscal Outlook (November 2020) and Welsh Taxes Outlook (December 2020).

165. The tax base analysis in Annex two can be used to consider the potential impact of changing the Welsh Rates of Income Tax on different groups of income tax payers. It finds:

- WRIT is generally progressive with income, so proportionately more tax is paid as incomes rise. As income up to the personal allowance (currently £12,500) is not subject to WRIT, those with lower incomes do not pay the tax or only pay it on a small proportion of their income.

- Men account for a higher proportion of WRIT payers than women. The differences are bigger amongst those paying the higher and additional rates than the basic rate.

- On average, more WRIT is paid as age increases, peaking amongst 45 to 54 year olds, before steadily declining for older groups. Those aged between 35 and 54 account for nearly half of WRIT revenue, whilst making up less than a third of the 16+ population.

- Over half of Welsh taxpayers are either pensioners or public sector workers. These groups, together with production sector workers, account for higher proportions of revenues in Wales than in England and Northern Ireland.

<u>Outcome and next steps</u>

166. The Welsh Government will continue to provide analysis of the revenue impacts of the Welsh Rates of Income Tax and of the tax payer base. It will explore what further analysis can be undertaken and data sources developed.

12. Share good practice on tax strategy and policy

Work with the UK Government, the devolved administrations, and international governments and organisations, to exchange good practice, collaborate on shared challenges and promote Wales' approach to tax policy.

Background

167. Positive relationships have been developed with other treasury bodies and tax authorities in the UK, both by the Welsh Revenue Authority (WRA) and the Welsh Treasury.

168. The Welsh Government is working with the Organisation for Economic Cooperation and Development's (OECD) Network on Fiscal Relations across Levels of Government, to share good practices on the design of country policies and institutions related to strengthening fiscal capacity, delineating responsibilities across levels of government, and improving intergovernmental coordination.

Evidence and Analysis

169. Welsh Treasury officials meet regularly with tax officials from the UK Government and the other Devolved Administrations to exchange information and share good practice. This occurs formally in a twice-monthly meeting of officials, and on an ad hoc basis around specific tax and policy issues. 2020 also marked the second annual 'Working Together on Tax' workshop between officials from the four nations.

170. The Welsh Government's annual tax conference is another useful mechanism for engaging with key stakeholder groups on tax, and promoting our distinct Welsh approach to tax policy. Our third annual tax conference took place in October 2020 as a 'virtual' event.

171. Welsh Treasury officials participated in the 16th Annual Meeting of the OECD Network on Fiscal Relations Across Levels of Government, in December 2020, and the Network's Special 'Emergency' Meeting on the COVID-19 Pandemic Response.

172. Welsh Treasury officials collaborated with Demos' work on understanding the public's attitude to tax increases.[35] Demos presented its findings at the annual tax conference.

Outcome and next steps

173. Work will continue to build and enhance intergovernmental relationships further, and to continue to learn from international experiences with fiscal devolution.

[35] *A people’s budget: how the public would raise taxes*, Demos, September 2020: https://demos.co.uk/wp-content/uploads/2020/09/A-Peoples-Budget-Sept-2020-v5.pdf

13. Raise awareness and understanding of Welsh tax policy

Using a variety of methods, including social media and an annual tax conference, seek to better inform Welsh tax payers and stakeholder groups about developments in tax policy.

Background

174. The introduction of Welsh Rates of Income Tax (WRIT), in April 2019, was the final element of tax devolution brought about by the Wales Act 2014. It closed a unique period during which the Welsh Government sought to communicate information about the detail and impact of fiscal devolution in Wales.

175. The Welsh Government continues to look outwards at best practice for engaging on the subject of taxation, in particular this year drawing on insight gathered through links with the budget department of the State of Philadelphia. Devolution of taxes to Wales has broadened the Welsh budget from solely a spending event, to one which incorporates the fiscal measures supporting the spending priorities of the Welsh Government. As a result, our communications approach has expanded to explore the narrative of tax and spend as communicated through the Welsh Government's main fiscal events, in particular the draft Budget.

176. The Welsh Treasury is concentrating on producing digital communications content 'in house'. In addition to communicating policy development, proactive campaigns have been developed to produce content for Welsh Government channels which reach beyond the Welsh Treasury stakeholder base. For example, before the draft Budget in December 2019, an engagement programme was arranged to enable the Finance Minister to meet public service users. In the more challenging conditions of 2020, an awareness campaign was undertaken before the December draft budget. As part of this work, a new animation was created with the aim of reaching new audiences, communicating the role of the Finance Minister and how the Welsh Government raises and spends money in Wales.

177. Another step forward has involved sharing content created by the Welsh Treasury on other Welsh Government departmental channels, to amplify our communications about spend across different areas of the Welsh Government, extending the tax and spend narrative to illustrate its impact.

Evidence and Analysis

178. A series of case studies were identified to illustrate the impact of tax and spend in advance of the draft Budget in December 2019. Methods for communication included visual graphics and animations. Nine major areas of government spending were highlighted, and engagement with key stakeholders in these areas secured excellent performance across all government channels. The digital budget animation evidenced a 230% increase in engagement from the previous year.

179. Increased digital content was produced to publicise the draft budget in 2020. The impact of COVID-19 had cast a spotlight on devolution in Wales, and an awareness campaign ahead of the Budget sought to communicate the importance of this fiscal event for stating both tax and spend priorities. The new digital animation was the

campaign's best performing piece of content with over 2,200 and 182 media views of the English and Welsh films respectively. This has been important for targeting new audiences.

180. The twitter channels @WelshTreasury and @TrysorlysCymru continue to be significant in communicating tax policy developments to our stakeholders at zero cost. During the period between October 2019 and January 2021, @WelshTreasury followers showed an increase of 17.6% from 2,285 to 2,775, and @TrysorlysCymru showed an increase of 9.1% from 977 to 1,075. A consistent flow of new and engaging content has proved effective in capturing attention, and ensuring the material is shared across Welsh Government and departmental channels, driving the continued growth of these channels. The high ratio of Welsh to English followers reflects the emphasis placed on Welsh language communications.

181. The Welsh Treasury has been proactive in pursuing digital engagement with stakeholders, which is critical for increasing our followers. For example, the publication of the National Audit Office's report on Welsh Rates of Income Tax on their social media channels meant it reached their 133,300 followers. A similar course of action was taken with HMRC, which has 61,000 followers. The Welsh Treasury also promoted the UK Government's consultation on a plastic packaging tax, highlighting opportunities for engagement and involvement. This digital content signposting Welsh stakeholders to the UK Government's consultation achieved a high level of engagement and demonstrated excellent partnership working with UK counterparts.

182. Engaging with partners continues to be a key method for communicating developments in tax policy. The Welsh Revenue Authority (WRA), the Welsh Government's non-ministerial government department which administers Land Transaction Tax (LTT) and Landfill Disposals Tax (LDT), has drawn on its established methods for informing and engaging its customer base with changes in LTT policy during the year. These include working with professional bodies, webinars and videos, to provide technical training and the dissemination of key information quickly through customer channels. The strength of these partnerships was evidenced in the low number of calls to the customer call centre following the change to LTT policy announced during the draft budget 2020. The WRA's dedicated customer relationship managers also continue to work closely with landfill site operators, to support them in correctly interpreting and paying LDT.

183. The Tax Advisory Group, which provided strategic advice to Welsh Government Ministers on issues of tax policy and administration during the development and introduction of the Welsh taxes, was disbanded in February 2020. A Tax Engagement Group has been established in its place to continue the critical work of discussing developments in tax policy with those who can represent the views of Welsh tax payers.

184. The third annual tax conference, which took place this year as a virtual event, was attended by over 100 stakeholders. A survey sent to attendees after the event showed that 51% of the respondents thought the conference was excellent, 43% thought it was good and 6% thought it was 'as expected'. The presentations were praised by attendees as being "a good mix of specialist tax and more broad-ranging content" and that "the variety was excellent". The virtual event proved a helpful and effective way to engage with stakeholders from all parts of Wales, and other parts of the UK, and the feedback will be used to inform planning for the next virtual event.

Outcome and next steps

185. The 2019 Tax Policy Report[36] noted that an important objective for the combined communication campaign activity in 2019 was to increase awareness that the Welsh Government would be able to set different Income Tax rates from 6 April 2019. Surveys were taken in March 2019 and June 2019, and measured against the baseline survey in result in June 2018. The findings from the later surveys, published in 2020, demonstrated an increase in awareness from 24% to 38%[37]. An increase of 14% is a positive result for communications and engagement activity, and has provided a strong platform to build upon. During 2020, a range of accessible, digital content has been produced to reach wider audiences, including film, animations and a calculator for WRIT.

186. Increasing awareness among stakeholders of the process for making changes to tax policy as part of a fiscal event – the Welsh budget – is vital to increase understanding of the implications of fiscal devolution for people and businesses. In order to measure the effectiveness of our communications and engagement in achieving this, further research is due to be commissioned through Beaufort Research Ltd to understand public understanding of the Welsh budget.

187. A youth engagement project is being piloted throughout 2021, engaging Economics and Welsh Baccalaureate students in schools in Wales. This project will explore new methods for informing and involving young people on the topics of budget literacy, tax and spend. The results of the project will be analysed at the end of 2021.

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[36] Welsh Tax Policy Report 2019:
https://gov.wales/welsh-tax-policy-report-2019

[37] *Public Understanding of tax devolution: update report*, February 2020. Page 18, 'Are you aware from 6 April 2019 the Welsh Government will be able to set different Income Tax rates in Wales?':
https://gov.wales/public-understanding-tax-devolution-update-report-2020

Annex one: Welsh Rates of Income Tax Ready Reckoner

Introduction

What is it?

A1.1 The ready reckoner for the Welsh Rates of Income Tax (WRIT) is a set of estimates for the revenue impact from a 1p (or one percentage point) change to each of the Welsh rates (basic, higher and additional).

A1.2 The ready reckoner shows the effect of changes to the Welsh rates on devolved income tax revenues – those which contribute to the Welsh Government's budget. It does not include any impact on UK Government tax revenues or wider effects on the economy and other devolved or local taxes in Wales.

A1.3 The ready reckoner includes estimates for all of the expected behavioural effects which may have a material effect on revenues. These include the possible impact on decisions about whether to work or not, how much to work, whether to incorporate (so individuals would be subject to business-related income taxes), and migration.

Who has developed it?

A1.4 The WRIT ready reckoner has been developed by HMRC and the Welsh Government. This approach has taken advantage of HMRC's experience in producing costings for UK and Scottish income tax policy changes on behalf of HM Treasury for UK fiscal events and the Office for Budget Responsibility's fiscal forecasts. HMRC also has access to detailed tax data which is useful in the production of these estimates and is not available to others for confidentiality reasons.

A1.5 The Office for Budget Responsibility (OBR) has been consulted in the development of the WRIT ready reckoner. The OBR provides independent tax forecasts for the Welsh Government and its forecasts form the basis of the ready reckoner. In the event of a WRIT policy change, the OBR would be asked to scrutinise and approve the associated costing to be applied to the Welsh Government's budget. Under the legislation which established the OBR, it can only certify policy costings for stated Government policy. Its role in relation to the ready reckoner has been to review the methods used. It has deemed these to be reasonable, drawing on established models and methods wherever possible.

A1.6 The OBR also highlighted what is judged to be the key sources of uncertainty which could lead an actual policy costing to differ from the ready reckoner. In particular, it noted coronavirus-related uncertainties around the baseline forecast for revenues from the Welsh rates; data-related uncertainties pending the full outturn data for the Welsh rates in 2019-20; and behavioural uncertainties in respect to cross-border migration, particularly among additional rate taxpayers, for which evidence on which to base estimates is limited.

Estimates

A1.7 The table below shows the revenue forecasts based on the current tax rates and the ready reckoner estimates. These include behavioural effects as outlined in paragraph 3.

Table twelve: Ready-reckoner estimates for the Welsh Rates of Income Tax (£ million)

			2021-22	2022-23
Basic rate	Current rates		1,779	1,854
		+1p	*177*	*185*
		-1p	*-177*	*-185*
Higher rate	Current rates		241	248
		+1p	*23*	*24*
		-1p	*-23*	*-24*
Additional rate	Current rates		44	49
		+1p	*3*	*3*
		-1p	*-3*	*-3*

Estimates based on OBR's Economic and Fiscal Outlook (November 2020) and Welsh Taxes Outlook (December 2020).

How are the estimates produced?

A1.8 The estimates are built up in two stages. First, the static costs from changes to the rates are estimated (these exclude behavioural responses). The static estimates are based on the OBR's Economic and Fiscal Outlook from November 2020 and the Welsh Taxes Outlook from December 2020. As the WRIT rates used in these forecasts are 10p, a static cost of plus or minus 1p is just 10% of the WRIT forecast for the particular band.

A1.9 The second stage includes the expected behavioural effects. Changing tax rates is likely to affect people's behaviour, which in turn may affect the amount of tax which is subsequently generated. These behaviours include decisions around whether or not to work, how much to work and the extent to which individuals engage in tax planning and avoidance. The extent of these effects depends on the taxpayer's income, so someone with a larger income is assumed to have a relatively greater response than someone with a lower income. With the exception of migration, the behavioural effects are estimated using the assumptions HMRC and OBR employ when costing UK income tax changes. These are known as taxable income elasticities.

A1.10 The ready reckoner also includes the impact of rate changes on tax motivated incorporation. Changes to income tax rates affect the differential with corporation tax/dividend income tax rates, and therefore alter the incentives for individuals to incorporate. Changes to incorporation behaviour will have an impact on income tax revenues. HMRC models the incentive to incorporate based on UK non-devolved taxes and non-savings non-dividend income tax to provide an estimate of tax motivated incorporation which reflects Welsh individual and company populations.

A1.11 In addition to the above, the ready reckoner includes an estimate of migration behavioural effects. Some cross-border migration is expected from divergences in income tax rates between Wales and elsewhere in the UK. Estimates are only applied to changes in the additional rate. The absolute impact of changes to the basic or higher rates is more limited than the impact of changes to the additional rate, particularly on those with very high incomes. There is also a body of empirical literature which finds that those with the highest incomes are most likely to migrate as a result of income tax changes[38].

A1.12 The estimated migration effect depends on a number of factors. These include the size of the tax change, tax payers' incomes, existing migration flows between locations and the intensity of the behavioural response or elasticity. Higher income earners are able to reduce their tax liabilities by a larger amount by migrating to or from Wales, depending on the tax change. Therefore, the higher the income, the more likely a tax payer is to migrate in response to a tax change. It is also possible that those with more than one residence may be able to switch their main residence for tax purposes with relatively little disruption to their lifestyle.

A1.13 Migration flows and population estimates can be used to calculate the existing likelihood of moving into and out of Wales by location. The data show that individuals who live in communities close to the border are more likely to migrate. This may be because moving shorter distances results in minimal changes to lifestyle, social networks and work arrangements. In general, the further people live from the border, the less likely they are to migrate between Wales and other parts of the UK.

A1.14 The size of the behavioural response, or elasticity, captures to what extent the existing migration flows are expected to alter from a tax change. This is taken from the empirical literature. The central estimate is taken from a study in Switzerland[39] which reports findings on the changes to migration flows due to income tax changes. This study is based on income tax data, so will capture those with more than one residence, switching their main residence for tax purposes. However it is possible that the ease of such switching, or paper migration, in the UK is different from Switzerland.

Limitations and areas of uncertainty

A1.15 The estimates show the expected revenue impact from a 1p (or one percentage point) increase or decrease to each of the WRIT rates, independent of each other. Given the way income tax has been devolved to the Welsh Government, different rates may be altered at the same time, and perhaps in different directions and to different degrees. For example, a 1p reduction in the basic rate could be combined with a 2p rise in the additional rate. Separate estimates of the revenue impact from different combinations of rate changes have not been produced. Changes can be combined across bands and scaled up or down to provide a guide to the potential effects of larger rate changes. For example, a reduction of 2p in a tax rate is likely

[38] For a summary see Welsh Tax Policy Report 2018, Welsh Government (2018) from page 55, available from here:
https://gov.wales/sites/default/files/publications/2018-10/welsh-tax-policy-report-2018.pdf

[39] Martinez, Isabel, Beggar-Thy-Neighbour Tax Cuts: Mobility after a Local Income and Wealth Tax Reform in Switzerland (2017). Luxembourg Institute of Socio-Economic Research (LISER) Working Paper Series 2017-08, available at SSRN:
https://ssrn.com/abstract=2979275 or http://dx.doi.org/10.2139/ssrn.2979275

to cost around twice as much as a reduction of 1p. This approximation is reasonable for changes of up to a few percentage points in either direction.

A1.16 The ready reckoner makes use of the current prevailing UK tax rates. It assumes these will remain unchanged for the years which apply for the ready reckoner. Further to this, it is assumed the UK personal allowance and higher rate threshold will increase with CPI inflation and that the additional rate threshold will remain unchanged in line with the UK Government's current stated policy.

A1.17 As noted, the estimates provided here are consistent with the OBR's Economic and Fiscal Outlook November 2020 and Welsh Taxes Outlook December 2020. Those forecasts are characterised by an unusually high degree of uncertainty due to current economic circumstances. The estimates are therefore likely to change with future OBR forecasts.

A1.18 In addition, and in common with most other tax policy costings, the behavioural effects included in these estimates are considered highly uncertain. Where possible, established estimates have been used. Where new methods have been applied, as with intra-UK migration, the best available evidence and information has been utilised. However, the evidence base is limited and of uncertain relevance to Welsh circumstances.

A1.19 The ready reckoner provides a robust costing of potential WRIT changes based on current information. However, given the risks and limitations outlined above, the costing of any future WRIT changes applied to Welsh Government budgets may differ from the estimates in this document.

What other ready reckoners already exist?

A1.20 This is the first ready reckoner for the Welsh Rates of Income Tax. It adds to the existing set of ready reckoners for UK Government tax changes produced by HMRC.

A1.21 HMRC's latest ready reckoners provide estimates of the revenue effects of illustrative changes to UK Government taxes between 2021-22 and 2023-24, including each of the UK Government income tax rates.[40]

Next steps

A1.22 The Welsh Government will aim to publish updates of the ready reckoner to keep the estimates relevant. In the meantime, it will continue to work with HMRC, the OBR, the Scottish Government, and the Scottish Fiscal Commission to ensure a collaborative approach for gaining more insights into UK income tax, especially the elements which relate to the devolved revenue streams. It is hoped that this will enable better understanding of the tax base and its dynamics, which may in turn improve the estimates in the ready reckoner and future potential WRIT policy costings and forecasts. The key assumptions and judgments will also be kept under review and any new evidence which may help inform the estimates will be considered and reflected in future updates.

[40] Available from here:
https://www.gov.uk/government/statistics/direct-effects-of-illustrative-tax-changes

Annex two: Analysis of the income tax base

Introduction

A2.1 Since income tax devolution in Wales in 2019, the performance of income tax revenues has directly fed into and impacted on the Welsh Government's budget. A comprehensive understanding of the strengths and weaknesses of the tax base in Wales is an important input to both the tax and wider policy processes in the Welsh Government.

A2.2 Income tax devolution in Wales has involved a 10p reduction in each of the UK tax rates on non-savings non-dividend (NSND) income. The Welsh Government then sets its own rate in each of the three tax bands, the Welsh Rates of Income Tax (WRIT).

A2.3 The WRIT base is analysed here primarily by utilising HMRC's Survey of Personal Incomes (SPI). This is a sample of anonymised UK tax records grossed up to represent the UK taxpayer population.

A2.4 Due to the reporting arrangements for tax returns, there is a lag between when the SPI becomes available and the financial year it relates to. At the time of publication, the latest version corresponds to 2017-18 tax records, therefore all charts and figures relate to 2017-18, unless otherwise stated. The analysis assumes that each of the Welsh rates is set at 10p, as has been the case since devolution.

A2.5 The COVID-19 pandemic will have a substantial impact on the income tax base in the near term, but we do not yet know what the longer term effects will be. For the time being, the detailed SPI data for 2017-18 provides the best available detailed dataset to look at the tax base in Wales.

A2.6 As WRIT and the accompanying 'C' codes did not apply until 2019-20, tax payers who are identified as living in Wales are assumed to be potential WRIT payers.

A2.7 Analysis of the income tax base is split into 3 sections: characteristics, past and projected performance of employment and earnings, and the possible differential impact of the COVID-19 pandemic on Wales, and England and Northern Ireland (E&NI).

Income tax base – characteristics

<u>Gender</u>

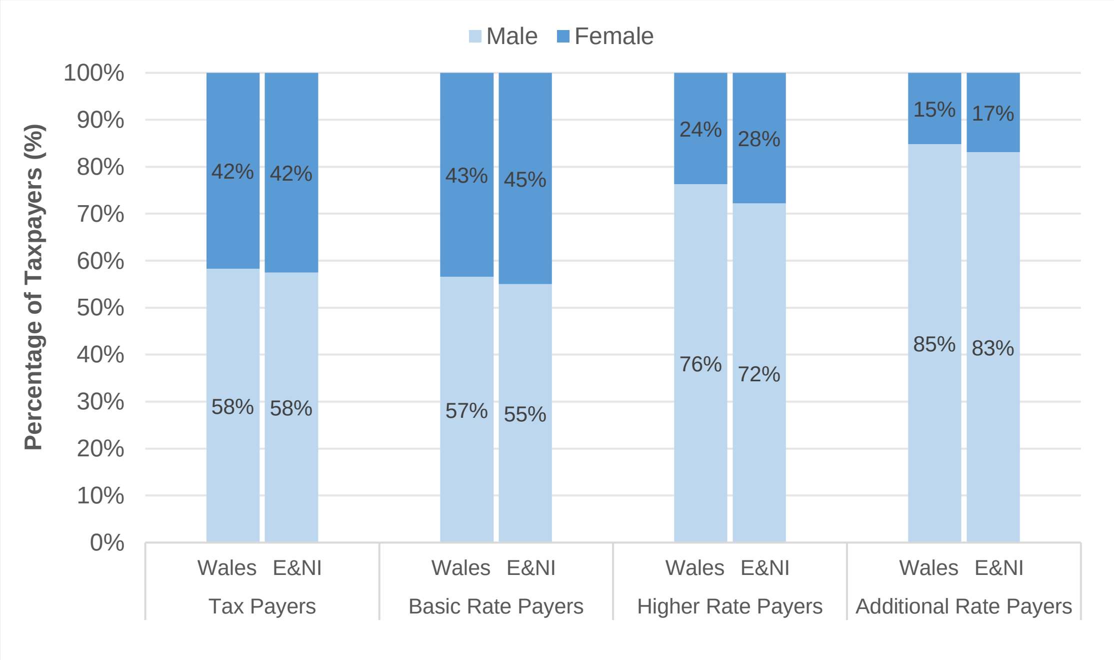
A2.8 Men account for 62% of Wales' income taxpayers and 71% of income tax revenues[41], reflecting gender differences in both employment and incomes.

A2.9 Figure two presents the gender split of NSND income tax payers by their marginal rate, for both Wales and E&NI. Women account for a smaller proportion of taxpayers in the higher and additional tax bands.

[41] HMRC Personal Income Statistics, Table 3.12, 2017-18.

A2.10 Men account for the same share of NSND income tax payers in both Wales and E&NI (58%). Across all marginal rates, males correspond to a slightly higher share in Wales than in E&NI, reflecting the different income distributions between the two regions. The gender split of WRIT revenue is more uneven, with males accounting for 67% of WRIT revenues in Wales and 70% of E&NI's equivalent.

Figure two: Gender split of NSND income taxpayers, by their marginal rate (%)



Data Source: SPI 2017-18

Age

A2.11 Welsh tax payers aged between 35 and 54 years account for nearly half of income tax revenue in Wales, whilst making up less than a third of the 16+ population[42]. This shows the importance of mid-life age groups in the tax base.

A2.12 The average, per person WRIT liability by age group is shown in Figure three. Individuals aged 16 to 24 years typically have the lowest WRIT liabilities (£150), mainly reflecting the lower proportion of individuals in employment[43]. Average liabilities rise with age, peaking amongst 45-54 year olds, and then declining steadily for older groups.

A2.13 The different level and composition of WRIT liabilities is driven by the varied income distributions across age groups. On average, 55 to 64 year olds paid more WRIT at the Additional Rate than the 45 to 54 age group, despite having a £250 lower overall WRIT liability. This suggests a relatively greater range in incomes in the 55 to 64 group.

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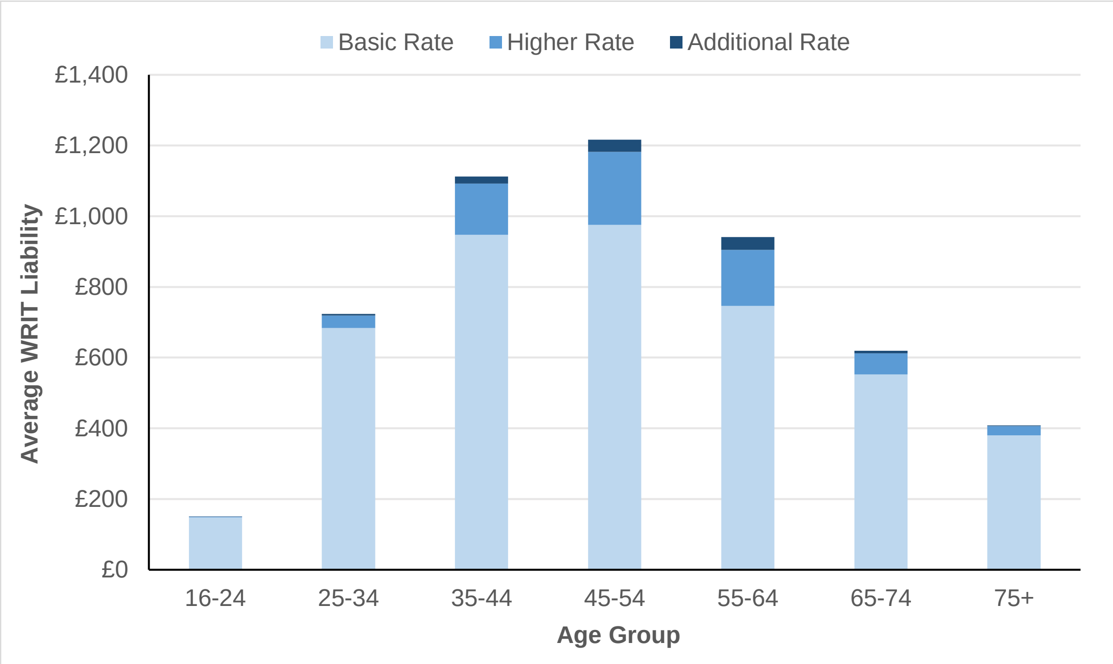
[42] Estimates of the population for the UK, England and Wales, Scotland and Northern Ireland: https://www.ons.gov.uk/peoplepopulationandcommunity/populationandmigration/populationestimates/datasets/populationestimatesforukenglandandwalesscotlandandnorthernireland
[43] Regional Labour Market: Estimates of Employment, by Age

Figure three: Average WRIT liability per person, by Age Group

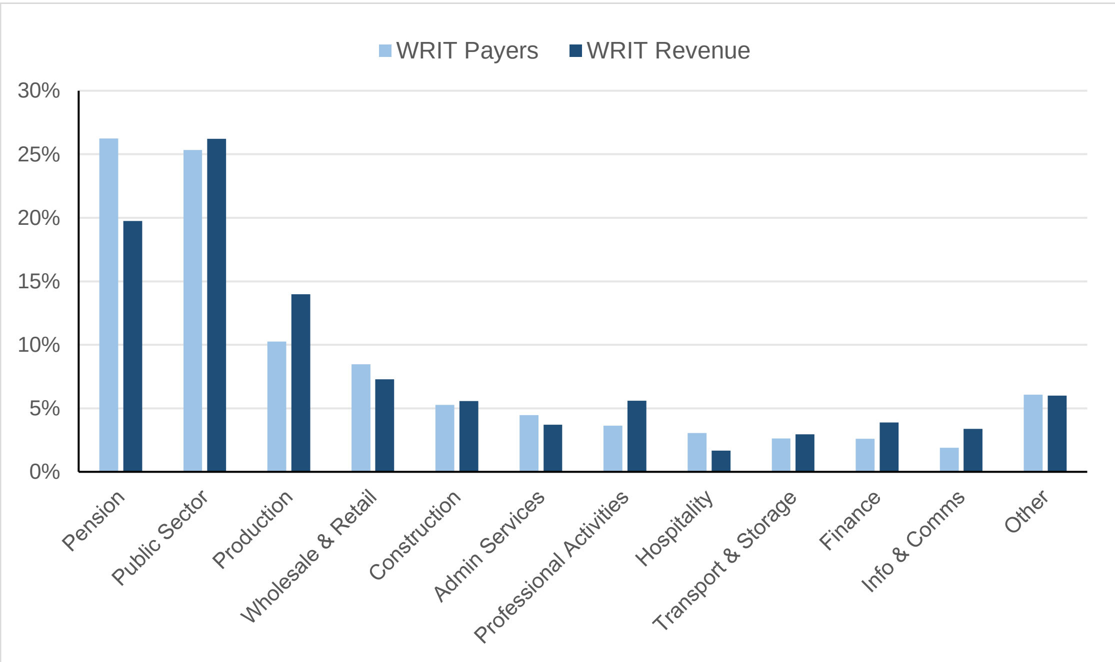


Data Source: SPI 2017-18

Industry sector

A2.14 Figure four shows a sectoral breakdown of WRIT payers and revenue. Pensioners and public sector workers each account for around a quarter of Welsh taxpayers. Owing to their lower than average incomes, pensioners only account for around 20% of WRIT revenues. Other sectors, such as production and professional activities, contribute a higher proportion of revenues than their taxpayer share.

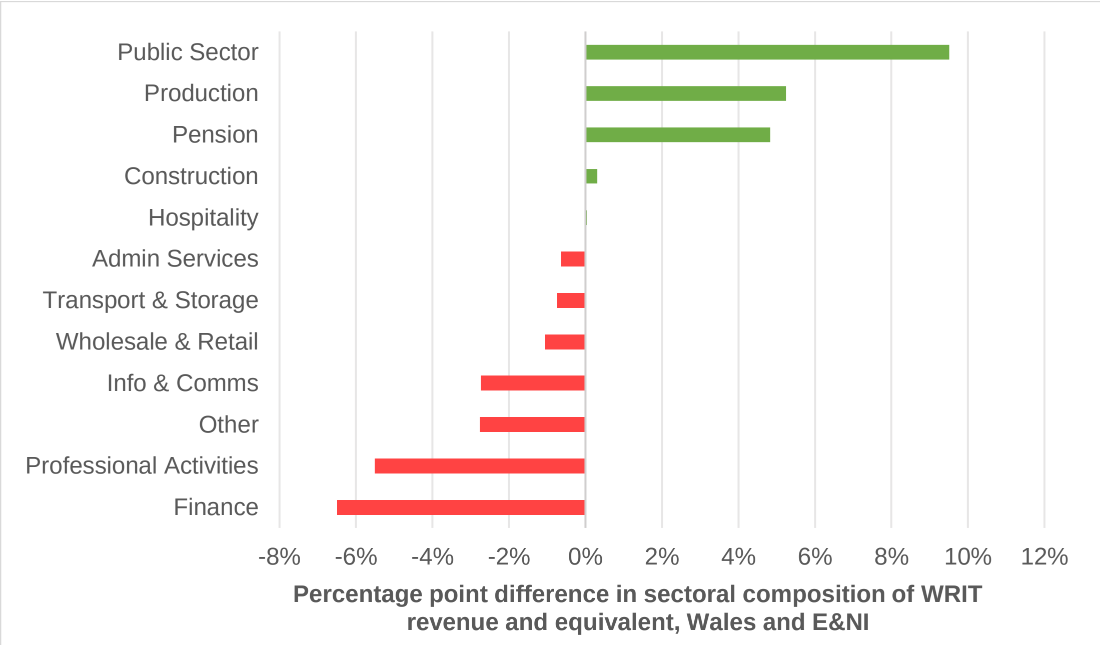
Figure four: Sectoral breakdown of WRIT payers and WRIT revenue (%)



Data Source: SPI 2017-18. 'Other' is comprised of the Agriculture, Real Estate, Arts, Other Services and Private Household industries, as well as those which are unclassified or unknown.

A2.15 Figure five shows the relative difference in the sectoral composition of WRIT revenue and equivalent between on Wales, and England and Northern Ireland (E&NI). Wales, as shown by the green bars, has a notably higher share of revenues from the public, production and pension sectors.

Figure five: Percentage point difference in sectoral contribution to WRIT revenue and equivalent, Wales and E&NI

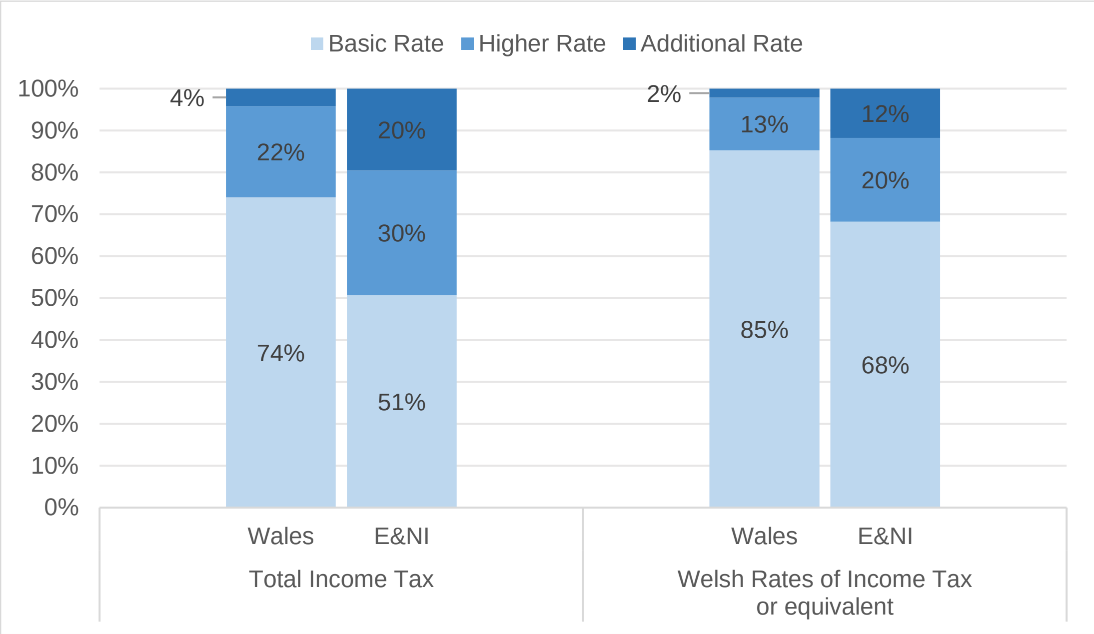


Data Source: SPI 2017-18

Tax by band and marginal rate

A2.16 Figure six shows the relative importance of basic rate revenues in total income tax receipts. The basic rate accounts for three-quarters of income tax revenues in Wales compared to a half in E&NI. For WRIT (10p of each tax rate), the basic rate accounts for 85% of total revenues in Wales.

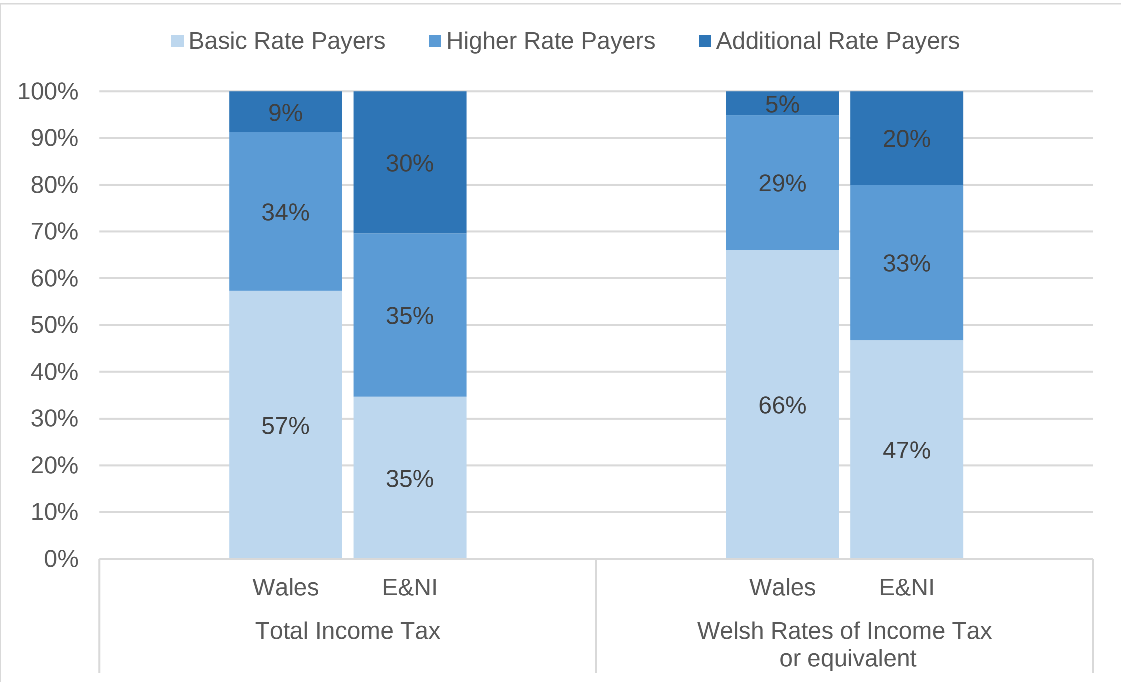
Figure six: Proportion of income tax revenue, by tax band



Data Source: SPI 2017-18

A2.17 Although WRIT revenue is primarily generated through the basic rate, those who *solely* pay income tax at the basic rate (basic rate payers) account for only a portion of this share. This can be seen in Figure seven, which shows the proportion of income tax revenue generated by taxpayers in each marginal rate group. In Wales, only 15% of WRIT revenue is generated through the higher and additional rates (figure six), however tax payers who pay WRIT at these rates contribute over a third (34%) of overall WRIT revenue. This reflects the relatively high contribution to WRIT revenues from higher earners, predominantly through the basic rate of WRIT.

Figure seven: Proportion of income tax revenue, by taxpayers' marginal rate



Data Source: SPI 2017-18

Typical tax liabilities and average tax rates in Wales

A2.18 Table thirteen shows the median full-time earnings, associated income tax liabilities, and average income tax rates (income tax liability divided by income), across a variety of professions in Wales.

A2.19 Average tax rates increase with income, showing that both total income tax and WRIT are progressive with respect to income. WRIT is progressive for incomes up to £125,000. Above that level the average tax rate is a flat 10%, because there is no personal allowance from that level of income.

Table thirteen: Welsh annual median full-time earnings, income tax liabilities and average tax rates, across a number of professions

Profession	Annual Median Full-time Earnings	Income Tax liability (Average Income Tax Rate)	Of which: WRIT liability (Average WRIT rate)
Air Traffic Controller	£94,000	£25,100 (27%)	£8,150 (9%)
Aircraft Maintenance	£43,000	£6,100 (14%)	£3,050 (7%)
75th Percentile	**£38,000**	£5,100 (13%)	£2,550 (7%)
Vet	£35,000	£4,500 (13%)	£2,250 (6%)
Electrician	£29,000	£3,300 (11%)	£1,650 (6%)
Wales Median	**£27,000**	**£2,900 (11%)**	**£1,450 (5%)**
Postal Worker	£26,000	£2,700 (10%)	£1,350 (5%)
Decorator	£22,000	£1,900 (9%)	£950 (4%)
25th Percentile	**£20,000**	£1,500 (8%)	£750 (4%)
Baker	£19,000	£1,300 (7%)	£650 (3%)
Retail Assistant	£18,000	£1,100 (6%)	£550 (3%)
Cleaner	£16,000	£700 (4%)	£350 (2%)

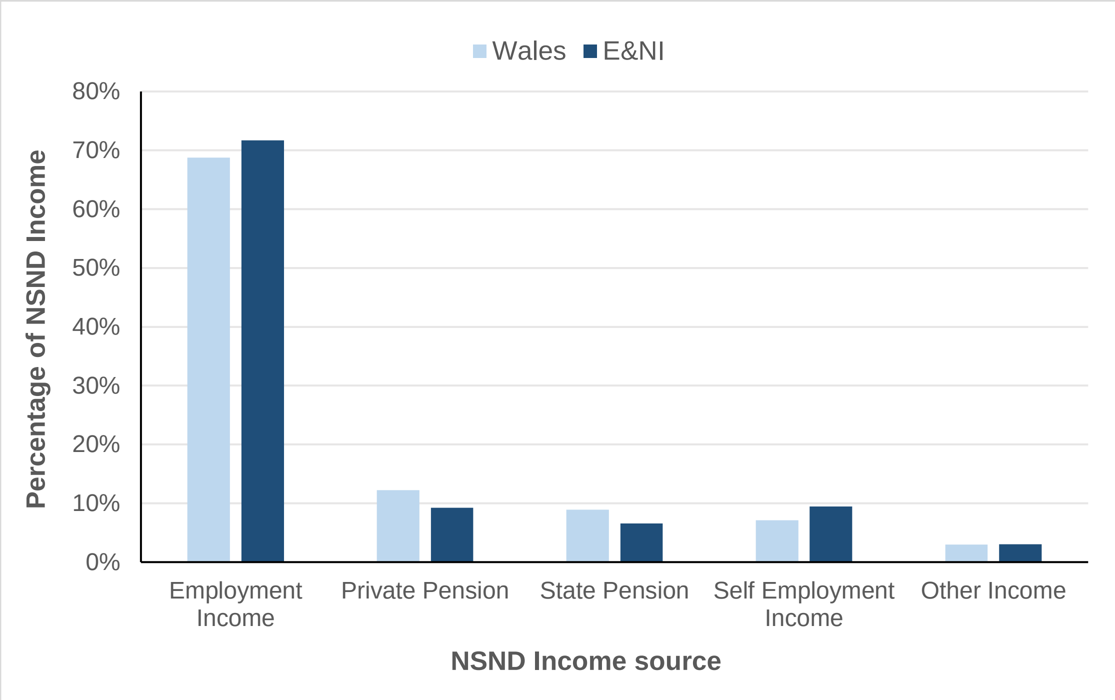
Data source: ONS – Annual Survey of Hours and Earnings (2019)
Tax liabilities assume all earnings are non-savings or non-dividends sourced, are taxable and have no other reliefs or deductions applied to them.

A2.20 For non-savings and non-dividend incomes up to £50,000, half of all income tax liabilities are devolved (10p of the overall 20p basic rate). For higher incomes this share declines as WRIT represents a smaller proportion of the overall higher and additional tax rates. In table thirteen, only the air traffic controller falls into this group.

Source of Income

A2.21 Figure eight shows the shares of non-savings, non-dividend income from different sources. Employment accounts for the bulk of income in both Wales (69%) and E&NI (72%). Private and state pensions account for larger shares in Wales than E&NI. Wales has a relatively low share of income from self-employment.

Figure eight: Proportion of Non-Saving and Non-Dividend income, by source



Data Source: SPI 2017-18

Earnings and employment relative performance

A2.22 With devolution, the performance of income tax revenues in Wales has a direct effect on the Welsh Government's budget.

A2.23 Due to the way the Welsh Government's Fiscal Framework44 operates, it is the relative growth in WRIT revenue, compared to equivalent revenues in E&NI, which determines the net impact of income tax on the Welsh Government's overall resources.

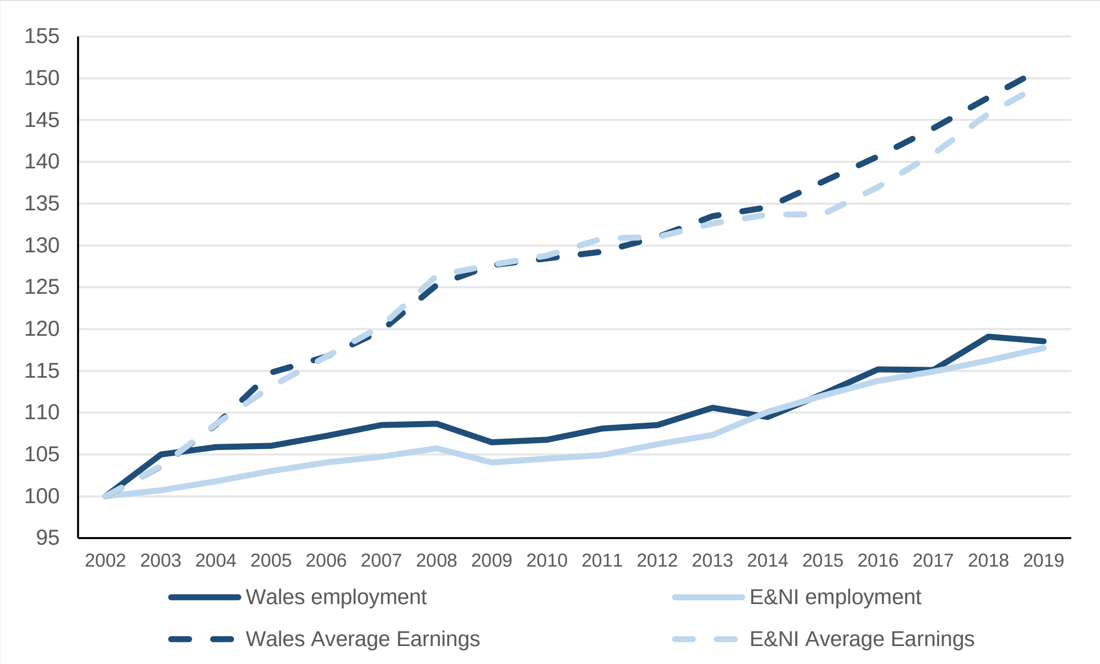
A2.24 Past relative earnings and employment trends can be examined to provide an indication of how devolved income tax may perform into the future.

A2.25 Figure nine shows Welsh and E&NI earnings and employment over the last two decades or so, indexed to 2002. Growth in Wales for both measures has tracked E&NI closely over this period.

A2.26 This implies that if income tax had been devolved over this period, and rates kept the same, then there would not have been a substantial financial impact on the Welsh Government's budget.

[44] https://gov.wales/sites/default/files/publications/2018-11/agreement-on-welsh-government-fiscal-framework.pdf

Figure nine: Index of Employment and Earnings for Wales and E&NI (2002=100)



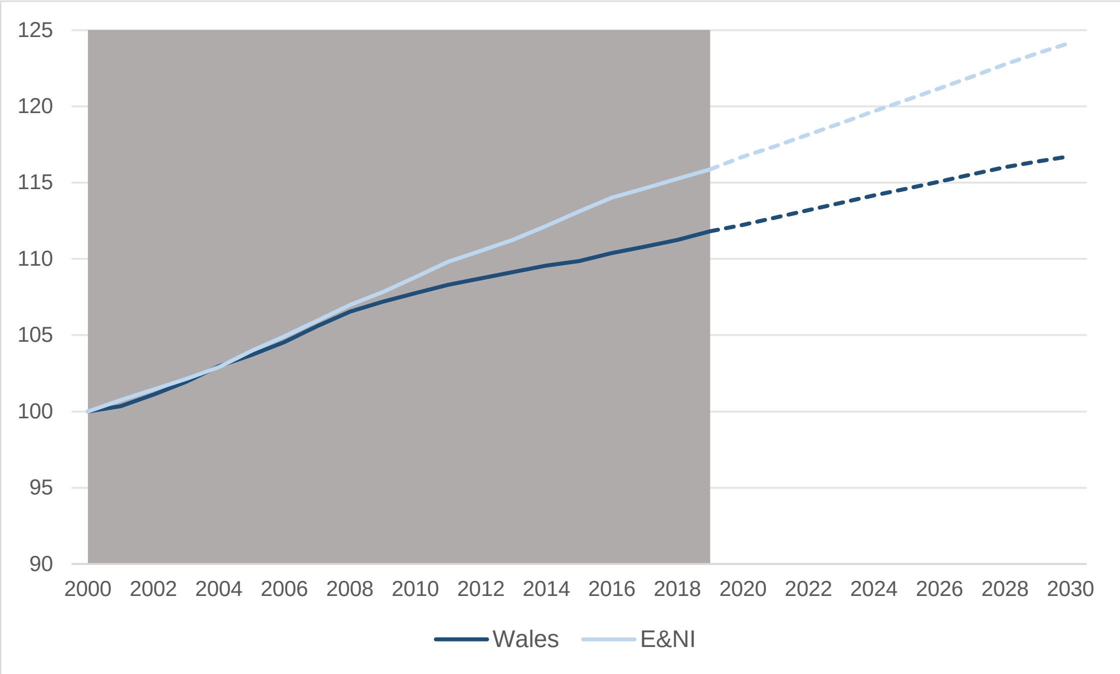
Data Source: ONS Annual Survey of Hours and Earnings, Labour Force Survey

Future projections

A2.27 In the long run, the growth of the 16+ population provides a general indicator for how the taxpayer base may grow. Figure ten shows growth in the 16+ population between 2000 and 2019, and projected growth from 2020 to 2030. From 2000 to 2008, the growth rate in Wales was similar to that in E&NI. However, since 2008, growth in Wales has slowed, causing an increasing divergence with the E&NI. This is not reflected in the employment numbers in figure nine because the employment rate in Wales has increased, relative to E&NI.

A2.28 ONS population projections show this divergence increasing through to 2030. If this were to occur, and in the absence of a continuing relative improvement in the employment rate in Wales, then there is likely to be a relative weakening of the Welsh tax base in the longer run. The projections used here were compiled before the onset of the pandemic and were based on recent population trends. It is too early to say whether the pandemic will have a significant and lasting impact on population trends in the UK.

Figure ten: Index of the 16+ population for Wales and E&NI (2000=100)



Data source: ONS Mid-year population estimates and 2018-based population projections

Income Tax Base – COVID-19 Analysis

A2.29 The COVID-19 pandemic has had a direct effect on employment and incomes in 2020-21, causing great uncertainty about future earnings and employment growth, and therefore income tax projections. The differential impact of the pandemic on the tax bases in Wales and E&NI will play a significant role in determining the relative performance of WRIT receipts over the medium term.

A2.30 The COVID-19 pandemic has had varying effects on the different sectors of the economy[45]. While some sectors have been adversely affected, others have grown. Understanding the sectoral composition within Wales can help to understand how the pandemic may affect tax payers and WRIT revenues.

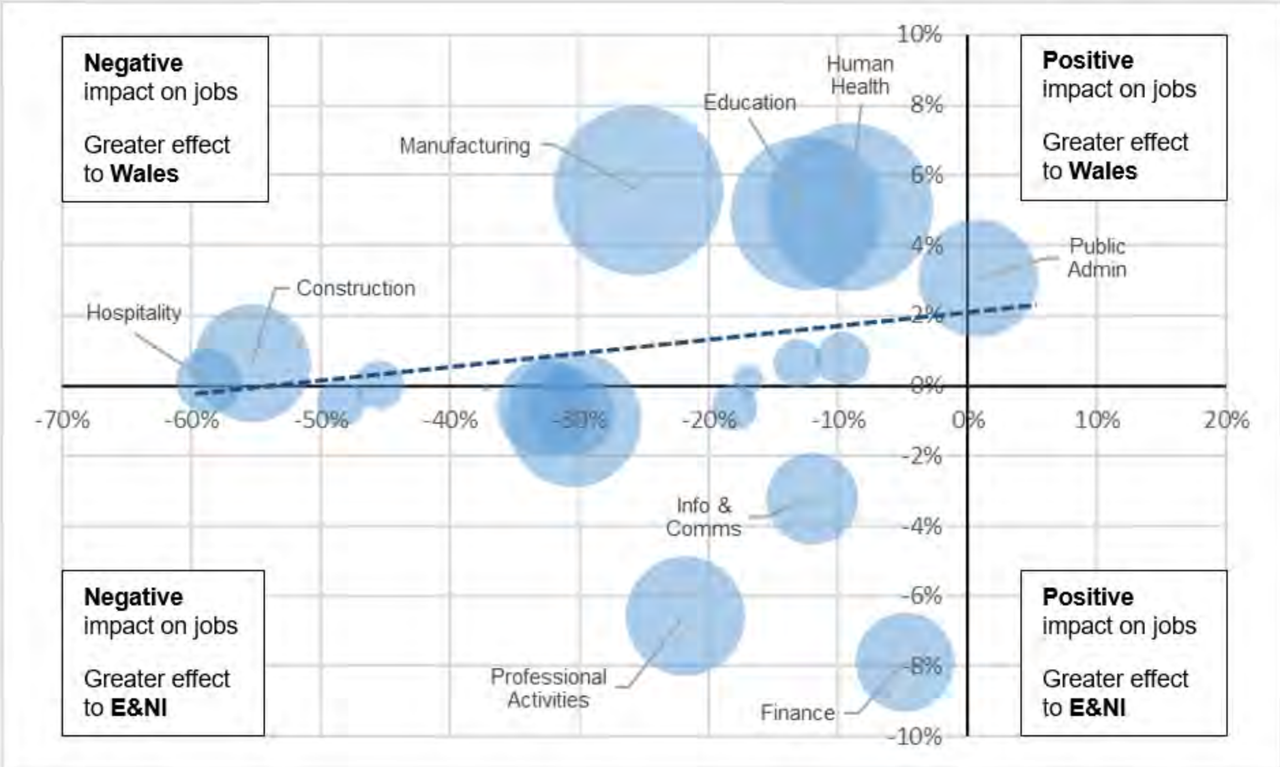
A2.31 Figure eleven illustrates the differential impact of the pandemic on working jobs in different sectors and the extent to which those sectors are more or less important to the Welsh tax base relative to E&NI. To capture the impact of the first wave of the pandemic, data relating to the UK labour market in June 2020 is examined. The sectoral shock of the pandemic is assumed to be UK-wide.

A2.32 Larger bubbles reflect industries which account for a greater share of WRIT revenue generated in Wales. The horizontal axis shows the percentage reduction in the number of workforce jobs between Dec 2019 and June 2020[46], including jobs supported by the Coronavirus Job Retention Scheme (CJRS) or Self-Employment Income Support Scheme (SEISS)[47].

[45] ONS: Monthly GDP, by GVA
[46] ONS: Workforce Jobs by Industry
[47] HMRC: Coronavirus (COVID-19) Statistics

A2.33 The vertical axis is the percentage point difference in the sectoral share of WRIT revenue or equivalent, between Wales and E&NI. Sectors accounting for a greater share of WRIT revenue in Wales have a positive value.

Figure eleven: Difference in sectoral composition of WRIT revenue or equivalent (ppt), and change in working jobs between Dec 2019 and June 2020 (%)



Data sources: SPI 2017-18, ONS Workforce Jobs, HMRC Coronavirus (COVID-19) statistics
P-value = 0.57, R^2 = 0.22, slope coefficient = 0.036

A2.34 An insignificant relationship is found, therefore there is no evidence to suggest Wales is more exposed to the impact of the pandemic than E&NI. Wales is more reliant on sectors relatively unaffected by the pandemic for WRIT revenue, such as education and public admin. However, other fairly insulated sectors (professional activities and finance) account for a greater share of equivalent WRIT revenues generated in E&NI, resulting in no regional difference being estimated.

A2.35 No differential impact is seen when replicated for September 2020, a period of relatively relaxed restrictions, again providing little evidence the pandemic had an asymmetric impact on WRIT revenues and equivalent between Wales and E&NI.

A2.36 In addition, regional labour market statistics show there was a minimal difference in the percentage reduction to working jobs in Wales (33%), compared to E&NI (34%)[48][49] between December 2019 and June 2020.

Future Developments

A2.37 The first outturn data for the Welsh Rates of Income Tax is expected this summer, when HMRC is due to publish outturn for 2019-20. This may have important

[48] ONS: Regional Workforce Jobs statistics
[49] HMRC: Regional CJRS and SEISS statistics

implications for future Welsh Government budgets and for the analysis included in this document.

A2.38 The Welsh Government will continue to analyse the income tax base in Wales to ensure it has a comprehensive and up to date understanding of its characteristics. The Welsh Government will also work with HMRC to continue to improve the income tax data so further analysis can be undertaken and look to make this available for researchers more generally, wherever possible.

Annex three: Land Transaction Tax rates and bands changes

Introduction

A3.1 This section outlines the recent changes which have been made to Land Transaction Tax (LTT) and what their expected impacts are likely to be.

A3.2 There have been three main changes to LTT in 2020-21. These are:
- i) A temporary increase to the main residential rates zero rate threshold;
- ii) An increase to the higher residential rates; and
- iii) An increase to the non-residential zero rate thresholds.

A3.3 Each of these is discussed below.

i) A temporary increase to the main residential rates zero rate threshold

Background

A3.4 On 14 July, the Welsh Government announced a temporary increase to the main residential rates zero rate threshold. The change increased the starting threshold from £180,000 to £250,000. This provides for a tax reduction of up to £2,450. The measure applies to completed transactions between 27 July 2020 and 30 June 2021. No changes were made to the tax rules applying to higher rates residential property transactions, which mainly affect buyers of buy-to-let or second home properties.

A3.5 The LTT measure followed a reduction to stamp duty land tax (SDLT) payable on residential transactions in England and Northern Ireland. That measure increased the starting threshold to £500,000 and applied to all residential purchases, including second homes and buy-to-let purchases. The SDLT measure is also due to end on 30 June 2021 with a threshold of £250,000 applying until 30 September, with the £125,000 threshold applying from 1 October 2021.

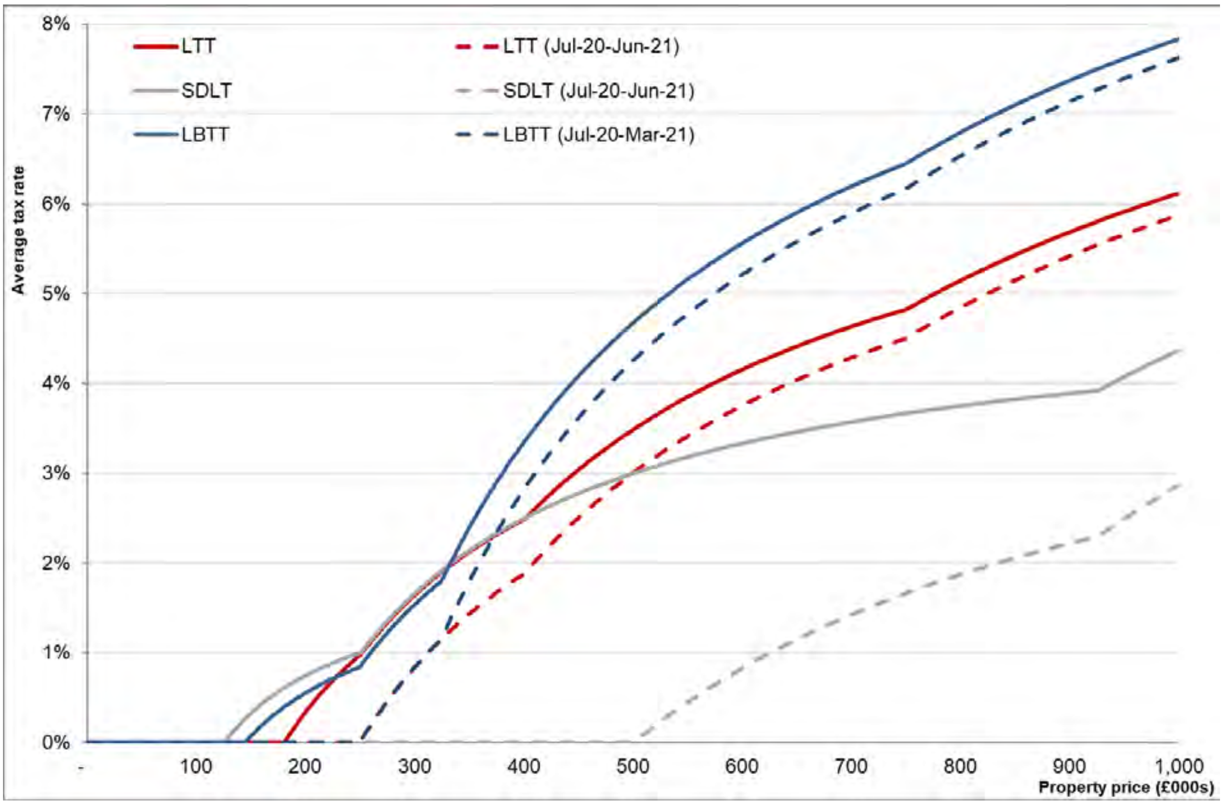
A3.6 The Scottish Government has also applied a temporary higher residential starting threshold for Land and Buildings Transaction Tax (LBTT). The threshold has been increased from £145,000 to £250,000. As with SDLT, the purchase of second homes and buy-to-let properties are also subject to this higher threshold. The policy applies to transactions occurring between 15 July 2020 and 31 March 2021.

A3.7 For both SDLT and LBTT taxpayers liable to the higher rates still had to pay the surcharge element, the tax reductions applied only to the element of liability calculated using the main residential rates.

A3.8 The impact of these changes to LTT, SDLT and LBTT on average tax rates is provided in Figure twelve. Without the temporary measures and reliefs, LTT has the highest starting threshold at £180,000 and the tax due is the same or lower than SDLT up to around £400,000.

A3.9 Under the temporary measures, LTT is most similar to LBTT, with the same tax applied for transactions up to £325,000. Average tax rates under LTT and LBTT are higher than under SDLT for transactions above £250,000.

Figure twelve: LTT, SDLT and LBTT main residential tax rates



Note: shows tax applying to main residences, not buy to let or holiday homes, and excludes first time buyer and any other reliefs.

Evidence and analysis

A3.10 The ONS's average house price in Wales was £170,000 in July and the first time buyer price was £146,000. Therefore even before the temporary measure, the permanent starting threshold in LTT was already higher than the average buyer price. This was not the case in England and Scotland where average prices were above the respective tax thresholds.

A3.11 As a result of the LTT change, using 2019-20 data, only the top 20% of Welsh residential transactions would be above the temporary zero rate threshold, up from around 40% with the £180,000 zero rate threshold. The temporary changes to SDLT means the top 10% of English and Northern Irish homebuyers pay tax under the main residential rates. The changes to LBTT mean around the top 20% of Scottish homebuyers will pay tax when purchasing their home.

A3.12 It is estimated that around 10,000 main rates residential transactions will benefit from the tax reduction in Wales, at a cost of £19 million in 2020-21[50].

A3.13 As the policy had a pre-announced end on 31 March 2021, the Office for Budget Responsibility (OBR) expected the policy to cause some forestalling – transactions will have been brought forward to take advantage of the lower tax regime ahead of the then 1 April 2021 change to LTT rates. Based on previous episodes of

[50] Available from:
https://obr.uk/welsh-taxes-outlook-december-2020/

forestalling in the property market at the UK level[51], the OBR estimates that around 1,000 transactions in Wales will be brought forward from 2021-22 into 2020-21. This increases LTT revenues in 2020-21 by around £3 million and reduces them by £4 million in 2021-22.

A3.14 As the measure reduces LTT, it is also expected to slightly increase the number of transactions in 2020-21, in addition to the forestalling impact, although this will be a smaller effect. A small positive effect on residential prices is also expected.

A3.15 Increasing residential property transactions in 2020-21 may also have a positive effect on the economy more generally this year. UK evidence relating to the economic downturn of 2008 to 2009 suggests reducing residential property transaction taxes boosted the property market and stimulated the economy[52]. Subsequent research for the Welsh Government suggests positive benefits from drawing transactions forward, but a smaller overall benefit in Wales than implied by the UK evidence[53]. However, the current economic downturn is very different to the one which occurred in 2008 and the tax system in Wales is also different (for example there was a shift from a 'slab' to a 'slice' system for residential property transactions in 2014). It is therefore difficult to directly apply these previous studies to the current situation.

A3.16 As a result of the temporary measures, there are substantial tax differences for purchases of more expensive property in Wales compared to SDLT in England. For homebuyers in Wales, tax differences occur from £250,000 upwards. In 2019-20, around 10% of properties were transacted for £300,000 or more. At that price, the difference in tax between LTT and SDLT with the current temporary measures in 2020-21 is £2,500. Around 5% sold for £380,000 or more in 2019-20, at that price the difference in tax is £6,500. Around 1% sold for £600,000 or more, at that price the difference in tax is £17,500.

A3.17 Evidence from Hilber and Lyytikäinen (2012)[54] suggests changes to, or differences in, property transaction taxes are more likely to affect short distance moves than long distance ones. Therefore, the transactions in Wales which are most likely to be affected by these new differences are those which are very close to England. This may affect some local property markets which straddle the England-Wales border, creating some property market distortion in those areas. However, given the few properties this is expected to affect, the overall effect is expected to be relatively small.

A3.18 Restricting the temporary tax reduction to those purchasing their main residence and not buy-to-let and second home transactions has increased the tax difference between different types of residential purchases in Wales. The relative reduction in tax for homebuyers compared to second home and buy-to-let purchases may also

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[51] For more details on forestalling see *Forestalling ahead of property tax changes* OBR (2016), available at: https://obr.uk/docs/dlm_uploads/Working-paper-No.10-1.pdf

[52] See Best, M. and Kleven, H. (2018) *Housing Market Responses to Transaction Taxes: Evidence from Notches and Stimulus in the UK*, The Review of Economic Studies, 85, pp. 157-193.

[53] See TARC (2019) *An Evaluation of the 2008-2009 Stamp Duty Holiday in Wales* available at: https://tarc.exeter.ac.uk/media/universityofexeter/businessschool/documents/centres/tarc/publications/reports/An_Evaluation_of_the_2008-2009_Stamp_Duty_Holiday_in_Wales.pdf

[54] Available at: http://www.spatialeconomics.ac.uk/textonly/SERC/publications/download/sercdp0115.pdf

change the composition of residential transactions. This may slightly increase the share of homebuyer transactions in Wales during the period July 2020 to June 2021.

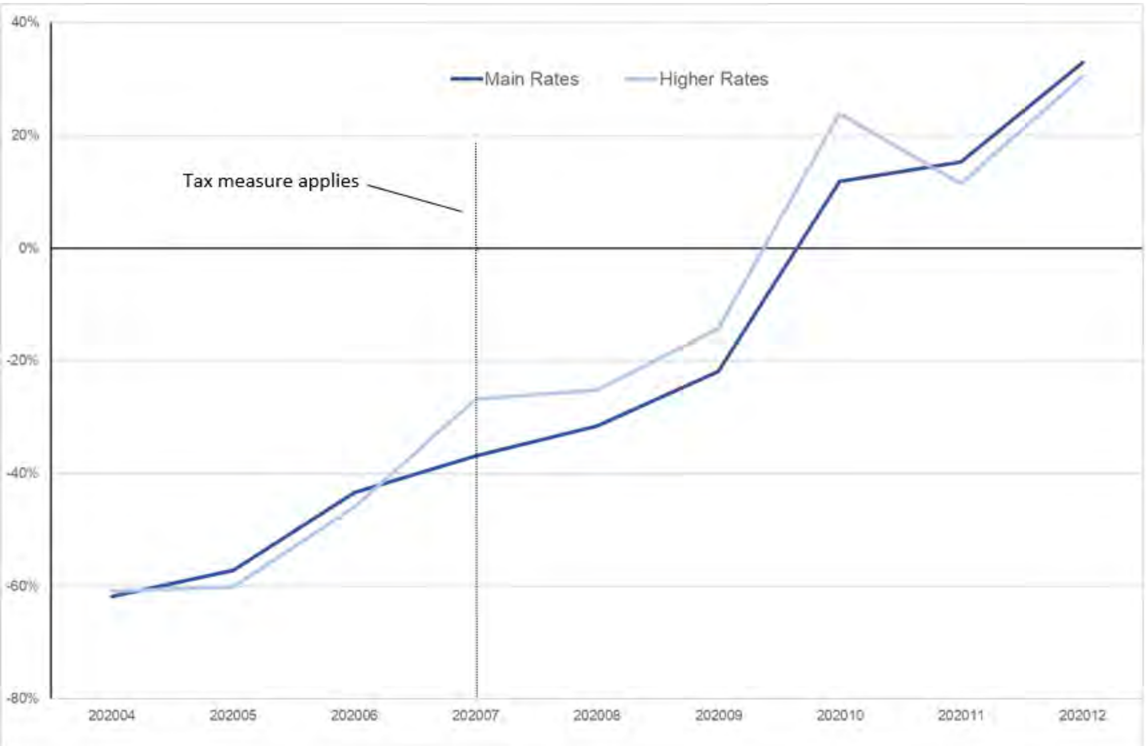
Outcome

A3.19 The potential impact of the tax can be investigated by comparing the performance of main rates transactions with higher rates residential transactions – which have not been subject to a tax reduction.

A3.20 Both types of transaction have recovered since start of this financial year, as shown in Figure thirteen. In April, higher rates and main rates transactions were both around 60 per cent lower than the monthly average for 2019-20. In July, higher rates transactions were 27% below their 2019-20 monthly average, while main rates transactions were 37% down. This may have been caused by the staged re-opening of the property market, with the full re-opening occurring on 27 July.

A3.21 Given the time lag between initiating and completing property transactions, there is likely to be a delay of perhaps a couple of months before the tax change will have effected recorded transactions. Transactions have continued to recover for both transaction types, but since September the recovery for main rates transactions has been more rapid than for higher rates transactions.

Figure thirteen: Residential transaction performance, relative to 2019-20 monthly average

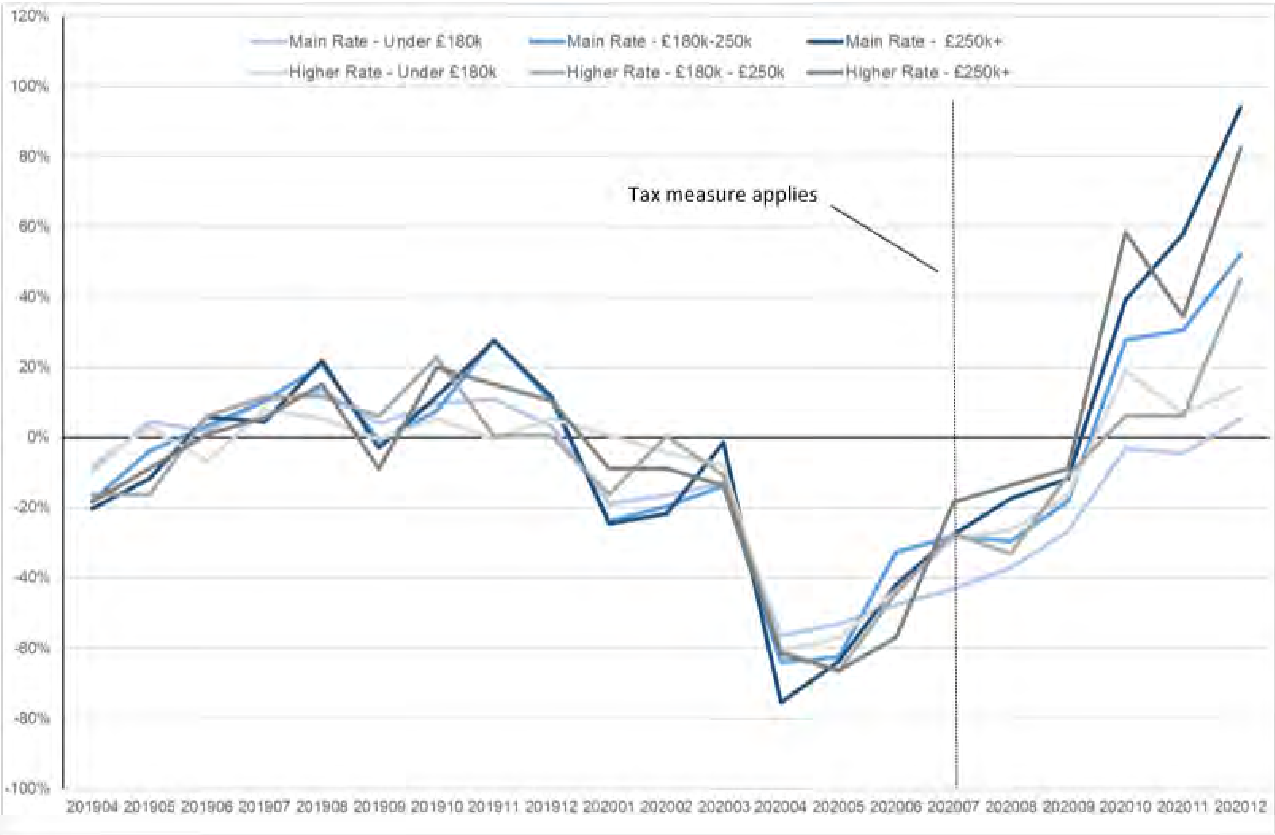


NB Higher rates shown are before any potential refunds are applied.
Source: Welsh Revenue Authority

A3.22 As well as varying by the type of transaction, the tax reduction in July also varied by price. For the main rate there was no change for transactions below £180,000 which already paid no tax, an increasing impact from £180,000 to £250,000, and a fixed reduction of £2,450 for transactions above that price. Figure fourteen shows the recent path of transactions in those three bands for main rates and higher rates.

A3.23 Looking at the period since July, higher priced transactions have generally recovered more strongly than lower priced transactions and, with the exception of the lowest band, main rates transactions have recovered more strongly than higher rates. This provides some tentative evidence that the tax change has had an impact on transactions. However, there are clearly wider influences on the property market arising from the current crisis. Isolating the effect of the tax change is very difficult when there are other large, property-market-wide effects in play. The OBR[55] has suggested that similar trends across the UK property market may be due to households using increased savings during the pandemic to finance more expensive house purchases. This would also explain the steeper recovery in relatively high value transactions.

Figure fourteen: Residential transaction performance by price band, relative to 2019-20 monthly average



NB Higher rates shown are before any potential refunds are applied.
Source: Welsh Revenue Authority

A3.24 Overall, this analysis shows there are a number of challenges to evaluating the potential effects of the temporary residential measure on transactions. Whilst there is currently around six months of LTT data since the measure was introduced, this is still fairly limited given the time lags mentioned above.

55 Oral evidence provided by the OBR at the Scottish Parliament's Finance Committee on 27 January 2021. Transcript available at:
https://www.parliament.scot/parliamentarybusiness/report.aspx

A3.25 In addition, a number of other factors are likely to be affecting the property market at the same time as the tax reduction. Lockdown and pent up demand followed by local lockdowns and then the Wales-wide firebreak, may all have affected the housing market. If so, these are all likely to distort the property market and make it very difficult to isolate the effect of the tax measure over this period.

ii) Increase to the higher residential rates

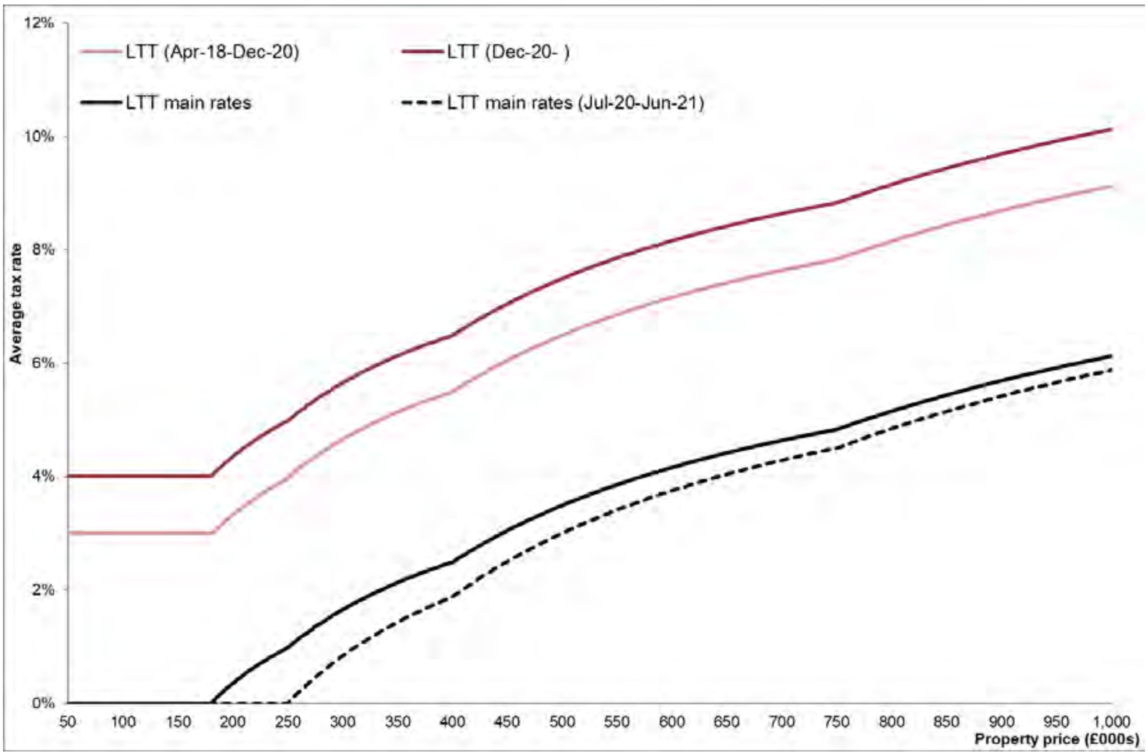
Background

A3.26 Additional LTT is applied to purchases when the buyer has more than one residential property at the time of purchase (such as owning a home and buying an investment property). The higher residential rates are also paid by companies acquiring any residential property. Until 27 July, this was a single flat rate of 3% over and above the main rates. However, in the period 27 July 2020 to 30 June 2021, the main rates residential tax threshold is temporarily increased from £180,000 to £250,000, which does not apply to additional residential properties. This means the tax difference between the higher rates and main rates is no longer a constant 3%. It increases to over 3% from £180,000 to just under 4% for properties with a price of £250,000.

A3.27 From 22 December, the higher residential rates increased from 3% to 4%. In the period 22 December 2020 to 30 June 2021, this difference from the main rates increases to just over 4% from £180,000 to just under 5% for properties with a price of £250,000. From July 2021, the higher tax rate will return to a flat rate of 4% in addition to the residential main rates. It is this amount of tax which will be repaid should a transaction become eligible for a refund over the 36 months following the original transaction completion date. Therefore the value of refunds over future years from transactions which occur from July 2020 and beyond will also increase as a result of this policy.

A3.28 Figure fifteen shows the average tax rates for higher residential rates which applied before 22 December 2020, those which apply from 22 December 2020, the main residential rates, and the main residential rates which only apply in the temporary tax reduction period 27 July 2020 to 30 June 2021 (both of which are also shown in Figure thirteen). It shows how the new higher residential rates are one percentage point higher across the price distribution. It also shows the gap between the higher rates and main rates (with and without the temporary main residential rates measure).

Figure fifteen: LTT higher residential rates – average tax rate by price



Evidence and analysis

A3.29 The average price of a higher residential rates transaction in 2019-20 was around £160,000. Therefore the tax increase adds around £1,600 to the average price of a higher rates transaction, increasing it to around £6,400.

A3.30 The OBR Welsh Taxes Outlook forecast (December 2020) includes 4,000 transactions which will be affected in the period December 2020 to March 2021, and around 16,000 a year thereafter. This measure is forecast to generate £16 million a year on average from 2021-22 onwards.

A3.31 The policy is expected to reduce both transactions and house prices slightly. These effects are likely to occur to those transactions which are subject to the higher residential rates and to a lesser degree to those which are subject to the main residential rates. The latter effect is caused by the expected replacement of some buy-to-let and second home purchasers by homebuyers.

iii) Increase to the non-residential zero rate thresholds

Background

A3.32 LTT has two sets of non-residential rates and bands. The first apply to non-residential property transfers of the freehold, 'premiums' (the upfront fee paid when taking out a new lease), and the 'assignment' of a lease (the transfer of an existing lease). These are referred to as the 'main non-residential rates'.

A3.33 The second set of rates and bands apply to the net present value (NPV) of non-residential lease rents over the duration of the leasehold. These only apply when a lease is newly granted and, generally, not when an existing lease is transferred or assigned.

A3.34 Both sets of rates and bands had a zero rate band up to £150,000 and then a 1% band from £150,000 to £250,000. The policy measure increased the thresholds for both schedules from £150,000 to £225,000, a 50% increase. This permanent change applied from 22 December 2020. The measure reduces the tax on both types of non-residential transaction by up to £750.

A3.35 In addition, a linked policy increased the 'relevant rent' amount by the corresponding increase to the thresholds, from £9,000 to £13,500 (a 50% increase). This is the level of annual rent which, if exceeded, results in transactions which have both a premium and lease rent NPV liable for tax losing the zero rate threshold which applies to the consideration given other than rents. This means the first tax rate (1%) is applied up to £250,000. By increasing the 'relevant rent' amount, fewer transactions will be subject to the loss of the zero rate band and will apply in the same proportional way as when the zero rate threshold was lower.

A3.36 These measures are more likely to benefit small and medium sized businesses (SMEs), whilst also providing the same maximum tax reduction for some larger non-residential transactions.

A3.37 Figure sixteen shows the non-residential main rates, those which apply to property transfers, premiums and lease assignments. LTT is the same as SDLT and LBTT up to £150,000. For transactions with consideration from £150,000 to just over £1m LTT is lower than both SDLT and SDLT. Above just over £1m, LTT is higher than both of the other two property transaction taxes in the UK.

A3.38 Figure seventeen shows the non-residential lease rent rates. As with the non-residential main rate, LTT is the same as SDLT up to £150,000, then lower than it up to £2m, and then higher where the lease rent net present value is over £2m. With LBTT, it is the same as LTT prior to December 2020, so LTT from December 2020 is the same as LBTT up to £150,000 and then is lower thereafter.

Figure sixteen: LTT non-residential main rates average tax rate by price

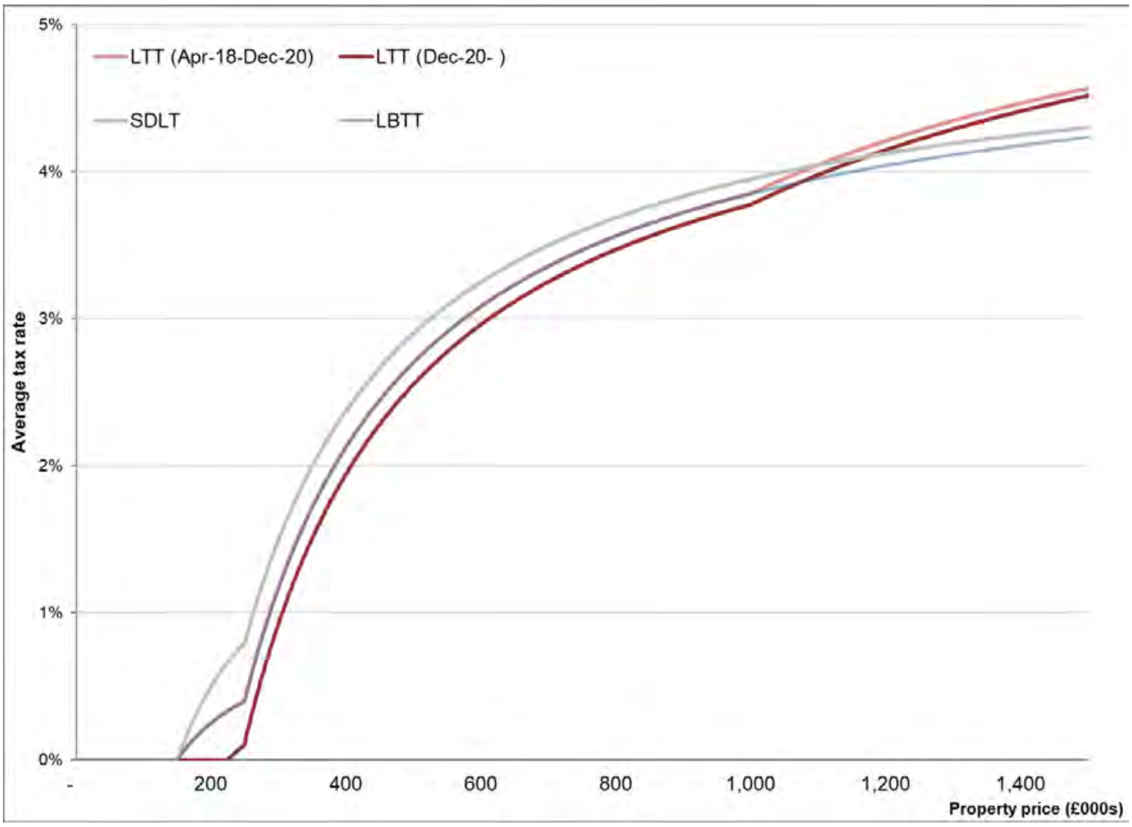
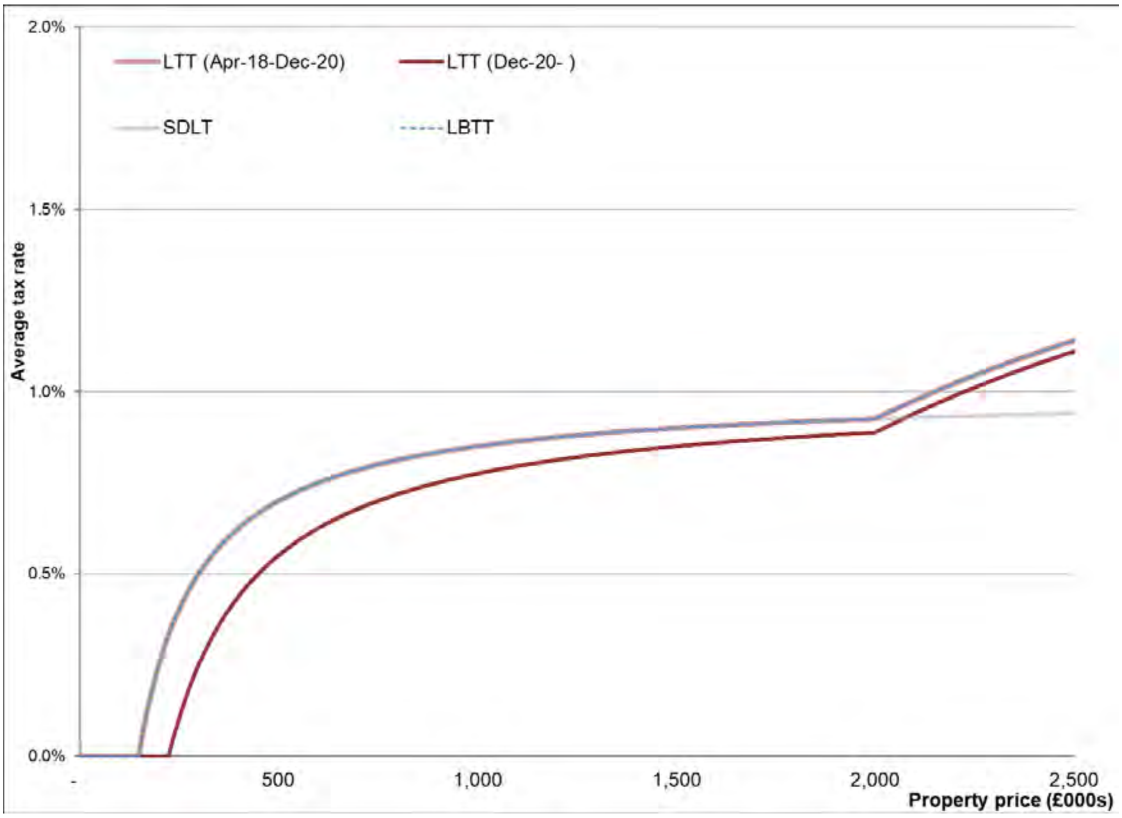


Figure seventeen: LTT non-residential lease rent rates average tax rate by lease rent NPV



Evidence and analysis

A3.39 The OBR's Welsh Taxes Outlook (December 2020) forecast includes around 1,500 non-residential lease assignments and premiums, and freehold transfer transactions per year subject to the new higher threshold of £225,000 from 2021-22 onwards. In addition, there are around 1,000 non-residential new leases granted per year, the rents (NPV) of which are also expected to be subject to a new higher threshold of £225,000. All of these transactions will have a reduced tax liability of up to £750. The changes are expected to have very small positive effects on non-residential property prices and transactions.

A3.40 The OBR estimates these measures to cost less than £1 million in 2020-21 and then £1 million a year thereafter.

Next steps

A3.41 As with all Welsh Government tax policies, we will continue to monitor the impact of the LTT polices announced in 2020-21. However, the considerable disruption to the property market caused by the pandemic will mean any potential future evaluation which seeks to isolate the effect of these policies will be very challenging. LTT data is published each month by the Welsh Revenue Authority[56]. This will continue to be publically available to allow wider analysis of LTT performance this year and in the future.

[56] Available from here:
https://statswales.gov.wales/Catalogue/Taxes-devolved-to-Wales/Land-Transaction-Tax

Annex four: Evaluation of the Welsh Government's Land Transaction Tax and Landfill Disposals Tax forecasts for 2019-20

Introduction

A4.1 The Welsh Government produced revenue forecasts of Land Transaction Tax (LTT) and Landfill Disposals Tax (LDT) for the 2019-20 final budget, published in December 2018. These forecasts were assured by Bangor Business School.

A4.2 Tax revenue outturn for 2019-20 is now available for LTT and LDT. Using this information, the Welsh Government forecasts for that year can be evaluated. The outturn will include some initial effects from the COVID-19 pandemic in the final weeks of the financial year. However, the impact on overall 2019-20 revenues will be very limited.

A4.3 This document follows the same methods used to evaluate the Welsh Government's 2018-19 forecasts, as published in the Tax Policy Report 2019[57].

A4.4 These forecasts were the last to be produced by the Welsh Government and assured by Bangor Business School. In accordance with the terms of the Welsh Government's fiscal framework agreement, tax forecasts for inclusion in Welsh Government budgets are now produced independently. The Office for Budget Responsibility produces the forecasts and will also be responsible for evaluating them.

Limitations to forecasting

A4.5 Forecasting involves the estimation of something which is uncertain: how tax revenues will change in the future. Therefore it is not unexpected for revenue outturns to differ from forecasts. As forecasts are expected to be different to outturn, it is important for these differences to be analysed in order to highlight any particular uncertainties or incorrect assumptions used which, if relevant, can be used to improve future forecasts.

A4.6 Deviations of the forecast from the outturn are not described as 'errors' here, consistent with the approach taken by the Office for Budget Responsibility (OBR). They are referred to as 'differences'. This is because they are largely unavoidable given the information available at the time of the forecast. This is different to genuine errors which can occur in forecasting models. It is important to make this distinction when evaluating forecasts.

A4.7 The forecasting models the Welsh Government used for these forecasts have been through a series of quality assurance processes which have then been given further external scrutiny by Bangor Business School[58]. The quality assurance processes should minimise the risk of modelling errors and ensure the assumptions or judgements applied were reasonable and based on the best information which was available at the time.

[57] Available in the annex from here:
https://gov.wales/sites/default/files/publications/2019-12/welsh-tax-policy-report-2019.pdf
[58] For further details see:
https://gov.wales/sites/default/files/publications/2018-12/bangor-final-report-december-2018.pdf

Land Transaction Tax

Outturn and forecasts summary

A4.8 The annual outturn for LTT in 2019-20 was £260.3m, as published in the Welsh Revenue Authority's public accounts.[59]

A4.9 Forecasts were produced for both the Draft and Final budgets for 2019-20. As it is the final Budget forecasts which are ultimately used to establish the Welsh Government's budget each year, these forecasts have been evaluated here. This forecast is analysed further in the following sections.

December 2018 forecast performance

A4.10 Table fourteen shows the outturn was £3.8m higher than the Welsh Government's Final Budget 2019-20 forecast in December 2018 (£256.4m). However, the outturn includes the revenue from the Core Valley Lines (CVL) transfer between Network Rail and Transport for Wales. This liability was fully funded by the Welsh Government. This exceptional transaction and the revenue yielded was not expected in December 2018, so was not included in the forecast at the time. Removing it results in outturn of £232.0m, £24m lower than the forecast.

A4.11 The outturn was lower than the December 2018 forecast for all three transaction types, but by varying degrees. The shortfall was proportionately bigger for non-residential (17%) than the other two transaction types (both around 9%).

Table fourteen: 2019-20 outturn and December 2018 forecast

Transaction type	Forecast Dec-18 (£m)	Outturn (£m)	Outturn difference to forecast (£m)	Outturn difference to forecast (%)
Residential (excluding additional residential)	111.6	102.1	-9.5	-9.3%
Additional residential	64.6	59.5	-5.1	-8.6%
Non-residential	80.2	68.5	-11.7	-17.1%
Other		30.2	+30.2	
Total	256.4	260.3	+3.8	+1.5%
Total (excluding CVL)		232.0	-24.4	-10.5%

[59] Available from: https://gov.wales/sites/default/files/publications/2020-07/welsh-revenue-authority-annual-accounts-2019-2020.pdf

Decomposition of outturn difference to December 2018 forecast

A4.12 To decompose the difference between the 2019-20 forecast and outturn, the following two elements are used, consistent with how the OBR evaluates its forecasts:
1. Economic factors
2. Modelling factors

A4.13 The economic factors for LTT are the property price and transaction growth forecasts. These are applied to the models to account for expected changes to the property market. The Welsh Government used the OBR's UK forecasts for these two factors.

A4.14 The modelling factors include all other elements of the difference between the forecast and outturn. Amongst other possible elements, these include: changes to the property price distribution from the base assumption used in the models and behavioural effects following tax rate changes[60]. Figure eighteen shows a decomposition of the outturn difference from forecast using these factors across the three main types of transactions.

A4.15 For the residential main rates, economic factors explain around half of the difference and modelling factors the other half. Both of these elements were relatively small.

A4.16 For the higher rates on additional residential properties, most of the difference in outturn from forecast was due to modelling factors. As this element of the tax system is a single flat rate, the changing distribution had no effect here. The main modelling issue in this case was the adjustment to take account of 2018-19 in-year data and its knock on effect in 2019-20.

A4.17 The judgement relating to in-year revenue and the effect this had on the forecast was also a feature of the evaluation of the 2018-19 forecast[61]. That evaluation highlighted the fact that the in-year profile used at that time did not fully capture the end-year fall in this type of property transaction activity. The profiling issue in the 2018-19 forecast in December 2018 meant that the 2019-20 forecast started from too high a base.

A4.18 Following the 2018-19 forecast evaluation, the way in which in-year higher rates on additional residential revenues are modelled and then judged has been updated. This was implemented as part of the 2020-21 Budget forecasts published by the Office for Budget Responsibility.

A4.19 For non-residential, there were relatively large, though partially offsetting differences to the forecast caused by the modelling and economic factors. The shortfall due to economic factors reflects lower than forecast average prices for non-residential transactions. The non-residential tax take was forecasted from a 2017 tax base, which included some exceptionally high value transactions. That high base in 2017 now appears to reflect one-off factors rather than a sustained level of revenues.

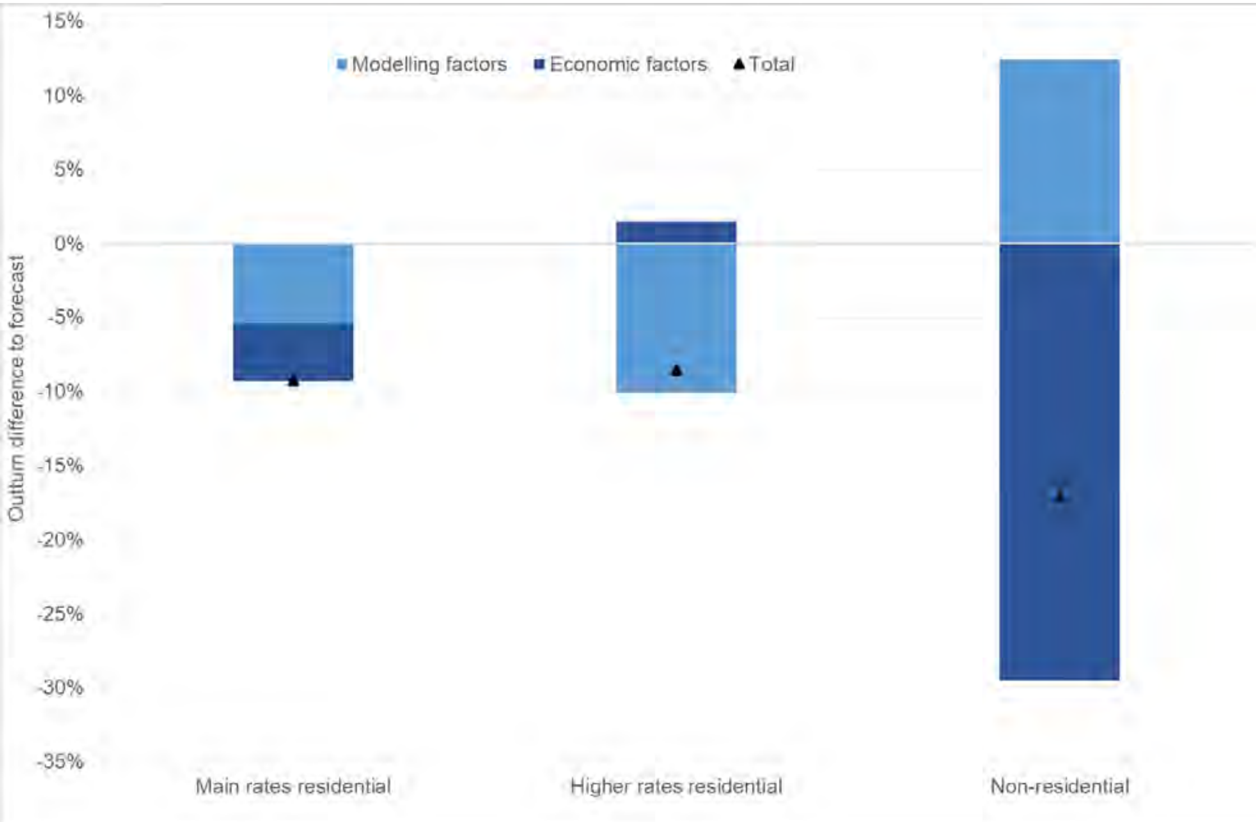
[60] A further potential reason for differences between outturn and forecasts would be policy changes announced after the forecast was made. There were no such changes in this case.
[61] See p. 60-61 of *Evaluation of Land Transaction Tax and Landfill Disposals Tax forecasts* available at: https://gov.wales/sites/default/files/publications/2019-12/welsh-tax-policy-report-2019.pdf

Forecasting from the high 2017 base out to 2019-20 meant that the average price was overstated.

A4.20 The modelling factors were also sizeable but served to reduce the overall size of the forecast difference caused by the economic determinants. This is because the modelling took account of in-year information in 2018-19 which was already signalling that the high 2017 base was not sustained.

A4.21 Overall there are significant risks with forecasting non-residential revenues due to a reliance on a few high value commercial transactions to generate revenues. As a result these revenues are highly volatile and therefore prone to forecast inaccuracy. This will continue to be an on-going risk with future LTT revenue forecasts.

Figure eighteen: Decomposition of 2019-20 December 2018 forecast



Source: Welsh Government

How does this compare to other forecasters?

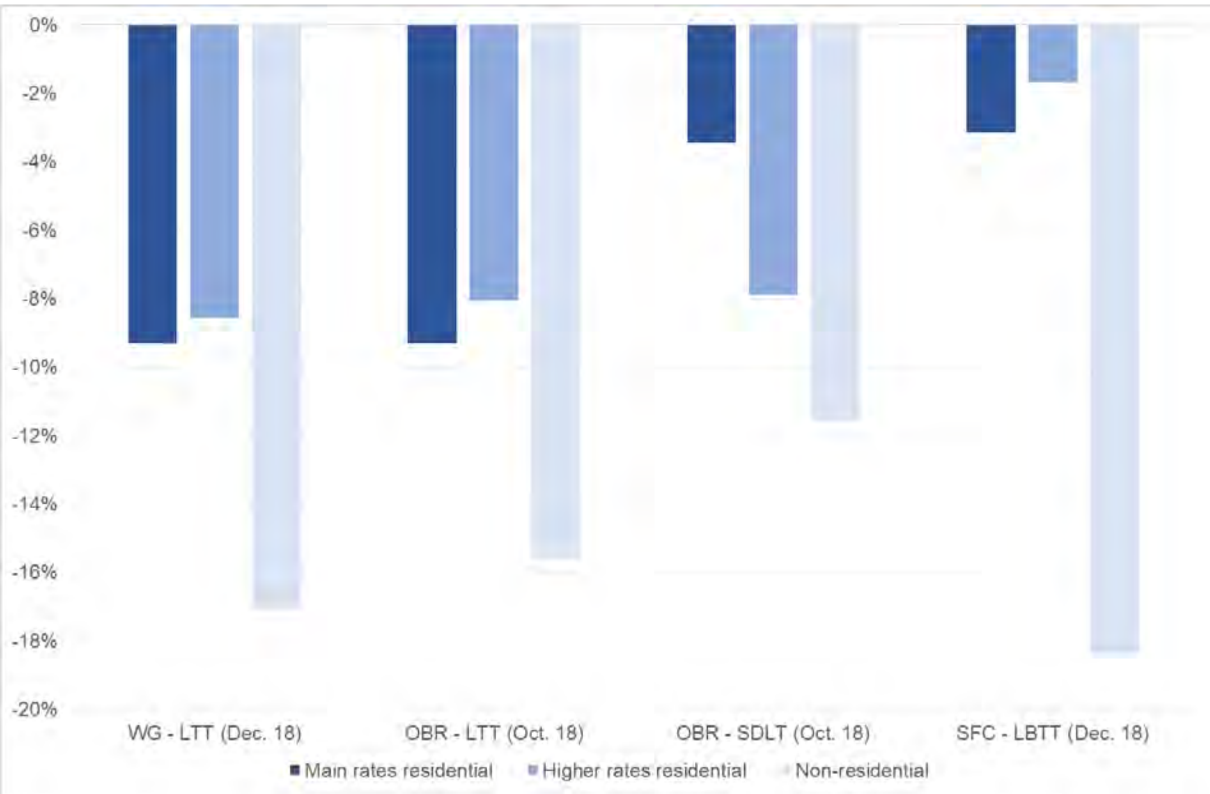
A4.22 The OBR produced forecasts of LTT and stamp duty land tax (SDLT) for 2019-20 in October 2018. The Scottish Fiscal Commission (SFC) produced a forecast of Land and Buildings Transactions Tax (LBTT)[62] for 2019-20 in December 2018. The lead times for these forecasts are comparable to the Welsh Government's. These are all shown in figure nineteen. The OBR's LTT forecast at that time was based on the Welsh Government models, explaining the similarity with the Welsh Government's forecast.

[62] LBTT is the equivalent tax to LTT and SDLT which operates in Scotland.

A4.23 The 2019-20 outturn across all three taxes and the elements within them was lower than any of the forecasts. The difference was largest for the non-residential element, exceeding 10% in all cases.

A4.24 For 3 of the 4 forecasts, the next biggest difference was for main rates residential – the exception being the OBR SDLT forecast. The SFC's forecast for the two residential elements of LBTT were the closest to outturn.

Figure nineteen: Welsh Government, OBR and SFC outturn relative to forecast differences, 2019-20



Source: OBR, SFC and HMRC (provisional outturn)

Conclusions

A4.25 Outturn for LTT revenue in 2019-20 was lower than the forecasts published in December 2018. This was mainly due to a relatively large difference between outturn and forecast in the non-residential element of the tax. The Welsh Government's LTT forecast performance was similar to that of the OBR and the SFC for property transaction taxes.

Landfill Disposals Tax

Outturn and Forecast Summary

A4.26 The 2019-20 outturn from LDT was £36.9m, as shown in the Welsh Revenue Authority (WRA) annual accounts[63]

[63] Available from:
https://gov.wales/welsh-revenue-authority-annual-accounts-2019-2020

A4.27 This is £6.1m lower than the Welsh Government's December 2018 forecast of £43m. This is a relative forecast difference of -17%[64].

December 2018 forecast performance

A4.28 Following the decomposition elements used for LTT and by the OBR, the differences between forecast and outturn have been allocated across a two-way classification:

1. Economic Factors
2. Modelling Factors[65]

A4.29 For LDT, the economic factors are limited. This is because the prices per tonne of waste are set in advance and increase in line with RPI.

A4.30 Modelling factors include any changes to the methodology, newly available waste data, changes to the assumptions regarding waste infrastructure and the interpretation of in-year revenue. The main elements of uncertainty are the total volume of waste and the split of waste between standard and lower rates, both of which would be classified as modelling factors.

A4.31 The model over-forecast both standard and lower rate waste for three reasons:

1. The main reason is that the model did not remove enough relieved and discounted waste. This meant that a greater proportion of waste was forecast to be taxable. At the time of the forecast there were only two quarters of WRA data available for LDT, meaning that there was very little information on the amount of discounts and reliefs that were likely to be claimed. The model was able to remove quarrying relief as this could be calculated using NRW data. However, water discounts and other reliefs could not be approximated using NRW data.

2. Volumes of lower rate waste were assumed to remain constant based on the trend over the previous three years. However, lower rate waste in 2019-20 fell substantially and was over 50% lower than forecast.

3. The model used an in-year revenue adjustment based on a profile derived from an eight year average of quarterly HMRC landfill tax data for the UK. This adjusted for the seasonal pattern to waste, with more waste being landfilled in the first two quarters of the financial year. The HMRC profile suggested that 54% of revenue would be due in the first two quarters. However in Wales in 2018-19 those two quarters accounted for 57% of LDT. The adjustment therefore over-estimated the amount which would be due in the final two quarters of 2018-19 and that higher tax base for 2018-19 as a whole was carried through to 2019-20.

How does this compare to other forecasters?

A4.32 The OBR's November 2018 forecast for 2019-20 LDT was £40m, £3m lower than the Welsh Government forecast. It did not take account of the second quarter of

[64] Relative forecast difference = (outturn-forecast)/outturn.
[65] The OBR also include policy factors, however the policy for landfill did not alter between the forecasts and therefore has had no impact.

LDT data, which actually pushed the Welsh Government's December estimate up and further away from the eventual outturn for 2018-19. The relative forecast difference between the OBR October forecast and outturn was -8%.

A4.33 The Scottish Fiscal Commission's December 2018 forecast for SLfT in 2019-20 was £15m lower than outturn. This is a relative forecast difference of +13%. The majority of this difference was due to delays in incineration capacity coming online.

Conclusions

A4.34 The December 2018 forecast for LDT was higher than outturn. Since this forecast, the model has been updated to address the highlighted issues where possible. As relieved and discounted waste cannot be estimated directly, NRW waste volumes are calibrated to WRA volumes excluding relieved and discounted waste. The Welsh seasonal profile is used for in-year adjustments rather than the HMRC profile. The forecast for lower rate waste has been updated to use a four-year average reduction. This means that atypical years have less of an impact on the forecast.

A4.35 Unlike LTT, there was no separate tax data for Wales for the predecessor to LDT. This forecast for 2019-20 was produced on the basis of two quarters of LDT data in 2018-19. Future LDT forecasts will benefit from a longer historical record.

Next steps for forecasting LTT and LDT

A4.36 Future forecasts for LTT and LDT revenues to accompany Welsh Government budgets will be published by the OBR. However, Welsh Government analysts will still play a role in the production of those forecasts using the models discussed here. The information obtained from this evaluation and from the process of undertaking the forecasts will help to inform future modelling changes and forecasting judgements.

A4.37 The OBR will publish evaluations of its devolved tax forecasts produced for the Welsh Government.

Annex five: Abbreviations used in this report

APD	Air Passenger Duty
CJRS	Coronavirus Job Retention Scheme
CVL	Core Valley Lines
CPI	Consumer Price Index
CTRS	Council Tax Reduction Scheme
DRS	deposit return scheme
E&NI	England and Northern Ireland
EPR	extended producer responsibility
EUSS	EU Settlement Scheme
GDP	Gross Domestic Product
HMRC	HM Revenue and Customs
IMG	Inter-Ministerial Group
LBTT	Land and Buildings Transaction Tax
LDT	Landfill Disposals Tax
LITRG	Low Income Tax Reform Group
LTT	Land Transaction Tax
NPV	net present value
NSND	non-savings non-dividend
OBR	Office for Budget Responsibility
OECD	Organisation for Economic Cooperation and Development
POM	placed on the market
SDLT	stamp duty land tax
SEISS	Self-Employment Income Support Scheme
SFC	Scottish Fiscal Commission
SPI	Survey of Personal Incomes

SSRN	Social Science Research Network
UKAL	UK Aggregates Levy
WRIT	Welsh Rates of Income Tax

Annex six: Contact details for further information

Further information about Welsh taxes is available on the Welsh Government's website:

https://gov.wales/welsh-taxes
https://llyw.cymru/trethi-cymru

You can contact us:

via the Welsh Treasury twitter accounts:

@WelshTreasury
@TrysorlysCymru

or by email:

WelshTreasury@gov.wales
TrysorlysCymru@llyw.cymru