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FSB Wales response

Implementation of the Wales Act 2014 and operation of the Fiscal Framework

September 2020

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About FSB Wales

FSB Wales is the authoritative voice of businesses in Wales, with around 10,000 members. It campaigns for a better social, political and economic environment in which to work and do business. With a strong grassroots structure, a Wales Policy Unit and dedicated Welsh staff to deal with Welsh institutions, media and politicians, FSB Wales makes its members' voices heard at the heart of the decision-making process.

Introduction

FSB Wales welcomes the opportunity to respond to the Senedd Finance Committee's inquiry into the operation of the Wales Act 2014 and the Fiscal Framework. Our primary interest in the inquiry relates to the first series of questions on taxation on which we have some evidence. We therefore make no comment on the fiscal framework and the operation of the Barnett Formula.

FSB Wales undertook a partnership with Bangor University funded by the ESRC to understand the impact of tax devolution to Wales. The report entitled *Funding Prosperity: Creating a New Tax System in Wales* looks at the experience of tax administration through the Land Transaction Tax.

The Welsh Government's tax principles, whether these have been met and whether the current tax regime and proposed new taxes align with these principles;

On the whole, FSB Wales believes the transition to devolved administration of taxation in Wales has been a positive experience. Of the Welsh Government's main aims such as a clear and stable tax system and a degree of involvement in tax policy, we are content that they have been achieved throughout this process. The devolved taxes have on the whole been well managed and as an organisation FSB Wales has been significantly involved and consulted on this process.

How successful the administration of Welsh taxes and the Welsh Rates of Income Tax has been;

The evidence gathered through our research partnership with Bangor University demonstrated that in respective of the Land Transaction Tax the Welsh Revenue Authority has performed well in its administration of the first of the devolved taxes. Despite this, significant challenges remain around awareness of devolved taxes amongst businesses in Wales.

In summary, our work which included the opinions of both businesses and professional services such as lawyers found that:

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1. The FSB survey responses and solicitor interview data indicate there is a low level of public awareness about Welsh devolved taxes, including LTT.

2. The majority of FSB member respondents reported they would like to receive information on devolved taxes from the Welsh Government. A small proportion reported they expect their accountants to make them aware of developing tax policy.

3. The WRA’s approach of engaging with, and encouraging participation from, solicitors who deal with LTT, has worked well in that there are very good levels of awareness and understanding reported by this targeted group.

4. Some solicitors pointed to a lack of clarity and guidance on certain aspects, including properties on the border between Wales and England.

5. The majority of FSB respondents perceived that the newly devolved taxes would increase complexity, and so the time and cost of compliance. This should be interpreted in the context of the low awareness and understanding of the newly devolved taxes. It suggests that a lack of awareness increases uncertainty for small business owners with concerns about increased complexity. It also indicates the scope to counter some of these concerns by helping taxpayers become better informed.

6. Solicitors are an important channel for increasing awareness of devolved taxes and disseminating information about the new LTT to taxpayers. Some solicitors reported an increased burden for making taxpayers aware of the new LTT, in cases where they had to deliver bad news about an increase in the tax payable.

7. There was an overwhelming preference reported from small business owners and solicitors to deal with Welsh Government officials, such as the WRA, rather than non-Welsh Government officials, such as HMRC. Solicitors reported receiving timely, detailed and meaningful assistance from WRA officials in comparison with HMRC.

8. Concerns were expressed about the potential for the different rates between LTT and SDLT to influence taxpayer behaviour, and lead to distortions in the property market, particularly close to the border.

9. The survey prompted some respondents to become aware of devolved taxes in Wales for the first time. This reinforces the importance of the work carried out by the FSB in keeping members up-to-date on important issues affecting them.

It is important to acknowledge that the data for the study above was gathered during the summer of 2018 at the very first instance of LTT being devolved. It is therefore

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reasonable to assume that some of the issues such as awareness of devolved taxes may have developed since.

Nonetheless, many of the issues identified will be relevant to the Committee's inquiry and the general point about the experience of transition on the whole being positive still stands.

What possible future tax changes could look like and what scope there is for a different approach to taxation in Wales;

FSB Wales feels that the scope of devolved taxation powers available to Welsh Government are now sufficient enough to clearly articulate a Welsh tax policy. As such, we have developed proposals for an enterprising Welsh tax policy that aims to support entrepreneurship and business growth during the next Welsh Parliament term. Our proposals can be found here, but in summary we advocate the following policies.

Non-domestic rates:
The general consensus is that the current system is unfit for purpose, but a complete abolition would cost too much. Abolition could also create a very imbalanced landscape across the UK. Options therefore focus on either replacing or reforming the current regime. Welsh Government has itself commissioned work from Bangor University into a Land Value Tax and has committed to reviewing both of those options in the medium term[1]. Similarly, in recent years small alterations have been made on a UK basis including moving from an RPI to CPI inflation measure, promising (although not yet delivering) more frequent revaluation and changes to the appeals process.

For our part, we believe the next Welsh Government could go further in reforming the tax, while continuing to review options for future replacement. Whilst not addressing all the issues with NDR, we believe the following would help facilitate a more enterprising tax policy:

1) **Relieve the rates burden by introducing a Business Rate Freeze for the life of the next Senedd**

Over time, business rates has increased as a cost faster than other taxes and general prices, making property and in particular property on the high street, less attractive. To rectify this, the next Welsh Government could introduce a business rates multiplier freeze. The impact on individual businesses would not be large, but over time a freeze would rebalance the size of rates as a tax and make occupying property more viable, particularly in more valuable locations such as the high street.

2) **Move from a revaluation cycle to rates indexing**

The revaluation process for business rates happens every five years at present and sees major winners and losers in terms of sectors and towns in Wales. It's a painful exercise and in recent

[1] Ap Gwilym, R; Jones, E; & Rogers, H. 2019. *A technical assessment of the potential for a local land value tax in Wales*. Cardiff: Welsh Government, GSR report number 17/2020 [Online]. Available at: https://gov.wales/sites/default/files/statistics-and-research/2020-03/technical-assessment-of-the-potential-for-a-local-land-value-tax-in-wales.pdf (accessed 31st July 2020)

years economic turbulence (following 2008 and the current crisis caused by Covid-19) have meant governments are unwilling to carry out revaluations. We believe the next Welsh Government could look to introduce local property indices instead which would be regularly updated and maintained by the VOA in Wales and would remove the need for a revaluation process. This has been proposed by Prof Gerry Holtham in a paper done for us previously and more recently by the Institute for Fiscal Studies in their submission to the Westminster Treasury Committee's review on NDR.

3) **Minimise the cost of appeals**

One benefit of more frequent revaluations or indexing is that it could lower the frequency of appeals. The present system generates a large number of appeals to the revaluation process and is often a cause of difficulties for businesses who often fall victim to unscrupulous agencies purporting to help with the appeals process. Furthermore, Wales should not introduce further costs for the appeals process as has happened in England through the *Check, Challenge, Appeal* process. Instead, where possible we should look to make the appeals system simpler and the overall process of rating and revaluations more approachable for SMEs.

4) **Increase the role of the Welsh Revenue Authority on Rates**

The creation of the Welsh Revenue Authority has created new possibilities for tax administration in Wales. FSB Wales would like to see the current system of 22 local authority billing authorities removed and the responsibility placed instead with the Welsh Revenue Authority.

5) **Introduce a new Investment Relief**

One of the largest issues around NDR is its disincentive to investment. Currently, new properties and elements of plant and machinery are included in the rating process and bring with them an increased bill. The Scottish Government has introduced a Business Growth Accelerator Relief to deal with these issues, leaving new build and improvements a 12 month period before rates liability applies. We think the next Welsh Government could match this and go further by removing certain types of new investments from the rating process completely by introducing an Investment Relief for improvements that accord with government ambitions on productivity and decarbonisation – for instance new plant and machinery and new energy efficiency investments.

6) **Review existing reliefs**

It is important that any reliefs introduced through the business rates system are subject to regular reviews in order to ensure they are effective in their stated aims and achieving good value for businesses and the taxpayer.

Income Tax

7) **Commit to no income tax rises above England during the next Senedd**

FSB Wales believes that the next Welsh Government should make a commitment to at the very least maintain the same tax rates as currently exist in England. By doing this, revenues will be maintained that can be used to fund public services and investment in infrastructure whilst businesses will not be at a competitive disadvantage to their counterparts in England in recruiting their workforce

Land Transaction Tax

8) **The next Welsh Government should maintain the 1 per cent lower band for the Land Transaction Tax between £150,000 and £250,000.**

The Welsh Government budget for 2018/19 set out the first rates and bands for the Land Transaction Tax. In relation to non-residential transactions the Welsh Government reduced the rate between £150,000 and £250,000 from 2 per cent (as currently applies in England) to 1 per cent.[2] This essentially halves the cost of tax on transactions between these values.

Corporation Tax

Corporation tax has a significant impact on the attractiveness of Wales not only as a location for foreign direct investment but on the profitability of domestic businesses.

9) **Revisit the proposals of the Holtham Commission on GVA weighted Corporation Tax reductions**

The Holtham Commission which undertook its work between 2008 and 2010 recommended that the then Welsh Government should explore the feasibility of corporation tax devolution. However, it did not favour a blanket devolution; rather it called for the ability to vary corporation tax in Wales in line with Wales' relative GVA performance. Whilst this recommendation has not come to pass, we believe it warrants further consideration.

New Taxes

10) **Introduce an SME test for any new Wales specific taxes**

The Welsh Parliament now has capacity to introduce new Welsh specific taxes in Wales through a consenting process through the UK Parliament. FSB Wales is not currently convinced of the need for new taxes at this moment in time, but should a future Welsh Government decide to pursue this route then an SME test should be introduced in order to ensure it does not disproportionately impact on SMEs. Such a test would involve ensuring new taxes do not provide barriers to entrepreneurship, innovation and business growth, is not unduly punitive on certain types of businesses and is not merely aimed at raising revenue without a reasonable justification for doing so.

How the mechanism for devolving powers for new Welsh taxes has been performing.

FSB Wales has little evidence upon which to judge the process for devolving powers for new Welsh taxes. We have been involved in various consultations on all four of the early proposals for new taxes. However, the proposals have all been at a very early stage and it has therefore been difficult to discern the direct business impact of some of the proposals. We are not aware of the progress of the intergovernmental discussion on new taxes and as such are unsure as to whether the new taxes are being pursued as a matter of priority.

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[2] Welsh Government. 2018. *Welsh Tax Policy Report* [Online]. Available at: https://beta.gov.wales/sites/default/files/publications/2018-06/welsh-tax-policy-report.pdf (accessed 11th September 2018). P.51

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Conclusion

FSB Wales welcomes the opportunity to inform the Finance Committee's inquiry into the operation of devolved taxes in Wales. We hope our evidence is of interest and would be happy to discuss the points raised with the committee further should it be of use.

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