

Agenda – Finance Committee

Meeting Venue:	For further information contact:
Video Conference via Zoom	Bethan Davies
Meeting date: 28 September 2020	Committee Clerk
Meeting time: 14.30	0300 200 6372
	SeneddFinance@senedd.wales

In accordance with Standing Order 34.19, the Chair has determined that the public are excluded from the Committee's meeting in order to protect public health. This meeting will be broadcast live on www.senedd.tv

1 Introductions, apologies, substitutions and declarations of interest

2 Paper(s) to note

(14.30)

(Pages 1 – 3)

Minutes of the meeting held on 21 September 2020

3 Inquiry into the implementation of the Wales Act 2014 and operation of the Fiscal Framework – Evidence session 1

(14.30–15.30)

(Pages 4 – 20)

Robert Chote, Chairman, Office of Budget Responsibility

Supporting papers:

[Consultation responses pack](#)

Summary of consultation responses

Research Brief

BREAK (15.30–15.40)



- 4 Inquiry into the implementation of the Wales Act 2014 and operation of the Fiscal Framework – Evidence session 2**
(15.40–16.20) (Pages 21 – 38)
Adrian Crompton, Auditor General for Wales

Supporting papers:

FIN(5)–17–20 P1 – Audit Wales
Research Brief

- 5 Motion under Standing Order 17.42 to resolve to exclude the public from the remainder of the meeting**
(16.20)
- 6 Inquiry into the implementation of the Wales Act 2014 and operation of the Fiscal Framework: Consideration of Evidence**
(16.20–16.35)
- 7 Inquiry into a legislative budget process**
(16.35–16:45) (Pages 39 – 41)
- Supporting papers:**
FIN(5)–17–20 p2 Welsh Government response

Concise Minutes – Finance Committee

Meeting Venue:

This meeting can be viewed

Video Conference via Zoom

on [Senedd TV](#) at:

Meeting date: Monday, 21 September
2020

<http://senedd.tv/en/6553>

Meeting time: 14.30 – 16.58

Attendance

Category	Names
Assembly Members:	Llyr Gruffydd MS (Chair) Alun Davies MS Mike Hedges MS Rhianon Passmore MS Nick Ramsay MS Mark Reckless MS
Witnesses:	Adrian Crompton, Auditor General for Wales, Audit Wales, Auditor General for Wales, Audit Wales Isobel Everett, Audit Wales Georgina Haarhoff, Welsh Government Andrew Hobden, Welsh Government Kevin Thomas, Audit Wales Kirsty Williams MS, Minister for Education Sara James, Welsh Government
Committee Staff:	Bethan Davies (Clerk) Leanne Hatcher (Second Clerk)



	Georgina Owen (Second Clerk) Mike Lewis (Deputy Clerk) Owen Holzinger (Researcher)
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1 Introductions, apologies, substitutions and declarations of interest

1.1 The Chair welcomed Members to the virtual meeting of the Finance Committee.

1.2 Apologies were received from Siân Gwenllian MS.

2 Paper(s) to note

The minutes were noted.

3 Curriculum and Assessment (Wales) Bill: Evidence session

3.1 The Committee took evidence from Kirsty Williams MS, Minister for Education; Georgina Haarhoff, Deputy Director, Curriculum, Bill – Senior Research Officer; Sara James, Head of Schools Research, Knowledge and Analytical Services; and Andrew Hobden, Economist, Economic Advice Division on the Curriculum and Assessment (Wales) Bill.

4 Oversight of the Wales Audit Office – Scrutiny of the Annual Report and Accounts 2019–20 and the Annual Plan 2020–21: Evidence session

4.1 The Committee took evidence from Adrian Crompton, Auditor General for Wales; Isobel Everett, Chair of the Wales Audit Office Board, Audit Wales; and Kevin Thomas, Executive Director Corporate Services, Audit Wales on the Annual Report and Accounts 2019–20 and the Annual Plan 2020–21.

4.2 Audit Wales agreed to provide further details on the calculation of the payback period for the management restructure.

5 Motion under Standing Order 17.42 to resolve to exclude the public from the remainder of the meeting

5.1 The motion was agreed.

6 Oversight of the Wales Audit Office – Scrutiny of the Annual Report and Accounts 2019–20 and the Annual Plan 2020–21: Consideration of evidence

6.1 The Committee considered the evidence received.

7 Curriculum and Assessment (Wales) Bill: Consideration of evidence

7.1 The Committee considered the evidence received.

Agenda Item 3

By virtue of paragraph(s) vi of Standing Order 17.42

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Reference: AC/207/SD

Date issued: 4 September 2020

Dear Llyr

Inquiry into the implementation of the Wales Act 2014 and operation of the Fiscal Framework

Thank you for giving me the opportunity to contribute to the above inquiry. Prior to my attendance in person at the Finance Committee on 28 September, I thought it would be useful to set out some key details of my work and responsibilities in this area.

As you'll be aware, as Auditor General for Wales, I am responsible for the statutory audit of the financial statements of the Welsh Revenue Authority (WRA), and I have the legal power to scrutinise the economy, effectiveness and efficiency of how the WRA and other Welsh public bodies use public money. Consequently, my responses here relate only to my areas of responsibility.

Some areas of this inquiry relate to the merits of government or taxation policy, rather than its implementation, and it would be inappropriate for me to provide responses in these areas.

I should also mention another limitation on my role in relation to Welsh tax matters. This concerns the administration of the Welsh Rates of Income Tax (WRIT), which is administered and collected by HM Revenue & Customs (HMRC), who in turn fall under the audit remit of the Comptroller & Auditor General. I understand that the C&AG will be responding separately to this inquiry and so may be able to provide further evidence on the administration of WRIT, as well as any other work that the National Audit Office has carried out on devolved funding mechanisms.

However, I set out the areas below where I can contribute to this inquiry and hope that the information proves to be of use.

Taxation

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

You will be aware that, between 2016 and 2018, I issued three reports monitoring the implementation of fiscal devolution in Wales, the establishment of the WRA and arrangements to collect Welsh Rates of Income Tax (WRIT). These reports are available on the Audit Wales website. In our closing 2018 report¹ we concluded that:

- the WRA has operated effectively to date to administer devolved taxes in Wales; and
- the Welsh Treasury has appropriate arrangements in place to obtain assurance over HMRC's implementation of Welsh Rates of Income Tax.

Since 2018, I have been responsible for the statutory audit of the accounts of the WRA and have recently completed my audit of the 2019-20 Annual Accounts. These statutory audits have not identified any significant issues in the WRA's financial statements, nor have I needed to report any shortcomings in controls or processes to the WRA Board. I have provided an unqualified audit opinion for the WRA's 2018-19 and 2019-20 financial statements.

As noted above, WRIT is administered and collected by HM Revenue & Customs (HMRC). The C&AG is responsible for the audit of HMRC and has issued two reports to date on the administration of WRIT for 2017-18² and 2018-19³. His key findings from 2018-19 were as follows:

- HMRC has established a project governance structure within its wider devolution and change programme and it is engaging with Welsh Government representatives across the full range of project activities;
- maintaining a complete and accurate database of Welsh taxpayers is important to ensuring that HMRC can collect the correct amount of tax from Welsh taxpayers and allocate this to the Welsh Government;
- HMRC regularly communicates with a diverse range of external audiences including employers, pension providers and other businesses that deliver payroll-related services to help ensure the Welsh rates of income tax project is implemented as intended; and

¹ <https://www.audit.wales/publication/fiscal-devolution-wales-devolved-taxes-and-welsh-rates-income-tax>

² <https://www.nao.org.uk/report/administration-of-welsh-income-tax-2017-18/>

³ <https://www.nao.org.uk/report/the-administration-of-the-welsh-rate-of-income-tax-2018-19/>

- in 2018-19, HMRC incurred and recharged £5.8 million of costs for implementing WRIT.

With the audit of HMRC and its administration of WRIT being a matter for the C&AG, my role in assessing the success of the administration of Welsh taxes and the WRIT, and making recommendations for improvements, is restricted to value for money examination and study powers in relation to the WRA and the Welsh Treasury⁴.

My ability to undertake data matching in relation to Welsh tax administration is not as well developed for the WRA and Welsh Treasury as it is for local government. And as I and my predecessor have mentioned before, my data-matching powers need updating⁵. In particular, my power to conduct data-matching exercises⁶ is confined to the purpose of 'assisting in the prevention and detection of fraud in or with respect to Wales', which precludes, for example, exercises to identify recoverable debt. Also, I am only able to require local authorities and NHS bodies in Wales to provide data; other bodies, such as the WRA, may provide information for such exercises on a voluntary basis, or they may choose not to.

Generally, I exercise my data-matching powers in conjunction with the UK-wide National Fraud Initiative (NFI)⁷. To date, the NFI has identified £42.9 million in fraud and overpayments in Wales, including in respect of local taxation. In the most recent exercise (2018-19), data-matching claims for Council Tax Single Persons Discount against sources such as the electoral register identified 3,939 fraudulent or erroneous claims resulting in Council Tax underpayments of £4.6 million. And currently I am piloting an approach to identify false claims for business rate relief under the Covid-19 relief measures.

Clearly, the implementation of Welsh tax-raising arrangements presents risks of fraud, error and uncollected debt, which may be addressed by data matching. Indeed, the WRA has recognised the value of data matching, and has already developed work using its own investigation powers and data sharing using the Digital Economy Act 2017. Nevertheless, I consider that there is scope for significant benefit to both the WRA and other Welsh public bodies from updating my data matching functions. The NFI holds data that would assist the WRA identify fraud and uncollected debt, and the WRA holds data that would similarly assist other public bodies.

⁴ Under section 32 of the Tax Collection & Management (Wales) Act 2016 and section 135 of the Government of Wales Act 2006, together with section 145A of the Government of Wales Act 1998

⁵ See for example [letter from Huw Vaughan Thomas of 5 April 2017](#)

⁶ Under s64A of the Public Audit (Wales) Act 2004

⁷ Together with the Minister for the Cabinet Office, Audit Scotland and the Comptroller & Auditor General Northern Ireland.

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

My comments in this area are largely restricted to my reviews of fiscal devolution between 2016 and 2018, as mentioned above. These reports found that the legislative framework for the devolution of Land Transaction Tax and Landfill Disposals Tax was scheduled and implemented effectively and in good time. Primary legislation was given Royal Assent well before the introduction of the taxes themselves, and relevant secondary legislation was also passed to ensure that the WRA was awarded the relevant powers and duties to collect these devolved taxes from 1 April 2018.

Furthermore, our 2018 report confirmed that UK legislation required for the implementation of WRIT was drafted and passed in time to allow tax collection from 1 April 2019. Outside these reports, we note that WRIT resolutions to confirm the Welsh rates each year were also passed prior to the start of each tax year by the Senedd:

- for the 2019-20 income tax year, the WRIT resolution was approved by the Senedd in plenary on 15 January 2019; and
- for the 2020-21 income tax year, the WRIT resolution was approved by the Senedd in plenary on 3 March 2020.

The fiscal framework

Consider the fiscal framework processes and how funding is allocated to the Welsh block grant

The bulk of the Welsh Government's funding comes through the Barnett Formula. On our Guide to Welsh Public Finances, we provided a simple explanation to help the public understand how the formula works. I have repeated the relevant sections from our guide to help support the Committee's consideration of the Barnett formula and the needs-based element introduced in the fiscal framework.

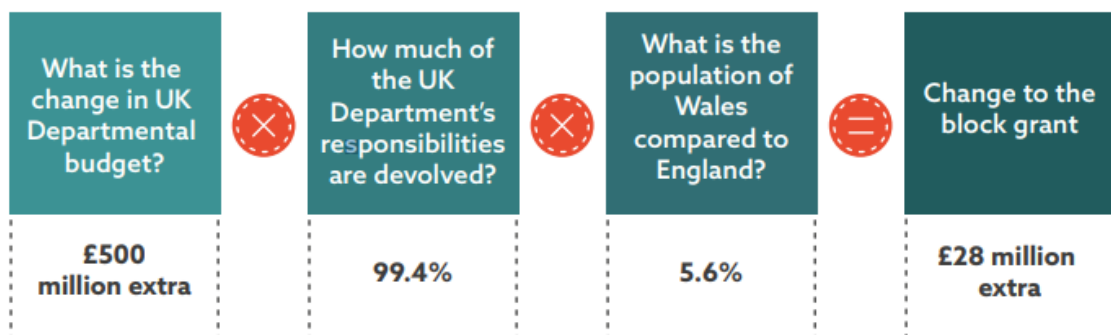
The UK Government makes no direct decisions about how much money to allocate to Wales for devolved services. The UK Government's decisions relate to its own departments, which cover spending in England and non-devolved spending elsewhere. Those decisions have an automatic impact on the block grant to Wales through the Barnett formula.

The formula is about annual changes. It determines how much more (or less) money Wales gets through the block grant each year of the spending review period. The 'baseline' for these changes derives from the block grant in the year preceding the spending review period. The Barnett formula then translates changes in UK Government departmental budgets into an amount that will be added to (or be taken from) the block grants for devolved bodies. The Barnett formula as it applies to Wales asks three simple questions:

1. How much has the UK Department's budget changed by?

2. What percentage of the policy area, the UK Department is responsible for, has been devolved?
3. What is the population of Wales compared with England?

Figure 1 shows how the formula would work in practice if the UK Government increased the budget of the UK Department for Health to spend £500 million more on the NHS in England

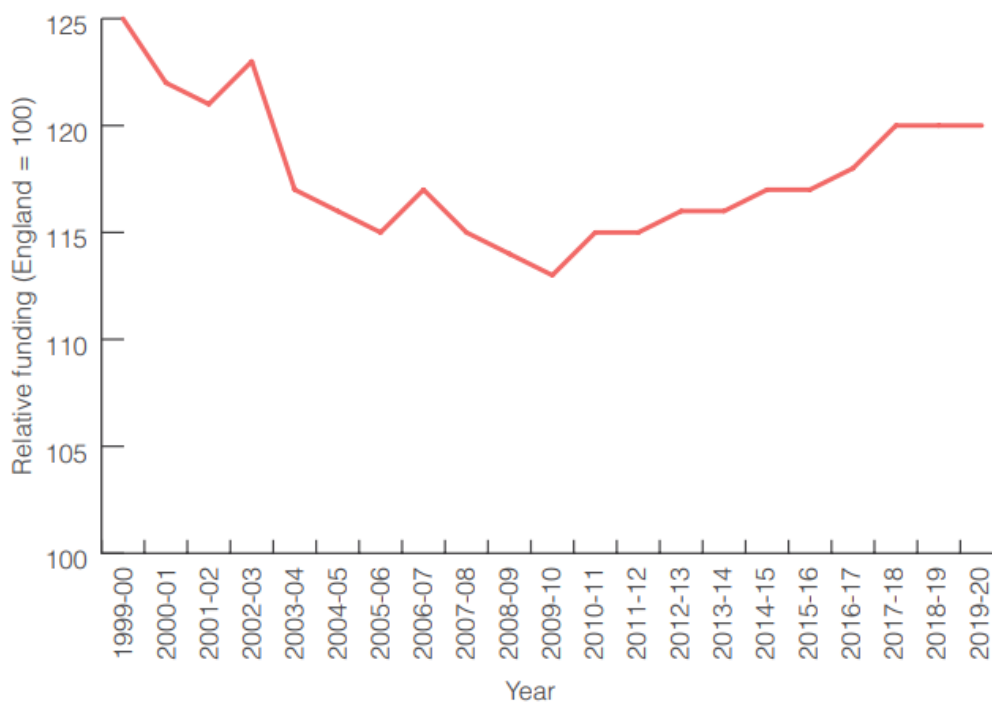


The UK Government runs this calculation across all of its departments to produce an overall net figure. Prior to 2018-19, this is where the calculation would end. The net change would be added to (or taken away from) the previous year's block grant, to produce the block grant for that year.

However, the 2017 Fiscal Framework agreed between the UK Government and the Welsh Government, introduces a 'needs factor' to address two long-standing concerns:

- that the Barnett formula failed to reflect the higher levels of need in Wales. Wales has an older, poorer, sicker and more dispersed population than England. As a result, Wales has a greater need for public services and funding. In 2010, the Holtham Commission identified that for every £1 spent on services in England, Wales needs between £1.14 and £1.17 for devolved services.
- 'convergence': one of the effects of the formula is that when budgets in England rise, spending in Wales, per head of population, gets squeezed towards the same level as England. Conversely, when the budgets in England fall, there is a tendency to diverge, with spending per head in Wales falling proportionately more slowly than in England.

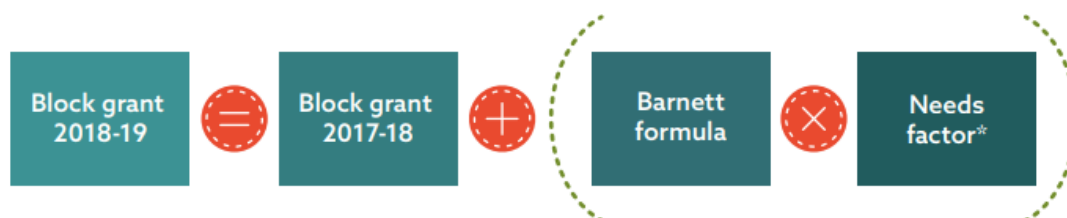
The 'needs factor' aims to ensure that Wales always gets at least 115% funding per head of population for devolved services, compared to England. The data set out in the Fiscal Framework shows that, since the start of devolution in 1999-2000 there were only two years – 2008-09 and 2009-10 – where the funding fell below the 115% level. In 2019-20, Wales had around £1.20 for every £1 allocated to equivalent services in England.



Source: The agreement between the Welsh Government and the UK government on the Welsh Government's fiscal framework (generally known as The Fiscal Framework)

The needs factor involves multiplying the change in funding as a result of the Barnett formula by a set percentage. Because Wales currently gets above the 115% level, the introduction of the needs factor is phased. Initially, the figure will be 105%. This will apply until funding levels gradually converge at 115%. At that point, the needs factor will change to 115%. It is difficult to estimate how long it will take to reach the point of convergence. The additional needs factor is applied to increases in spending relative to the 2017-18 baseline. **Figure 2** shows an example of how the needs formula combines with the Barnett formula to create the block grant for 2018-19.

Figure 2



*the needs factor only applies if the Barnett formula results in a net increase to the block grant relative to the 2017-18 baseline.

As part of its inquiry, the Committee may wish to explore with the Welsh Government how the new needs-based formula will work if we return to a period of austerity in future. As drafted, the needs-based formula involves multiplying the change as a result of the Barnett formula (whether that is an increase or a reduction) by either 105% or 115%. The Fiscal Framework sets out a degree of temporary protection from amplifying cuts, stating that:

‘From 2018-19 and for the remainder of the current spending review period, all uplifts to Welsh Government DEL above the level in 2017-18 will attract the 105% factor, while any reductions below the 2017-18 level will be applied without the additional factor.’

The wording of the Fiscal Framework suggests that in future spending review periods, cuts to devolved funding could be multiplied by either 105% or 115%, depending on relative funding levels at the time. It may seem perverse, but the cuts to the block grant will be bigger if the funding gap to England has reduced. This situation seems contrary to the purpose and spirit of the fiscal framework.

I hope you find this information useful to your inquiry and I look forward to attending in person on 28 September.

Yours sincerely



Adrian Crompton
Auditor General for Wales

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Finance Committee's Report: Inquiry into a legislative budget process

The Welsh Government has welcomed the opportunity of this inquiry to reflect on the changes to the Budget process over the course of this administration and the suitability of the current arrangements, building on close working between the Welsh Government and the Finance Committee over many years to improve these processes.

During this term there have been significant increases in the fiscal responsibilities of the Senedd, representing a significant milestone in the devolution journey for Wales and placing even greater emphasis on the Budget process.

Context for Review of the Budget Process

In recognition of these additional fiscal responsibilities, the Welsh Government engaged with the Finance Committee's inquiry into Best Practice Budget Process, which resulted in an agreed Budget Process Protocol in 2017. These changes were introduced in the 2018-19 Budget and followed in the two Budgets since then.

In this period a number of uncertainties, such as the UK's exit from the EU, more frequent UK elections and now the pandemic, have impacted on UK fiscal events and hence the timing of the Welsh Government's annual Budget. Under these exceptional circumstances the Budget Protocol has provided sufficient flexibility to enable Budgets to be produced by the Welsh Government without unduly compromising the scrutiny arrangements. The exceptional circumstances of the period since the changes agreed in 2017 has, however, also impacted on the ability to fully review the impact of these changes.

Despite these circumstances, the Welsh Government has continued to work to improve the transparency of Budget proposals and has included progressively greater levels of detail and supporting information. Working with the Committee, the Welsh Government has acknowledged the complexity of the information presented at various points of the cycle and the variety of purposes for which stakeholders use the information. This has led to the publication of a number of additional supporting documents as part of the Budget package to improve understanding and aid transparency.

Case for a legislative process

The Welsh Government agrees that any process needs to have the flexibility to cope with the UK Government's recent variable and unpredictable timetable for fiscal events. As identified earlier, the current process has provided sufficient flexibility to allow for 8 weeks scrutiny of the Welsh Government's budget proposals despite delays caused by the UK Government. However it is important to recognise that a legislative process will have additional time restrictions, including the Llywydd's determination period, and the intimation period before obtaining Royal Assent, all before the start of the financial year, factors which will adversely impact on timescale

flexibility and, potentially, scrutiny. This is also of significant importance to providing early funding certainty for delivery partners.

Whilst the Welsh Government acknowledges the principle of an equitable balance of control between the legislature and the executive, it is the Welsh Government's assessment that the current process allows the Senedd all the benefits identified in their inquiry that it would want from a legislative process. Before undertaking such reforms there would therefore need to be clear additional benefits identified which are not available within the context of the current process.

The Welsh Government notes the Committee's consideration of the position in Scotland. This current process provides for the Senedd to propose amendments following the laying of the Draft Budget that is equivalent to the legislative process for the Scottish Budget.

The Welsh Government's ambition to provide multi-year settlements whenever possible has been stated on many occasions. However the ability to provide longer-term funding certainty is dependent on the UK Government's spending rounds and not related to the Welsh Government's own budget process and any considerations of a legislative budget process.

Finance Bill

The Welsh Government agrees with the Finance Committee's view that a Finance Bill covering taxation and spending plans will raise a number of complexities and would need very careful consideration. It is also generally understood that Budget legislation is a method specifically for approving overall spending limits and tends to be a simplified legislative procedure that limits non-government amendments, with an accelerated timescale to ensure timely approval before the start of the financial year. Introducing other, potentially highly complex elements such as tax changes as part of the same legislative vehicle could either compromise the approval of spending plans before the start of the financial year, also impacting on the ability to provide funding certainty to partners and stakeholders, or could, conversely, reduce the time for proper scrutiny of tax changes.

The Welsh Government is already committed to using legislation where there is a demonstrable impact for doing so. As the Finance Committee has identified, the Welsh Government has issued a consultation on a proposal for a Bill for Year One of the next Senedd that will provide Welsh Ministers with a mechanism for making changes to the Welsh Tax Acts at short notice as required, while allowing for proper scrutiny by the Senedd. It is hoped that the Welsh Government and the Finance Committee can work collaboratively to bring this legislation forward and, following implementation, assess how well it meets Welsh tax legislation needs.

Alignment of Budget and Accounts

The Welsh Government continues to make progress to align budgeting and accounting boundaries to aid transparency and engagement of the Budget process. To date, 23 central government bodies are designated under the Government of Wales Act 2006 (Budget Motions and Designated Bodies) Order 2018 (as amended). It is aimed that this alignment exercise will be completed by March 2022.

Forecasting

For the first time the 2020-21 Draft Budget was accompanied by independent forecasts of devolved tax revenues from the Office for Budget Responsibility. The Welsh Government appreciates the Finance Committee welcoming the steps that have been taken with publication of taxation and borrowing plans and forecasts at the time of the outline Budget and the commitment to update these forecasts in-year and reporting on outturn.

Engagement

In line with the Finance Committee's own desire to engage with the public in Budget scrutiny, the Welsh Government is committed to improving wider transparency and understanding of spending priorities. This has included in recent years increased engagement and scrutiny prior to publication of the Welsh Government's Draft Budget. As part of this ongoing improvement, the continued input of the Committee on how Welsh Government engagement could be strengthened further is welcome.

Next Steps

Following discussions with the Finance Committee, the Welsh Government agreed to build on the steps taken last year and to hold a debate in Plenary before the summer recess, focusing on strategic issues. Further discussion on how improvements can be made to the current approach and the opportunity to further develop pre-Budget scrutiny would be welcomed.

The Welsh Government appreciates the consideration of the Finance Committee of the current position and, given the forthcoming election, agrees that consideration of any future changes is a matter for the sixth Senedd. As part of these future considerations, the Welsh Government would be open to considering establishing a joint body of the Government and Senedd, with invited independent experts as was the case in Scotland, to review the benefits and issues of introducing further reforms to the Budget process.