



Dadansoddi  
Cyllid Cymru  
Wales Fiscal  
Analysis

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Annwyl Gadeirydd,

14 Hydref 2021

### Session on Understanding the Financial Position in Wales

Thank you for the invitation to meet members of the Finance Committee for the Sixth Senedd. Because there was (as always) so much to discuss, I suggested that I would send a short letter to sum up some final points that we did not have chance to consider, namely those issues that colleagues at Wales Fiscal Analysis and I believe are likely to deserve the most scrutiny and attention during the forthcoming Senedd term. Other matters potentially deserving of committee attention such as Covid-19 funding and potential reforms to Council Tax were discussed during the session so are not included below.

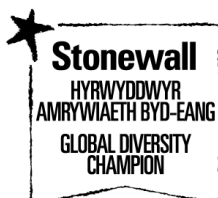
#### The Fiscal Framework and Devolved Taxes

Wales' fiscal framework has been tested by the coronavirus pandemic in a manner that could not have been imagined during the negotiations in 2016. It is to the credit of everyone involved in those negotiations that the complex mechanisms for implementing devolved taxes have proved more than fit for purpose. Not only have the block grant adjustment mechanisms protected the Welsh budget from a serious UK-wide economic shock in the way in which they were designed, but the new devolved-taxes-plus-block-grant system has increased funding to public services in Wales relative to the previous block grant-only system.

Three factors are worth considering when assessing the impact of the fiscal framework since its introduction. First, Wales' population relative to England's has stopped falling, with estimates for the year to mid-2020 suggesting that Wales' population grew more rapidly than every other UK country. Population decline was one of the areas in which the Welsh Government (unlike the Scottish Government) agreed to take on budgetary risk; so far this decision has paid off. Second, partly in return for accepting this risk (and the so-called Comparable Model for calculating block grant adjustments),<sup>1</sup> a 105% multiplier termed the Needs Based Factor was added to the Barnett Formula. Given the extraordinary increases to the Welsh budget required to respond to Covid-19, this multiplier alone has boosted the Welsh budget by approximately £471 million over recent years, based on our analysis of Block Grant Transparency data published in June 2021. Third, because the latest forecasts suggest devolved revenues are performing better than initial forecasts, we currently expect positive budget reconciliations with respect to income tax of approximately £30 million in 2023-24 and £66 million in 2024-25.



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Despite this strong performance, the Welsh Treasury and Finance Committee will need to remain vigilant in probing tax forecasts and the operations of Welsh taxes. Both the OBR and HMRC are under Welsh Government contracts to respectively forecast taxes and operate the Welsh income tax system, and these operations should necessitate at least annual scrutiny. For example, confirming that OBR's tax forecasts reflect factors specific to the Welsh economy, and that HMRC continue to ensure that all Welsh taxpayers are correctly identified with a C tax code (including hard-to-reach and transient populations). The Committee may also wish to continue to scrutinise the innovative tax collection approaches that have been adopted by the Welsh Revenue Authority, the body responsible for collecting Land Transaction Tax and Landfill Disposals Tax.

Finally, the Committee will also want to keep under review the upcoming renegotiation of the Scottish Fiscal Framework. While the Welsh Government and Senedd are not involved in this bilateral negotiation, if there are changes agreed to Scotland's fiscal framework these may set precedents which may influence future Welsh arrangements.

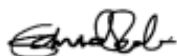
## Social Care

On 7 September 2021 the UK Government announced plans to reform how people pay for adult social care in England, and the following week Parliament passed plans for a 1.25 percentage point National Insurance increase, termed the Health and Social Care Levy. Because the amount of National Insurance raised in Wales is smaller than Wales' share of the UK population, the Welsh Budget stands to benefit from the decision to raise taxes at a UK-level (and to subsequently transfer funds via the Barnett Formula) rather than by using devolved tax levers. Moreover, because there is already a more generous asset threshold in place in Wales (£50,000 compared with £23,250 in England), and because self-funders constitute a smaller percentage of care home residents compared with the rest of the UK, the Barnett share of Health and Social Care Levy funding may go further than it will do in England.

However, the committee may wish to note several remaining challenges. Although the new levy is expected to raise approximately £36 billion for English services in the first three years, during this period only £5.4 billion will be directed at social care, while the remaining £30.3 billion will be directed at the NHS.<sup>2</sup> This would leave social care underfunded because the announced reforms in England are expected to require up to an additional £5 billion per year by the second half of the 2020s.<sup>3</sup> In the Welsh context, it will be important to ensure that additional funding allocated to local authorities and providers covers the cost of any proposed Welsh reforms, especially given the apparent funding gap that might be anticipated in England.

If you would like to discuss topics raised during the meeting or in this letter, or arrange any other meeting or briefing session, please don't hesitate to contact us.

Yr eiddoch yn gywir,



Dr Ed Gareth Poole  
Uwch Ddarlithydd, Prifysgol Caerdydd

cc. Owain Roberts, Clerc, Y Pwyllgor Cyllid

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<sup>1</sup> For full details on this method please see Poole, E.G., Ifan, G, and Phillips, D., *Fair Funding for Taxing Times? Assessing the Fiscal Framework Agreement*, February 2017. [Fair-Funding-for-Taxing-Times-Assessing-the-Fiscal-Framework-Agreement.pdf \(cardiff.ac.uk\)](https://cardiff.ac.uk/fair-funding-for-taxing-times-assessing-the-fiscal-framework-agreement.pdf)

<sup>2</sup> Oung, C. *How much of the health and care levy will social care receive and what is this intended to do?* Nuffield Trust, 10 September 2021. <https://www.nuffieldtrust.org.uk/resource/chart-of-the-week-how-much-of-the-health-and-care-levy-will-social-care-receive-and-what-is-this-intended-to-do>

<sup>3</sup> Ogden, K., Phillips, D. and Sion, C. *What's happened and what's next for councils?* IFS Green Budget chapter, 7 October 2021. <https://ifs.org.uk/publications/15673>

