WLGA Executive Board — Item 5

24 September 2021

THE SPENDING REVIEW AND THE LOCAL GOVERNMENT FINANCE SETTLEMENT 2022-23

Purpose

1. This paper sets out our current autumn finance timetable following the announcement of the Spending Review and future funding of health and social care announced on the 7 September.

2. At the last meeting of the Executive, the Welsh Government's Programme for Government and priorities around local taxation reform were touched upon. The second section of the paper summarises the research that the Welsh Government has carried out in the past.

3. In the final section we provide the latest feedback from the Welsh Government's Tax Engagement Group.

Spending Review and the Autumn timetable

4. The UK Government announced the Spending Review - Spending Review 2021 launch letter - GOV.UK (www.gov.uk) - on the same day as the health and social care announcement. The commissioning letter is set out in Appendix 1.

5. The three-year review will set UK government departments' resource and capital budgets for 2022-23 to 2024-25 and the devolved administrations' block grants for the same period.

6. According to the UK Government, core departmental spending will grow in real terms at nearly 4% per year on average over this Parliament. By 2024-25 that means that core departmental spending will be £140 billion more per year in cash terms than at the start of the Parliament.

7. The WLGA has commissioned a comprehensive survey of budget pressures that is due back from local authorities on the 17 September and the data from the survey will be used to inform a paper that will be presented to the Finance Subgroup later in the autumn. There are two possible dates for that meeting with final confirmation from the Welsh Government still awaited. A draft of the paper will be shared with Leaders to review on the 22 October.

8. The Welsh Government appear to be adhering to the proposed dates for their draft / provisional announcements in the run up to Christmas and final

announcements in March 2022. The current timetable for finance announcements is set out overleaf.

Autumn Timetable

07 September	Spending Review launched
14 September	WLGA Leaders and Senedd Session
14 September	Distribution Subgroup for 22-23 Settlement
17 September	Full SWT
17 September	**Survey Returns for Pressures 22-23 to 24-25**
24 September	WLGA Executive
06 October	WLGA Leaders and WG Ministers
12 October	Joint WLGA/LGA/COSLA/NILGA Finance Event
15 October	Joint Council for Wales
15 October	Full SWT
18 October (?)	Potential date for Finance Sub Group
25 October	Senedd Recess
27 October	OBR Forecasts published
27 October	**Spending Review and Budget**
01-12 November	UN Climate Change Conference (COP26)
04 November (?)	Potential date for Finance Sub Group
19 November	Full SWT
26 November	Last date for Finance Committee WG Budget consultation.
20 December	**Draft Welsh Government Budget published**
21 December	**Provisional LGF Settlement**
1 March	**Final Welsh Government Budget published (and LGF Settlement)**
8 March	**Final Budget debate**

Announcement on Health, Social Care and National Insurance

9. On the same day as the Spending Review announcement, the Prime Minister set out the UK government's plans for funding health and social care through a National Insurance increase.

10. The details affecting Social Care relate largely to England given the devolved nature of social care in Wales, Scotland and Northern Ireland. It will be a matter for the Welsh Government to implement the proposed changes. The details relating to National Insurance will affect the four nations as this is not a devolved matter. Whilst Health is devolved, the 7 September announcement covers funding for the NHS meaning there will be a share of the increase distributed to devolved administrations.

11. The announcement - [Build Back Better: Our Plan for Health and Social Care - GOV.UK (www.gov.uk)]() – represents the UK Government's attempt to address sustainable funding and reform of Adult Social Care.

12. On taking power the Prime Minister said he had a plan to reform social care. However, the intervening covid-affected period saw a concentration on dealing with the pandemic and this may explain why no detail has been forthcoming about the proposed reforms.

Scale of the Announcement

13. The Institute of Fiscal Studies (IFS) commented, 'the announcement constituted a Budget in all but name'. This is partly because it introduces a new tax (levy) and will see equivalent increases in health and social care spending. The announcement covers the next 3 years which means this is a major fiscal event.

14. From April 2022, there will be an increase of 1.25% on employee and employer national insurance contributions. This is in effect a 2.5% increase in the tax rate on employment earnings. It will also be extended to those in work who are over pension age. This is the first time that those over pensionable age will be required to pay national insurance. The IFS believes the combination of these factors means more unnecessary complication and has stated that 'a simple increase in income tax would have been preferable'.

15. The change means that from April 2022, everyone in the UK who currently pays National Insurance (NI) will have to pay an extra 1.25% contribution. Under the current system, people over retirement age who are still working don't pay NI. From April 2023, this extra contribution will no longer be taken from National Insurance but will be part of a new separate tax called the 'Health and Social Care Levy'. From April 2023, anyone working after state pension age will have to pay the extra tax. The IFS estimates that this will only contribute 2% of the overall tax rise from pensioner families whereas about two-thirds will come from families under the age of 50.

16. The use of National Insurance rather than income tax inevitably means the significant majority of the tax increase will be met by those of working age. Someone earning £30,000 per annum will pay an extra £255 in National Insurance.

17. The announcement means that a new tax has been created to fund Health and Social Care. It is a hypothecated, ring-fenced tax (levy) and to emphasise this it will be separated out on tax bills from 2023 following its introduction in April 2022. It is worth noting that hypothecated social care funding is not new in England; since 2016 local authorities in England have been able to hypothecate a social care council tax increase of up to 3% so long as they stay below what is in effect a 5% increase that would trigger a referendum requirement.

18. The main beneficiary of the announcement is the NHS. Over the next 3 years an estimated £36bn will be raised from which the NHS will receive around £25bn,

Social Care £5.4bn and approximately £6bn going to devolved administrations. On 6th September an extra £5.4bn was also announced for the next 6 months to deal with NHS backlog.

19. It has been stated that after 3 years the increased sums for the NHS will be redirected to social care because the Covid backlog will have been dealt with. However, commentators have raised the difficulties of stripping out this funding from the NHS and transferring it to the care system at a time when more demand for health services is likely.

20. The estimated £12bn raised annually is about 0.5% of GDP and comes on top of the £25bn increases in income tax (£8bn) and corporation tax (£17bn) already announced in the March 2021 Budget. The IFS indicate that the announcement pushes taxes to their highest sustained share of the economy and government spending is set to reach a record peacetime level.

21. The announcement also indicated an increase of 1.25% on dividend payments which will affect those receiving share dividends and self-employed limited company owners who are in receipt of dividends.

22. There is much of the Dilnot Commission's proposals included in the announcement. The approach has been described as a cap and floor arrangement. The key points are:

    22.1 From October 2023 someone will no longer pay more than £86,000 in care costs - that is, for actual care, rather than accommodation - over their lifetime.
    22.2 On reaching this cap, ongoing costs for personal care will be paid for by local authorities.
    22.3 If someone has between £20,000 and £100,000 in assets they will get means-tested help towards costs from their local authority.
    22.4 Those who own less than £20,000 will not have to pay towards care costs from their assets at all but might have to contribute from their income.

Impact of Announcement on Wales

23. The pre announcement position was that in England, Scotland and Wales, social care funding is via general grants to local government, locally raised funding and grants such as the Better Care Fund. The governments set requirements for what care should be provided but there is (was) no ringfenced funding for social care.

24. The devolved administrations all operate their own Health and Social Care systems. Current arrangements are that the three administrations are free to allocate funding received via the Barnett formula to meet national priorities and these need not reflect the approach taken in England. In fact, there has been divergence since devolution reflecting differences in policy. England's system is the least generous with the upper limit on means tested social care being

£23,250 compared with Wales where the limit is £50,000 for residential care and £24,000 for home care. In Wales home care costs are capped at £100 per week and home care is largely free in Northern Ireland.

25. In response to the announcement David Phillips, an associate director at the IFS said:

    "The prime minister has said that the funding the devolved governments in Scotland, Wales and Northern Ireland receive as a result of the health and social care levy will be "directed" by the UK government to health and social care services. However, the devolved governments will still be able to control how they allocate their other funding. Therefore, they could shift some of this to other services if they so wish – which they might do given that their social care systems are currently more generous than that in England. The only way the UK government could ensure the proceeds of the health and social care levy were used in full to fund increased health and social care spending outside England would be to take much greater control of the devolved governments' budgets - something the devolved governments would be fiercely critical of."

26. The method for 'directing' the use of the levy is unclear but as indicated above any direction would be a big change to existing devolution arrangements in an area that accounts for more than half of the spending of the three nations.

27. The other impact will be the increase to employer National Insurance contributions that amounts to a £47m annual funding pressure for local government unless there is a form of funding adjustment to account for this.

Does this address Social Care issues?

28. The announcement has primarily centred on England but there are common challenges facing social care across the four nations.

29. A review of the proposals shows this is more about the structure of social care funding despite being billed as the reform of social care. There is no clarity about how the quality of care will be improved or how pay and conditions will now support a sector with huge staff vacancies. According to Skills for Care in 2019/20 it was estimated that 7.3% (112,000 roles) of the roles in adult social care in England alone were vacant at any one time with significant numbers on zero hours contracts.

30. Even so, the additional funding will be welcomed but there is no doubt that the biggest beneficiary is the NHS. Commentary by the IFS suggests they believe the funding package should be enough to prevent post pandemic waiting lists spiralling. Longer term there must be some doubt about the additional money moving across to social care after 3 years when the covid backlog has been

addressed. This would be a difficult decision whatever government is in power in Westminster.

31. The absence of any accompanying documentation or policy papers means that further detail will be needed. The introduction of a hypothecated new tax will mean that future increases may 'crowd out' the room for increases in funding for other departments.

Reform of Local Taxation – Welsh Government Programme for Government

32. At the last meeting Leaders requested a summary of WG's research into the reform of local taxation and this section addresses that work. It summarises the different potential sources of finance and the advantages and disadvantages of each option.

33. In January 2017 Welsh Government outlined the approach it would take to considering reforms to local government finance. It has published annual updates of progress.

34. The work is guided by the principles Welsh Government outlined in its Tax Policy Framework. The approach is also informed by the requirements of Wellbeing of Future Generation Act.

35. Between 2019 and 2021 research was carried out in partnership with Bangor University, Institute of Fiscal Studies and University of Sheffield. An advisory group was also established.

Local Land Value Tax (LVT)

36. Bangor University's research estimated a land value for Wales and concluded residential land values totalled £123.4 billion and non-residential land values were £27.6 billion.

37. The taxation method would raise sufficient revenues to replace current local taxes but data requirements are not currently available.

38. The method 'would require much more work' (per Bangor University) to establish the structure of rates for the tax, legislative requirements and address constitutional issues. For example, a land value tax would affect the Crown Estates and therefore require Crown Consent. The public understanding of a land value tax may also be limited and the timeframe for its introduction would be more than a single five-year Senedd term.

39. A LVT would appear to be able to raise revenues for local services but considerable work would be needed on the legislative and data requirements. Implementation would be resource intensive.

Local Income Tax (LIT)

40. A locally administered income tax for Wales would be a unique system as this does not appear to be used elsewhere. A LIT would need an expansion of current local taxation resources and also retraining. A key advantage of LIT to achieve a fairer system would be the ability to put in place a minimum income floor (tax free allowance) at the start of the scheme.

41. The research to date indicates some gaps in in evidence would need to be closed and these include modelling the economic issues that a LIT could create. This would arise because of potential variations in tax rates between different parts of Wales. It is also unclear what impact changes to levels of economic activity could have on tax yields as there may not be sufficient revenue stability with a LIT.

42. There may be a tax setting issue that affects councils under a LIT. Councils are legally required to agree a budget before setting the level of council tax to fund the budget. This could lead to rates of LIT changing on a frequent basis to fund council services and this may not meet with public support.

43. There is a high degree of understanding about income tax so the LIT would be widely understood. However, the current self-assessment regime may require amendment as the administrative burden may fall on individuals through the process.

44. Any move to LIT would require considerable legislative change and would also remove the property valuation function in Wales via UK legislation.

45. This will likely require more than a single Senedd five-year term.

Council Tax Reform

46. The Institute of Fiscal Studies and University of Sheffield produced research on the reform of Council Tax. A revaluation of the existing tax base would see half of properties move bands and this is evenly split between those going up or down property bands.

47. The last revaluation was conducted in 2003 (England and Scotland have not revalued since the introduction of Council Tax in 1993). Current valuations are out of date and it is acknowledged that as a minimum this should be addressed.

48. A redesign of bands could a progressive measure having the potential to help narrow inequalities that exist via effects on property prices. Wales is unique in having an additional council tax band compared with England and Scotland (Band I).

49. A key area of uncertainty would be if Welsh Government were to adjust grant funding at the same time as reforming council tax. If this were done it would have an impact on councils.

50. Longer term the issue of revaluation on a regular basis may be assisted by some movement to a statistical approach to establish market valuations. Whatever approach is adopted it is evident that more frequent valuations will be needed to avoid the drift away from historic values.

51. There may be a case for some form of 'damping' or protection given that nearly two decades have elapsed since the last revaluation.

52. The current system is relatively cost effective with a high percentage of tax collected per annum.

Tax Engagement Group

53. Leaders should also be aware that the Finance Minister's Tax Engagement Group met last week (16 September – Cllr Anthony Hunt attends) which discusses more general issues of taxation reform. Taxation on second homes and a tourism tax were both on the agenda

54. The Welsh Government is planning a consultation on a local tourism levy and is has been under consideration for a while. It will be engaging with various groups of stakeholders prior to setting out a consultation. The focus will be on occupancy taxes – room/bed taxes. Some countries use the receipts to support local investment and infrastructure, or it goes into central funds for reallocation.

55. The Welsh Government is also currently consulting on tax levers in relation to second homes and self-catering accommodation (Local taxes for second homes and self-catering accommodation | GOV.WALES). The consultation is taking a three-pronged approach at present to assess the impact, the regulatory framework and how to make it fairer. The WLGA will draft a response for Leaders' consideration before the closing date of 17 November.

Recommendations

56. **Members are asked to:**

56.1 Note the contents of the report.

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Appendix 1

HM Treasury, 1 Horse Guards Road, London, SW1A 2HQ

7 September 2021

Dear Secretary of State,

SPENDING REVIEW 2021

I am writing to you about our plans for Spending Review 2021 (SR21).

The Prime Minister and I have agreed that this will be a multi-year Spending Review which will set resource and capital budgets for 2022-23 to 2024-25 and conclude on 27 October 2021, alongside Autumn Budget 2021.

SR21 will set out how we will Build Back Better, deliver the priorities of the British people and continue to support businesses and jobs through:

a. **Ensuring strong and innovative public services** – making people's lives better across the country by investing in the NHS, education, the criminal justice system and housing;

b. **Levelling up** across the UK to increase and spread opportunity; unleash the potential of places by improving outcomes UK-wide where they lag and working closely with local leaders; and strengthen the private sector where it is weak;

c. **Leading the transition to Net Zero** across the country and more globally;

d. **Advancing Global Britain** and seizing the opportunities of EU Exit;

e. **Delivering our Plan for Growth** – delivering on our ambitious plans for an infrastructure and innovation revolution and cementing the UK as a scientific superpower, working in close partnership with the private sector.

Our plans for public spending

Since the start of the pandemic, this government has acted on an unprecedented scale to protect people's jobs and livelihoods and to support businesses and public services across the UK. Despite the worst economic recession in 300 years, we have not only got people back into work through the Plan for Jobs but maintained momentum on delivering our promises to the British people.

While doing this, we have also been clear on the need to put the public finances on a sustainable path in the medium term so that we are resilient to future challenges. This was central to the plans that I set out at Spending Review 2020 and at the Budget earlier this year.

The Prime Minister and I have agreed that the envelope for Spending Review 2021 will follow the path of resource and capital spending that we set out at Budget 2021, with the addition of the net revenue raised by the new Health and Social Care Levy and increase to dividends tax rates announced today. The pandemic has demonstrated the challenges facing our health and social care system require a new approach and the additional steps we have announced today reflect this.

Our record and our plans will see core departmental spending grow in real terms at nearly 4% per year on average over this Parliament – a £140 billion cash increase, and the largest real-terms increase in overall departmental spending for any Parliament this century. This includes a step-change in capital investment, building on the significant multi-year commitments we have already made at SR20, as we continue with our plans to deliver over £600 billion in gross public sector investment from 2020-21 to 2024-25. Departments will be expected to carefully prioritise their bids, and we will need to make trade-offs to ensure that this increased spending is focused on the delivery of our key commitments.

Given the continued uncertainty around the path of the virus, we recognise that some additional spending on top of these plans may be required in the immediate term as part of the remaining response to Covid-19. This will be considered in exceptional circumstances only, where reform and efficiencies are not sufficient to fund essential activity.

Public sector pay

To help protect jobs at a time of crisis and ensure fairness between the private and public sectors, SR20 temporarily paused pay rises for public sector workers earning £24,000 or more. NHS workers were exempted from this pause. Those working in the public sector have, on average, better remuneration packages than those in the private sector, with Covid also demonstrating the significant value of job security. For reasons of fairness and sustainability of the public finances, we must continue to ensure that public sector pay growth at SR21 (including all elements of earnings growth and pay drift) retains broad parity with the private sector and is affordable.

Ensuring that every pound is well-spent

As the Prime Minister and I set out to you in April, we also owe it to the British people to ensure that our spending plans are underpinned by a clear focus on delivering our priorities efficiently. The outcomes and real-world impacts of our spending must be at the heart of decisions, underpinned by the best data and evaluation. SR21 must also build on the progress we have made to identify genuine opportunities across the public sector to deliver reforms, level up across the UK and capitalise on productivity gains made through the pandemic. Your returns must deliver these opportunities and address the actions from the Savings & Efficiency Review to ensure that we can provide a better service for the British public, at lower cost.

The Chief Secretary will write to you shortly to confirm details on the expectations for your department. As set out in the commission received by your officials before Summer recess, your returns for the Spending Review must be **completed by no later than 13 September**, followed by a short window for discussion.

This letter has been copied to the Prime Minister, the Chief Secretary to the Treasury and the Cabinet Secretary.

Best wishes,

RISHI SUNAK