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

Jocelyn Davies AM
Chair, Finance Committee
National Assembly for Wales
Cardiff Bay,
Cardiff
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19th August 2015

Dear Mr. Davies,

INQUIRY INTO FUTURE FUNDING

Thank you for your letter of 21 July on the National Assembly's Finance Committee inquiry into future funding.

Please find attached my response to the questions you included in your letter.

Yours sincerely,

A handwritten signature in blue ink, appearing to read "G Hands".

GREG HANDS

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Annex – response to questions

1. A number of Parliamentary and other inquiries have concluded that there is a need for an independent body to monitor the application of the Barnett formula. Please can you confirm whether this option is currently being considered?

The government has committed to maintaining the Barnett formula, which is a fair, transparent and simple mechanism for determining changes to the devolved administrations' funding allocations. The UK Government is not currently considering the option of introducing an independent body to monitor the application of the Barnett formula.

2. Is it possible to regularly release full calculations of the operation of the Barnett formula to identify how spending decisions in England impact on Wales?

The outcome of the application of the Barnett formula to UK Government departmental allocations is announced both at Spending Reviews and at individual fiscal events. These figures are then represented in the Estimates laid before Parliament. HM Treasury's *Statement of Funding Policy* contains the relevant detail on the factors used when the Barnett formula is applied.

3. Does HM Treasury accept that there is sufficient evidence that the Barnett formula should incorporate a needs-based component, at least in relation to Wales?

The UK Government has agreed to introduce a floor in the level of relative funding it provides to the Welsh Government, in the expectation that the Welsh Government will call a referendum on income tax powers in the next Parliament. The precise level of the floor, and the mechanism to deliver it, will be agreed alongside the next Spending Review, as set out in the St David's Day Command Paper. Outside of the funding floor, we are not considering any other options to introduce further needs-based components in to the Barnett formula.



4. An initial block grant adjustment has been agreed for the taxes devolved under the Scotland Act 2012. Is it expected that the same block grant adjustment mechanism will apply to Wales?

We have agreed a one-off adjustment with the Scottish Government for 2015-16 in relation to stamp duty land tax and landfill tax. An ongoing mechanism will be agreed as part of the wider fiscal framework for Scotland, alongside the Scotland Bill 2015. We have also agreed an adjustment mechanism for the Scottish rate of income tax, although this will be superseded by the full devolution of income tax rates and thresholds. We will therefore also need to revisit these arrangements as part of the fiscal framework. We will be taking forwards discussions with the Welsh Government on block grant adjustments related to devolved Welsh taxes in due course.

5. How will the 'funding floor' for Wales which was announced alongside the St David's day agreement operate?

The St. David's Day Command Paper committed to introducing a funding floor with the details agreed at the next Spending Review. The Chancellor has indicated that the Spending Review outcome will be announced in November 2015. The Command Paper also set out that the funding floor would be introduced in the expectation that the Welsh Government will call a referendum on income tax powers in the next Parliament.

6. The Wales Bill Command Paper outlines certain conditions which must be met before new Welsh taxes could be approved. Please can you explain how the full approval process would operate in practice and the tests which must be met?

The Command Paper, published in March 2014, set out a clear list of the criteria against which any proposals for new taxes from the Welsh Government would be assessed by the UK Government. The paper set out that the criteria would include the extent to which the new tax:

- affects UK macro-economic or fiscal policy and/or the single market;



- may be non-compliant with EU legislation;
- increases tax avoidance risks; or
- creates additional compliance burdens for businesses and/or individuals;
- is aligned with devolved responsibilities.

Consistent with the process set out alongside the Scotland Bill, any proposal from the Welsh Government for a new tax would need to include full details on the following:

- the tax base (i.e. taxable activity);
- estimated revenue and economic impact;
- estimated impact on UK revenue or interaction with UK-wide taxes;
- expected impacts on business and individuals (including a distributional impact);
- assessment against all relevant legislation and directives, including the Human Rights Act, EU State Aid rules, Equality Act etc; and
- collection and compliance plans.

The UK Government will work with the Welsh Government to assess any such proposals in a timely manner. If at the end of that process the UK Government decides not to grant powers to the Assembly to create a new devolved tax, it will explain its reasoning.