

Office for
**Budget
Responsibility**

Economic and fiscal outlook
Devolved taxes forecast

July 2015

1 Introduction

- 1.1 The Office for Budget Responsibility (OBR) was established in 2010 to provide independent and authoritative analysis of the UK's public finances. Alongside the Budget and Autumn Statement, we produce forecasts for the UK economy and the public finances. We publish these in our *Economic and fiscal outlook (EFO)*.
- 1.2 Since 2012, we have forecast some tax streams that are devolved to the Scottish Parliament, and since last year we have also produced forecasts of taxes that are likely to be devolved to the National Assembly for Wales. Our forecasts for devolved taxes are published alongside each *EFO* and are consistent with our main UK forecasts. As with those UK forecasts, these extend over a five-year forecast period – to 2020-21 in this *EFO*.

The Scotland Act 2012

- 1.3 The Scotland Act 2012 gave new powers to the Scottish Parliament relating to taxation and borrowing. In April 2015, stamp duty land tax (SDLT) and landfill tax was fully devolved to the Scottish Parliament. The Scottish Government replaced SDLT with a new land and buildings transaction tax (LBTT). From April 2016, the Scottish Parliament will be asked to set a Scottish rate of income tax, to replace a 10p reduction from each rate of UK income tax.
- 1.4 The Command Paper: *Strengthening Scotland's Future*¹ – published alongside the Scotland Bill in 2010 – set out our role in providing forecasts of Scottish income tax, landfill tax, stamp duty land tax and aggregates levy receipts. Currently, the Treasury notionally assigns the forecast receipts for Scottish income tax and aggregates levy to the Scottish Budget to show how much of what is currently grant funding would be replaced by tax. The Scottish Budget will not be varied in line with fluctuations in tax receipts until the devolution of these taxes takes place.
- 1.5 In September 2014 the Smith Commission recommended the devolution of air passenger duty (APD) to the Scottish Parliament and the assignment of a share of VAT revenues. In May 2015 the UK government committed to implement the Smith Commission recommendations in full. The government will also be publishing a discussion paper on devolving APD to the English regions².

¹ *Strengthening Scotland's Future*, November 2010, Cm 7973.

² *Discussion paper on options for supporting English regional airports from the impacts of air passenger duty devolution*.

The Wales Act 2014

- 1.6 The Wales Act 2014 gave new powers to the Welsh Assembly relating to taxation and borrowing. It provides for the full devolution of SDLT and landfill tax from April 2018. Subject to the outcome of a referendum in Wales on the introduction of Welsh rates of income tax, the Welsh Assembly will also be able to set new Welsh rates for each band of income tax that would replace a 10p reduction in the rates of UK income tax. The timing of such a change has not yet been specified. The Government is also intending to devolve aggregates levy, subject to the resolution of current legal challenges.
- 1.7 The Command Paper: *Wales Bill: Financial Empowerment and Accountability*³ – published alongside the Wales Bill in 2014 – required us to begin to forecast Welsh taxes alongside Autumn Statement 2014 and twice a year thereafter. This currently includes forecasts for stamp duty land tax, landfill tax, aggregates levy and the Welsh rate of income tax. Our forecasts will reflect any Welsh replacement taxes – as with Scotland’s LBTT – when details of any changes become sufficiently clear. The Treasury will notionally assign these forecast receipts to the Welsh Budget to show how much of what is currently grant funding would be replaced by tax. Again, the Welsh Budget will not be varied in line with fluctuations in tax receipts until the devolution of these taxes has been fully implemented.

Methodology

- 1.8 We published a methodology note in March 2012 that described how we planned to forecast Scottish tax receipts.⁴ It explained that it is not possible to replicate in full the methodology we use to produce our UK-wide forecasts. In particular, the macroeconomic data that we would need to produce a Scottish macroeconomic forecast and economic determinants were generally not available at a Scottish level or were only available with a long lag. That remains the case. We are therefore not able to produce a Scottish macroeconomic forecast to drive the Scotland tax forecast. These challenges apply equally to forecasting Welsh taxes.
- 1.9 Given these challenges, the methodologies we use are generally based on estimating and projecting Scottish and Welsh shares of relevant UK tax streams. We typically assume that the shares will continue at recent average levels, unless available evidence suggests we should adjust those assumptions to ensure our forecasts are central. For example, if a newly announced policy can be expected to have a disproportionate impact on the Scottish or Welsh share of a particular tax, or there is evidence pointing to different trends in an underlying tax base.
- 1.10 The exception to this is our LBTT forecast. As the Scottish Government has to date only published a forecast of LBTT receipts for one year, we sought assistance from HM Revenue and Customs (HMRC) in producing a five-year LBTT forecast. As a new tax, this forecast will clearly be subject to even greater uncertainty than our previous forecasts for the Scottish

³ *Wales Bill: Financial Empowerment and Accountability*, March 2014, Cm 8838.

⁴ *Forecasting Scottish taxes*, March 2012.

share of UK SDLT receipts. That forecast was itself subject to considerable uncertainty given its sensitivity to the growth of property transactions, which can be volatile from year to year.

- 1.11 As with our UK forecasts, the methodology and the forecasts represent the collective view of the three independent members of the OBR's Budget Responsibility Committee (BRC). The BRC takes full responsibility for the judgements that underpin them.
- 1.12 We consider these methodologies to remain work-in-progress. The OBR's role in forecasting started three years ahead of the initial devolution of these taxes in Scotland. This has allowed us to develop and improve forecasts in light of experience and the availability of new information sources.

The forecast process

- 1.13 The process for producing the devolved tax forecasts has been as follows:
- HMRC officials produced draft Scottish and Welsh tax forecasts on our behalf using a near-final pre-measures UK economic and fiscal forecasts. This took into account the tax forecasts for 2015-16 contained in the Scottish Government's Draft Budget, published in October 2014 and the subsequent update when residential LBTT rates were revised in January 2015. The BRC and OBR staff discussed these forecasts with HMRC, Scottish Government, Scottish Fiscal Commission and Welsh Government officials on 17 and 25 June; and
 - in the final week before the Budget, HMRC officials provided us with a final set of Scottish and Welsh forecasts using our final post-measures UK economic and fiscal forecasts, and taking into account Budget policy measures. Due to the confidentiality of the measures, we were unable to involve the Scottish Government and Welsh Government in this stage of the process.
- 1.14 The Scottish Government produced a forecast for 2015-16 receipts from the new Scottish LBTT and landfill tax in its Draft Budget. The Scottish Government has not provided us with information about expected receipts from these taxes over the remainder of our five-year forecast period, so HMRC produced these forecasts at our request. We will continue to work with the Scottish and Welsh Governments, and with the Scottish Fiscal Commission, to ensure that we can bring all relevant information to bear in producing these forecasts. At this stage, the forecast we present in this document is our own. Differences between our own forecast and the Scottish Government forecasts for 2015-16 are explained in Chapters 3 and 4.

Summary of forecasts

1.15 Tables 1.1 and 1.2 detail the forecasts for the Scottish and Welsh taxes. This includes receipts from the new LBTT from 2015-16 onwards.

Table 1.1: Summary of July 2015 Scottish tax forecasts

| | £ million | | | | | |
|-----------------|-------------|-------------|-------------|-------------|-------------|-------------|
| | 2015-16 | 2016-17 | 2017-18 | 2018-19 | 2019-20 | 2020-21 |
| Income tax | 4590 | 4868 | 5147 | 5431 | 5781 | 6187 |
| LBTT | 540 | 616 | 689 | 780 | 874 | 974 |
| Landfill tax | 94 | 88 | 87 | 90 | 96 | 103 |
| Aggregates levy | 47 | 44 | 43 | 45 | 48 | 51 |
| Total | 5271 | 5616 | 5966 | 6345 | 6800 | 7314 |

Table 1.2: Summary of July 2015 Welsh tax forecasts

| | £ million | | | | | |
|-----------------|-------------|-------------|-------------|-------------|-------------|-------------|
| | 2015-16 | 2016-17 | 2017-18 | 2018-19 | 2019-20 | 2020-21 |
| Income tax | 1996 | 2107 | 2228 | 2357 | 2515 | 2695 |
| SDLT | 179 | 197 | 220 | 248 | 277 | 307 |
| Landfill tax | 47 | 44 | 43 | 45 | 48 | 51 |
| Aggregates levy | 25 | 27 | 28 | 28 | 28 | 28 |
| Total | 2248 | 2375 | 2518 | 2678 | 2868 | 3082 |

2 Income tax

Scottish rate of income tax

- 2.1 Under the Scotland Act 2012, the existing basic, higher and additional rates of income tax levied by the UK Government will, from April 2016, be reduced by 10p in the pound for those individuals defined as Scottish taxpayers. The Scottish Parliament will then levy a new Scottish rate of income tax, which will apply equally to Scottish taxpayers in all of the main UK bands. The new Scottish rate of income tax will need to be set every year by the Scottish Parliament. The block grant from the UK Government to Scotland will then be reduced to reflect the fiscal impact of the devolution of these tax-raising powers.
- 2.2 The Scottish rate of income tax will be paid by Scottish taxpayers, who will be defined as a UK taxpayer either resident in Scotland or whose closest connection is with Scotland. It will be levied on non-savings, non-dividend income liabilities (i.e. earnings from employment, self-employment, pension income, foreign income, taxable benefits and income from property). Tax liabilities for a particular year would include both PAYE (pay-as-you-earn income tax, which is largely paid in the same year as the activity that created the tax liability) and self-assessment (which is usually paid in the year after the activity that took place to create the tax liability).
- 2.3 In our forecast, we assume a 10p rate is levied in every year.

Welsh rate of income tax

- 2.4 The Wales Act 2014 includes provision for a referendum to determine whether the Welsh Assembly will be able to introduce a Welsh rate of income tax. The income tax levied by the UK Government would be reduced by 10p in the pound for those individuals defined as Welsh taxpayers. The Welsh Assembly would then levy separate Welsh rates for each band of income tax. The new Welsh income tax rates would need to be set every year by the Welsh Assembly. The block grant from the UK Government to Wales would then be reduced to reflect the fiscal impact of the devolution of these tax-raising powers.
- 2.5 The forecasts presented in this document assume that the referendum results in the implementation of a Welsh rate of income tax and that the Welsh Assembly then levies a 10p rate across all the income tax bands in every year. It will also be levied on non-savings, non-dividend income liabilities.

Methodology

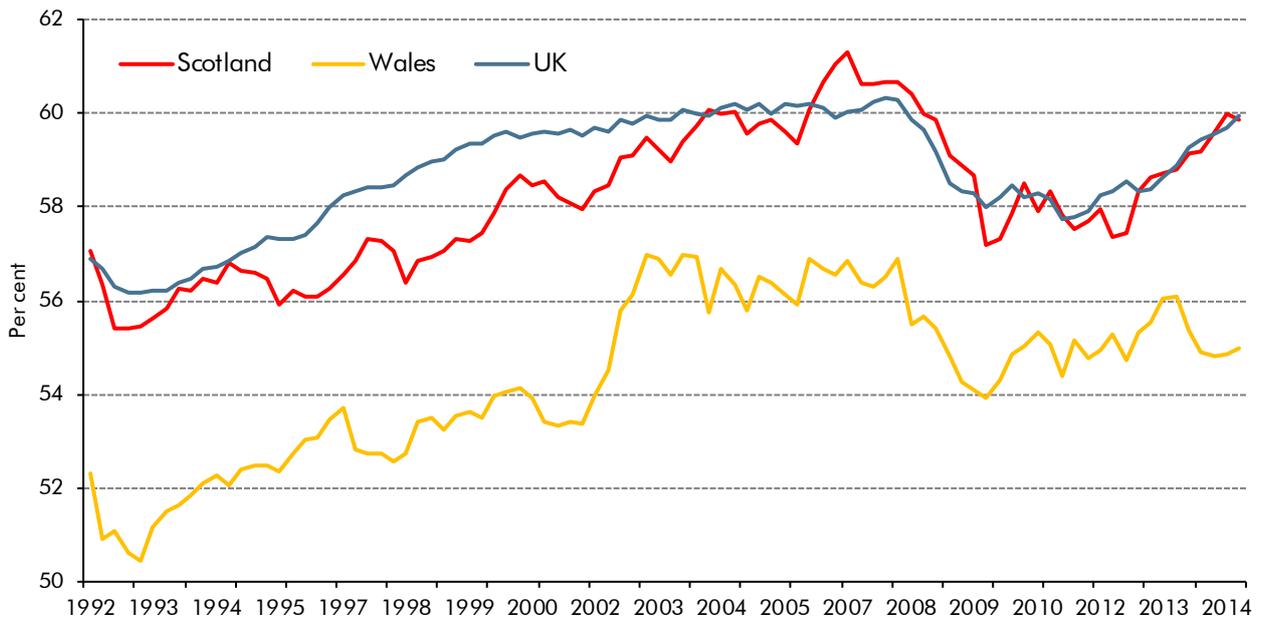
- 2.6 We generate a UK forecast for non-savings, non-dividend income tax liabilities from the full UK income tax receipts forecast published in our *EFO*. The key components of the UK forecast are:
- total pay-as-you-earn (PAYE) liabilities;
 - self-assessment (SA) liabilities on non-savings, non-dividend income. The UK forecast for SA in the *EFO* is on a receipts basis (i.e. when the cash is received). For this forecast this is adjusted to be on a liabilities basis (i.e. when the activity occurred) and to exclude the savings and dividend elements of SA; and
 - PAYE repayments and repayments to pension providers, from our income tax repayments forecast.
- 2.7 We then apply the latest estimated Scottish and Welsh shares to the UK total of these forecast components. We then include deductions in respect of the Scottish and Welsh shares of Gift Aid repayments. Finally, we add estimates of the Scottish and Welsh income tax element of new policy measures announced in this Budget.
- 2.8 Information on the share of UK income tax in Scotland and Wales is derived from the Survey of Personal Incomes (SPI), an annual survey based on a sample of about 700,000 individuals in contact with HMRC during the course of the year through the PAYE, SA or repayment claim systems. This is only available with a long lag, with data currently only available up to 2012-13. In the run up to the devolution of the Scottish rate of income tax, HMRC will identify each individual taxpayer as Scottish or not, and flag them as such on its PAYE and SA systems. Once this has been done, it will be possible to determine the Scottish share of UK liabilities with much greater precision.
- 2.9 The Scottish and Welsh shares can be affected by a number of factors. These include:
- different economic trends between Scotland/Wales and the UK as a whole;
 - different movements in the income distribution between Scotland/Wales and the UK; and
 - different effects of policy measures.
- 2.10 The Scottish share was very stable from 2001-02 to 2010-11 – with the share close to 3.15 per cent in most years – but fell in both 2011-12 and 2012-13. The share in Wales has been more varied and there is some indication of a downward trend in the share from 2003-04. Table 2.1 shows the estimates of the Scottish and Welsh share from the SPI.

Table 2.1: Scottish and Welsh historic income tax shares

| | Per cent of UK total for non-savings, non-dividend liabilities | | | | | | | | | | | | | |
|----------|--|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|
| | 99-00 | 00-01 | 01-02 | 02-03 | 03-04 | 04-05 | 05-06 | 06-07 | 07-08 | 08-09 | 09-10 | 10-11 | 11-12 | 12-13 |
| Scotland | 3.04 | 3.03 | 3.14 | 3.15 | 3.23 | 3.15 | 3.13 | 3.15 | 3.14 | n/a | 3.16 | 3.15 | 3.08 | 3.04 |
| Wales | 1.45 | 1.40 | 1.48 | 1.51 | 1.55 | 1.53 | 1.50 | 1.47 | 1.44 | n/a | 1.42 | 1.42 | 1.37 | 1.34 |

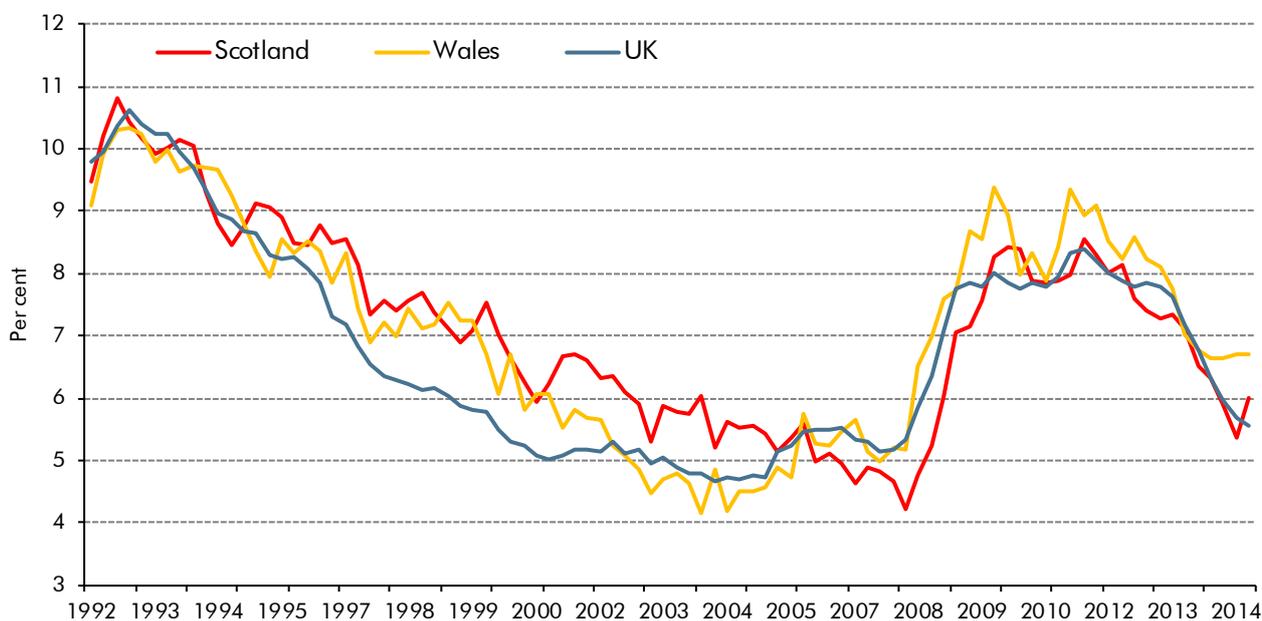
2.11 These different shares of UK income tax can partly be explained by different labour market trends in Wales and Scotland relative to the rest of the UK. Charts 2.1 and 2.2 show that employment and unemployment trends in Scotland have generally been more similar to the UK as a whole than has been the case in Wales. In particular, the employment rate has typically been lower in Wales, mainly reflecting a higher inactivity rate. The latest unemployment rate for Wales is around 1 per cent higher than in Scotland and the UK as a whole.

Chart 2.1: Employment rates in the UK, Scotland and Wales



Source: ONS

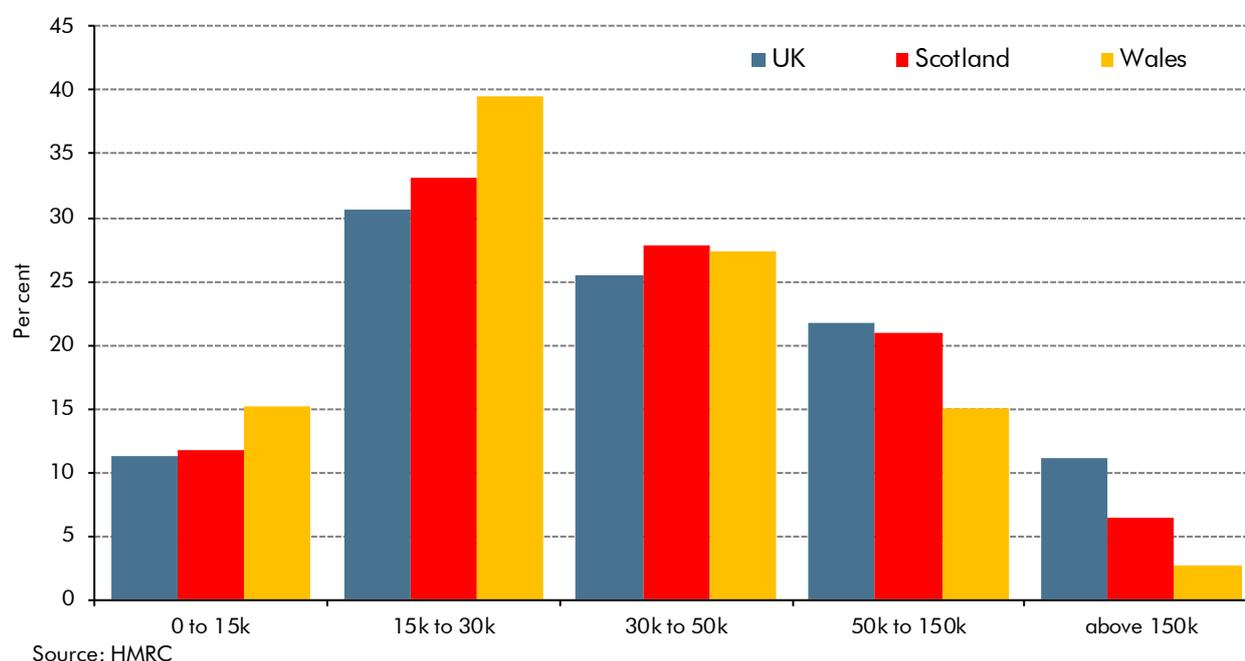
Chart 2.2: Unemployment rates in the UK, Scotland and Wales



Source: ONS

- 2.12** The main factor behind the drops in Scottish and Welsh shares of income tax since 2009-10 is likely to be the asymmetric effect from policy measures. In recent years, revenue-raising policies have generally affected the top end of the income distribution. These include the additional rate of income tax for incomes over £150,000, the withdrawal of personal allowances over £100,000, freezes in the basic rate limit and higher rate thresholds and anti-avoidance measures. In contrast, tax cuts such as raising the personal allowance to £11,000 by 2016-17 have had more of an effect at the lower end of the income distribution.
- 2.13** Chart 2.3 shows the proportion of total taxpayer income by income bands. The proportion of taxpayer income generated from individuals with incomes below £30,000 is higher in Scotland, and particularly so in Wales. We have therefore made adjustments to the Scottish and Welsh share to account for recent policy measures that are not yet reflected in the SPI data.

Chart 2.3: Proportion of total taxpayer income by income bands (2012-13)



2.14 Finally, we add the estimated Scottish and Welsh share of newly announced policy measures to generate the post-measures forecast.

UK forecast

2.15 Table 2.2 shows the UK forecast of tax liabilities on non-savings, non-dividend (NSND) income. To aid comparison we present both the current and previous March forecast before the effect of policy measures. ONS have revised up receipts in 2012-13 and 2013-14, provisional UK outturn in 2014-15 is higher than we forecast in March, and our latest forecasts are also higher in each year from 2015-16 onwards. Receipts are expected to grow by 36 per cent over the forecast period.

Table 2.2: UK forecast of tax liabilities on non-savings, non-dividend income

| | £ billion | | | | | | | | |
|--|-----------|---------|---------|---------|---------|---------|---------|---------|---------|
| | 2012-13 | 2013-14 | 2014-15 | 2015-16 | 2016-17 | 2017-18 | 2018-19 | 2019-20 | 2020-21 |
| March 2015 (a) | 141.6 | 146.6 | 152.0 | 158.6 | 167.8 | 178.6 | 189.4 | 202.4 | |
| July 2015 (inc March measures) | 142.2 | 147.2 | 153.3 | 160.5 | 171.7 | 182.0 | 191.8 | 203.7 | 217.6 |
| July 2015 (excluding March measures) (b) | 142.2 | 147.2 | 153.3 | 160.4 | 171.2 | 182.0 | 192.3 | 204.0 | |
| Difference (b) - (a) | 0.6 | 0.6 | 1.3 | 1.8 | 3.4 | 3.4 | 2.9 | 1.6 | |

2.16 PAYE income tax is forecast to be higher in each year than in our March forecast. Receipts in 2014-15 were stronger due to higher bonuses in both the financial and business services sectors in the final two months of the year and also due to HMRC revisions to earlier months of the year. Stronger 2014-15 receipts have been pushed through to future years.

- 2.17 Employment is expected to be modestly higher through the forecast, while the change in the profile for earnings growth boosts receipts in 2016-17 but lowers receipts in the final years of the forecast. The bringing forward to 2016-17 of the increase in the personal allowance to £11,000 and the rise in the higher rate threshold to £43,000 reduce receipts by around £1.5 billion, although there is some offset from the restriction in pension tax relief for those earning over £150,000.
- 2.18 The Government has announced that from April 2016 it will introduce a Living Wage Premium that will apply on top of the National Minimum Wage (NMW) for employees aged 25 and over to deliver a National Living Wage (NLW) for those people. The main NMW will continue to be set for employees aged 21 and over, so that those aged 21 to 24 will continue to be subject only to that rate. The NLW could have a disproportionate effect in Scotland and Wales with implications for our devolved income tax forecast. However, at this stage we have not attempted to quantify this effect and instead note it as a source of potential uncertainty. Please refer to Annex B of the *EFO* for more on the NLW.
- 2.19 Our forecast for self-assessment income tax (SA) liabilities is little changed from March on a pre-measures basis. SA liabilities are forecast to grow strongly between 2013-14 (the year to which most 2014-15 receipts related to) and 2015-16, reflecting a combination of rising self-employment, higher property income and the effect of a number of policy measures, such as those affecting partnerships and accelerated payments. There is a further boost to the UK forecast for NSND liabilities from lower income tax repayments. These were lower than expected in 2014-15, boosting the UK forecast by around £0.4 billion a year.
- 2.20 A number of policy measures that significantly affect income tax receipts have been announced in this Budget. Those that lower receipts include:
- personal allowance: increase to £11,000 in 2016-17, with equal gains to higher rate taxpayers;
 - higher rate threshold: increase to £43,000 in 2016-17;
 - tax free childcare: updated rollout; and
 - annual investment allowance: set at new permanent level of £200,000.
- 2.21 Those measures that increase receipts include:
- a number of measures, funded by new investment, that increase HMRC's compliance activity;
 - non-domiciles: abolish permanent status;
 - pensions tax relief: restrict for gross income over £150,000 from 2016-17; and
 - two changes around landlords' finance relief and wear and tear allowance.

2.22 The rise in dividend tax announced in the Budget will boost SA receipts by around £2.9 billion by the end of the forecast period. However, this measure will have no effect on the definition used in either the Scottish or the Welsh rate of income tax.

Scottish forecast

2.23 Table 2.3 shows our latest forecast of the Scottish share of income tax. Data from the 2012-13 SPI became available in January 2015 and suggests that the Scottish share in 2012-13 was 3.04 per cent. We used this share in both our March and latest forecast. We expect a further fall in the Scottish share over the forecast period as a result of the asymmetric effect of policy measures in recent years. This pattern continues with the new policy measures announced in this Budget, with gains typically for lower income individuals and losses for those with higher incomes, both of which reduce the Scottish share. We have not made any further adjustments to the share as the effects of the measures are dealt with separately.

Table 2.3: Scottish share of income tax

| | Per cent of UK total for non-savings, non-dividend liabilities | | | | | | | | |
|------------|--|---------|---------|---------|---------|---------|---------|---------|---------|
| | 2012-13 | 2013-14 | 2014-15 | 2015-16 | 2016-17 | 2017-18 | 2018-19 | 2019-20 | 2020-21 |
| March 2015 | 3.04 | 2.91 | 2.91 | 2.89 | 2.89 | 2.89 | 2.89 | 2.88 | |
| July 2015 | 3.04 | 2.91 | 2.91 | 2.89 | 2.89 | 2.89 | 2.89 | 2.88 | 2.88 |

2.24 Table 2.4 provides a forecast for Scottish income tax liabilities on non-savings, non-dividend income. These are the liabilities specifically for the Scottish rate. Prior to a decision in the Scottish Parliament on the new Scottish tax rate for 2016-17, the forecast assumes that a 10p Scottish rate will be levied. In line with the UK forecast, we expect more rapid growth in tax liabilities from 2016-17 onwards.

Table 2.4: Scottish income tax forecast

| | £ million | | | | | | | |
|---|-----------|---------|---------|---------|---------|---------|---------|---------|
| | 2013-14 | 2014-15 | 2015-16 | 2016-17 | 2017-18 | 2018-19 | 2019-20 | 2020-21 |
| Scottish income tax liabilities (pre-measures) | 4240 | 4415 | 4586 | 4906 | 5205 | 5480 | 5820 | 6219 |
| New measures | | | 4 | -39 | -58 | -49 | -39 | -32 |
| Scottish income tax liabilities (post-measures) | 4240 | 4415 | 4590 | 4868 | 5147 | 5431 | 5781 | 6187 |

2.25 Table 2.5 provides a breakdown of the change in the Scottish income tax forecast since March. Receipts are higher for every year of the forecast. The main factor is the increase in the UK NSND forecast outlined above. There is also a positive effect from previously announced policy measures. This outweighs the reduction in receipts from measures announced at this Budget, which is largely driven by the disproportionate effect of the personal allowance increase in Scotland. The measures on restricting pension tax relief for those with incomes over £150,000 and the changes to non-domicile status will affect the top end of the income distribution and have a smaller proportionate effect in Scotland.

Table 2.5: Changes in Scottish income tax since March

| | £ million | | | | | | |
|-------------------------------------|-----------|---------|---------|---------|---------|---------|---------|
| | 2013-14 | 2014-15 | 2015-16 | 2016-17 | 2017-18 | 2018-19 | 2019-20 |
| March 2015 | 4223 | 4379 | 4532 | 4791 | 5087 | 5370 | 5748 |
| July 2015 | 4240 | 4415 | 4590 | 4868 | 5147 | 5431 | 5781 |
| Change in income tax | 17 | 36 | 58 | 76 | 61 | 61 | 33 |
| of which: | | | | | | | |
| Scottish share | 0 | 0 | 0 | -1 | 2 | 2 | 1 |
| Other (including previous measures) | 0 | 0 | 2 | 18 | 19 | 24 | 23 |
| New measures | 0 | 0 | 4 | -39 | -58 | -49 | -39 |
| UK forecast | 17 | 36 | 52 | 98 | 97 | 84 | 47 |

Welsh forecast

2.26 Table 2.6 shows our forecast for the Welsh share of income tax. The SPI data published in January 2015, covering 2012-13, indicates a Welsh share of 1.34 per cent. We have used this share in both our March and latest forecast. As with the Scottish share, the asymmetric effect of policy measures is likely to be the key factor behind the recent drop in the share and the expected further drop over the forecast period. Again, the policies announced in this Budget are likely to contribute to that trend.

Table 2.6: Welsh share of income tax

| | Per cent of UK total for non-savings, non-dividend liabilities | | | | | | | | |
|------------|--|---------|---------|---------|---------|---------|---------|---------|---------|
| | 2012-13 | 2013-14 | 2014-15 | 2015-16 | 2016-17 | 2017-18 | 2018-19 | 2019-20 | 2020-21 |
| March 2015 | 1.34 | 1.27 | 1.27 | 1.26 | 1.26 | 1.26 | 1.26 | 1.26 | |
| July 2015 | 1.34 | 1.27 | 1.27 | 1.26 | 1.25 | 1.25 | 1.26 | 1.26 | 1.26 |

2.27 Table 2.7 provides a forecast for Welsh income tax liabilities on non-savings, non-dividend income. These are the liabilities specifically for the Welsh rate. It assumes that a 10p rate is implemented by the Welsh Assembly. Again, in line with the UK forecast we expect more rapid growth in tax liabilities from 2016-17 onwards. With the income distribution more skewed towards the bottom end in Wales, the raising of the personal allowance has a larger than proportionate effect on Welsh income tax liabilities than in Scotland.

Table 2.7: Welsh income tax forecast

| | £ million | | | | | | | |
|--|-----------|---------|---------|---------|---------|---------|---------|---------|
| | 2013-14 | 2014-15 | 2015-16 | 2016-17 | 2017-18 | 2018-19 | 2019-20 | 2020-21 |
| Welsh income tax liabilities (pre-measures) | 1846 | 1924 | 1994 | 2128 | 2257 | 2381 | 2533 | 2710 |
| New measures | | | 2 | -21 | -29 | -24 | -18 | -15 |
| Welsh income tax liabilities (post-measures) | 1846 | 1924 | 1996 | 2107 | 2228 | 2357 | 2515 | 2695 |

2.28 Table 2.8 provides a breakdown of the changes in the Welsh income tax forecast since March. Receipts are expected to be higher throughout the forecast period, mostly due to a stronger UK NSND forecast. There is also a positive effect from previously announced policy measures. This outweighs the reduction in receipts from measures announced at this Budget. As with Scotland, this is largely driven by the disproportionate effect of the personal allowance increase in Wales, while the measures on restricting pension tax relief and the changes to non-domicile status will affect the top end of the income distribution and have a smaller proportionate effect in Wales.

Table 2.8: Changes in Welsh income tax since March

| | £ million | | | | | | |
|-------------------------------------|-----------|---------|---------|---------|---------|---------|---------|
| | Forecast | | | | | | |
| | 2013-14 | 2014-15 | 2015-16 | 2016-17 | 2017-18 | 2018-19 | 2019-20 |
| March 2015 | 1839 | 1910 | 1972 | 2084 | 2216 | 2344 | 2514 |
| July 2015 | 1846 | 1924 | 1996 | 2107 | 2228 | 2357 | 2515 |
| Change in income tax | 7 | 15 | 24 | 23 | 12 | 13 | 1 |
| <i>of which:</i> | | | | | | | |
| Welsh share | -1 | -1 | -1 | 0 | 0 | 0 | 0 |
| Other (including previous measures) | 0 | 0 | 1 | 1 | -2 | 0 | -2 |
| New measures | 0 | 0 | 2 | -21 | -29 | -24 | -18 |
| UK forecast | 7 | 16 | 23 | 43 | 43 | 37 | 21 |

3 Taxes on property transactions

Scottish land and buildings transaction tax

3.1 The Scotland Act provided for stamp duty land tax (SDLT) to be entirely devolved to Scotland in April 2015, which included the power to change the tax system as well as tax rates. The Land and Buildings Transaction Tax (Scotland) Act 2013 received Royal Assent on 31 July 2013.

3.2 In April 2015, the land and buildings transaction tax (LBTT) replaced UK-wide SDLT within Scotland. Prior to that there were also reforms to the UK SDLT tax system that took place in December 2014. The main changes that have affected the taxation of property transactions in Scotland are:

- on 4 December 2014, the UK residential SDLT regime moved from a 'slab' to a 'slice' system. As a result, until the end of March 2015 property transactions were taxed under the new UK SDLT regime, before moving to the LBTT regime in April 2015. The UK changes were discussed in detail in our December 2014 *EFO*;
- a requirement to pay LBTT prior to registration of the title, intended to encourage prompt payment; and
- modifications to reliefs and exemptions, including the withdrawal of sub-sale relief arrangements.

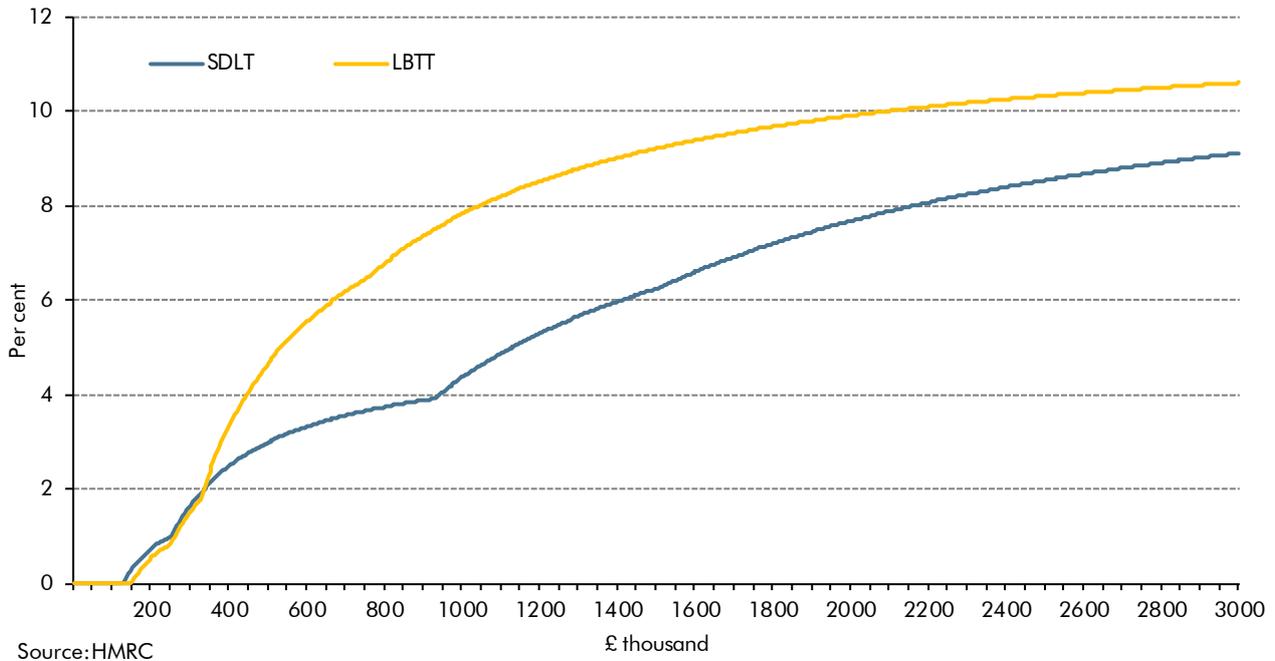
3.3 The Scottish Government announced LBTT rates and bands in its October 2014 Draft Budget and subsequently announced amendments to them in January 2015. For residential property the rates are:

- 0 per cent on residential property transactions up to £145,000;
- 2 per cent on the portion to £250,000;
- 5 per cent on to £325,000;
- 10 per cent on to £750,000; and
- 12 per cent on value above £750,000.

3.4 Chart 3.1 shows how the amount of tax paid on transactions at different property prices differs between the reformed SDLT regime and the Scottish LBTT system. It shows that there are substantial differences at some prices. For example, the purchaser of a £260,000 house

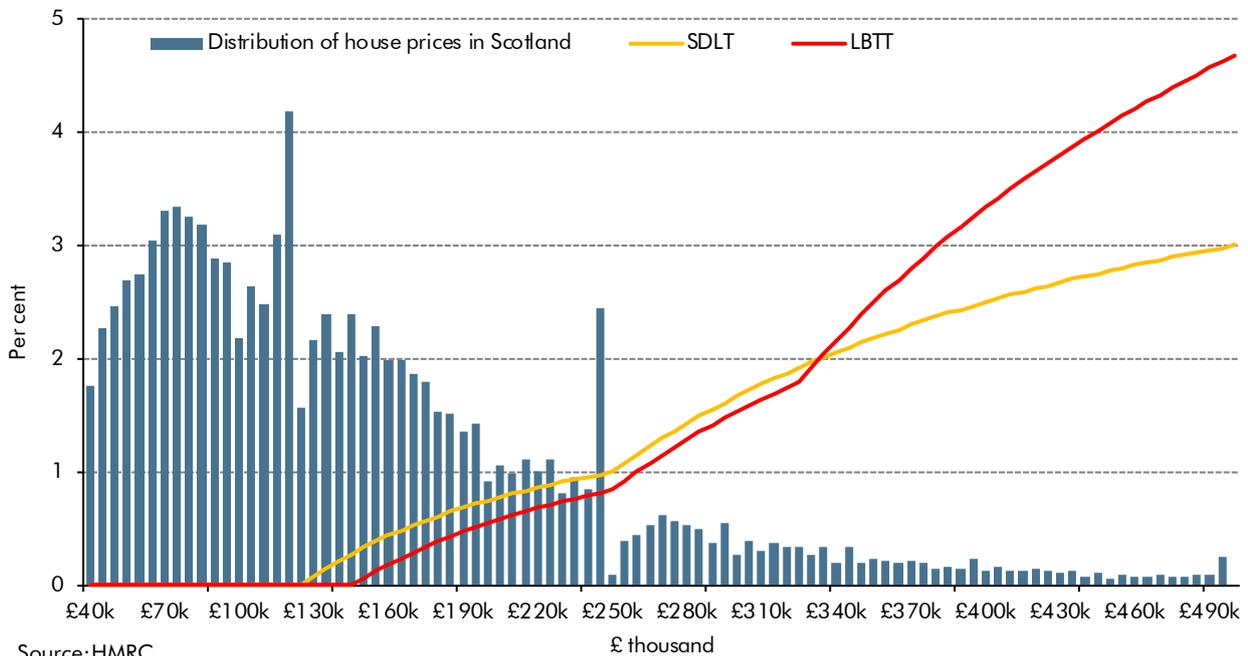
– just above the 2 per cent threshold in the UK SDLT system and the 2 per cent threshold in the Scottish LBTT system – would pay £400 less in tax in Scotland. By contrast, the purchaser of a £1.5 million house would pay £45,000 more tax under the Scottish system.

Chart 3.1: UK SDLT and Scottish LBTT tax schedules for residential property



3.5 Chart 3.2 shows LBTT and SDLT tax schedules for properties up to £500,000, and also adds the distribution of house prices in Scotland. From this it is clear that for a majority of properties in Scotland there would be a zero rate under either tax regime. It is also clear a significant proportion is likely to face a lower rate under LBTT than SDLT. A relatively low proportion would likely be subject to the higher rates under LBTT. There are very few properties in Scotland that would be subject to the 10 and 12 per cent LBTT rates.

Chart 3.2: Distribution of house prices in Scotland under LBTT and SDLT, 2013-14



3.6 The new rates for Scottish commercial property are:

- 0 per cent on commercial property transactions up to £150,000;
- 3 per cent between £150,000 and £350,000; and
- 4.5 per cent above £350,000.

Welsh rate

3.7 The Wales Act provides for SDLT to be fully devolved to Wales in April 2018. The Welsh Assembly has not yet announced any change from the UK system. Until any announcements are made and sufficient detail is available, our Welsh forecast will assume that the new UK SDLT system would remain after the tax is fully devolved.

Methodology

3.8 The forecast for residential LBTT uses the HMRC stamp duty model (SDM). This is a microsimulation model that allows us to apply the tax schedules for LBTT to a representative 10 per cent sample of transactions from a given year and grow them in line with our price and transactions forecasts for the residential markets. We assume that Scottish prices and transactions grow in line with those for the UK as a whole from 2015-16 forwards.

3.9 For this forecast there is a change in the way that commercial LBTT is modelled. HMRC's stamp duty plus model (SDM+) is used for the first time. This works in a similar way to SDM, with the main difference being that rather than a sample, it takes all Scottish property

transactions from a given year, before applying price and transactions forecasts for the commercial sector.

3.10 Our Welsh residential SDLT forecast has also been produced using HMRC's SDM. This replaces the use of a time series model that had been estimated on data that reflected the previous UK slab structure of SDLT, so was no longer appropriate for use in our forecasts. Welsh commercial SDLT receipts are still forecast by assuming a constant share of UK receipts, which, since there have not been reforms to the UK commercial SDLT system, continue to be forecast using an econometric model. We assume that Welsh prices and transactions grow in line with those for the UK as a whole from 2015-16 forwards.

3.11 Table 3.1 shows how the Scottish and Welsh shares of SDLT receipts have evolved since 2007-08. It shows that they have generally been on a declining path, which has reflected the relative strength of London prices over the period. UK SDLT receipts fell sharply in 2008-09 and only returned to their pre-crisis levels in 2014-15.

3.12 Any additional effect from new policy measures are added to the post-measures forecast.

Table 3.1: Historical Scottish and Welsh shares and SDLT receipts

| | £ million | | | | | | |
|-------------------|-----------------------------|-------------|-------------|-------------|-------------|-------------|-------------|
| | 2007-08 | 2008-09 | 2009-10 | 2010-11 | 2011-12 | 2012-13 | 2013-14 |
| UK: | 9958 | 4796 | 4885 | 5960 | 6130 | 6907 | 9273 |
| <i>of which</i> | | | | | | | |
| Residential | 6680 | 2950 | 3290 | 4040 | 4220 | 4905 | 6450 |
| Commercial | 3278 | 1846 | 1595 | 1920 | 1910 | 2002 | 2823 |
| | Totals | | | | | | |
| Scotland: | 565 | 320 | 250 | 330 | 275 | 283 | 389 |
| <i>of which:</i> | | | | | | | |
| Residential | 340 | 185 | 135 | 165 | 155 | 170 | 215 |
| Commercial | 225 | 135 | 115 | 165 | 120 | 113 | 175 |
| Wales: | 210 | 115 | 100 | 115 | 125 | 105 | 150 |
| <i>of which:</i> | | | | | | | |
| Residential | 130 | 55 | 55 | 65 | 65 | 70 | 90 |
| Commercial | 80 | 60 | 45 | 50 | 60 | 35 | 60 |
| | Per cent of UK total | | | | | | |
| Scotland: | | | | | | | |
| Residential share | 5.1 | 6.3 | 4.1 | 4.1 | 3.7 | 3.5 | 3.3 |
| Commercial share | 6.9 | 7.4 | 7.2 | 8.6 | 6.3 | 5.5 | 6.2 |
| Wales: | | | | | | | |
| Residential share | 1.9 | 1.9 | 1.7 | 1.6 | 1.5 | 1.5 | 1.4 |
| Commercial share | 2.4 | 3.2 | 2.8 | 2.6 | 3.1 | 1.7 | 2.1 |

UK forecast

3.13 Our UK SDLT forecast rises strongly across the forecast period from £10.9 billion in 2014-15 to £18.9 billion in 2020-21, driven by a 19 per cent rise in residential property

transactions and a 34 per cent rise in house prices. Compared with our March forecast, SDLT receipts are expected to be £1.1 billion higher in 2015-16 but £0.7 billion lower by 2019-20. Residential property transactions were higher than expected at the end of 2014-15, which we expect to persist in the early years of the forecast. But we expect transactions to converge to a similar long-run trend as in March, so the upward revision diminishes over the forecast period. Lower house prices relative to our March forecast reduce receipts by around £1.2 billion in 2019-20. Revisions to our commercial property forecasts broadly offset, with higher prices – reflecting higher consensus expectations of capital value growth – and lower transactions.

Scottish forecast

3.14 Our forecast for Scottish LBTT takes on the LBTT rates for residential property announced in January 2015. Table 3.2 shows our latest forecasts for residential and commercial LBTT. Total LBTT receipts are expected to grow by 80 per cent from 2015-16 to 2020-21, higher than the growth rate in UK SDLT receipts. As with SDLT in the rest of the UK, strong growth in LBTT receipts is explained by higher house prices and rising residential property transactions. However, rising prices will lead to a steeper rise in the effective tax rate for LBTT, given the marginal tax rates shown in Chart 3.1.

Table 3.2: Land and buildings transaction tax forecast

| | £ million | | | | | |
|-------------------------|------------|------------|-----------|-----------|------------|---------|
| | 2015-16 | 2016-17 | 2017-18 | 2018-19 | 2019-20 | 2020-21 |
| Total LBTT | | | | | | |
| March 2015 | 431 | 510 | 598 | 704 | 810 | |
| July 2015 | 540 | 616 | 689 | 780 | 874 | 974 |
| Difference | 109 | 106 | 91 | 76 | 64 | |
| Residential LBTT | | | | | | |
| March 2015 | 226 | 297 | 375 | 467 | 554 | |
| July 2015 | 264 | 324 | 385 | 462 | 541 | 623 |
| Difference | 38 | 27 | 10 | -5 | -13 | |
| Commercial | | | | | | |
| March 2015 | 205 | 213 | 223 | 237 | 256 | |
| July 2015 | 275 | 291 | 304 | 318 | 333 | 351 |
| Difference | 70 | 79 | 81 | 81 | 78 | |

3.15 Tables 3.3 and 3.4 show the sources of changes since our March forecast. Compared to our March forecast residential LBTT is higher from 2015-16 to 2017-18 and then down slightly after that. There is a positive effect from moving the SDM base data forward from 2012-13 to 2013-14. The 2012-13 base data used a modified form of residential house prices in 2012-13. Using the 2013-14 data means this modification is no longer required and this increases the forecast. There is also a positive effect from the increased transactions forecast. This outweighs the effect of a downward revision in residential prices.

Table 3.3: Changes in residential LBTT since March

| | £ million | | | | |
|----------------------------|-----------|---------|---------|---------|---------|
| | 2015-16 | 2016-17 | 2017-18 | 2018-19 | 2019-20 |
| Change in residential LBTT | 38 | 27 | 10 | -5 | -13 |
| <i>of which:</i> | | | | | |
| House prices | -2 | -11 | -30 | -52 | -69 |
| Property transactions | 19 | 11 | 4 | 1 | 0 |
| Modelling changes | 21 | 27 | 36 | 46 | 56 |

3.16 Our forecast for commercial LBTT has been increased for every year. Again, this is mostly due the use of 2013-14 base year data in the SDM, which increases receipts by £59 million by 2019-20.

Table 3.4: Changes in commercial LBTT since March

| | £ million | | | | |
|---------------------------|-----------|---------|---------|---------|---------|
| | 2015-16 | 2016-17 | 2017-18 | 2018-19 | 2019-20 |
| Change in commercial LBTT | 70 | 79 | 81 | 81 | 78 |
| <i>of which:</i> | | | | | |
| Property prices | 25 | 32 | 33 | 31 | 25 |
| Property transactions | -2 | -2 | -4 | -5 | -6 |
| Modelling changes | 47 | 49 | 51 | 55 | 59 |

3.17 Our forecast for Scottish LBTT in 2015-16 of £540 million is higher than the Scottish Government's estimate of £381 million. This difference is concentrated in the commercial LBTT forecast. Such are the uncertainties around estimating the fiscal effect of the introduction of new taxes that the difference between the two estimates should not be regarded as significant. In particular, differences in the number of property transactions in Scotland could result in LBTT receipts in 2015-16 that are higher than our forecast or lower than the Scottish Government's forecast. Forecast revisions to residential property transactions can be substantial. More detail on the modelling undertaken to estimate the impact of reforms to UK SDLT and the introduction of the Scottish LBTT can be found in Box 4.5 of the December 2014 EFO.

3.18 Our forecast takes into account the bringing forward of some higher-priced transactions in order to avoid the higher rates in 2015-16 and some delayed transactions at the lower end. These behavioural responses reduce the LBTT forecast by £20 million in 2015-16 with the effect concentrated in the earlier months of the year.

3.19 At the time we closed this forecast, two months of LBTT receipts outturn had been published by Revenue Scotland. In April 2015 there were 7510 total transactions (6900 residential and 610 commercial) raising £17.9 million (£7 million residential and £10.8 million commercial). In May 2015 receipts were £24 million (£11.4 residential and £12.6 million commercial) from 8660 transactions (7840 residential and 820 commercial). Increases of 63 per cent in residential receipts and 17 per cent in commercial receipts in May suggest

there may have been some purchases brought forward from April before the introduction of LBTT.

Welsh forecast

3.20 As described above, the Welsh residential SDLT forecast has been estimated using HMRC's SDM and UK-wide house price and residential transaction forecasts. Welsh commercial SDLT has been forecast as a constant share of UK commercial SDLT. We then include the assumed Welsh share of SDLT policy measures in order to produce a final post-measures forecast. The only new policy measure that affects the UK SDLT forecast is *Non-domiciles: IHT on UK residential property* but the effect on the Welsh forecast is less than £1 million.

Table 3.5: Welsh SDLT forecast

| | £ million | | | | | |
|-------------------------|-----------|---------|---------|---------|---------|---------|
| | 2015-16 | 2016-17 | 2017-18 | 2018-19 | 2019-20 | 2020-21 |
| Total SDLT | | | | | | |
| March 2015 | 165 | 188 | 221 | 259 | 295 | |
| July 2015 | 179 | 197 | 220 | 248 | 277 | 307 |
| Difference | 14 | 9 | -1 | -11 | -18 | |
| Residential SDLT | | | | | | |
| March 2015 | 89 | 110 | 141 | 175 | 208 | |
| July 2015 | 101 | 116 | 136 | 162 | 188 | 215 |
| Difference | 12 | 6 | -5 | -13 | -20 | |
| Commercial | | | | | | |
| March 2015 | 76 | 77 | 80 | 83 | 87 | |
| July 2015 | 78 | 81 | 84 | 86 | 89 | 92 |
| Difference | 2 | 4 | 4 | 3 | 2 | |

3.21 Table 3.5 shows that the forecast for Welsh SDLT is to increase by 71 per cent across the forecast period. Since our March forecast, Welsh residential SDLT has been revised up in 2015-16 and 2016-17 and revised down for the remainder of the forecast. This is in line with the UK forecast as described above. Table 3.6 shows that the latest receipts outturn and higher transactions in 2015-16 and 2016-17 are driving the increase in the early part of the forecast. House prices are lower throughout the forecast, and in the later years these are the main reason for the drop off in receipts.

Table 3.6: Changes in Welsh residential SDLT forecast since March

| | £ million | | | | |
|-----------------------------|-----------|---------|---------|---------|---------|
| | 2015-16 | 2016-17 | 2017-18 | 2018-19 | 2019-20 |
| Changes to residential SDLT | 12 | 6 | -5 | -13 | -20 |
| <i>of which:</i> | | | | | |
| House prices | -1 | -4 | -10 | -17 | -23 |
| Property transactions | 7 | 4 | 1 | 0 | 0 |
| Modelling changes | -2 | -3 | -3 | -4 | -5 |
| Latest receipts | 8 | 8 | 8 | 8 | 8 |

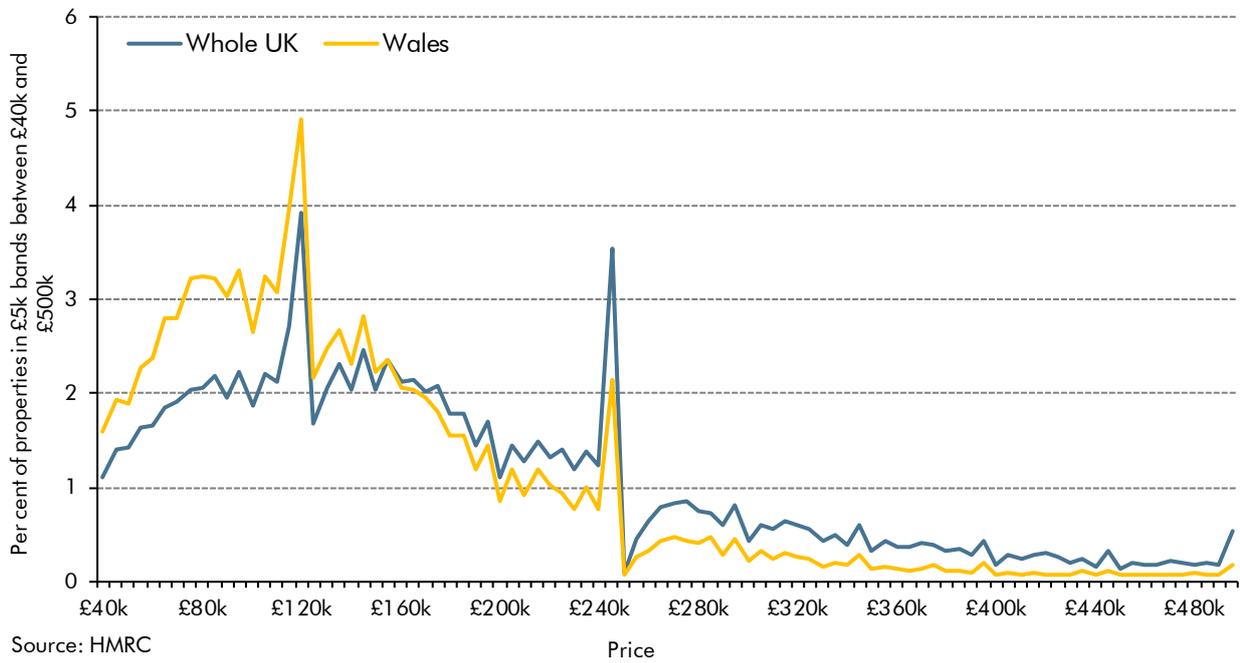
3.22 We have increased commercial SDLT revenues for each year of the forecast. Table 3.7 shows that this is mainly due to the modelling changes highlighted above and higher prices. This offsets lower transactions and updated 2014-15 receipts outturns.

Table 3.7: Changes in Welsh commercial SDLT forecast since March

| | £ million | | | | |
|----------------------------|-----------|---------|---------|---------|---------|
| | 2015-16 | 2016-17 | 2017-18 | 2018-19 | 2019-20 |
| Changes to commercial SDLT | 2 | 4 | 4 | 3 | 2 |
| <i>of which:</i> | | | | | |
| Property prices | 2 | 3 | 3 | 3 | 2 |
| Property transactions | -1 | -1 | -1 | -2 | -2 |
| Modelling changes | 3 | 4 | 4 | 3 | 3 |
| Latest receipts | -2 | -1 | -2 | -1 | -2 |

3.23 There are a relatively high proportion of transactions in Wales close to the 2 per cent threshold in the new UK SDLT regime (£125,000), as shown in Chart 3.3. This creates greater fiscal drag in Wales in the SDM modelling of Welsh SDLT receipts than was implied under the old slab regime, which encouraged bunching below thresholds because of the substantial impact on the amount of tax paid when moving from below to above a threshold. The change to a slice system in December 2014 means that transactions at prices just below the threshold are more likely to move up into the SDLT regime over time.

Chart 3.3: Distribution of house prices in Wales compared to the UK, 2013-14



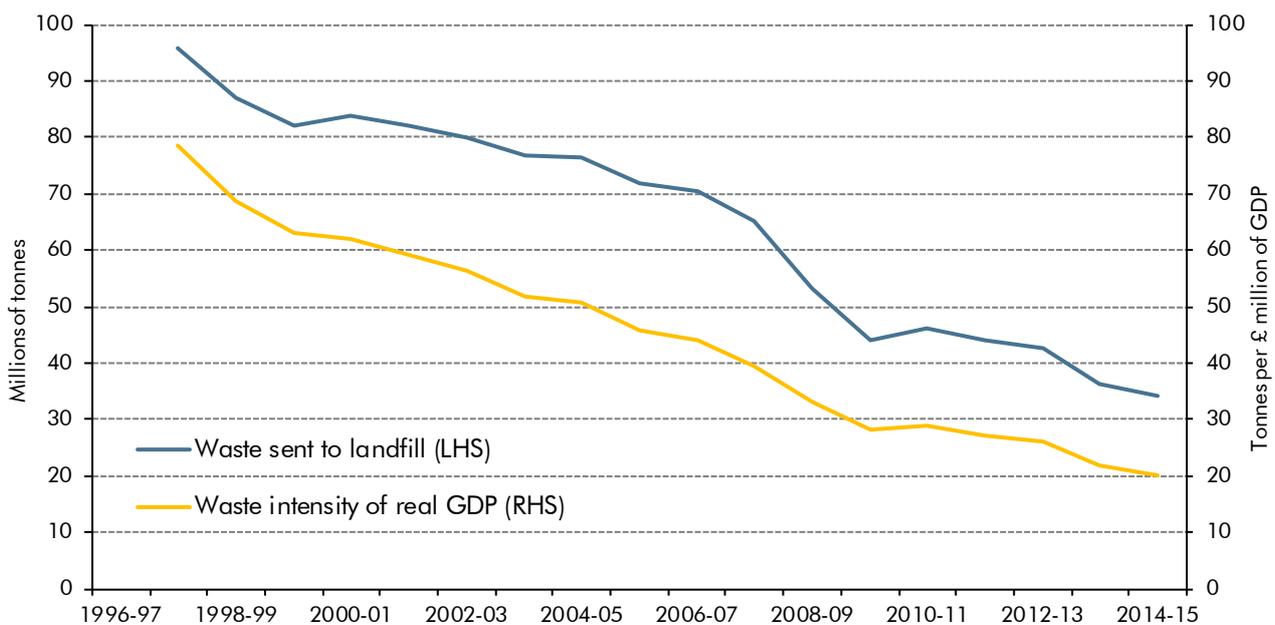
4 Environmental taxes

Landfill tax

Trends in UK landfill tax receipts

- 4.1 Landfill tax is a tax on the disposal of waste that was introduced in 1996. It applies to all waste disposed of by way of landfill at a licensed landfill site unless the waste is specifically exempt. Our forecast for UK landfill tax is driven by the tax base (the amount of waste sent to landfill) and the effective tax rate that will be paid (largely driven by policy decisions on the rates paid, but also by the composition of waste sent to landfill as there are two different tax rates). Both elements represent sources of uncertainty in the forecast.
- 4.2 Since waste is largely a by-product of economic activity, we would expect the tax base to be associated with GDP growth. And since the tax is paid on the volume of waste (per tonne), the relationship should be with real GDP. As Chart 4.1 shows, that relationship has been one of declining volumes of waste per unit of real GDP. Indeed, since landfill tax was introduced, there has been a clear downward trend in the amount of waste sent to landfill in the UK, falling from 97 million tonnes in 1997-98 to 34 million tonnes in 2014-15.

Chart 4.1: UK landfill waste tonnage relative to economic activity

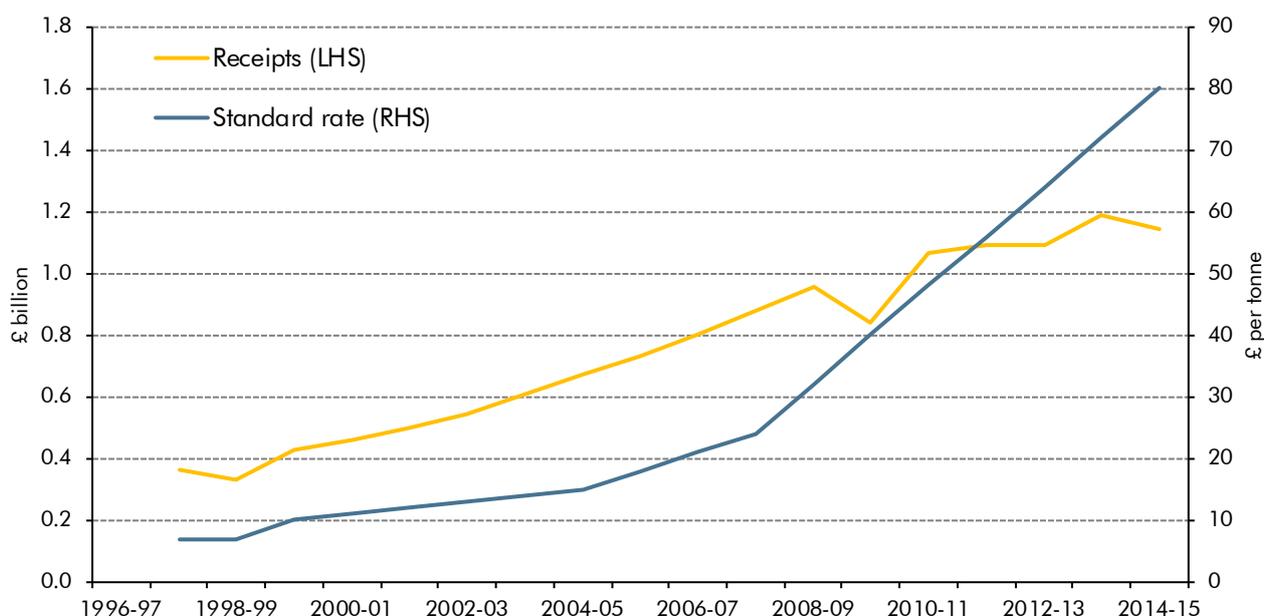


Source: HMRC, ONS, OBR

- 4.3 As Chart 4.2 shows, despite a declining tax base, landfill tax receipts have risen significantly over the past 15 years, mainly due to large increases in the duty rate. The standard rate has

been raised from £7 a tonne in 1997-98 to £80 a tonne in 2014-15. This has more than offset the reduction in the effective tax rate caused by a steady decline in the proportion of waste sent to landfill that is subject to the standard rate – itself partly due to HMRC losing a court case that led to a narrowing of the scope of the standard rate.

Chart 4.2: UK landfill tax standard rate and receipts



Source: HMRC, ONS, OBR

Scottish rate

4.4 Landfill tax was fully devolved to the Scottish Government in April 2015. In October 2014, as part of the Scottish Government’s Draft Budget, it was announced that landfill tax rates will be set in line with those in the rest of the UK in 2015-16.

Welsh rate

4.5 The Wales Act provides for landfill tax to be fully devolved from April 2018. As with SDLT, we assume that the Welsh Assembly will implement the UK regime and forecast landfill tax on that basis. We will update this assumption when sufficient detail about any replacement tax is available.

Methodology

4.6 The Scottish and Welsh landfill tax forecasts are produced by applying an assumption about the path of the Scottish and Welsh share of landfill tax to the UK forecast.

4.7 As noted above, the UK forecast is compiled using a forecast for the tonnage of waste sent to landfill, which is multiplied by the appropriate tax rate. The tonnage forecast is generated from separate Department for Environment, Food and Rural Affairs (DEFRA) projections of municipal solid waste, and commercial and industrial waste, sent to landfill. The expected

amount of municipal waste sent to landfill is estimated by comparing the cost of alternative waste treatment options. DEFRA's detailed models cover England, so are scaled up to get to a UK-wide forecast. The split between standard and lower tax rates is based on historical trends. The tax rates are assumed to be updated in line with RPI inflation in the absence of announced policy.

4.8 Data on the Scottish and Welsh shares of landfill tax receipts are not currently available, since landfill operators submit data returns that cover sites throughout the UK. The shares are therefore estimated from various data sources on landfill tonnages. The Scottish share uses data from the Scottish Environment Protection Agency that covers only Scotland. The Welsh share is calculated using data from Natural Resource Wales. This is a detailed dataset that offers comprehensive coverage of the amount of waste sent to landfill in Wales. Data for Northern Ireland are sourced from the Department of the Environment Northern Ireland to allow us to complete the picture for total UK landfill tonnage and calculate the Scottish and Welsh shares.

4.9 We add the effect of any new policy measures to produce a post-measures forecast.

UK forecast

4.10 The latest available landfill tonnage data is shown in Table 4.1. Since our March forecast data for 2013-14 has been released and shows a continuation in the downward trend. There has been a 38 per cent decline in since 2006-07 for the UK overall and there has been a steeper decline in both Scotland (42 per cent) and Wales (44 per cent).

Table 4.1: Landfill tonnage in the UK

| | Tonnes (million) | | | | | | | |
|------------------|----------------------|---------|---------|---------|---------|---------|---------|---------|
| | 2006-07 | 2007-08 | 2008-09 | 2009-10 | 2010-11 | 2011-12 | 2012-13 | 2013-14 |
| England | 63.9 | 59.0 | 51.4 | 43.9 | 43.8 | 44.0 | 41.6 | 40.4 |
| Scotland | 7.3 | 7.1 | 5.9 | 4.7 | 4.6 | 4.6 | 4.4 | 4.3 |
| Wales | 3.8 | 3.1 | 2.8 | 2.5 | 2.3 | 2.2 | 2.2 | 2.1 |
| Northern Ireland | 2.0 | 1.9 | 1.7 | 1.6 | 1.5 | 1.3 | 1.2 | 1.1 |
| UK | 77.0 | 71.1 | 61.8 | 52.7 | 52.3 | 52.1 | 49.4 | 47.9 |
| | Per cent of UK total | | | | | | | |
| Scotland | 9.5 | 10.0 | 9.5 | 9.0 | 8.9 | 8.9 | 9.0 | 8.9 |
| Wales | 4.9 | 4.4 | 4.5 | 4.7 | 4.4 | 4.2 | 4.4 | 4.5 |

4.11 The UK landfill tax forecast¹ in Table 4.2 has been revised down slightly since March and continues to reflect lower DEFRA projections of local authority waste sent to landfill. Receipts for 2014-15 came in 1 per cent lower than forecast and this has been pushed through to the remaining years of the forecast. There are no landfill tax policy measures at the Budget.

¹ The UK, Scottish and Welsh landfill forecasts in March were restated after errors were found in the UK-wide tax base forecast. These restated forecasts can be found at: <http://budgetresponsibility.org.uk/wordpress/docs/Correction-to-landfill-tax-revenue-forecast-March-2015-Economic-and-fiscal-outlook.pdf>

Table 4.2: UK landfill tax forecast

| | £ million | | | | | | |
|------------|-----------|---------|---------|---------|---------|---------|---------|
| | 2014-15 | 2015-16 | 2016-17 | 2017-18 | 2018-19 | 2019-20 | 2020-21 |
| March 2015 | 1135 | 1070 | 1003 | 984 | 1016 | 1092 | |
| July 2015 | 1122 | 1059 | 990 | 974 | 1008 | 1084 | 1156 |
| Difference | -13 | -11 | -13 | -10 | -8 | -8 | |

Scottish forecast

4.12 The forecast for Scottish landfill tax in Table 4.3 has been revised down in line with our UK forecast, with most of the change due to lower than expected receipts in 2014-15. Receipts are forecast to decline to £87 million in 2016-17 before increasing to £103 million by 2020-21. We hold the Scottish share of landfill tax constant at 8.9 per cent, in line with the 2013-14 proportion of landfill tonnage in Table 4.1, the most recent year available. It is possible the Scottish share has risen since 2013-14 and may be one reason why our 2015-16 forecast is lower than the £118 included in the Scottish Government's Draft Budget.

4.13 This forecast has not taken into account the aspirations of the Scottish government to reduce landfill tonnage more rapidly than rates in England. If this aspiration can be translated to a firm policy target with relevant supporting analysis we can then consider it for the forecast. For now it is noted as a fiscal risk.

Table 4.3: Scottish landfill tax forecast

| | £ million | | | | | | |
|------------|-----------|---------|---------|---------|---------|---------|---------|
| | 2014-15 | 2015-16 | 2016-17 | 2017-18 | 2018-19 | 2019-20 | 2020-21 |
| March 2015 | 103 | 97 | 91 | 90 | 92 | 99 | |
| July 2015 | 100 | 94 | 88 | 87 | 90 | 96 | 103 |
| Difference | -3 | -3 | -3 | -3 | -2 | -3 | |

Welsh forecast

4.14 The Welsh landfill tax forecast in Table 4.4 moves in line with our UK forecast, with lower outturn receipts in 2014-15 pushed through to the remaining years of the forecast. The Welsh share of UK receipts is assumed to remain flat at 4.5 per cent, so the forecast follows the same path as the UK forecast; 4.5 per cent is the Welsh share of landfill tonnage from the most recent available year of data, as shown in Table 4.1. Receipts are unchanged for every year of the forecast: dropping from £49 million in 2014-15 to £43 million in 2017-18 before rising to £49 million in 2020-21.

4.15 Once again, this forecast does not make allowance for the Welsh government's aspiration to reduce landfill tonnage at a greater rate than in England. If this can be converted to a firm policy target with relevant supporting analysis we can then consider it for the forecast. For now it is noted as a fiscal risk.

Table 4.4: Welsh landfill tax forecast

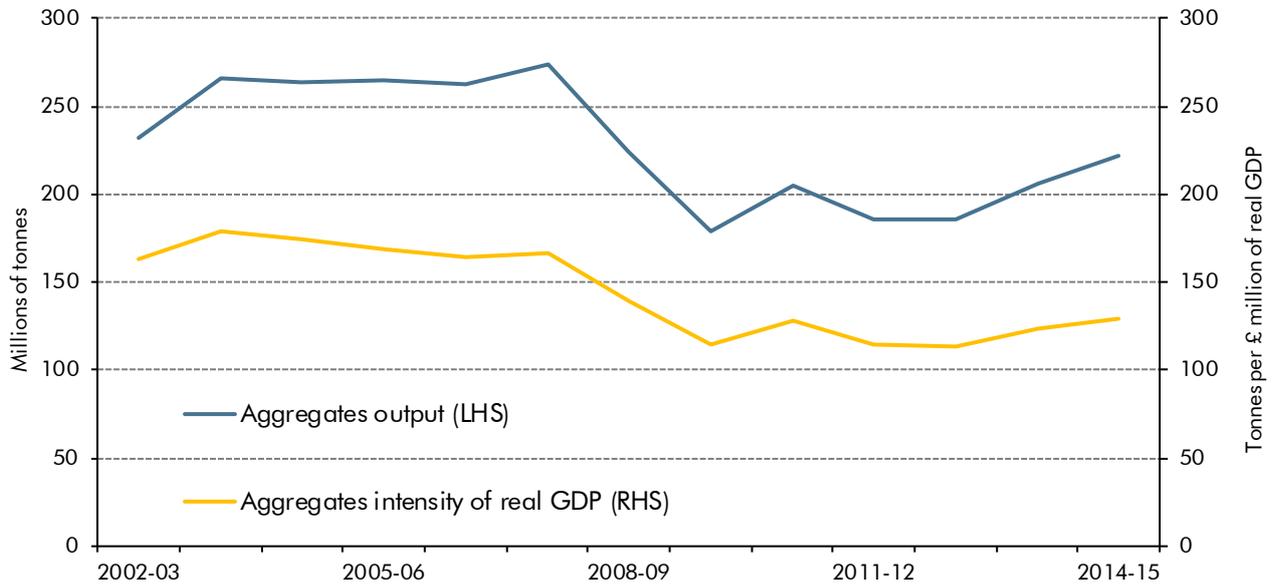
| | £ million | | | | | | 2020-21 |
|------------|-----------|---------|---------|---------|---------|---------|---------|
| | 2014-15 | 2015-16 | 2016-17 | 2017-18 | 2018-19 | 2019-20 | |
| March 2015 | 50 | 47 | 44 | 43 | 45 | 48 | |
| July 2015 | 50 | 47 | 44 | 43 | 45 | 48 | 51 |
| Difference | 0 | 0 | 0 | 0 | 0 | 0 | |

Aggregates levy

Trends in UK aggregates levy receipts

- 4.16 The aggregates levy is a tax on the commercial exploitation in the UK of rock, sand and gravel. It is due from any business that quarries, dredges or imports these products. The levy came into effect in 2002. Our forecast for UK aggregates levy is driven by the tax base (the volume of aggregates) and the effective tax rate that will be paid (largely driven by policy decisions on the rates paid, but also by the composition of the tax base as some aggregates are relieved or exempt from the levy). The tax base represents the main source of uncertainty in the forecast.
- 4.17 Since aggregates are largely an input into broader economic activity, we would expect the tax base to be associated with GDP growth. And since the tax is paid on the volume of aggregates (per tonne), the relationship should be with real GDP. As Chart 4.3 shows, that relationship has been one of relatively stable volumes of aggregate per unit of real GDP, with a shift in the level during the late 2000s recession that has persisted. Since the aggregates levy was introduced, output in absolute terms was relatively stable during the pre-crisis period, then fell sharply in 2009-10, and has again been relatively stable since, though the recently updated 2014-15 data hints at an upturn.

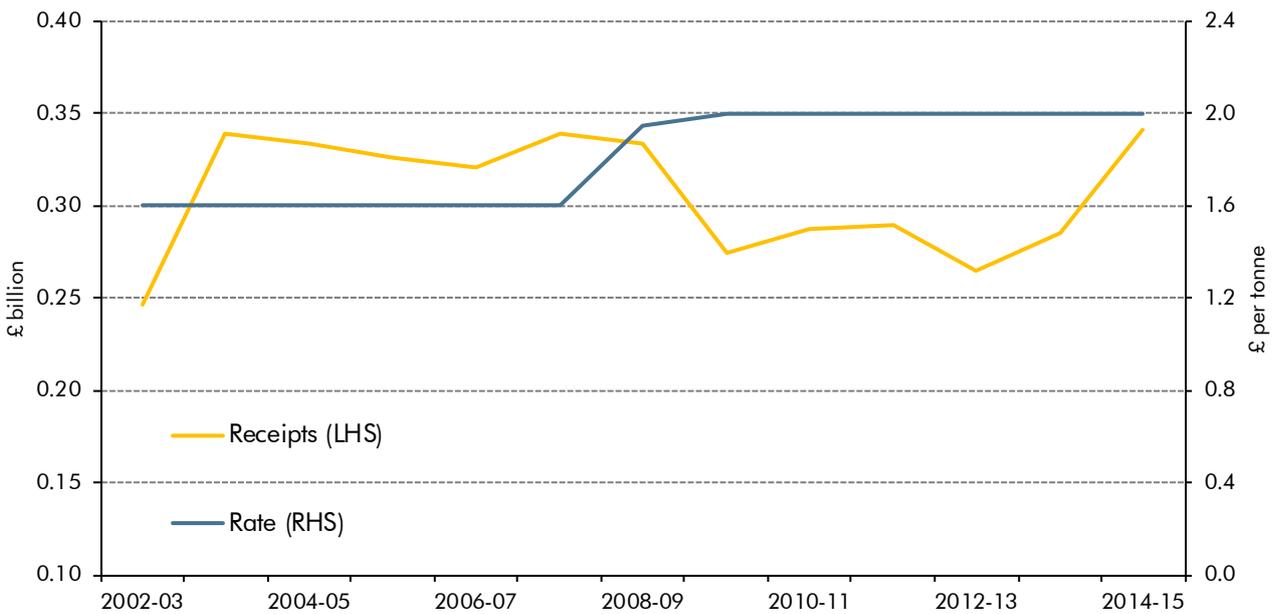
Chart 4.3: UK aggregates output relative to economic activity



Source: HMRC, ONS, OBR

4.18 As Chart 4.4 shows, aggregates levy receipts fell significantly after 2008-09 but have now returned to their pre-crisis levels. The increases in the rate per tonne in 2008-09 and 2009-10 were not sufficient to offset the fall in the tax base in 2009-10, which meant annual receipts fell from slightly above £300 million a year in the pre-crisis period to slightly below £300 million a year.

Chart 4.4: UK aggregates levy rate and receipts



Source: HMRC

Scottish and Welsh rates

4.19 The Government has committed to keeping the devolution of aggregates levy to Scotland and Wales under review. It intends, subject to the resolution of a legal challenge in the European courts, to devolve this tax in the future. In the interim, the Treasury will assign aggregates levy receipts to Scotland and Wales.

Methodology

4.20 The UK forecast is generated from a projection of the tax base multiplied by the tax rate. An econometric model relates the sales of primary aggregates to construction sector growth. The model also allows for the usage of recycled aggregates to increase over time and for substitution away from the extraction of primary aggregates. The tax rate is assumed to be updated in line with RPI inflation in the absence of announced policy.

4.21 To produce Scottish and Welsh aggregates levy forecasts, we apply our assumptions for their respective shares to the UK receipts forecast. These shares are estimated using data on the Scottish and Welsh share of aggregates production from the United Kingdom Mineral Yearbook 2013, which are shown in Table 4.5.

Table 4.5: Aggregates tonnage in the UK

| | Tonnes (million) | | | | | | |
|------------------|----------------------|--------------|--------------|--------------|--------------|--------------|--------------|
| | 2006-07 | 2007-08 | 2008-09 | 2009-10 | 2010-11 | 2011-12 | 2012-13 |
| England | 152.8 | 140.1 | 136.8 | 106.2 | 95.4 | 104.8 | 95.9 |
| Scotland | 33.3 | 37.2 | 32.3 | 28.4 | 28.6 | 27.5 | 24.8 |
| Wales | 21.0 | 20.8 | 18.0 | 12.2 | 12.6 | 13.6 | 12.3 |
| Northern Ireland | 6.1 | 6.7 | 5.3 | 4.8 | 3.9 | 20.0 | 18.4 |
| UK | 213.3 | 204.8 | 192.5 | 151.6 | 140.5 | 165.9 | 151.3 |
| | Per cent of UK total | | | | | | |
| Scotland | 15.6 | 18.2 | 16.8 | 18.7 | 20.3 | 16.6 | 16.4 |
| Wales | 9.9 | 10.2 | 9.4 | 8.1 | 9.0 | 8.2 | 8.1 |

4.22 Finally, we add the Scottish and Welsh element of any policy measures to produce the post-measures forecast.

UK forecast

4.23 Table 4.5 shows that the decline in aggregates tonnage across the UK since 2006-07 has been 29 per cent. For Scotland it is slightly lower, 26 per cent, but it is significantly higher in Wales, which has seen a 41 per cent decline. The major change to the UK forecast was the result of a European Commission ruling on the treatment of aggregate levy exemptions. The levy allows for a number of exemptions but these were suspended from April 2014 as part of a Commission investigation over whether they breached state aid rules. Following suspension of the exemption they were removed from the forecast. In March 2015 the Commission ruled the exemptions were lawful and the government subsequently reinstated

them, so we have included them in our latest forecast. Very little else has changed since our March forecast though there is a slight positive effect from receipts in 2014-15 coming in marginally higher than forecast. There are no aggregates levy policy measures at the Budget.

Table 4.6: UK aggregates levy forecast

| | £ million | | | | | | |
|------------|-----------|---------|---------|---------|---------|---------|---------|
| | 2014-15 | 2015-16 | 2016-17 | 2017-18 | 2018-19 | 2019-20 | 2020-21 |
| March 2015 | 349 | 334 | 335 | 338 | 342 | 345 | |
| July 2015 | 352 | 314 | 335 | 340 | 343 | 346 | 349 |
| Difference | 3 | -20 | 0 | 2 | 1 | 1 | |

Scottish forecast

4.24 The Scottish share of aggregates is relatively high as shown in Table 4.5, around 15 to 20 per cent of the UK total. For this forecast we hold the Scottish share constant at 16.4 per cent, which is the most recent year for which data is available. The forecast therefore follows the UK forecast very closely. Receipts drop to £51 million in 2015-16 due to the reinstatement of levy exemptions before steadily rising to £57 million in 2020-21.

Table 4.7: Scottish aggregates levy forecast

| | £ million | | | | | | |
|------------|-----------|---------|---------|---------|---------|---------|---------|
| | 2014-15 | 2015-16 | 2016-17 | 2017-18 | 2018-19 | 2019-20 | 2020-21 |
| March 2015 | 57 | 55 | 55 | 55 | 56 | 57 | |
| July 2015 | 58 | 51 | 55 | 56 | 56 | 57 | 57 |
| Difference | 0 | -3 | 0 | 0 | 0 | 0 | |

Welsh forecast

4.25 The Welsh share of aggregates is also relatively high as a proportion of the UK, around 8 to 10 per cent as in Table 4.5. For this forecast we hold the Welsh share constant at 8.1 per cent, which is the most recent year for which data is available. The forecast therefore follows the UK forecast very closely. Receipts drop to £25 million due to the reinstatement of levy exemptions before steadily rising to £28 million in the latter years of the forecast.

Table 4.8: Welsh aggregates levy forecast

| | £ million | | | | | | |
|------------|-----------|---------|---------|---------|---------|---------|---------|
| | 2014-15 | 2015-16 | 2016-17 | 2017-18 | 2018-19 | 2019-20 | 2020-21 |
| March 2015 | 28 | 27 | 27 | 27 | 28 | 28 | |
| July 2015 | 29 | 25 | 27 | 28 | 28 | 28 | 28 |
| Difference | 0 | -2 | 0 | 0 | 0 | 0 | |

