

Explanatory Memorandum to the Land Transaction Tax (Tax Bands and Tax Rates) (Wales) (Amendment) Regulations 2022

This Explanatory Memorandum has been prepared by the Economy, Treasury and Constitution Group of the Welsh Government and is laid before Senedd Cymru in conjunction with the above subordinate legislation and in accordance with Standing Order 27.1.

Minister's Declaration

In my view, this Explanatory Memorandum gives a fair and reasonable view of the expected impact of the Land Transaction Tax (Tax Bands and Tax Rates) (Wales) (Amendment) Regulations 2022. I am satisfied that the benefits justify the likely costs.

Rebecca Evans MS
Minister for Finance and Local Government
07 October 2022

1. Description

- 1.1 The purpose of this instrument is to specify a change to the land transaction tax (“LTT”) rates and bands that will apply to purchases of certain residential property transactions.

2. Matters of special interest to the Legislative, Justice and Constitution Committee

- 2.1 This instrument is made under the provisional affirmative procedure set out in section 25(2) of the Land Transaction Tax and Anti-avoidance of Devolved Taxes (Wales) Act 2017 (“the 2017 Act”). These regulations are therefore made without a draft having been laid before, and approved by, the Senedd. Further details about this procedure can be found in paragraph 3.2, below.
- 2.2 This instrument contains regulations made under section 78(1) of the 2017 Act to make transitional provision in connection with certain transactions where contracts are substantially performed or exchanged before 10 October 2022, but completion takes place on or after that date. Section 79(3) and (4) of the 2017 Act provides that regulations made under section 78(1) are subject to the negative procedure unless the Welsh Ministers consider the effect of the regulations is that the amount of tax chargeable is more than the amount which would be chargeable if the regulations are not made, which would then invoke the draft affirmative procedure. In these regulations, whilst the amount of tax chargeable is more for transactions over £345,000 (up to a maximum of £550), the buyer has an option to elect to pay the new or former bands and rates and such an election can only be made if it would not result in more tax being chargeable than would otherwise have been the case. The transitional rules therefore do not have the effect of increasing the tax chargeable and accordingly are subject to the negative procedure.
- 2.3 Where there are two separate procedures for provisions which are required to be included in the same regulations, section 40 of the Legislation (Wales) Act 2019 provides a hierarchy of procedures by which to determine which procedure should be used. In this instance, where there are both negative and provisional affirmative procedures, the provisional affirmative procedure will be the correct procedure.

3. Legislative background

- 3.1 Section 24(1) of 2017 Act provides the Welsh Ministers with powers to vary the tax rates and tax bands for LTT through regulations.
- 3.2 Regulations made under this section are subject to a provisional affirmative procedure, which means the regulations are made (signed) by the Ministers and can come into force immediately. Once the regulations have been made, they must be laid before the Senedd and will have temporary effect until they are voted on by the Senedd. That vote must happen within 28 calendar days of the regulations being made, not counting days when the Senedd is in recess. If the vote does not occur, or is lost, the former tax rates and tax bands again apply and any taxpayer who has paid a higher amount of tax under the regulations that failed to achieve Senedd approval can reclaim the difference between that payable under those regulations and the rates previously, and again, in force. This means that the risk of the regulations failing to achieve Senedd approval will rest with the Welsh Government and not Welsh taxpayers.
- 3.3 The 28-day period commences on 6 October 2022 and, as the Senedd is in recess from 31 October to 6 November 2022, the vote to approve the regulations must occur by 9 November 2022.

4. Purpose & intended effect of the legislation

- 4.1 The purpose of these regulations is to change the tax bands and percentage tax rates of LTT used to calculate liabilities for main rates residential property transactions with an effective date¹ on or after 10 October 2022, as announced by the Minister for Finance and Local Government on 27 September 2022. These changes are being made to reflect house price growth since the previous rates came into force in April 2018 and reduce tax for the majority of taxpayers without reducing tax for those in the top 15% of transactions by price.
- 4.2 The effect of these regulations is to increase the threshold of the zero-rate tax band from £180,000 to £225,000, and amend the first tax band so that it covers transactions of 'more than £225,000 but not more than £400,000'. The regulations also change the rate in that first tax band to 6%. The tax bands which cover transactions of 'more than £400,000 but not more than £750,000' and above, and the rates which apply in those bands are unchanged.
- 4.3 The new zero rate threshold is £45,000 higher than the current starting threshold for residential property transactions subject to the main rates and, in combination with the change to the rate for the first tax band, the effect of the regulations will be to reduce tax for transactions up to £345,000 up to a maximum of £1,575. For those transactions where consideration given is over £345,000 the amount of tax payable will increase by up to a maximum of £550. This provides support for the majority of taxpayers, who may need additional support because of house price growth, while reducing the amount of revenue foregone by a more modest increase in tax payable for transactions in the top 15% of transactions by price.
- 4.4 These regulations do not make any changes to the tax bands and percentage tax rates applicable to higher rates residential property transactions, non-residential property transactions, or transactions where the chargeable consideration consists of rent². The higher rates and thresholds for buyers of properties such as buy to let or as a second home therefore remain unchanged and significantly higher than the main rates.

¹ The 'effective date' is, broadly, the date of completion of the contract to purchase the property.

² The Land Transaction Tax (Tax Bands and Tax Rates) (Wales) Regulations 2018 (S.I. 2018/128 (W. 32)) makes provision as to the rates and bands of LTT applicable to higher rates residential property transactions, non-residential property transactions, and transactions where chargeable consideration consists of rent.

4.5 The LTT residential property main rates will, for transactions completed on or after 10 October 2022, be:

Table 1: Residential Property Transactions - Rates and Bands from 10 October 2022

Main rates residential property transactions		
<u>Tax band</u>	<u>Relevant consideration</u>	<u>Percentage tax rate</u>
Zero rate band	Not more than £225,000	0%
First tax band	More than £225,000 but not more than £400,000	6%
Second tax band	More than £400,000 but not more than £750,000	7.5%
Third tax band	More than £750,000 but not more than £1,500,000	10%
Fourth tax band	More than £1,500,000	12%

5. Consultation

5.1 There is no statutory requirement to consult on this instrument. The increase to the zero-rate band was announced by the Minister for Finance and Local Government on 27 September 2022. The timing takes account of calls from some stakeholders and taxpayers for amended rates and bands to be introduced and achieves the Welsh Government's aim of ensuring that those buying homes at the lower to middle of the market pay no or low amounts of tax. However, the setting of rates and thresholds for taxes is not an area of policy where consultation is undertaken, as any such consultation with a 'live' tax is highly likely to have a distortive effect on behaviours and, in relation to transaction taxes, the timing of those transactions.

6. Regulatory Impact Assessment

- 6.1 The revenue impact of these changes will be provided alongside the next Welsh Government draft Budget. The costing of the policy will be agreed with the Office for Budget Responsibility and included as part of its forecast of land transaction tax (LTT) revenues for the Welsh Government.
- 6.2 When setting rates and tax bands there are many possible options. This assessment covers a no change option and the policy within these regulations only. The decision to increase the zero-rate threshold has been made to respond to house price growth and provide support to the majority of homebuyers.
- 6.3 The decision to increase the rate for the new first tax band has been made to limit the tax reduction provided by the zero-rate threshold to transactions up to £345,000. Transactions over £345,000 are in the top 15% of transactions. In the context of challenging budgets, the decision has been made not to provide support to those purchasing the most expensive

properties in Wales, thereby reducing the cost of the changes and ensuring the Welsh Government has funding available for essential public services as a result.

No change

- 6.4 The no change option would have left all main residential rates and thresholds as they have been since April 2018 when land transaction tax first applied in Wales. In 2018, these rates meant 64% of homebuyers did not pay any tax when buying their home, including the vast majority of first-time buyers. In April 2018, the average house price was around £154,000 and the average first-time buyer price was £133,000. In July 2022³, the average house price had risen to around £220,000 and the average first-time buyer price to around £190,000.
- 6.5 Leaving the rates and thresholds unchanged from 2018 would not be responsive to rapidly rising house prices and would be forecast to result in 53% of transactions being liable for tax in 2023-24, compared to 36% when the rates were introduced in 2018-19.

£225,000 zero-rate threshold and 6% rate for transactions of more than £225,000 and not more than £400,000

- 6.6 This option is an increase to the residential main rates zero-rate threshold from £180,000 to £225,000, and a change to the first tax band to cover transactions over £225,000 up to and including £400,000 with a rate for that new band to be 6%. This change will, broadly, not apply to transactions where the purchaser already owns an interest in another residential property (a dwelling), see paragraph 6.8 below.
- 6.7 As a result of this change around 85% of Welsh homebuyers will either pay no tax or less tax than currently. For properties costing up to £345,000 there will be a tax reduction of up to £1,575. For properties costing more than £345,000, representing the top 15% of homebuyers, there will be a tax increase of up to £550. This option means tax reductions are not provided to those with the resources to purchase the most expensive properties in Wales and instead those transactions will pay more tax to help mitigate the reduction in revenue from the increase in the zero-rate threshold.
- 6.8 This option does not provide a tax reduction for those properties that are subject to the higher residential rates of land transaction tax. The higher residential rates apply to companies buying any dwellings and to individuals, broadly, who are buying residential properties when they, or an individual they are buying with, already own an interest in another dwelling. This is most likely to apply to the purchases of dwellings to be used as second homes and buy-to-let properties.
- 6.9 This option ensures the benefits of the tax savings are restricted to those with only an interest in the property they are buying (or who meet the replacement of a main residence rules) and not those purchasing buy to let properties, second or holiday homes. Purchasers who pay the higher residential rates account for around 25% of all residential purchases each year. Some of these transactions may subsequently be refunded the higher residential rates and then be subject to the main residential rates when the buyer is bridging between two homes.
- 6.10 Based on the latest Office for Budget Responsibility forecasts (March 2022), this option means 61% of transactions are forecast to be below £225,000 in 2023-24. This provides a tax reduction for around 20,000 (around 40%) of transactions in 2023-24 for those transactions priced between £180,000 and £345,000 where the main residential rates apply. Around 7,000 (15%) of transactions would be expected to pay up to £550 more in tax with this option. The majority of first-time buyers are expected to be below the new threshold and pay no tax. These changes are expected to have relatively minor effects on

³ The most recent House Price Index, relating to July 2022, was published on 14 September 2022.

the housing market. It is expected to provide a small boost to transactions by around 0.5% (less than 500) and a very small positive impact on prices (less than 0.1%).

- 6.11 There will be little additional administrative cost to the Welsh Revenue Authority ('WRA') as a result of updating its online tax calculators and responding to taxpayer queries about the change. These costs will be met within its current budget. Businesses involved in the various stages of house purchases, especially estate agents and conveyancers and solicitors have dealt with many rate (and method of calculation) changes before through SDLT, the introduction of LTT in Wales, and subsequent changes. This option will be limited to a single table of tax rates. There has been clear communication of the changes and the WRA has provided a revised LTT calculator to establish liability. The additional costs to these businesses should therefore be minimal.

7. Post Implementation review

- 7.1 Section 77 of the 2017 Act provides that the Welsh Ministers must make arrangements for an independent review of land transaction tax to be completed within six years of the day after the day of the 2017 Act receiving Royal Assent. A review of LTT is currently underway and will encompass all of the subordinate legislation made under the 2017 Act.