A tourist levy

What, where and how

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What, where and how

Tourism is a significant contributor to the UK Exchequer. Revenues are derived directly from tourist expenditure via taxes such as Air Passenger Duty and VAT, and indirectly from the effects of tourist expenditure on taxes such as corporation tax and income tax.[1]

The idea of a local tourist levy in the UK has recently risen in prominence – Bath, Liverpool, Edinburgh, Birmingham and London have all raised the prospect of introducing one. With numerous cities across the world having a charge on tourist visitors, there are plenty of examples of how a tourist levy works in practice (see, below).[2]

Examples of different tourist occupancy taxes in Europe

- **Paris** has a charge per person per night, with the rate of charge varying by the star rating of the hotel. For instance, 5* rated accommodation has a nightly charge of €3.30 and 2* rated accommodation has a nightly charge of €0.99.
- **Bruges** charges a flat rate of €2 per night per person, with children under the age of 18 exempt from the tax.
- **Berlin's** City Tax is 5 per cent of the net room rate (the room rate net of VAT and fees for services). The tax is capped at 21 successive days. Business travelers are exempt from the tax but have to prove the purpose of their trip.

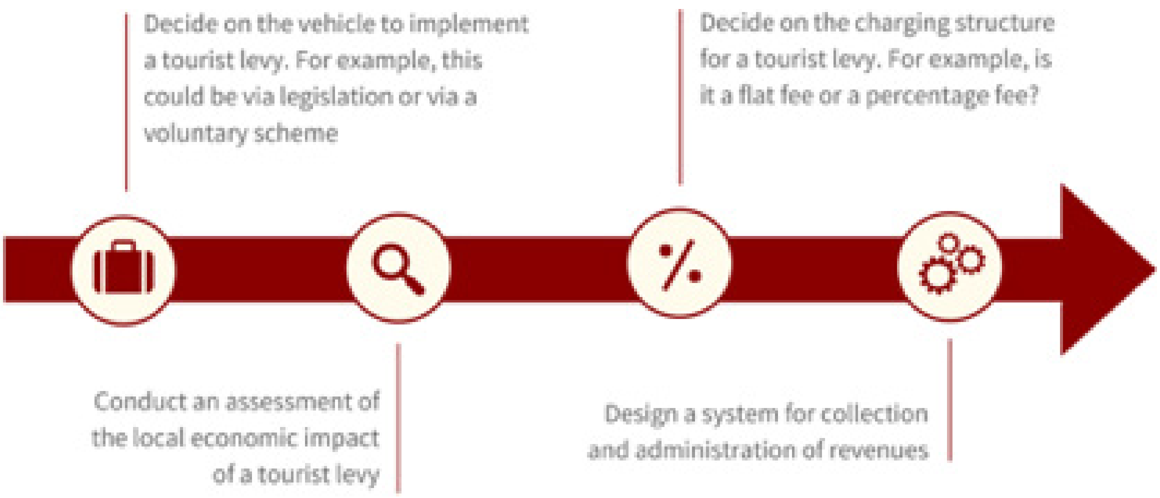
In these cities – and in many others which impose a tourist levy – the revenues from occupancy charges are loosely allocated to tourism or cultural investment. To use technical terminology, there the revenues from tourist levies tend to have some kind of soft hypothecation attached.

Sources[3,4,5]

1 www.visitbritain.org/sites/default/files/vb-corporate/Documents-Library/documents/Tourism_Jobs_and_Growth_2013.pdf
2 www.london.gov.uk/sites/default/files/tourism-levy-for-london-wp83.pdf
3 https://en.parisinfo.com/practical-paris/money/tourist-tax
4 www.visitbruges.be/tourism-tax
5 www.berlin.de/en/tourism/travel-information/3298255-2862820-city-tax-in-berlin-who-is-to-pay-how-muc.en.html

There is a four-stage process to implementing a tourist levy, described below:

The process for introducing a tourist levy



This briefing note looks at the process for introducing a tourism levy by using two pieces of analysis. The first lists the considerations that both local and national policymakers should contemplate when designing a tourist levy. The second shows the results of a modelling exercise related to a tourist levy, which presents:

- an illustration of how much gross revenue local areas can expect to receive from the introduction of a tourist levy
- an illustration of how much net revenue local areas can expect to receive from the introduction of a tourist levy (in other words, whether it is worth a local area introducing a tourist levy or not).

Key considerations for introducing a tourist levy

The following are the key considerations for local and national policymakers when designing a tourist levy. They are based on discussions with policymakers and a literature review. The broad themes could equally be applied to the introduction of any new local levy:

- **The design of a tourist levy**. There are several options for tourist levy design. For example, hotel occupancy could be charged, but the charge itself could be a flat fee, a percentage fee, per person, per room, or several other variations.
- **The economics of a tourist levy**. Introducing a levy increases the price of a holiday. Price changes can affect the spending behaviour of a tourist, but the extent and magnitude of these behavioural changes are unknown and depend on factors like the size of the levy.
- **Practical implementation of a tourist levy**. A tourist levy would ideally need primary legislation to be introduced. But there are other options, such as a voluntary scheme or using Business Improvement Districts as a tool.

These considerations are discussed in more detail below.

The design of a tourist levy

What is the consideration? Local areas would have to decide upon the type of levy that they want to introduce.

What is the implication for greater fiscal freedoms? The type of levy that is introduced will affect the revenues that are raised.

What is the potential solution? Assess overseas examples for the different options to introduce a tourist levy, and model how much revenue they would raise within a local area.

There are three fundamental issues that need to be considered in the design of a tourist levy – the type of levy to be introduced, how the levy is administered and how the proceeds of the levy are used:

- **The type of levy**. The most common type of tourist levy is a charge on the occupancy of a hotel room, but there are variants of it. For example, the charge could be per person or per room, it could be a flat-rate fee or a percentage of the room charge (both of which could vary according to the star-rating of the hotel), and it could apply to all nights spent in the hotel or be capped at a certain number of nights spent in the hotel.
- **The administration of the levy**. One administrative issue to contend with is the growth of the sharing economy – such as Airbnb – which has disrupted the market for tourist accommodation. It would be unfair to levy a charge on more traditional accommodation and not on recent market entrants, as it would distort competition. But there is a question about how to make the new market entrants comply. Indeed, the authorities in Paris addressed this problem by requiring platforms such as Airbnb to collect and remit tourist taxes on behalf of accommodation providers.[6] It should also be noted that a tourist levy would create a burden on hoteliers to collect and remit the tax, but this burden would likely be small given that it is a relatively simple calculation to make. Local areas would also need to employ people to administer the levy, with previous research suggesting that this would require three-quarters of a full-time employee's resource.
- **The proceeds of the levy.** While not a practical barrier to introducing a tourist levy, the political barriers to introducing a levy should be recognised. The conversations that contributed to this research suggested that a way to 'sell' a new levy to businesses and residents is to hypothecate – at least in part – the revenues that are derived from it. For example, the Workplace Parking Levy in Nottingham is ring-fenced for improving public transport in the city (see in box below) and Edinburgh's proposal for a tourist levy is linked to upgrading the infrastructure that is put under strain arising from tourist visitors.[7] To note, using the rationale of introducing a new local charge to fund local services does not always work out – the idea to impose a congestion charge in Manchester to fund a substantial package of transport upgrades was dismissed in a local referendum in 2008.

Sources[8,9]

CASE STUDIES OF RING-FENCING

It is common for tourist levies to use revenues for specific purposes. Indeed, in the discussions held for this research some argued that ring-fencing was necessary to justify a new charge. Two examples of ring-fencing the revenues of a local charge are:

1. **The Workplace Parking Levy (WPL), Nottingham.** All funds raised from the WPL are ring-fenced for investing to meet the objectives of the Local Transport Plan. Therefore, the WPL has paid for extending the tram network, redeveloping Nottingham Railway Station and improving and maintaining the city's bus service.
2. **A payroll levy, France.** The authorities that organise transport at an urban level in France have the option to establish a dedicated transport tax, known as Versement Transport (VT). In the urban areas where VT is imposed, it applies to all employers that have more than 11 employees. The rate of the VT is capped by law.

6 www.europarl.europa.eu/cmsdata/130660/The%20Impact%20of%20Taxes%20on%20the%20Competitiveness%20of%20European%20tourism.pdf
7 www.scotsman.com/business/companies/media-leisure/edinburgh-tourist-tax-voted-through-by-council-1-4748077
8 http://researchbriefings.parliament.uk/ResearchBriefing/Summary/SN00628
9 www.itf-oecd.org/sites/default/files/docs/public-transport-contracts-france.pdf

The economics of a tourist levy

What is the consideration? The potential effects of a tourist levy are many and varied, with little conclusive evidence on what the effects are (or even the size of the effects).

What is the implication for greater fiscal freedom? Despite there being numerous precedents for a tourist levy, there are still a lot of unknowns about the economic effects of introducing one.

What is the potential solution? There is nothing to suggest that introducing a relatively low tourist levy – one that would be a small percentage of the typical tourist spend – as a starting point would cause any economic harm whatsoever.

In general terms, tourist demand is highly responsive to price. But this statement is not true of all types of tourist spending. Those wanting to go on a beach holiday may not be indifferent to location, so long as they get an affordable week in the sun; those wanting to climb the Eiffel Tower will not be indifferent to location, as they can only do it by travelling to Paris.

It is almost impossible to discern the nature – and the magnitude – of the impacts that a tourist levy on room occupancy would have. One unknown is who would bear the cost of the levy. Accommodation providers might soak up the entire cost of the levy or they may pass on the entire cost to the tourist visitor (or the costs may be shared between them both). Another unknown is how tourist visitors might alter their spending in response to the levy – eg the revenue of tourist attractions and restaurants may be affected (which would have subsequent implications for national tax receipts like VAT). Equally, if the levy is not particularly transparent – and it is paid at the end of a stay – then there may be no effect on overall expenditure (although, there could be an effect on repeat tourist visitors).

But there are potential positive effects too – if the proceeds of a tourist levy are put into tourism promotion then a positive effect on tax revenues and spending from increased visitor numbers could be realised.

There have been numerous estimates made of how tourist demand would be affected by a change in price – which is known in economic terms as the 'price elasticity of demand'. The estimates come with a number of caveats attached to them – there are simply too many factors that contribute to a tourist's decision-making to give say anything about demand conclusively.

It should also be stressed, however, that a room occupancy charge could only have a relatively small impact on a tourist's spending. A £1 per night room charge for the average stay of a European visitor to the UK would equate to a 1 per cent increase in their average spend (the average stay is five nights and the average spend level of spending while on the trip is £451). To put this in context, it is the equivalent of the value of the pound relative to the euro strengthening by just over 1 per cent (not an uncommon fluctuation), reducing the European visitor's purchasing power.[10]

Legislating for a tourist levy

What is the consideration? Unless a voluntary scheme is introduced – for which there is little precedent or evidence – a legislative route or use of a Business Improvement District would be needed.

What is the implication for greater fiscal freedoms? It will take time to put a tourist levy in place.

What is the potential solution? Proposing and implementing a Business Improvement District would be the shortest route to implementing a tourist levy, but it is more convoluted and restrictive than implementing a tourist levy through primary legislation.

10 www.ons.gov.uk/peoplepopulationandcommunity/leisureandtourism/datasets/overseasresidentsvisitstotheuk

There are three options for a local area to introduce a tourist levy:

- **Primary legislation**. For example, the Greater London Authority Act 1999 provided the legislative basis for London's congestion charge. The Transport Act 2000 provided the legislative basis for the Workplace Parking Levy in Nottingham. This would require parliamentary time to get the legislation through.
- **Introduce a Business Improvement District (BID)**. A BID is a partnership between a council and local businesses. The basic concept is that selected non-domestic ratepayers in a defined area are charged a levy, usually in the form of a percentage of the rateable value of a ratepayer's property. The funds arising from the levy are ring-fenced for a specific purpose within the BID area. A BID can be applied to a specified class of property, eg a retailer. Non-domestic rate payers who would be liable for the proposed levy get to vote on the BID proposal in a ballot.[11] This means that a local area could propose a BID that applies to hotels – ring-fence the funds for tourist-related expenditure. The hotels could recoup the cost of the BID levy by charging tourists a uniform fee.
- **A voluntary levy**. Previous research has referenced voluntary schemes in both Hackney and the Lake District. However, there is very little information on how these schemes work.[12]

A new tourist levy – the quantitative picture

This section describes what a tourist levy would mean in revenue terms. The analysis has the following characteristics:

- It looks at the revenues that could have been generated from an occupancy charge in 2017.
- It uses 20 local areas as the basis for analysis (fewer local areas than in the income tax assignment due to data limitations).
- The local areas have been anonymised.
- London has been excluded from the analysis (its unique economic characteristics make it an outlier in the analysis and distorts the results). Nevertheless, the key points of the analysis remain relevant to any local area considering greater fiscal freedoms.

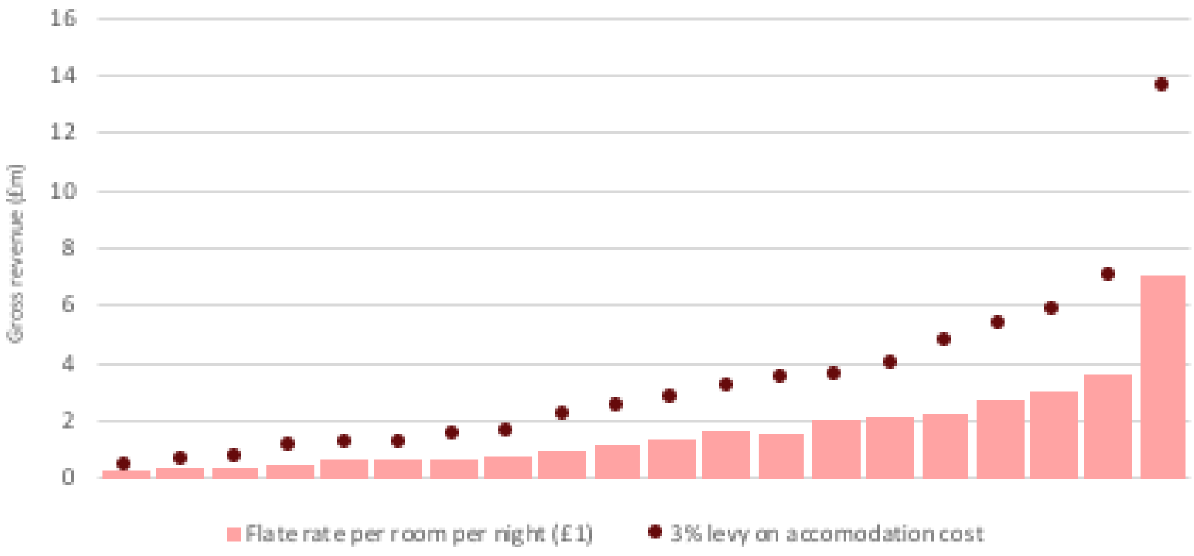
How much would a tourist levy raise for local areas?

Key point: The type of occupancy charge can make a big difference to revenues.

The graph below shows the distribution of tourist levies under a flat rate per room, per night of £1 and a 3 per cent levy on the nightly cost of the room. Average room rates tend to be less than £100 a night, meaning that a 3 per cent levy raises much higher projected revenues. Flat rate revenues vary across local area, from £238,000 at the lower end, to over £7 million at the upper end. The revenues from a percentage levy vary from £505,000 at the lower end to over £13.7 million at the upper end.

11 http://researchbriefings.parliament.uk/ResearchBriefing/Summary/SN04591
12 www.london.gov.uk/sites/default/files/tourism-levy-for-london-wp83.pdf

Revenues arising within local areas from different versions of a tourist tax



Source: WPI Economics analysis, see Annex I for sources

The chart shows that different areas of the country have very different capability to raise revenue form a tourist levy. It also shows that the type of tourist levy can have a very different impact on revenues – this raises the question: if central government are legislating for the introduction of a tourist levy, what would they legislate for? Would it be a specific type of tourist levy? Or a range? This is ultimately a choice between granting degrees of fiscal freedom.

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