HMRC update on Scottish rate of Income Tax for Finance Committee

Readiness

1. HMRC is confident that it will be ready for the implementation of the Scottish rate of Income Tax (SRIT) in April 2016. Good progress has been made in relation to amending HMRC's IT systems – the first phase of development has been completed, which will allow HMRC to identify Scottish taxpayers. A second phase of development, dealing with changes to the PAYE system, is underway. Further phases will then follow to cover amendments to the Self Assessment system and the Relief at Source (RAS) process for pensions.

2. Alongside this, HMRC has also been working to ensure its staff are ready for the implementation of the SRIT. Detailed guidance is being prepared to assist contact centre staff in dealing with queries from customers and this will be in place ahead of the main issue of letters to potential Scottish taxpayers planned for December of this year. Customers will be able to amend their address details using the facility for this on the GOV.UK website.

3. In addition to amending its own systems, HMRC has also produced detailed specifications for employers, payroll software providers and pension scheme administrators covering the changes that those organisations will need to make to their own systems. HMRC does not anticipate this being a significant change for employers. As a result of the need to comply with the Scottish Variable Rate legislation, employers should already have some of functionality required for SRIT built into their systems and, additionally, HMRC will not require employers to identify Scottish taxpayers among their workforce – HMRC will advise employers who should be taxed at the SRIT via PAYE coding notices and the employer's responsibility will be to operate this code, if necessary using a different set of tax tables.

4. However, to support the implementation of the SRIT, HMRC has been carrying out a comprehensive programme of communications activity, such as publishing written material on GOV.UK, featuring detailed articles about the SRIT implications for employers in its Employer Bulletin and appearing at a number of face-to-face stakeholder events, including the annual conference of the Chartered Institute of Payroll Professionals earlier this month. Further details on communications activities were included in HMRC's update to the Committee of 28 August 2015.

5. Guidance for customers will also be published shortly on GOV.UK. This includes basic guidance, for customers with straightforward affairs, and more detailed, technical guidance for customers with more complex circumstances, for example, having more than one place of residence.

6. Major programmes and projects in central government are subject to OGC (Office of Government Commerce) Gateway™ Reviews, which provide assurance of the key stages so they can progress successfully to the next stage. In May 2015, the OGC undertook a Gateway 3 strategic assessment of the project to implement the SRIT. This stated that successful delivery of the Project was feasible and identified key areas for the Project to focus on, including identifying Scottish taxpayers and communications. The report also recognised that the project team had embedded a successful approach to collaborative working, which many interviewees commented was exceptional in their experience of project work. This report will be published in 2016.

Identifying Scottish taxpayers

7. An individual's Scottish taxpayer status is determined by the location of their main place of residence for the majority of the tax year. If this is in Scotland, they will be a Scottish taxpayer. The strategy for identifying Scottish taxpayers is based around address

information held on HMRC's systems. In order to assess the accuracy of the data it holds, HMRC has carried out exercises to compare this against third party data held elsewhere.

8. The address data HMRC holds for taxpayers has been compared with other address databases (e.g. the Post Office) – in around 85% of cases HMRC held an address for a taxpayer that could be matched against an address held elsewhere. Analysis by HMRC of those cases where a match could not be achieved suggests that the vast majority of these individuals are living at a different address in Scotland indicated by, for example, a link to a local employer – this would mean that they were still Scottish taxpayers and would be treated as such by HMRC until notified otherwise. By this means we have established evidence that about 98% of the taxpayers for whom HMRC holds Scottish addresses are correctly identified as likely to be Scottish taxpayers.

9. HMRC plans to write to taxpayers for whom they hold a Scottish address in December to inform them that they will be treated as a Scottish taxpayer and advise them of how to report a change of address. HMRC will also undertake additional communications and publicity activity to raise awareness of the SRIT and remind customers of the importance of notifying HMRC when they move house. The communications activity is likely to be a mix of proactive communications, offering material to the media and stakeholders, to inform them about HMRC's activity regarding SRIT and use their assistance in reinforcing our messages, combined with a limited amount of paid for marketing to target specific customer groups to increase the confidence that we have reached the target audience in a way that represents the best value for money. This could include oil and gas sector workers, the fishing industry and students. Additionally, HMRC will write to taxpayers for whom a Scottish correspondence address (as opposed to the main address) is held, as these taxpayers clearly have an established link with Scotland and it will be important to confirm which of these addresses held is their main place of residence.

10. HMRC also has undertaken extensive work to ensure that people who live in Scotland but do not appear on our current records with a Scottish address can be included in the planned communications. This has included using third party data that could be used to corroborate HMRC address data. This is not straightforward, as there is no single set of address data that is constantly updated at all times. HMRC has worked with a third party data supplier (Transactis) as part of this work to assess the accuracy of its data.

11. Transactis has undertaken a comparison of HMRC's UK wide data with the Scottish Electoral Register. The scan has produced a list of individuals for whom HMRC holds an address elsewhere in the UK, but who appear at a Scottish address on the electoral register. HMRC will be writing to these individuals separately to confirm whether they are Scottish taxpayers.

12. HMRC has also worked with the Scottish Government on the possibility of being able to access address information from NHS Scotland records. This is not available at this point in time and HMRC is satisfied that it can implement and operate the SRIT without access to this data. HMRC will continue to consider different sources of data to best maintain the Scottish taxpayer population.

13. All this should give confidence that there will be a good starting point for the Scottish rate. But it will still be up to taxpayers to tell HMRC their correct address, and HMRC will be reminding them to do so later this year, when writing to all those for whom we hold Scottish addresses to tell them about the Scottish rate. As set out above, taxpayers are already able to amend their address using GOV.UK and this will also be possible using the personal tax account, to be rolled out next year.

14. From a financial perspective, the system for adjusting the Scottish Government's block grant to take account of Scottish Income Tax receipts is designed to minimise the level of financial risk to which the Scottish Government could be exposed if taxpayer status is not determined correctly.

15. In particular, the transitional arrangements which will be in place for the first 2-3 years of operation of the SRIT will allow further time for HMRC, individuals and employers to become accustomed to operating the system – during this time, the block grant adjustment will be recalculated each year to reflect the amount of revenue generated by a SRIT of 10%. So, if taxpayer status is determined incorrectly, the impact on Scottish Government tax revenues will be offset by the block grant adjustment. The simplest scenario is where the Scottish Parliament sets a SRIT of 10% during this period, as the reduction in the block grant will exactly offset the tax revenue generated.

16. It is therefore important that HMRC continues to maintain the accuracy of its address data once SRIT is in place (both to ensure the Scottish Government receives the correct level of tax receipts, and to ensure that taxpayers pay the correct amount of income tax). HMRC's activity here will include encouraging taxpayers to notify them of changes of address and cross-checking against other sources of information. This would also involve making use of data received from other sources. HMRC receive address details from employers and DWP and we will be able to use this information as a basis for approaching customers proactively to confirm their current main place of residence, if we suspect that they have moved and not notified us.

17. If the Scottish rates diverge from the rates which apply elsewhere in the UK, there will be an incentive for taxpayers to claim that they live on one side of the border, when they live on the other. HMRC will use external data to highlight changes of address, and identify high risk cases such as mobile employees and taxpayers with high incomes and will undertake appropriate compliance activity to address any risks that arise. HMRC is already undertaking preparatory work in these areas. Additionally, it is worth noting that, as HMRC continues to work on reducing the overall tax gap and bring more individuals into the tax system, this will increase overall revenues, including those paid at the Scottish rate.

Costs

18. The UK Government's third annual implementation report on the Scotland Act 2012 (published in March), confirmed that the cost of implementing the SRIT was now estimated to be in the region of £30m-£35m (made up of £10m-£15m of IT costs and £20m of non-IT costs). This remains the current estimate.

19. The previous estimate for the annual running costs was £4.2m per year – this was the original estimate prepared in November 2010 when the Scotland Bill was introduced to Parliament. Since then, further work has been carried out to refine this figure. As outlined in previous evidence to the Committee, HMRC has always anticipated that, if the Scottish and UK rates diverge, there will be an increase in running costs. The customer insight research supported this, by clarifying that Scottish taxpayer customers would be more likely to call HMRC if the Scottish rates were higher than the UK rates and as set out above a divergence in the rates would increase the amount of compliance activity required.

20. If the SRIT is set at 10%, the running costs are estimated to be £2m-£2.5m. If the rate is set at a figure other than 10%, the figure is estimated to be £5.5m-£6m. These figures do not include costs arising from the long-term solution for RAS pension schemes, which will be implemented in 2018-19, as the details of this solution are still under development.

HM Revenue & Customs
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HMRC Scottish Rate of Income Tax - Risk Register October 15

Risk Title & Description	Owner	Control Effectiveness	Residual RAG Quarterly Trend: Previous Month Aug 15	Residual RAG Quarterly Trend: Previous Month Sept 15	Residual RAG Quarterly Trend: Current Month Oct 15	Trend	Forecast
There is a risk that - the Project team does not manage the Employer/Pension Provider/Payroll/ Software Developer dependencies and lead times.	Comms Manager	High	13	13	13	◄►	12
There is a risk that - the Project may not be able to identify an acceptable strategy and approach for identifying the potential Scottish taxpayer population.	Project Manager	Moderate	17	17	17	◄►	13
There is a risk that - the Project does not keep abreast of wider transformational change, which could result in the solution not sitting within the HMRC operating model circa 2016.	Project Manager	Moderate	14	14	14	◄►	8
There is a risk that communications are unclear for those who are not SRIT taxpayers (e.g. non UK residents living in Scotland or the rest of the UK taxpaying population) resulting in possible confusion and erroneous customer contact.	Comms Manager	Moderate	8	8	8	◄►	7
There is a risk that - the Project does not manage the IT complexity and planned technological change when integrating the SRIT solution into the wider HMRC IT estate.	CDIO Project Manager	Moderate	8	8	8	◄►	8
There is a risk that - the Project is unable to accurately forecast the likely levels of customer contact generated as a result of the introduction of SRIT.	Benefits Manager	Moderate	7	7	7	◄►	7
There is a risk that - the Project does not manage its relationship and dependency with the Digital Programme.	Project Manager	Moderate	14	14	14	◄►	13
There is a risk that - the degree of concurrent changes across HMRC results in a cumulative impact on key HMRC events and products (such as the Basic PAYE tool).	Requirements Manager	High	13	13	13	◄►	13
There is a risk that - other organisations publish information about SRIT that is incorrect, misleading or wrongly timed, leading to customer confusion and contact.	Comms Manager	Moderate	8	8	8	◄►	8
There is a risk that DWP and HMRC are not joined up in their delivery of SRIT.	Project Manager	Moderate	13	13	13	◄►	11
There is a risk that communication products designed to inform the UK population in relation to SRIT (Scottish and non-Scottish taxpayers) are not delivered to time and specification.	Comms Manager	Moderate	12	12	12	◄►	11
There is a risk that the Scottish Parliament does not agree the Scottish Government's Scottish Rate Resolution, resulting in a late change of rate.	Project Manager	Low		17	17	◄►	17
There is a risk associated with the current uncertainty surrounding the content and timing of the notification letter which impacts on customer experiences and HMRC resources	Project Manager	Very Low		19	19	◄►	11
In the event that the Scottish Government varies the rate of SRIT in 2016/17 or 2017/18, so that the interim RAS solution has to be implemented, there is a risk of associated customer contact arising.	Project Manager	Moderate	14	14	14	◄►	14
Specialist PT Pensions do not have sufficient specialist resources available to them to support the RAS project adequately.	Specialist PT	Low	14	14	14	◄►	14
There is a risk that pension providers may not provide NINOs on all of their returns, making it difficult for HMRC to accurately match RAS accounts with HMRC systems. This is caused by a mismatch between DWP legislation on auto-enrolment for pension schemes, and HMRC regulations on the provision of information by pension providers in relation to RAS. It appears that the former does not require an individual scheme member to supply a scheme administrator with a NINO. However HMRC regulations enable us to require scheme administrators to supply the NINO of each scheme member (except special cases).	Specialist PT	Moderate	13	13	13	◄►	12
There are resource pressures on the RAS project team which could negatively impact the effective management of the project in the short- to mid-term.	Project Manager	High	13	13	13	◄►	13
There is a risk of reputational damage to the Department caused by reconciling pension RAS against tax accounts, which may not be well received or understood by taxpayers.	Project Manager	Moderate	8	8	8	◄►	7