



**PUBLIC AUDIT COMMITTEE**

**AGENDA**

**4th Meeting, 2016 (Session 4)**

**Wednesday 27 January 2016**

The Committee will meet at 10.00 am in the Mary Fairfax Somerville Room (CR2).

1. **Decision on taking business in private:** The Committee will decide whether to take items 4 and 5 in private.
2. **The administration of the Scottish Rate of Income Tax 2014-15:** The Committee will take evidence on the Comptroller & Auditor General report entitled "The administration of the Scottish Rate of Income Tax 2014-15" and the Auditor General for Scotland report entitled "The administration of the Scottish Rate of Income Tax 2014/15 - Report to the Scottish Parliament's Public Audit Committee" from —

Caroline Gardner, Auditor General for Scotland;

Sir Amyas Morse, Comptroller & Auditor General, and Steven Corbishley, Director, National Audit Office;

Sarah Walker, Deputy Director and Head of Devolution Team, HM Revenue and Customs.

3. **Section 23 report - Implementing the Scotland Act 2012: an update:** The Committee will take evidence on the Auditor General for Scotland report entitled "Implementing the Scotland Act 2012: an update" from —

Caroline Gardner, Auditor General for Scotland;

Mark Taylor, Assistant Director, and Gordon Smail, Senior Manager, Audit Scotland.

4. **Section 23 report - Implementing the Scotland Act 2012: an update:** The Committee will consider the evidence received at agenda item 3 and take evidence from —

Caroline Gardner, Auditor General for Scotland;

Mark Taylor, Assistant Director, and Gordon Smail, Senior Manager, Audit Scotland.

5. **The administration of the Scottish Rate of Income Tax 2014-15:** The Committee will consider the evidence received at agenda item 2.

Anne Peat  
Clerk to the Public Audit Committee  
Room T3.60  
The Scottish Parliament  
Edinburgh  
Tel: 0131 348 5390  
Email: [Anne.peat@scottish.parliament.uk](mailto:Anne.peat@scottish.parliament.uk)

The papers for this meeting are as follows—

### **Agenda Item 2**

Auditor General for Scotland report on the administration of the Scottish Rate of Income Tax (SRIT)	PA/S4/16/4/1
National Audit Office Report on the administration of SRIT	PA/S4/16/4/2
Written submission from Audit Scotland	PA/S4/16/4/3
Written submission from the Comptroller & Auditor General	PA/S4/16/4/4
Correspondence from the Scottish Government	PA/S4/16/4/5

### **Agenda Item 3**

PAC briefing paper	PA/S4/16/4/6
<a href="#">Auditor General for Scotland report</a>	PA/S4/16/4/7

### **Circulated for information**

Member's Bulletin	PA/S4/16/4/8
<a href="#">Public Audit Committee 1st Report, 2014 (Session 4) - Framework for auditing the Scottish rate of income tax</a>	PA/S4/16/4/9
<a href="#">AGS report - Preparations for the implementation of the Scotland Act 2012</a>	PA/S4/16/4/10

Mr Paul Martin MSP  
Convener  
Public Audit Committee  
T3.60  
Scottish Parliament  
Edinburgh  
EH99 1SP

26 November 2015

Dear Convener

**The administration of the Scottish rate of income tax**

As you know, from April 2016 the Scottish Parliament will set a new Scottish rate of income tax (SRIT). HM Revenue and Customs (HMRC) will collect and administer the SRIT and is responsible for the project to implement it.

HMRC's accounts are audited by the National Audit Office (NAO). The Comptroller and Auditor General is required to report to the Scottish Parliament on HMRC's administration of the SRIT. The Comptroller and Auditor General's first report on the SRIT will be laid in the Scottish Parliament today.

When the Public Audit Committee published its report *Framework for auditing the Scottish rate of income tax* in 2014, the Committee recommended that I should provide additional assurance on the NAO's audit work on the SRIT. I attach my report in response to that recommendation.

I understand that the Committee plans to take evidence from the Comptroller and Auditor General, HMRC and me in relation to the SRIT in due course.

Yours sincerely

Caroline

**Caroline Gardner**  
**Auditor General for Scotland**

**THE ADMINISTRATION OF THE SCOTTISH RATE OF INCOME TAX 2014/15  
REPORT TO THE SCOTTISH PARLIAMENT'S PUBLIC AUDIT COMMITTEE  
BY THE AUDITOR GENERAL FOR SCOTLAND**

## **Introduction**

1. From April 2016, the Scottish Parliament will set a new Scottish rate of income tax (SRIT). The main UK rates of income tax will be reduced by ten pence for each tax band for Scottish taxpayers. Each year, the Scottish Parliament will vote to approve the Scottish rate to be added to the reduced UK rates. Taxes raised by the SRIT will be added to the Scottish Government's budget and a corresponding reduction will be made to the block grant funding that the Scottish Government receives from the UK Government.
2. HM Revenue and Customs (HMRC) will collect and administer the SRIT and is responsible for the project to implement it. The Scottish Government is responsible for funding this project and ensuring that the cost of the SRIT represents value for money and for seeking assurances that the new system will collect the correct amount of tax.
3. The reimbursement by the Scottish Government of HMRC's costs incurred in implementing the SRIT is identified separately in HMRC's Resource Accounts. From 2014/15, HMRC provides the relevant audited extracts of its accounts to the Scottish Parliament for scrutiny each year.<sup>1</sup> For 2014/15 and 2015/16, the accounts will relate only to the setting up of systems to calculate and collect the SRIT. From 2016/17, the first year of operation of the SRIT, HMRC's Trust Statement will disclose the SRIT collected and the application of related rules and procedures.

## **Audit and assurance**

4. HMRC's accounts are audited by the National Audit Office (NAO). The Comptroller and Auditor General is required to report to the Scottish Parliament on HMRC's administration of the SRIT by 31 January of the financial year after the one to which the report relates.<sup>2</sup> Specifically, the Comptroller and Auditor General is required to report on:
  - the adequacy of any of HMRC's rules and procedures put in place, in consequence of the Scottish rate provisions, for the purpose of ensuring the proper assessment and collection of income tax charged at rates determined under those provisions
  - whether these rules and procedures are being complied with
  - the correctness of the sums brought to account by HMRC which relate to income tax which is attributable to a Scottish rate resolution; and
  - the accuracy and fairness of the amounts which are reimbursed to HMRC as administrative expenses incurred as a result of the charging of income tax.

---

<sup>1</sup> Memorandum of understanding on the Scottish rate of income tax, Scottish Government and HM Revenue and Customs, February 2013.

<sup>2</sup> Section 80HA of the Scotland Act 1998, inserted by section 297 of the Finance Act 2014.

5. The Public Audit Committee of the Scottish Parliament recommended that I should provide additional assurance on the NAO's audit work on the SRIT.<sup>3</sup> I make this report in response to that recommendation.
6. The Comptroller and Auditor General and I have confirmed to the Public Audit Committee that we will work together to ensure that the Scottish Parliament receives appropriate reports on the operation of the SRIT. We have agreed a Memorandum of Understanding that describes our respective powers and responsibilities and sets out a framework for collaborative working.
7. I am reporting separately on the preparations for the implementation of the Scotland Act 2012.<sup>4</sup> This includes my assessment of how the Scottish Government is working with HMRC to prepare to introduce the SRIT in April 2016.

#### **Audit Scotland's review of the NAO's audit work on SRIT**

8. The Comptroller and Auditor General made his first report to the Scottish Parliament on SRIT on 26 November 2015. As the SRIT has yet to be introduced, his report considers the accuracy and fairness of the amounts reimbursed to HMRC by the Scottish Government and the progress HMRC has made in implementing systems that will ensure the proper collection and assessment of income tax under the SRIT.
9. Audit Scotland considered the NAO's planning and approach to its audit work on the SRIT, discussing this with the NAO staff involved in the work. On completion of the NAO's audit work, Audit Scotland met with the NAO to review its documentation and the basis for the findings and conclusions included in the Comptroller and Auditor General's report.
10. In particular, Audit Scotland considered:
  - the NAO's approach to identifying the key risks to the successful implementation of SRIT
  - the NAO's audit working files, with particular focus on the audit evidence underpinning the key findings and conclusions in its report; and
  - the NAO's arrangements for ensuring the quality of the audit work and reporting.
11. Audit Scotland's review was limited to consideration of the NAO's audit work; it did not directly review evidence obtained from HMRC or discuss any matters relating to SRIT directly with HMRC. The judgements and conclusions set out in the report of the Comptroller and Auditor General are his alone, based on the audit work undertaken by the NAO on his behalf.

---

<sup>3</sup> Public Audit Committee, 1st Report, 2014 (Session 4): Framework for auditing the Scottish rate of income tax

<sup>4</sup> Preparations for the implementation of the Scotland Act 2012, Auditor General for Scotland, December 2014

## Conclusion

12. On the basis of Audit Scotland's review, I am satisfied that the NAO's approach was sufficient and robust and that its audit work covered the key audit risks. I am also satisfied that the findings and conclusions in the Comptroller and Auditor General's report are reasonably based.
13. In relation to the key findings in the Comptroller and Auditor General's report, I would in particular draw the Committee's attention to the following matters:

- (C&AG key finding 4). *HMRC is aware of the risk of tax avoidance and evasion presented by the possibility of a different rate of income tax in Scotland from April 2016. But so far it has put only limited resources into specific planning for potential tax loss as result of SRIT.*

HMRC has developed a clear and detailed compliance strategy that considers the SRIT's impact on taxpayer behaviour and potential tax avoidance and evasion but has yet to confirm the exact nature of the compliance activity it will undertake from April 2016. The most obvious form of non-compliance is cross-border tax avoidance and evasion if there is disparity between the SRIT and the rate of income tax in the rest of the UK. Whether or not there is an overall rate disparity, and even if there is a limited risk of cross-border tax avoidance, the Scottish Government needs assurance that compliance activity that HMRC undertakes will support the effective collection of the SRIT.

- (C&AG key finding 7). *Due to a delay by the Scottish Government in announcing the Scottish Government's budget, letters to individuals will not advise them on the actual SRIT they will pay in the 2016/17 tax year. The delay in announcing the rate leaves an increasingly narrow timeframe for HMRC to react to responses from taxpayers and refine its taxpayer data before SRIT begins in April 2016.*

The UK Government published the outcome of its spending review on 25 November 2015. This included the amount of funding that the Scottish Government will receive by way of block grant. The Scottish Government decided not to publish its draft budget for 2016/17, including the proposed rate for the SRIT, until after this. Consequently, HMRC's communication with Scottish taxpayers will not be able to illustrate the financial impact of the SRIT as intended. This may affect taxpayers' engagement with the new arrangements. It also compresses the time available for HMRC to ensure its taxpayer information is as robust as possible.

14. This is the first year of audit reporting on the SRIT. I will continue to work with the Comptroller and Auditor General to develop our approach to the audit and assurance process relating to the SRIT, taking account of views and comments the Committee may have.



National Audit Office

---

## **Report**

by the Comptroller  
and Auditor General

---

## **HM Revenue & Customs**

# The administration of the Scottish Rate of Income Tax 2014-15



---

Our vision is to help the nation spend wisely.

Our public audit perspective helps Parliament hold government to account and improve public services.

The National Audit Office scrutinises public spending for Parliament and is independent of government. The Comptroller and Auditor General (C&AG), Sir Amyas Morse KCB, is an Officer of the House of Commons and leads the NAO, which employs some 810 people. The C&AG certifies the accounts of all government departments and many other public sector bodies. He has statutory authority to examine and report to Parliament on whether departments and the bodies they fund have used their resources efficiently, effectively, and with economy. Our studies evaluate the value for money of public spending, nationally and locally. Our recommendations and reports on good practice help government improve public services, and our work led to audited savings of £1.15 billion in 2014.

---



National Audit Office

---

HM Revenue & Customs

# The administration of the Scottish Rate of Income Tax 2014-15

Report by the Comptroller and Auditor General

Ordered by the House of Commons  
to be printed on 26 November 2015

Presented to the House of Commons pursuant to  
Section 9 of the National Audit Act 1983

Presented to the Scottish Parliament pursuant to  
Section 80HA of the Scotland Act 1998 as amended  
by the Finance Act 2014

Sir Amyas Morse KCB  
Comptroller and Auditor General  
National Audit Office

24 November 2015

---

© National Audit Office 2015

The material featured in this document is subject to National Audit Office (NAO) copyright. The material may be copied or reproduced for non-commercial purposes only, namely reproduction for research, private study or for limited internal circulation within an organisation for the purpose of review.

Copying for non-commercial purposes is subject to the material being accompanied by a sufficient acknowledgement, reproduced accurately, and not being used in a misleading context. To reproduce NAO copyright material for any other use, you must contact [copyright@nao.gsi.gov.uk](mailto:copyright@nao.gsi.gov.uk). Please tell us who you are, the organisation you represent (if any) and how and why you wish to use our material. Please include your full contact details: name, address, telephone number and email.

Please note that the material featured in this document may not be reproduced for commercial gain without the NAO's express and direct permission and that the NAO reserves its right to pursue copyright infringement proceedings against individuals or companies who reproduce material for commercial gain without our permission.

Links to external websites were valid at the time of publication of this report. The National Audit Office is not responsible for the future validity of the links.

---

## Contents

**Key facts** 4

**Key findings** 5

**Part One**

Introduction 7

**Part Two**

Costs incurred to date 10

**Part Three**

Implementing the Scottish Rate  
of Income Tax 11

**Appendix One**

Board membership and terms  
of reference 18

**Appendix Two**

Summary of recommendations  
raised by Office of Government  
Commerce (OGC) and HM Revenue  
& Customs Internal Audit 22

The National Audit Office study team consisted of:  
Chris Coyne, Wifgi Gebrial and  
Andrea Scott, under the direction  
of Steven Corbishley.

This report can be found on the  
National Audit Office website at  
[www.nao.org.uk](http://www.nao.org.uk)

For further information about the  
National Audit Office please contact:

National Audit Office  
Press Office  
157–197 Buckingham Palace Road  
Victoria  
London  
SW1W 9SP

Tel: 020 7798 7400

Enquiries: [www.nao.org.uk/contact-us](http://www.nao.org.uk/contact-us)

Website: [www.nao.org.uk](http://www.nao.org.uk)

Twitter: @NAOorguk

---

## Key facts



---

HMRC's estimate of the number of Scottish income taxpayers

---



---

high-end forecast of the total costs of implementing the Scottish Rate of Income Tax up to 2018-19

---



---

amount reimbursed to HMRC by the Scottish Government in respect of implementing the Scottish Rate of Income Tax during 2014-15

---

# Key findings

**1 HM Revenue & Customs' (HMRC's) process for responding to the upcoming Scottish Rate of Income Tax (SRIT) has been thorough.** HMRC has prepared a detailed strategy for identifying Scottish taxpayers, and tested its assumptions in a variety of ways. There is no pre-existing dataset of Scottish taxpayers to compare HMRC's data against. HMRC's decision to use third-party data to verify its population data has helped provide greater assurance on the completeness and accuracy of the Scottish taxpayer data that it already holds. HMRC estimates that there are 2.6 million income taxpayers in Scotland.

**2 Maintaining an accurate record of the Scottish taxpayer population depends on keeping up-to-date address information.** The possibility of a different income tax rate for Scotland and the rest of the UK for the first time means individuals could pay the incorrect rate of income tax if the address held by HMRC is incorrect. Address information can only be updated if taxpayers inform HMRC of a change of address. HMRC has engaged with employers and other stakeholders to encourage this. However, actively ensuring taxpayers keep HMRC informed of their correct address remains a key challenge to HMRC's objective of recovering the correct amount of income tax from Scottish taxpayers.

**3 SRIT is subject to a sound governance process, and HMRC is engaging proactively with the Scottish Government in the run-up to April 2016.** HMRC's relationship with the Scottish Government has allowed timely challenge throughout the project. This has also allowed a greater level of scrutiny of the costs that HMRC has incurred in relation to the SRIT project. The project has been reviewed regularly by the independent Office of Government Commerce, and HMRC has implemented the recommendations in a timely and constructive manner.

**4 HMRC has developed a clear and detailed compliance strategy that considers SRIT's impact on taxpayer behaviour and potential tax avoidance and evasion.** HMRC is aware of the risk of tax avoidance and evasion presented by the possibility of a different rate of income tax in Scotland from April 2016. But so far it has put only limited resources into specific planning for potential tax loss as a result of SRIT. Given the significance and complexity of the SRIT project, HMRC will need to react quickly to the changing compliance environment within the UK from April 2016.

**5 By building on existing and long-standing IT capability, HMRC has minimised the risks and costs associated with the need to develop an entirely new system to administer the SRIT.** HMRC has also designed a comprehensive phased plan for delivery that considers the impact of these changes to the SRIT, and how costs associated with future devolution to other regions could be reduced.

**6 HMRC has developed a clear plan and strategy for communicating about SRIT to different stakeholders.** HMRC has engaged with various stakeholder groups, including employers and pension providers. It has conducted market research to refine its strategy for communicating with the Scottish taxpayer population. HMRC plans to write to potential Scottish taxpayers for the first time in December 2015. HMRC is trying to minimise contact from those who receive its letters. At the same time, it wants to ensure its communication in the lead-up to April 2016 helps refine its data on Scottish taxpayers to make it as accurate and complete as possible. There will be a short window between the responses to HMRC's letters and the rate coming into force in April 2016. Therefore, it is important for HMRC to maximise the impact of its communication strategy during this period.

**7 HMRC plans to communicate with Scottish taxpayers in December 2015.** Due to a delay by the Scottish Government in announcing the Scottish Government's budget, letters to individuals will not advise them on the actual SRIT they will pay in the 2016-17 tax year. The delay in announcing the rate leaves an increasingly narrow timeframe for HMRC to react to responses from taxpayers and refine its taxpayer data before SRIT begins in April 2016.

# Part One

## Introduction

### The Scottish Rate of Income Tax

**1.1** The Scotland Act 2012 introduced powers for the Scottish Parliament to apply a Scottish Rate of Income Tax (SRIT) to the non-savings, non-dividend income of Scottish taxpayers from 6 April 2016.

**1.2** The UK government will deduct 10p from the basic, higher and additional rates of income tax. The Scottish Parliament will then be able to levy an additional Scottish rate applied equally across the three main tax bands. HM Revenue & Customs (HMRC) will continue to collect income tax and will pay over to the Scottish Government the amount of revenue it collects relating to the SRIT.

**1.3** Section 25 of the Scotland Act 2012 sets out the definition of a Scottish taxpayer. A Scottish taxpayer is someone whose main place of residence in a given tax year is Scotland, or who spends most of that tax year living in Scotland. There are a number of exceptional cases whereby a taxpayer would always be deemed Scottish, for example if they are a member of Parliament for a Scottish constituency. HMRC is responsible for accurately identifying individuals as Scottish taxpayers in each tax year to ensure they pay the correct rate of income tax.

**1.4** At the time of reporting, the Scottish Government has not confirmed the actual rate of income tax to be recovered from Scottish taxpayers for 2016-17. This is not expected to be announced until mid-December 2015 at the earliest.

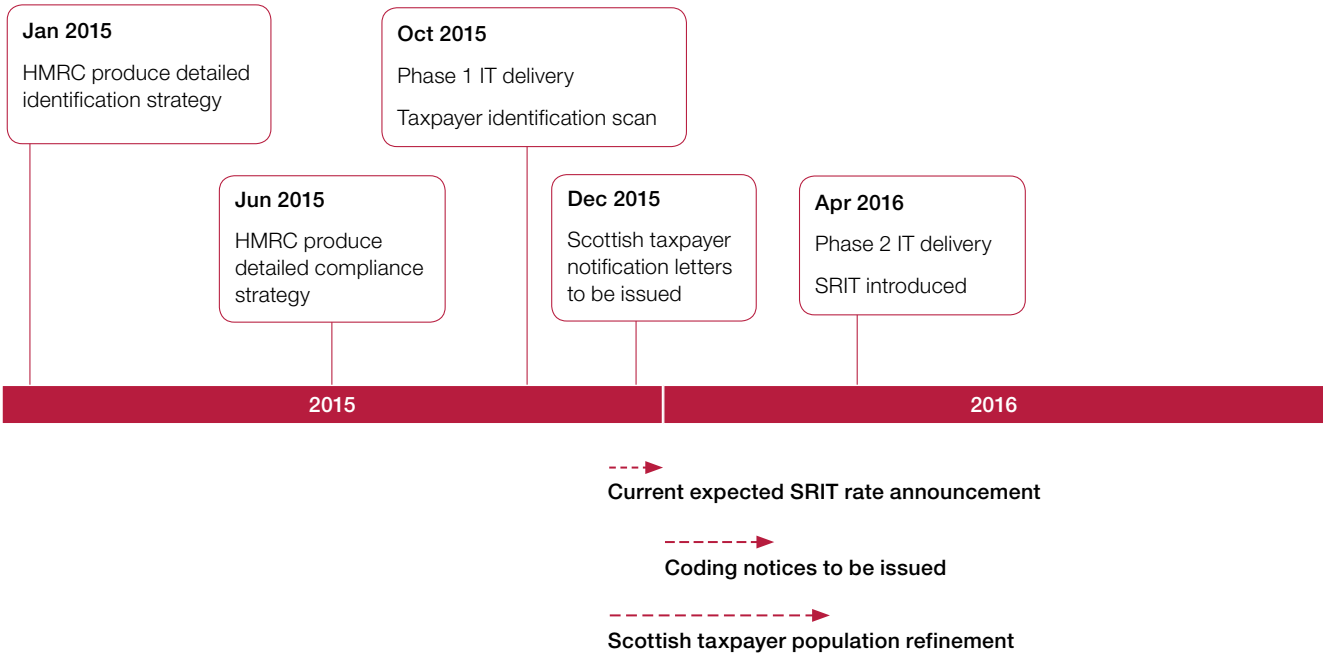
### Systems and procedures

**1.5** Since the Scotland Act received Royal Assent in May 2012, HMRC has been developing its systems for collecting income tax and assessing the data it holds on taxpayers. **Figure 1** overleaf shows the most recent timeline of key stages for the SRIT project in the run-up to April 2016.

**1.6** HMRC will implement the SRIT project in phases until 2018-19. We will reflect on expenditure incurred by HMRC throughout the project in our future reports.



**Figure 1**  
HMRC’s recent timeline of activities to introduce the SRIT



Source: HM Revenue & Customs timelines

## Remit of the Comptroller and Auditor General

**1.7** Under section 80HA of the Scotland Act 1998 (the Act), as amended by the Finance Act 2014, the Comptroller and Auditor General (C&AG) is required for each financial year from 2014-15 to prepare a report on:

- the adequacy of any of HMRC's rules and procedures put in place, in consequence of the Scottish rate provisions, for the purpose of ensuring the proper assessment and collection of income tax charged at rates determined under those provisions;
- whether these rules and procedures are being complied with;
- the correctness of the sums brought to account by HMRC which relate to income tax which is attributable to a Scottish rate resolution; and
- the accuracy and fairness of the amounts reimbursed to HMRC as administrative expenses incurred as a result of the charging of income tax.

**1.8** In discharging his remit under the Act, this is the C&AG's first report presented to the Scottish Parliament. As the SRIT has yet to be introduced, this report considers:

- whether the amounts reimbursed to HMRC by the Scottish Government are accurate and fair (Part Two); and
- the progress HMRC has made so far in setting up systems to ensure that income tax levied under the Scottish rate is assessed and collected properly (Part Three).

**1.9** This report does not consider the correctness of sums brought to account in relation to the SRIT or whether rules and procedures have been complied with. We will consider these matters when we report on activity relating to 2016-17 once the SRIT has been implemented.

## Part Two

### Costs incurred to date

#### Costs incurred by HM Revenue & Customs

**2.1** The total cost incurred so far by HM Revenue & Customs (HMRC), and reimbursed by the Scottish Government, from the start of the project to 31 March 2015, is £2.70 million. **Figure 2** shows how this is broken down by financial year.

**2.2** The costs reimbursed to HMRC by the Scottish Government in 2014-15 amounted to £1.74 million. This consisted of IT costs of £0.75 million and non-IT costs of £0.99 million.

**2.3** We examined HMRC's methodology for estimating the costs of collecting and administering the Scottish Rate of Income Tax (SRIT) for the year to ensure this was reasonable. On the basis of our procedures, the amount reimbursed to HMRC by the Scottish Government for the year ended 31 March 2015 is fairly stated.

**2.4** HMRC currently estimates the final total costs of implementing SRIT to be in the range of £30 million to £35 million over the seven-year period from 2012-13 to 2018-19. This is split between IT expenditure of between £10 million and £15 million, and non-IT expenditure of £20 million.

#### Figure 2

Scottish Rate of Income Tax costs reimbursed by the Scottish Government to HMRC by year (£000)

	2012-13 (£000)	2013-14 (£000)	2014-15 (£000)
Q1	–	151	208
Q2	–	208	345
Q3	–	191	463
Q4	165	240	728
<b>Total</b>	<b>165</b>	<b>790</b>	<b>1,744</b>

#### Notes

1 2013-14 figures from HM Revenue & Customs, Annual Report and Accounts 2013-14, HC 19 (p. 145).

2 2014-15 figures from HM Revenue & Customs, Annual Report and Accounts 2014-15, HC 18 (p. 157).

Source: HM Revenue & Customs

# Part Three

## Implementing the Scottish Rate of Income Tax

### Collection and assessment

**3.1** HM Revenue & Customs (HMRC) has invested significant time and resources in preparing for the roll-out of the Scottish Rate of Income Tax (SRIT). Although we are unable to comment on the success of HMRC's preparations at this point in time, given that collection of the SRIT is not due to begin until 6 April 2016, we can comment on HMRC's approach in implementing the SRIT and the progress it has made so far.

**3.2** Therefore, in this Part, we will set out the governance arrangements HMRC has in place to manage the SRIT project and the progress HMRC is making in tracking the key risks to implementing the project successfully.

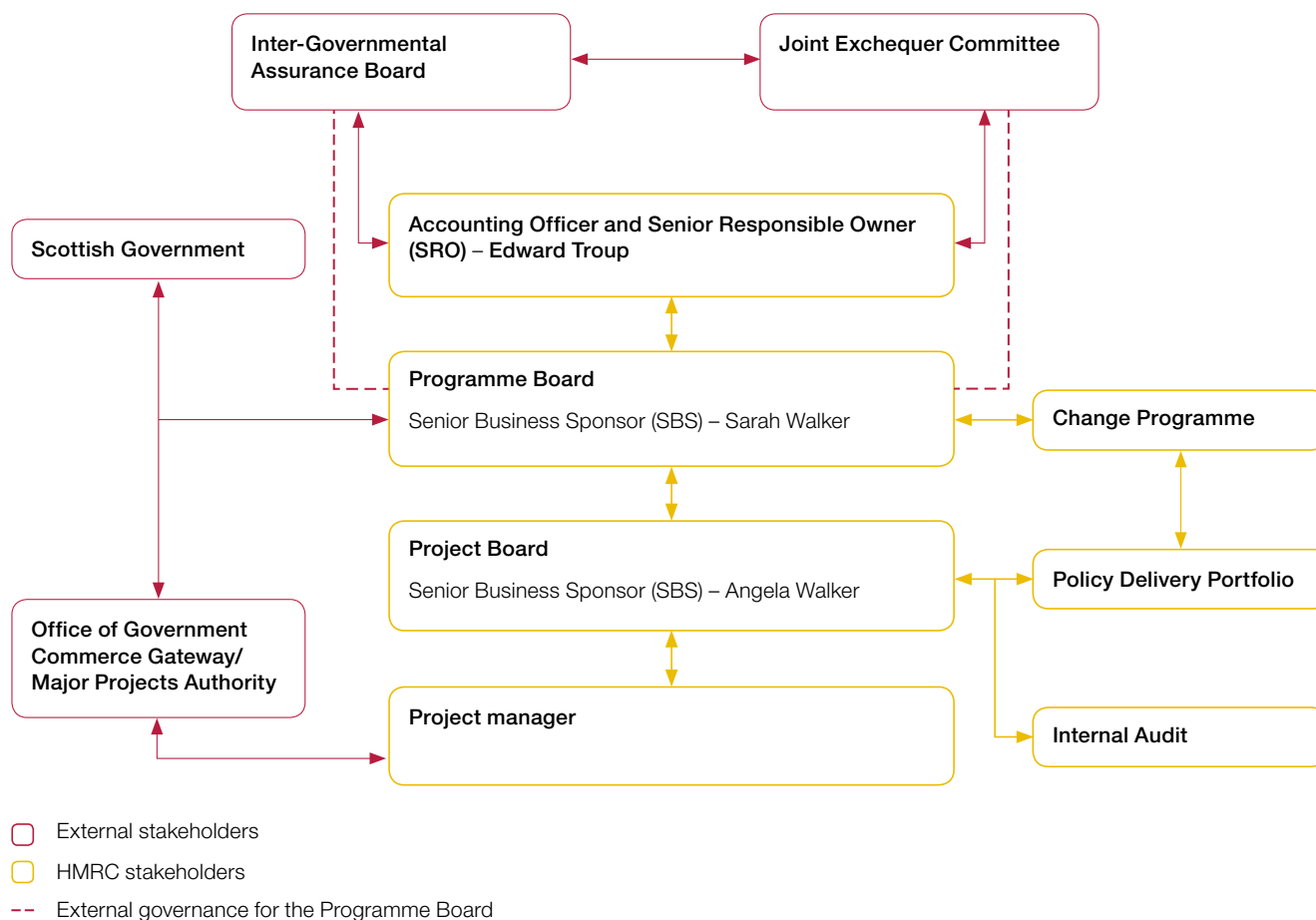
### Governance arrangements

**3.3** **Figure 3** overleaf shows the governance arrangements in place to manage the SRIT project. These arrangements have been developed to reflect the partnership created between HMRC and the Scottish Government. At a senior level, the Inter-Governmental Assurance Board monitors the implementation of the Scotland Act 2012. Additionally, the Scotland Act Programme Board is accountable for the implementation programme and oversees the SRIT project. Finally, the SRIT Project Board is responsible for ensuring the solutions for implementing the SRIT are delivered successfully. Both the Programme and Project Boards include members from HMRC and the Scottish Government. They meet every four to six weeks. Appendix One sets out the terms of reference and membership of each Board.

**3.4** Edward Troup, Second Permanent Secretary, is HMRC's Accounting Officer with responsibility for collecting the SRIT.

**Figure 3**

Governance structure for implementing the Scottish Rate of Income Tax



Source: HM Revenue &amp; Customs

**3.5** HMRC has worked effectively to manage its relationship with the Scottish Government. Representatives from the Scottish Government attend the regular Programme and Project Board meetings. HMRC's project team has also held a number of workshops to assure the Scottish Government of progress and refine future management information requirements when SRIT begins. In the immediate lead-up to April 2016, HMRC has arranged three check-points to allow the Scottish Government to challenge and approve HMRC's progress. These are taking place in November 2015, and January and March 2016. This sustained level of communication has been useful in ensuring that HMRC's costs in respect of the SRIT project have been monitored and scrutinised effectively by the Scottish Government during the project.

**3.6** The SRIT project has been reviewed several times by the Office of Government Commerce (OGC) gateway process and HMRC's Internal Audit unit. Appendix Two summarises the key recommendations raised by OGC and Internal Audit and how they have been addressed by HMRC. Overall, they concluded that the project is well governed and HMRC has responded proactively to recommendations made throughout.

## Risks

**3.7** HMRC maintains a risk register to help the Project Board manage issues that may impact on delivering the project successfully. **Figure 4** overleaf illustrates those risks currently classed as 'open' on this risk register.

**3.8** The Project Board risk register has been effective in managing and monitoring the key risks identified by the Board throughout the SRIT project.

**3.9** In the following section, we examine the key risks in detail, assess HMRC's progress in managing these, and highlight the wider challenges facing HMRC ahead of SRIT beginning in April 2016. We will focus on:

- the progress HMRC is making in identifying the Scottish taxpayer population;
- HMRC's approach and strategy for assuring the appropriate flow of income tax revenue to the Scottish Government;
- how effectively HMRC's IT systems are equipped to deal with SRIT; and
- HMRC's plans for communicating the SRIT to taxpayers and key stakeholders.

## Identifying the Scottish taxpayer population

**3.10** Identifying the Scottish taxpayer population with certainty has proven a major challenge to HMRC, as there is no existing independent population against which to benchmark the data it already holds. HMRC produced a comprehensive identification strategy in 2014-15, which set out the use of a range of internal and external data to test whether HMRC's data on the taxpayer population are reasonable and complete.

**3.11** Key to HMRC's strategy was the decision to use a taxpayer's postcode as the best way of identifying whether they live in Scotland or in the rest of the UK. Of all possible alternatives, HMRC considered that this was the most appropriate because it built on HMRC's existing taxpayer address data. HMRC attempted to validate its approach through three separate exercises with third-party data-matching specialists (Transactis Ltd):

- assessing the robustness of using postcodes as a proxy for the taxpayer;
- testing the association of an individual taxpayer with an address; and
- matching HMRC's data against an extract from the Scottish electoral roll.

**Figure 4****SRIT Project Board risk register**

<b>Risk</b>	<b>HMRC's assessment of the effectiveness of controls in place</b>
The Scottish Parliament does not agree the Scottish Government's Scottish Rate Resolution, resulting in a late change of rate.	Low
Current uncertainty surrounding the content and timing of the notification letter, which impacts on customer experiences and HMRC resources.	Very low
The project team does not manage the employer/pension provider/ payroll/software developer dependencies and lead times.	High
The project may not be able to identify an acceptable strategy and approach for identifying the potential Scottish taxpayer population.	Moderate
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.	Moderate
Communications are unclear for those who are not Scottish taxpayers (eg non-UK residents living in Scotland, or the rest of the UK population) resulting in possible confusion and erroneous customer contact.	High
The project does not manage the IT complexity and planned technological change when integrating the SRIT solution into the wider HMRC IT estate.	Moderate
The project is unable to accurately forecast the likely levels of customer contact generated as a result of the introduction of SRIT.	Moderate
The project does not manage its relationship and dependency with the Digital Programme.	Moderate
The degree of concurrent changes across HMRC results in a cumulative impact on key HMRC events and products.	High
Other organisations publish information about SRIT that is incorrect, misleading or wrongly timed, leading to customer confusion and contact.	Moderate
Department for Work & Pensions and HMRC are not joined up in their delivery of SRIT.	Moderate
Communication products designed to inform the UK population in relation to SRIT are not delivered to time and specification.	Moderate

**Note**

- 1 There are nine additional risks in respect of Relief-at-Source (RAS), which is being managed as a separate project. Control effectiveness ratings: low (1), moderate (7) and high (1). See paragraphs 3.27 and 3.28 for further information on RAS.

Source: Project Board Risk Register, HM Revenue & Customs, September 2015

**3.12** These exercises have given HMRC and the Scottish Government some assurance over the initial identification of the Scottish taxpayer population. The exercises have also enabled HMRC to cleanse corrupt postcode data on its own systems, and target specific areas within the population that were highlighted as mismatches.

**3.13** However, there remain risks in maintaining a complete and accurate Scottish taxpayer population:

- Keeping accurate addresses on HMRC's systems is vital to maintaining an accurate and complete record of the Scottish taxpayer population. The taxpayer is responsible for providing up-to-date address information, as employers cannot notify HMRC on behalf of their employees. There are no controls in place within HMRC's systems to confirm that any change in a taxpayer's address is accurate. As a result, HMRC is working with employers and other stakeholders to increase taxpayers' awareness of their responsibilities.
- If Scottish taxpayers are subject to a different rate of income tax from the rest of the UK from April 2016, HMRC will need to manage the risks of tax avoidance and evasion. These include taxpayers being unaware of the requirement to tell HMRC their new address and taxpayers deliberately avoiding paying a higher rate of income tax by giving HMRC an incorrect address.
- The final element of HMRC's preparation for finalising the initial Scottish taxpayer population is the response from Scottish taxpayers to HMRC's initial direct mailshot. The mailshot is to be sent to the full Scottish income-tax-paying population, which is currently estimated at approximately 2.6 million. It was expected that this would be sent in November 2015 and would include confirmation of the Scottish rate taking effect from April 2016. However, because of the delay in announcing the 2016-17 Scottish rate, the mailshot will now take place in December 2015. HMRC has chosen to send this letter before it knows the actual rate to allow it time to react to the response from the mailshot and refine its Scottish population data accordingly. The short window between sending the letters and the rate coming into force means HMRC must maximise the impact of its communication strategy during this period to ensure affected individuals pay the correct amount of income tax.

## Compliance

**3.14** HMRC's SRIT project team has developed a clear and detailed compliance strategy that considers the impact of SRIT on taxpayer behaviour and potential tax avoidance and evasion. This has not yet translated into compliance activity. However, HMRC has begun centralising expertise in specialist compliance teams, most notably within its High Net Worth Unit, which monitors individual taxpayers that have a higher risk profile due to the value of their tax liabilities.



**3.15** HMRC has not yet confirmed the exact nature of the compliance activity it will undertake from April 2016. This will depend on whether the Scottish rate differs from the rate for the rest of the UK for the 2016-17 tax year. HMRC has prepared different compliance strategies to address the impact of any potential difference in rates between Scotland and the rest of the UK.

**3.16** Non-compliance in its most obvious form will take the form of cross-border tax avoidance and evasion if there is a disparity between the Scottish rate of income tax and the rate of income tax for the rest of the UK. This is heightened by the risk of address manipulation by individual taxpayers.

**3.17** However, even if there is no overall difference in rates between Scotland and the rest of the UK in 2016-17, and therefore a limited risk of cross-border tax avoidance and evasion, the Scottish Government still needs to know the accurate value of tax revenue collected from Scottish taxpayers.

**3.18** As the SRIT for 2016-17 is unlikely to be announced until mid-December 2015 at the earliest, this leaves a tight timeframe to refine and finalise HMRC's planned compliance activity before April 2016. Given the significance and complexity of the SRIT project, HMRC will need to react quickly to the changing compliance environment within the UK from April 2016.

### **IT capability**

**3.19** As established in paragraph 2.2, IT costs incurred in 2014-15 were £0.75 million. Existing HMRC IT systems were initially unable to identify Scottish taxpayers separately from the rest of the UK taxpayer population. To identify and administer the tax affairs of Scottish taxpayers, HMRC modified its existing IT systems so that PAYE and self-assessment Scottish taxpayers are 'flagged' and the associated tax calculations reflect the appropriate rate of income tax. As HMRC has been able to modify its existing IT system capability, it has reduced both the cost and the risk associated with delivering SRIT to the Scottish taxpayer population.

**3.20** HMRC began to develop its IT solution in 2013-14. It identified high-level requirements in August 2013 and then developed these into a comprehensive phased delivery plan. Supplier and business testing is in progress, with the first phase of delivery planned to go live around the time of reporting.

**3.21** HMRC also decided to design system changes with the future in mind. In doing so, it has aimed to ensure it can react to future changes in the Scottish rate, as well as potential devolution to other regions, without needing further significant IT change. This should serve to reduce spending on IT in future years.

### **Strategy for communication**

**3.22** HMRC has developed a clear strategy for communicating about SRIT with different stakeholders.

**3.23** For individual taxpayers, a mailshot to the initially identified Scottish taxpayer population is currently planned for December 2015. Due to an unexpected delay in announcing the Scottish rate, these letters will not be able to illustrate the financial impact of SRIT, as was originally intended. HMRC will also send a targeted mailshot to those individuals it has identified where there is a mismatch between its taxpayer data and that on the Scottish electoral roll extract (paragraph 3.11).

**3.24** Throughout 2014-15, Ipsos MORI has helped HMRC to tailor its approach to communicating with the Scottish taxpayer population through focus groups and extensive research predicting individuals' responses. HMRC continues to engage Ipsos MORI where appropriate.

**3.25** HMRC is attempting to minimise contact from those who receive its letter. At the same time, it is ensuring that its communication in the lead-up to April 2016 helps refine its Scottish taxpayer population to make it as accurate and complete as possible. HMRC's resources are particularly stretched in January 2016 due to the self-assessment return peak. The annual coding exercise – which is vital to ensuring employers pay the appropriate level of tax through the taxpayer's tax code – also takes place in the months leading up to April 2016. There is a fine balance to be struck between managing resources over this period and ensuring the campaign to publicise the start of the SRIT is fully understood by all Scottish taxpayers.

**3.26** HMRC has also been working with employers to prepare them for the upcoming change. This has involved workshops, bulletins and a continued programme of education about SRIT. Employers have been asked to encourage employees to notify HMRC when they change address. As noted in paragraph 3.13, employers cannot notify HMRC on behalf of their employees.

**3.27** Pension providers are another main stakeholder group. In 2014-15, HMRC noted a risk around relief-at-source (RAS). Personal pension contributions are made after tax, so the pension scheme administrator can claim RAS from HMRC. The pension provider industry notified HMRC that some pension providers would not be in a position to implement the required changes brought about by the SRIT to their systems and processes by April 2016. Ministers agreed to a two-year transitional period to allow the pension industry to ready its systems for the SRIT. During this period, the pension industry will continue to apply the standard UK rate of income tax to all scheme members. Therefore, if the Scottish rate differs from the rate for the rest of the UK in 2016-17 and 2017-18, HMRC will be responsible for calculating any RAS shortfall or excess payment given by pension providers to Scottish taxpayers.

**3.28** HMRC responded to this risk by setting up a project team to focus on the RAS issue. While the two-year transitional period granted by ministers gives HMRC some extra time to resolve the RAS issue with pension providers, there remains a risk from 2018-19 onwards that Scottish taxpayers do not get the correct income tax relief on pension contributions when individuals contribute through personal pension schemes.

# Appendix One

## Board membership and terms of reference

### **Intergovernmental Assurance Board**

**1** The remit of the board is:

- to approve, own and review a joint implementation programme of agreed key milestones and activities to implement these provisions;
- to take a joint approach to quality assurance of the implementation process and to agree and review how progress towards these milestones should be driven and measured;
- to ensure that adequate resources are made available in each administration to drive forward necessary progress;
- to identify risks to implementation and oversee appropriate mitigating actions;
- to identify, and resolve, any concerns about the implementation process;
- to anticipate, and seek to resolve at an early stage, any arising disputes;
- where agreement cannot be reached, to advise on appropriate routes for escalation; and
- to consider relevant issues in advance of the Joint Exchequer Committee (JEC) and to report to the JEC on key assurance activities.

**2** Membership of the Board:

Scottish Government:

- Director General Finance/Deputy Director Fiscal Responsibility (Finance).
- Director General Strategy & External Affairs/Director (Strategy/External Affairs).
- Chief Economic Adviser (Economics).

UK government:

- Director of Public Services (HM Treasury).
- Deputy Director Devolution (HM Revenue & Customs (HMRC)).
- Director (Scotland Office).
- Director with responsibility for intergovernmental relationships (Cabinet Office).

The board is chaired jointly by the Director General Finance (Scottish Government) and the Director of Public Services (HM Treasury).

## **Programme Board**

3 The board will:

- act as a decision-making body for the Programme, except where it delegates authority to another body (for example, at project level); and provide clarity on who authorises what decisions;
- support the projects to deliver against their critical path and plans, and assess priorities and monitor the status of key milestones, taking into account any potential or known changes or decisions;
- ensure Programme-level risks and issues that impede or threaten delivery are effectively managed to resolution or mitigated;
- ensure the Programme and Scottish Rate of Income Tax (SRIT) project maximise value for money and accurately forecast costs;
- approve and sign off all programme-related documentation;
- authorise any change in the scope of the Programme;
- challenge project activity and provide comment and feedback on issues escalated by the projects;
- set the overall governance and assurance framework for the Programme implementation, and provide clear guidance and support on go-live recommendations;
- provide an update on progress towards implementation at each meeting of the JEC until SRIT is delivered; and
- provide updates to the Intergovernmental Assurance Board and to ministers when key delivery milestones have been achieved.

**4 Membership of the Board:**

- Deputy Director Devolution/Senior Business Sponsor HMRC.
- Representative from Policy Delivery Portfolio (HMRC).
- SRIT Senior Responsible Owner (HMRC).
- Representative from Internal Audit (HMRC).
- Representative from Scottish Government.
- Representative from HM Treasury.
- Representative from Scotland Office.

The board is chaired by the Deputy Director Devolution/Senior Business Sponsor.

**Project Board****5 The board will:**

- provide overall direction and leadership for the project;
- report to the Scotland Act Programme Board, providing updates on progress, consulting on key decisions and seeking approval to proceed through gates and project stage boundaries;
- agree the Project Board membership and revise the Project Board structure and terms of reference (as necessary) as the project moves through the life-cycle into delivery;
- agree stage plans, monitor milestone progress against plan and authorise next stage activity;
- authorise the assignment of project resources and the commitment of key HMRC stakeholder resources in line with the agreed stage plan deliverables;
- serve as a point of escalation for project risks and issues, and review the project CRAIDD (log of constraints, risks, assumptions, issues, dependencies and decisions) to support risk mitigation;
- serve as a change control authority, consider proposed changes to both the IT and non-IT specification/solution by balancing risks and benefits against costs;
- recommend and facilitate the appropriate alternative escalation route for any risks or issues that cannot be addressed or managed by the Project Board;

- act as the approvals body signing off key project documentation at major decision points;
- make decisions and invoke exception plans when tolerances are triggered for timeline slippage, product delay and benefits/costs variance;
- provide guidance, direction and decisions to the project manager and advice to the senior responsible owner;
- approve formal project closedown and agree handover strategy;
- nominate a single point of contact (SPOC) at project working level for their respective directorate; and
- provide an escalation point and sounding board for their respective SPOC within their directorate.

**6** Membership across the following areas:

- Personal Tax Product and Process (HMRC).
- Personal Tax Policy (HMRC).
- Personal Tax Change Policy and Other Government Department Project Delivery (HMRC).
- Scotland Act Policy (HMRC).
- Compliance and Enforcement (HMRC).
- Digital Service (HMRC).
- Personal Tax Customer and Strategy (HMRC).
- Personal Tax Operations (HMRC).
- Internal Audit (HMRC).
- Data Integrity Programme (HMRC).
- Finance (HMRC).
- Scottish Government.
- Scotland Office.
- HM Treasury Fiscal Devolution Policy.

The board is chaired by the SRIT Senior Business Sponsor.

## Appendix Two

### Summary of recommendations raised by Office of Government Commerce (OGC) and HM Revenue & Customs Internal Audit

Body	Recommendation	Date	Rating per report	Action taken by HMRC
OGC Gateway Process Review	Engage fully with all key Scottish Government stakeholders.	July 2013	Essential	Recommendation implemented
OGC Gateway Process Review	Enhance the structure and resource of the Programme Management Office.	July 2013	Essential	Recommendation implemented
OGC Gateway Process Review	Review all key stakeholders in order to establish their interrelationships and interdependencies.	July 2013	Essential	Recommendation implemented
OGC Gateway Process Review	Produce and manage a comprehensive programme-level Stakeholder and Communications Plan in order to ensure a consistent approach and accountability.	July 2013	Essential	Recommendation implemented
OGC Gateway Process Review	Develop and manage an integrated programme and customer communications strategy and delivery plan.	July 2013	Recommended	Recommendation implemented
OGC Gateway Process Review	Develop an end-to-end Programme plan identifying key milestones and decision points.	July 2013	Recommended	Recommendation implemented
OGC Gateway Process Review	Appoint a suitable deputy to the project manager, working full-time on the project, and aiming to have them in post by June 2014.	February 2014	Essential	Recommendation implemented. A deputy project manager was introduced shortly after the OGC review
OGC Gateway Process Review	Review the composition and size of the Project Board with a view to refocusing it for the increased delivery pace ahead (complete and implement in Q1 of 2014-15).	February 2014	Essential	Recommendation implemented. The Project Board has been reconstituted
OGC Gateway Process Review	Plan now for increased communications resource, to be fully deployed by December 2014.	February 2014	Essential	Recommendation implemented. A second briefings manager was added to the project team

Body	Recommendation	Date	Rating per report	Action taken by HMRC
OGC Gateway Process Review	Formalise and extend the existing practice, and presume that Scottish Government representatives should be actively invited to any project meeting, workshop or forum – excepting only those where HM Revenue & Customs policy issues or privileged data makes this inappropriate.	February 2014	Essential	Recommendation implemented
OGC Gateway Process Review	The project should establish a target level of accuracy in identifying Scottish taxpayers that can be shared and communicated to all stakeholders.	February 2014	Essential	Recommendation implemented. Discussions with Scottish Government continue to take place
OGC Gateway Process Review	The Project Board should agree and monitor an action plan to ensure Scottish Rate of Income Tax (SRIT) is properly recognised and represented on the HMRC Digital Roadmap, with requirements for SRIT digital services documented.	February 2014	Critical	Recommendation implemented
OGC Gateway Process Review	Review the role and tasks of the Programme Board and respective responsibilities of the Programme Management Office in order to maximise successful delivery of the Programme.	May 2014	Essential	Recommendation implemented
OGC Gateway Process Review	The Programme Board should ensure that the Joint Communication Group regularly reviews the Programme's communications activity to ensure that there is consistency of message from strategic to tactical levels.	May 2014	Essential	Recommendation implemented
OGC Gateway Process Review	Develop a comprehensive risk register for the Programme Board as a standing agenda item.	May 2014	Essential	Recommendation implemented
OGC Gateway Process Review	Baseline the end-to-end delivery plan and document, publish and maintain a 'critical path' of activities for delivery. The critical path activities are to be monitored at the Project Board.	June 2015	Critical	Recommendation implemented. A draft 'critical path' plan has been developed and shared with key stakeholders
OGC Gateway Process Review	Prepare, agree and publish a compelling narrative describing the activity in place to identify the dataset of Scottish taxpayers and secure stakeholder endorsement, particularly from the Scottish Government sponsor, to this approach.	June 2015	Critical	Recommendation implemented. A draft narrative has been developed and shared with the Scottish Government
OGC Gateway Process Review	Following the initial analysis carried out by the relief-at-source (RAS) project, define the scope and explore the options for ownership and establishment of a project to deliver the digital solution. (This may include addressing the improvement of pension data quality).	June 2015	Essential	Work is ongoing



Body	Recommendation	Date	Rating per report	Action taken by HMRC
OGC Gateway Process Review	In conjunction with the Corporate Communication team, define and agree a comprehensive communication strategy and plan for the launch and ongoing adoption of SRIT.	June 2015	Critical	Work is ongoing
Internal Audit	<ol style="list-style-type: none"> <li>1 The project should define its strategy, clearly stating assumptions/caveats used to identify the Scottish taxpayer while articulating deep dives so far along with defined tolerances.</li> <li>2 Draw up contingency plans to address the gaps in the identification of the Scottish taxpayer and agree a way forward.</li> </ol>	January 2015	Corrective action required	HMRC has worked closely with all stakeholders to develop the Scottish taxpayer identification strategy, and work is ongoing to agree with the Scottish Government the assumptions and acceptance criteria for the identification of Scottish taxpayers

**Note**

1 Progress on recommendations up-to-date as at the time of reporting.

Source: HM Revenue & Customs

## SCOTTISH PARLIAMENT PUBLIC AUDIT COMMITTEE

WEDNESDAY 27 JANUARY 2016

## REPORT BY THE AUDITOR GENERAL FOR SCOTLAND

The administration of the Scottish rate of income tax 2014/15

---

1. From April 2016, the Scottish Parliament will set a new Scottish rate of income tax (SRIT). HM Revenue and Customs (HMRC) will collect and administer the SRIT and is responsible for the project to implement it. The Scottish Government is responsible for funding this project and ensuring that the cost of the SRIT represents value for money and for seeking assurances that the new system will collect the correct amount of tax.
2. HMRC's accounts are audited by the National Audit Office (NAO). The Comptroller and Auditor General is required under statute to report to the Scottish Parliament on HMRC's administration of the SRIT. He made his first annual report to the Scottish Parliament on the SRIT on 26 November 2015.
3. The Public Audit Committee's report *Framework for auditing the Scottish rate of income tax* set out what audit information the Scottish Parliament can expect to receive to enable it to undertake its accountability role in relation to the SRIT.<sup>1</sup> In relation to Audit Scotland, the Committee recommended that:
  - Audit Scotland provides additional assurance on the NAO's audit of HMRC and the SRIT. The Committee also recommended that Audit Scotland works with the NAO on its future priorities for any performance audit work on the SRIT.
  - the joint working relationship between the Comptroller and Auditor General and the Auditor General for Scotland should be set out in a memorandum of understanding.
  - Audit Scotland reports annually on its assurance work in relation to the SRIT.
4. I sent my first annual report providing additional assurance on the NAO's audit work on the SRIT to the Public Audit Committee on 26 November 2015. On the basis of Audit Scotland's review, I am satisfied that the NAO's approach was sufficient and robust. I am also satisfied that the

---

<sup>1</sup> Public Audit Committee, 1st Report, 2014 (Session 4): Framework for auditing the Scottish rate of income tax

findings and conclusions in the Comptroller and Auditor General's report are reasonably based. Audit Scotland's review was carried out in accordance with the memorandum of understanding agreed between me and the Comptroller and Auditor General. This describes our respective powers and responsibilities and sets out a framework for collaborative working.

5. I have reported separately on the preparations for the implementation of the Scotland Act 2012. This includes my assessment of how the Scottish Government is working with HMRC to prepare to introduce the SRIT in April 2016.



## National Audit Office

Comptroller and Auditor General  
Sir Amyas Morse KCB

Gary Cocker  
Assistant Clerk to the Public Audit Committee  
Room T 3.60  
The Scottish Parliament  
Edinburgh  
EH99 1SP

### Helping the nation spend wisely

Telephone +44 (0)20 7798 7777  
Facsimile +44 (0)20 7798 7990  
Email amyas.morse@nao.gsi.gov.uk

Reference AM/1016/15  
Date 14 January 2016

*Dear Mr Cocker,*


### SCOTTISH RATE OF INCOME TAX

Thank you for your letter of 4<sup>th</sup> December inviting me to attend the Public Audit Committee on 27<sup>th</sup> January 2016 as part of its hearing on the Scottish Rate of Income Tax.

I would be delighted to attend. I will be accompanied by my Director, Steven Corbishley.

I know Steven has talked with you on our preparations for this hearing. As promised, I attach a brief background paper for the Committee to accompany our report. I also enclose for the Committee a copy of the Memorandum of Understanding between the National Audit Office and Audit Scotland that has been signed by myself and Caroline Gardner.

Please let me know if we can be of any further help.

  
AMYAS MORSE

## BACKGROUND NOTE TO THE SCOTTISH PUBLIC AUDIT COMMITTEE FROM THE COMPTROLLER AND AUDITOR GENERAL

### THE ADMINISTRATION OF THE SCOTTISH RATE OF INCOME TAX 2014-15 (SG/2015/236)

#### *Introduction*

1. The Scotland Act 2012 introduced powers for the Scottish Parliament to apply a Scottish Rate of Income Tax (SRIT) to the non-savings, non-dividend income of Scottish taxpayers from April 2016. The UK government will deduct 10p from the basic, higher and additional rates of income tax. The Scottish Parliament will then be able to levy an additional Scottish rate applied equally across the three main tax bands, in advance of each tax year from 2016-17. HM Revenue & Customs (HMRC) will continue to collect income tax and will pay over to the Scottish Government the amount of revenue it collects relating to the SRIT.
2. Under Section 80HA of the Scotland Act 1998, as amended by the Finance Act 2014, the Comptroller and Auditor General (C&AG) is, from the 2014-15 financial year, required to report on:
  - the adequacy of any of HMRC's rules and procedures put in place, in consequence of the Scottish rate provisions, for the purpose of ensuring the proper assessment and collection of income tax charged at rates determined under those provisions;
  - whether these rules and procedures are being complied with;
  - the correctness of the sums brought to account by HMRC which relate to income tax which is attributable to a Scottish rate resolution; and
  - the accuracy and fairness of amounts reimbursed to HMRC as administrative expenses incurred as a result of the charging of income tax.
3. Our report, which the Committee will consider on 27th January 2016, is the first in a series of reports to be produced by the C&AG under these powers to consider HMRC's on-going implementation of the Scottish Rate of Income Tax. This first report focuses on HMRC's activities during 2014-15 and, therefore, primarily looks at HMRC's preparedness for a future Scottish rate being in force. Our report was published on 26 November 2015.
4. Since we reported, HMRC announced at the end of November 2015 that it will start sending letters to potential Scottish taxpayers as part of their next stage of preparations for the introduction of the Scottish Rate of Income Tax. The letters are intended to confirm the accuracy of HMRC's records of taxpayers who live in Scotland and will pay the new rate. They set out that taxpayers do not need to take any action if the address details HMRC holds for them are correct. The letters will go to around 2.6 million people in Scotland who are expected to be taxpayers in the 2016-17 tax year.
5. Also, on 16 December 2015, the Scottish Parliament announced an additional rate of 10p for the 2016-17 tax year, therefore ensuring that Scottish income tax payers would pay tax at the same rate as the rest of the United Kingdom for the upcoming tax year.

#### *Previous discussions between the Comptroller and Auditor General and the Scottish Public Audit Committee*

6. As part of their consideration of the legislation setting out our and HMRC's respective responsibilities, the Committee has previously discussed with the C&AG how the audit arrangements for the SRIT might work in practice. The C&AG outlined his commitments to the Public Audit Committee in respect of this and future reports at the Committee's 15 January 2014 meeting.
7. As part of this discussion, the C&AG outlined that:
  - he is responsible for auditing the whole of HMRC and our primary work is focussed on forming

opinions and views over HMRC's operations and financial statements – in discharging our SRIT remit, we would look at any additional information and give whatever assurance we were able to give, depending on the quality of that information and how much Scotland-specific information is available to the NAO;

- within this context of examining the overall taxpaying system (which we do on a UK-wide basis), we will report on the reasonableness of HMRC's calculations over the portion of tax that relates to Scotland;
- legislation requires the NAO to report in a particular style, providing a narrative report that gives the NAO's view over the accuracy of the sums that are brought to account by HMRC and, where appropriate, the economy, efficiency and effectiveness of these arrangements;
- his reports may differ in depth and nature each year depending on the relative stability of HMRC's control environment in respect of SRIT;
- we remain committed to work with the Auditor General for Scotland, and Audit Scotland, when producing our reports (*there is a signed Memorandum of Understanding between the NAO and Audit Scotland which sets out the principles of our working arrangements and this has been provided separately to the Committee*);
- if the C&AG had serious concerns about the quality of the calculations supporting the tax receipts arising as a result of the SRIT, he would report these to the Committee; and
- while there is no legal obligation for the C&AG to appear before the Committee, he and his successors will continue to do so if invited to relevant Committee hearings given the C&AG's role as the external auditor of HMRC.

#### *Direction of future reports*

8. Our first report provides a useful opportunity for the Committee to consider how these audit arrangements have worked in practice. The report itself sets the scene for potential future developments in respect of HMRC's administration of the SRIT. It also considers the reasonableness of costs incurred so far by HMRC in preparation for the SRIT. It also introduces the key challenges facing HMRC in their objective of successfully delivering SRIT.
9. For future reports, we will monitor developments with the project and revisit some of these initial challenges. We will continue to work with HMRC, as well as with Audit Scotland, to ensure we meet our legislative reporting requirements. The depth and nature of future reports will be influenced by emerging risks and issues as SRIT evolves. For instance, it will not be until our third report, focussing on the 2016-17 financial year, that we will be able to report on the proper assessment and collection of tax revenues attributable to the Scottish rate of income tax.

## **MEMORANDUM OF UNDERSTANDING**

**For cooperation between the Comptroller and Auditor  
General and the Auditor General for Scotland, on the audit  
of the Scottish rate of income tax**

## Introduction

1. The Scotland Act 1998 ("the 1998 Act"), as amended by the Scotland Act 2012 ("the 2012 Act"), gives the Scottish Parliament the power to set a Scottish rate of income tax (SRIT) for Scottish taxpayers (as defined in a new section 80D of the 1998 Act). SRIT will commence from a date to be set by the UK Government, expected to be April 2016. It will be administered by HM Revenue and Customs (HMRC) as part of the UK-wide income tax system and applied to non-savings income. The Scottish Parliament will be able to set a rate of SRIT from zero to any number of pence or half-pence in the pound. This rate will be added to each of the main UK rate bands after ten pence in the pound has been deducted from each rate.
2. An amount equal to ten pence of each rate will be deducted from the Scottish Block grant whether the Scottish Parliament sets a rate or not and replaced by the amount received through SRIT will be included in the overall Scottish Block grant for each year based on estimated figures, with a reconciliation to actual amounts raised taking place twelve months after the end of the year
3. The Command Paper which accompanied the draft 2012 Act, entitled *Strengthening Scotland's Future*<sup>1</sup>, outlined the arrangements that the UK Government proposed to put in place to ensure accountability in relation to HMRC implementing and operating the SRIT:
  - The UK Government will invite the Comptroller and Auditor General (C&AG), as head of the National Audit Office (NAO), to prepare a report to the Scottish Parliament on HMRC's administration of the SRIT.
  - The Scottish Parliament will receive a report from HMRC on the administration of the Scottish income tax receipts;
  - Scottish Parliamentary Committees will be able to request HMRC's Accounting Officers to give evidence.
  - An HMRC Additional Accounting Officer will be made specifically accountable for the collection of the SRIT.
  - The UK Government will also inform Scottish Ministers in writing of HMRC Commissioner appointments.
4. The UK Finance Act 2014 places a duty on the C&AG, as the statutory external auditor of HMRC, to prepare a report on the administration of the SRIT for each financial year, to be laid before the Scottish Parliament not later than 31 January of the financial year following that to which the report relates.
5. HMRC is governed by the Commissioners for Revenue and Customs Act 2005 which prohibits disclosure of HMRC's information except under specific circumstances. Audit Scotland is not HMRC's auditor, nor does it have any statutory right of access to HMRC information.

<sup>1</sup> Command Paper CM 7973 November 2010

<https://www.gov.uk/government/publications/strengthening-scotland-s-future-hm-command-paper>



6. The C&AG and the Auditor General for Scotland have confirmed to the Public Audit Committee of the Scottish Parliament that they are happy to work together to ensure that the Parliament receives appropriate reports on the operation of the SRIT.
7. This Memorandum of Understanding describes our respective powers and responsibilities and sets out a framework for collaborative working. This framework is designed to optimise the skills and experience involved in audits, reviews or investigations, avoid duplication of effort and ensure that the Scottish Parliament receives the assurance it requires about the implementation and operation of the SRIT.

### **Statutory role of the Comptroller and Auditor General and the NAO**

8. The National Audit Office (NAO) scrutinises public spending on behalf of the UK Parliament and its audit of central government has two main aims. By reporting the results of audits to the UK Parliament, it helps Parliament to hold government departments and bodies to account for the way they use public money, thereby safeguarding the interests of taxpayers. In addition, its work aims to help public service managers improve performance and service delivery.
9. The audit and inspection rights are vested in the head of the National Audit Office, the Comptroller and Auditor General (C&AG). The NAO undertakes these tasks on his behalf.
10. The C&AG is an Officer of the House of Commons. Both he and the NAO are independent of government and are not subject to the control or direction of the UK Government or Parliament.
11. There are a number of Acts of Parliament that give the C&AG the right to audit, or examine the receipt of revenue of, HMRC:
  - The Exchequer and Audit Departments Act 1921 provides that the C&AG audits the revenues collected by HMRC, as accounted for in HMRC's Trust Statement (as directed by HM Treasury) and to examine these *"to ascertain that adequate regulations and procedure have been framed to secure an effective check on the assessment, collection, and proper allocation of revenue"* and to satisfy himself that any such regulations and proceedings are being duly carried out, and as to the correctness of sums brought to account in respect of revenue. This examination takes the form of a separate report (the Standard Report) by the C&AG on HMRC's Annual Accounts;
  - The Government Resource and Accounts Act 2000 provides that the C&AG audits the departmental accounts produced by UK central government departments, including those produced by HMRC; and
  - The National Audit Act 1983 allows the C&AG to undertake examinations into the economy, efficiency and effectiveness of how certain bodies, including HMRC, have used their resources in discharging their functions.

12. Subject to certain constraints, the C&AG has complete discretion in the carrying out of the functions of that office including what is reported to Parliament.
13. The Scotland Act 2012 makes no changes to the way the C&AG and the NAO undertakes their existing roles in respect of HMRC.
14. From 2014-15, under section 80HA of the Scotland Act 1998 (inserted by section 297 of the Finance Act 2014), the C&AG is required to report to the Scottish Parliament on:
  - the adequacy of any of HMRC's regulations and procedures relating to the Scottish rate provisions;
  - whether these rules and procedures are being complied with;
  - the correctness of the sums brought to account by HMRC which relate to SRIT; and
  - the accuracy and fairness of the administrative expenses reimbursed to HMRC.
15. The C&AG may also include in the report an assessment of the economy, efficiency and effectiveness with which HMRC has used its resources in carrying out relevant functions.
16. It is currently envisaged that HMRC will report the revenue collected under the SRIT in notes to the Trust Statement. Costs associated with its collection will be shown in HMRC's Resource Account. HMRC will use these notes to compile a specific report to the Scottish Parliament.
17. The C&AG is required to report to the Scottish Parliament on these activities, and assurances over these figures, from 2014-15. The report must be laid before the Scottish Parliament by 31 January of the financial year following the one to which the report relates. The C&AG might also exercise his rights under the National Audit Act 1983 to report to the UK Parliament on these activities.

#### **Statutory roles of the Auditor General for Scotland and Audit Scotland**

18. Under the Scotland Act 1998, the Auditor General for Scotland (AGS) and those who exercise functions on her behalf are not subject to the control or direction of any member of the Scottish Government or the Scottish Parliament. She is responsible for ensuring propriety and value for money in the spending of public funds. She investigates whether public bodies are achieving the best possible value for money and adhering to the highest standards of financial management.
19. Scottish Ministers, the Lord Advocate and every other person to whom sums are paid out of the Consolidated Fund in a financial year must prepare accounts of their expenditure and receipts for that year to be audited by the AGS. The AGS is responsible for securing the audit of the Scottish Government and most other public bodies in Scotland except local authorities. Annual financial audit reports are produced for all of the public bodies that the AGS is responsible for auditing.

20. Section 23 of the Public Finance and Accountability (Scotland) Act 2000 (the 2000 Act) gives the AGS specific powers to examine the economy, efficiency and effectiveness with which resources are being used by specified public bodies.
21. The AGS is required to lay reports in Parliament which are then scrutinised by the Public Audit Committee (and which may also be considered by other relevant Committees).
22. Audit Scotland is a statutory body set up in April 2000 under the 2000 Act. It provides services to the AGS and the Accounts Commission. Audit Scotland provides independent assurance to the people of Scotland that public money is spent properly and provides value for money. It supports improvement in public services by holding to account those responsible for spending public funds.
23. The 2012 Act makes no changes to the role of the AGS or Audit Scotland.
24. The estimated receipts from the SRIT and any subsequent adjustments to reflect actual receipts will flow into the Scottish Consolidated Fund as an adjustment to the overall Scottish Block Grant. This is the first point at which the SRIT flows become subject to audit by the AGS.
25. As part of its audit of the Scottish Government, Audit Scotland will consider and, where appropriate, report on
  - The Scottish Government's governance arrangements for the development of SRIT;
  - Scottish Government arrangements to prepare information about the proposed Scottish rate;
  - Expenditure paid to HMRC for administrative costs incurred under Section 80H, through the audit of the Scottish Government; and
  - The assurance obtained from NAO on overall arrangements.
26. The Public Audit Committee of the Scottish Parliament has recommended that Audit Scotland should provide additional assurance on the NAO's audit of HMRC and to work with the NAO on the future priorities and focus of its work. This MOU sets out how these recommendations will be fulfilled.

#### **A framework for collaborative working**

27. The C&AG and the AGS are committed to ensuring that we deliver our audits, reviews and investigations efficiently and effectively. We have agreed the following arrangements for collaborative working. Specifically we are committed to:
  - Maintaining effective communication and liaison;
  - Sharing relevant information and respecting confidentiality of shared information; and
  - Sharing knowledge, skills, expertise and experience.

28. We will evolve approaches to sharing knowledge and expertise to build mutual confidence in the quality of our audit work. The NAO and Audit Scotland will meet regularly to ensure effective communication and information sharing between the two organisations.
29. As part of the framework to deliver assurance on the implementation and operation of SRIT, each year the NAO will discuss with Audit Scotland:
  - their audit planning to ensure that attention is focused on the key risk areas of the audit, that potential problems are identified and resolved timeously and that the audit timetable will meet stakeholder requirements. This will include any plans for value for money work.
  - the NAO's approach to risk assessment undertaken at the start of the audit process. The process will enable the NAO to identify the key risk areas and control systems and develop an audit approach designed to address these risks in the most efficient manner.
  - their application of the concept of materiality to the audit of SRIT. Materiality is concerned with the extent to which auditors can tolerate error and is relevant for determining which account areas are significant from an audit perspective and the nature, timing and extent of audit procedures required. Materiality has both quantitative and qualitative factors; however, the final assessment of what is material is a matter of professional judgement.
  - the NAO's testing strategy to deliver appropriate assurance that the control systems are operating as intended.
  - the NAO's testing strategy for the financial and other information included in the HMRC report.
  - the findings arising from the audit.
  - the draft report on the audit.
30. The first NAO audit report to be prepared under the 2012 Act will cover the financial year ending 31 March 2015 and will have to be published by January 2016 at the latest. The AGS will report on the same period and that report will:
  - summarise the extent and nature of work performed by Audit Scotland in relation to NAO's audit on the SRIT;
  - provide views and comments on the reasonableness of NAO's audit approach, findings and conclusions; and
  - highlight any specific aspects of NAO's findings or conclusions that are considered pertinent from a Scottish perspective.

**Resolving disagreements**

31. The C&AG and AGS are committed to working together in an environment of professional respect and promoting a culture of openness. This approach should minimise the risk of disagreements. Any disagreements will normally be resolved at a working level between the individuals involved. If this is not possible, it will be referred upwards through normal management reporting channels until resolution is achieved. Ultimately a disagreement may be referred to the C&AG and the AGS who will be responsible for ensuring a mutually satisfactory resolution.

**Reviewing the Memorandum of Understanding**

32. We will formally review this Memorandum at least every three years, or when there are relevant changes to legislation, to ensure both organisations are working within our agreed framework, and consider whether the arrangements needs to be revised to meet changing circumstances.

Signed Angus Mc

Date 14<sup>th</sup> January 2016

**Comptroller and Auditor General**

Signed Caroline Gordon

Date 15 Dec 2015

**Auditor General for Scotland**

## Appendix 1: EXTRACT FROM THE UK FINANCE ACT 2014

290 Report on administration of the Scottish rate of income tax

(1) In Chapter 2 of Part 4A of the Scotland Act 1998, after section 80H insert—

"80HA Report by the Comptroller and Auditor General

(1) The Comptroller and Auditor General must for each financial year prepare a report on the matters set out in subsection (2).

(2) Those matters are—

(a) the adequacy of any of HMRC's rules and procedures put in place, in consequence of the Scottish rate provisions, for the purpose of ensuring the proper assessment and collection of

income tax charged at rates determined under those provisions,

(b) whether the rules and procedures described in paragraph (a) are being complied with,

(c) the correctness of the sums brought to account by HMRC which relate to income tax which is attributable to a Scottish rate resolution, and

(d) the accuracy and fairness of the amounts which are reimbursed to HMRC under section 80H (having been identified by it as administrative expenses incurred as a result of the charging of income tax as mentioned in paragraph (a)).

(3) The "Scottish rate provisions" are—

(a) any provision made by or under this Chapter, and

(b) any provision made by or under the Income Tax Acts relating to the Scottish basic rate, the Scottish higher rate or the Scottish additional rate.

(4) A report under this section may also include an assessment of the economy, efficiency and effectiveness with which HMRC has used its resources in carrying out relevant functions.

198

(5) "Relevant functions" are functions of HMRC in the performance of which HMRC incurs administrative expenses which are reimbursed to HMRC under section 80H (having been identified by it as administrative expenses incurred as a result of the charging of income tax as mentioned in subsection (2)(a)).

(6) HMRC must give the Comptroller and Auditor General such information as the Comptroller and Auditor General may reasonably require for the purposes of preparing a report under this section.

(7) A report prepared under this section must be laid before the Scottish Parliament not later than 31 January of the financial year following that to which the report relates.

(8) In this section "HMRC" means Her Majesty's Revenue and Customs."

(2) The amendment made by this section has effect in relation to the financial year ending on 31 March 2015 and subsequent financial years.

T: 0845 774 1741

E: scottish.ministers@scotland.gsi.gov.uk



Paul Martin MSP  
 Convener, Public Audit Committee  
 The Scottish Parliament  
 Edinburgh  
 EH99 1SP

10 December 2015

## SCOTTISH RATE OF INCOME TAX: DEPARTMENT OF WORK AND PENSIONS IMPLEMENTATION COSTS – EXCHANGE OF LETTERS

As you are aware, under the settlement for the Scotland Act 2012, it was agreed that the Scottish Government would pay the costs incurred as a result of implementing and administering the financial provisions. In respect of the Scottish Rate of Income Tax (SRIT) provisions, the main costs are attributable to work that HMRC is doing as the body responsible for the collection and management of SRIT as part of the UK income tax system. Edward Troup, HMRC's Second Permanent Secretary and Additional Accountable Officer for SRIT appeared before the Finance Committee on 28 October. He confirmed that the estimates for implementation remain between £30m - £35m, as reported in the UK Government's [\*Third Annual Report on the Implementation and Operation of Part 3 \(Financial Provisions\) of the Scotland Act 2012\*](#) in March this year, as well as providing an update on potential running costs.

The UK Government's March report identified that the Department of Work and Pensions (DWP) was also making changes to its systems to reflect the introduction of SRIT. DWP need to make changes to ensure that its systems recognise and process information on Scottish taxpayers from April 2016 in the way they currently do for UK taxpayers. At this time, DWP estimates the implementation costs associated with this work to be £1.8m, with no ongoing running costs.

My officials have worked with DWP's SRIT Project Team to: understand the work being done by DWP to ensure that DWP is compliant with SRIT; identify the changes that are being incurred wholly and necessarily as a result of SRIT's introduction and their associated costs; and, agree appropriate governance arrangements to allow the Scottish Government to work with DWP to scrutinise these costs and achieve value for money.



I enclose a copy of the exchange of letters between officials within the Scottish Government and DWP agreeing the arrangements under which our organisations will work together and make the changes necessary to ensure a smooth implementation of SRIT from April 2016. These arrangements, while taking into account the different role and estimated implementation costs of DWP, are closely modelled on the [Memorandum of Understanding](#) in place for SRIT between the Scottish Government and HMRC.

These arrangements apply only to the implementation of the Scottish income tax powers introduced under the Scotland Act 2012 and, therefore, will be reviewed or replaced at such time as any further income tax powers are devolved to the Scottish Parliament.

I am writing in similar terms to the Conveners of the Finance and Devolution (Further Powers) Committees.



JOHN SWINNEY

**Encl. Exchange of letters on the Arrangements between the Scottish Government and the Department of Work and Pensions for the Scottish Rate of Income Tax**



Finance Directorate  
Fiscal Responsibility Division

T: 0131-244 4948  
E: Sean.Neill@gov.scot



Michael Boughey  
Deputy Director  
Technology Platforms  
Department of Work and Pensions  
Second Floor, Birchwood Park  
Warrington, WA3 6XF



E: [Michael.Boughey@dwp.gsi.gov.uk](mailto:Michael.Boughey@dwp.gsi.gov.uk)

19 November 2015

Dear Michael

**SCOTTISH RATE OF INCOME TAX (SRIT): ARRANGEMENTS BETWEEN THE SCOTTISH GOVERNMENT AND THE DEPARTMENT OF WORK AND PENSIONS (DWP)**

Thank you for your helpful letter of 16 October confirming that you are now responsible for the delivery and implementation of SRIT within DWP.

In March, the UK Government identified, in its *Third Annual Report on the Implementation and Operation of Part 3 (Financial Provisions) of the Scotland Act 2012*, that DWP was making changes to its systems to reflect the introduction of SRIT. The Scottish Government understands that these are changes that will ensure that DWP systems can continue to recognise and process information on Scottish taxpayers from April 2016.

Under the settlement for the Scotland Act 2012, it was agreed that the Scottish Government pay the costs incurred as a result of implementing the financial provisions of the Scotland Act 2012.

Scottish Government officials have, therefore, been working with DWP's SRIT Project Team to: understand the work being done by DWP to ensure that DWP is compliant with SRIT; to identify the changes that are being incurred wholly and necessarily as a result of SRIT's introduction and their associated costs; and, to agree appropriate governance arrangements to allow the Scottish Government to work with DWP to scrutinise these costs to achieve value for money.

I now seek your formal agreement to the arrangements proposed in the Annex of this letter which will provide the transparent framework under which our organisations will continue to work together to ensure that value for money is achieved as DWP make the changes necessary to ensure a smooth implementation of SRIT from April 2016.

Victoria Quay, Edinburgh EH6 6QQ  
[www.gov.scot](http://www.gov.scot)



These arrangements apply only to the implementation of the Scottish rate of income tax powers introduced under the Scotland Act 2012 and, therefore, will be reviewed or replaced at such time as any further income tax powers are devolved to the Scottish Parliament.

A copy of these arrangements will be provided to the Scottish Parliament's Finance and Public Audit Committees.

Yours sincerely



SEAN NEILL  
Deputy Director

Encl. ANNEX: Arrangements between the Scottish Government and the Department of Work and Pensions for the Scottish Rate of Income Tax (5 pages)

**From:** Michael Boughey  
Deputy Director  
Technology Platforms  
DWP Technology

**To:** Sean Neill  
Deputy Director  
Scottish Government  
Area 2F South  
Victoria Quay  
Edinburgh  
EH6 6QQ

**Date:** 1st December 2015

**Scottish Rate of Income Tax (SRIT)**

**Arrangements between the  
Scottish Government and the Department for Work and Pensions (DWP)**

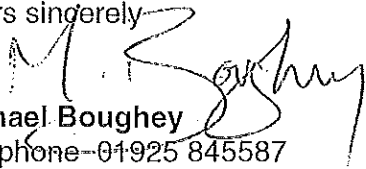
Dear Sean,

Thank you for your letter of the 19 November 2015, which included an Annex with proposed arrangements between the Scottish Government and the Department for Work and Pensions for the Scottish Rate of Income Tax.

I formally provide agreement to the arrangements proposed in the Annex, which will provide the transparent framework under which our organisations will continue to work together to ensure that value for money is achieved as DWP make the changes necessary to ensure a smooth implementation of SRIT from April 2016.

I also fully agree that the arrangements only apply to the implementation of the Scottish Rate of Income Tax powers introduced under the Scotland Act 2012 and therefore, that they will be reviewed or replaced at such time as any further Income Tax powers are devolved to the Scottish Parliament.

Yours sincerely

  
**Michael Boughey**  
Telephone 01925 845587

**Copy List:**

Ray Long  
Steve Faill  
Una Wiatrek  
Richard Cornish  
James Pike  
Simon Boniwell

**ANNEX TO THE EXCHANGE OF LETTERS BETWEEN THE SCOTTISH GOVERNMENT AND THE  
DEPARTMENT OF WORK AND PENSIONS DATED 19 NOVEMBER 2015 AND 1 DECEMBER 2015**

**Arrangements between the Scottish Government  
and the Department of Work and Pensions  
for the Scottish Rate of Income Tax**

***Introduction***

1. The Scottish rate of income tax (SRIT) will be set, each year, through a Resolution passed by the Scottish Parliament on the basis of a proposal made by Scottish Ministers. SRIT is not a devolved tax. It forms part of the UK income tax system and will be administered along with the rest of the income tax system by Her Majesty's Revenue and Customs (HMRC).
2. As certain aspects of the current tax and benefit systems are inter-dependent, the introduction of SRIT has consequential impacts for the Department of Work and Pensions (DWP). DWP requires, therefore, to ensure that its systems and processes are ready to recognise SRIT when it is introduced from April 2016.
3. Scottish Ministers will be responsible for proposing the tax rate but not for any other element of the tax nor for its administration. However the Scottish Government's (SG's) budget will bear the agreed costs of setting up and operating SRIT and will benefit from revenue collected. This Annex sets out arrangements for the SG to meet the costs of changes to DWP administrative and IT systems made necessary by the introduction of SRIT. The arrangements in place between the Scottish Government (SG) and HMRC for setting up and operating SRIT are covered by a separate Memorandum of Understanding.

***Scottish rate of income tax***

4. The Scotland Act 1998 as amended by the Scotland Act 2012 ('the 2012 Act') gives the Scottish Parliament the power to set a Scottish rate of income tax (SRIT) to be charged on Scottish taxpayers. It will be administered by HMRC as part of the UK wide tax system and applied to non-savings income. The Scottish Parliament will be able to set a rate of SRIT from zero to any number of pence or half pence in the pound. The rate will be added to each of the main UK rate bands after ten pence in the pound has been deducted from each rate. The 2012 Act repeals the provisions for the Scottish Variable Rate with effect from the date SRIT begins. SRIT will be set each year through a resolution passed by the Scottish Parliament on the basis of a proposal made by Scottish Ministers.

***Purpose of this annex***

5. This Annex sets out the arrangements agreed between the SG and DWP for ensuring DWP administered taxable benefits and associated IT systems recognise and interact with SRIT in order that benefit recipients who are Scottish taxpayers continue to receive the correct amount of benefits and that the correct tax information is recorded for HMRC purposes. It sets the respective responsibilities of the SG and DWP in relation to these aspects of SRIT implementation and provides a framework for inter-Government work on this issue. It has no formal legal force, nevertheless both Governments expect it to be followed.

6. These arrangements reflect:

- The Memorandum of Understanding and Supplementary Agreements between the United Kingdom Government, The Scottish Ministers, the Welsh Ministers and Northern Ireland Executive Committee;
- Cabinet Office Devolution guidance notes; and
- HM Treasury's statement of funding policy, "Funding the Scottish Parliament, National Assembly of Wales and Northern Ireland Assembly".

***Date and Timing***

7. This Annex and arrangements described within it come into effect when the last of the parties' to signify their acceptance of those arrangements through an exchange of letters signifies acceptance. It has no expiry date but will cease to have effect if SRIT is repealed. The arrangements may be brought to an end by agreement between DWP and SG and will be reviewed at the request of either party.

***Senior responsible officers and Parliamentary reporting***

8. The DWP Permanent Secretary is the Accounting Officer with overall responsibility for ensuring that the correct IT and administrative systems are in place within DWP to support the timely introduction of SRIT. Scottish Parliamentary Committees may request that DWP provides a senior official to give evidence, and DWP will consider these requests in line with Cabinet Office guidance on officials' attendance at such Committees. The senior officials with responsibility for matters covered by this Annex are the Deputy Director, Fiscal Responsibility for the Scottish Government and the nominated Deputy Director DWP Technology Platforms.
9. Section 33 of the 2012 Act lays a duty on the Secretary of State to make a report each year until 2020 at the earliest on the implementation and operation of Part 3 of the 2012 Act (Finance) which will include a report on the implementation and operation of SRIT. This report must be laid in each House of Parliament and sent to Scottish Ministers who must lay a copy before the Scottish Parliament. Scottish Ministers are similarly required to make a report each year to the Scottish Parliament, which in turn is sent to the UK Government and laid before the Westminster Parliament. These reports must include a report on progress with implementing and operating the financial provisions in the 2012 Act and DWP will contribute to the UK report.

***Roles and responsibilities of DWP and SG***

10. DWP will continue to have in place appropriate governance arrangements to ensure DWP IT systems, relevant staff guidance, customer forms and letters comply with SRIT provisions in the Scotland Act 2012. The process will take an inter-governmental approach to quality assurance, reviewing progress against milestones and ensuring value for money.
11. The SG will be represented within DWP's internal governance arrangements for implementing SRIT at both project and programme level. The SG may also request that DWP commission an external assurance review at the SG's expense.

12. DWP will make the necessary changes to benefit IT platforms which interface with the UK tax systems to enable them to recognise the new Scottish tax code. At the same time and where appropriate, staff guidance and customer forms and letters will be amended accordingly.
13. DWP will develop and test the IT and administration of SRIT in consultation with HMRC and the SG.
14. DWP will invoice SG for agreed items of expenditure as set out in paragraph 30 below.
15. SG will make payment to DWP for amounts invoiced for agreed items of expenditure as set out in para 30 below.
16. DWP will have no role in relation to determining an individual's tax liability nor for the publicity of SRIT other than ensuring, where appropriate, customer communications reflect the Scottish rate.

***DWP IT and Administrative impacts of SRIT Implementation***

17. DWP will remain responsible for ensuring that the correct IT and administrative systems are in place to support the timely introduction of SRIT.
18. DWP will keep the SG informed of, and will consult with the SG on plans, timetables, estimated costs, risks and progress. Where there are options for developing and amending such systems, DWP will discuss these, together with the cost, risk, efficiency, effectiveness or customer impact factors, with the SG before an option is selected.
19. DWP will upgrade and test all IT systems for all areas of DWP business that will be impacted by SRIT. This will be done through contracted IT suppliers and in accordance with its normal IT development practice.
20. The cost and functionality of each part of the IT system will be notified to the SG, subject to any confidentiality rules in prevailing DWP contracts.
21. The SG will have an opportunity to review plans for IT testing and the results of such tests.
22. DWP will develop non IT systems for all areas of DWP business that will be impacted by SRIT. This will be done in accordance with normal DWP practice.
23. A breakdown of the expected costs and activities for both IT system and non IT system changes will be shared with the SG before such costs are incurred.
24. DWP and the SG will scrutinise the IT and non IT System costs with a view to ensuring value for money. Where the SG have any concerns about the cost of a particular item that joint discussions cannot resolve, the SG – or DWP on behalf of the SG – may request an independent assessment of the estimated costs in question. All associated costs of the independent assessment will be met by the SG. Any contracts and costs finalised after this Annex takes effect, will be discussed and agreed with the SG in advance.

***Continuing operations***

25. After IT changes have been made to deliver SRIT, DWP will maintain its IT and administrative systems so that SRIT continues to operate effectively in respect of the administration of benefits.

***Funding***

26. DWP will test existing infrastructure put in place pre-1998 in preparation for Scottish Variable Rate of Tax to extract value for money from this earlier investment, but also needs to undertake new work to cover benefits and IT systems that have been developed and come on-line in the intervening time to ensure the current social security system will recognise Scottish taxpayers and that the respective IT systems interface with HMRC SRIT systems.

27. Where DWP charges for its services, it does so (following HM Treasury policy) at the full economic cost of providing the service seeking to make clear the breakdown of the calculation. Full economic cost is based on the average salary cost for the relevant grade plus per capita overheads such as superannuation. Where costs are under contract by third parties including DWP's IT supplier, these will be charged at cost.

28. The SG will meet costs which it is satisfied have wholly and necessarily been incurred as a result of the introduction of SRIT.

29. Once the changes are made to DWP's IT systems to recognise SRIT as introduced in the Scotland Act 2012, there will be no additional annual expenditure to maintain these changes.

30. Costs will be borne by the SG and DWP as set out below:

***Costs borne by SG – DWP will invoice and the SG will pay for:***

- Capital and project costs of making IT changes to DWP IT systems and ancillary costs (i.e. non-IT) relating to staff guidance and customer forms and letters required as a result of the introduction of SRIT.
- If suppliers consume more time and materials than agreed estimates, DWP will discuss with SG with the expectation that SG will meet costs if these increases have been incurred wholly and necessarily as a result of the introduction of SRIT and not as a result of error on the part of suppliers.

***Costs borne by DWP – DWP will not charge for:***

- Cost of changes to DWP IT systems where no specific provision needs to be made for SRIT.
- Supplier issues covered under DWP contract warranties.
- If a supplier fails to deliver, the SG should not pay for any consequence of costs incurred by the DWP Business invoking manual processes due to supplier issues. For example additional changes to Letters and Guidance.
- Costs involving changes to the IT systems where aspects of SRIT cannot reasonably be costed separately.

***Invoicing***

31. DWP will invoice SG for costs quarterly in arrears. SG will make payment to DWP within 30 days of the invoice date, or within 30 days of receipt of the invoice if there is a delay of more than 5 days between invoice date and date of receipt.
32. Separate arrangements may be agreed between DWP and the SG for Quarter 4 payments to ensure that payments are made in the appropriate financial year.

***Dispute resolution***

33. Where a dispute arises over a payment in relation to matters set out in this above, it will be discussed at the DWP Technology Platforms Functional Board or its successor at which the Scottish Government is represented. If agreement is not reached between DWP and SG the matter will be escalated to the SG's Director of Financial Strategy and DWP's Director of Technology Platforms or successor Director.

***Information sharing***

34. DWP will provide SG with information that will enable Scottish Ministers and officials to discharge their duties in respect of Parliamentary accountability. This includes information in relation to the reporting requirements of Section 33 of the 2012 Act.

***Limitations***

35. DWP operates within the legal constraints of customer confidentiality, the Data Protection Act 1998 and Social Security Administration Act 1992.



**SCOTTISH PARLIAMENT PUBLIC AUDIT COMMITTEE**

**WEDNESDAY 27 JANUARY 2016**

**REPORT BY THE AUDITOR GENERAL FOR SCOTLAND**

**IMPLEMENTING THE SCOTLAND ACT 2012: AN UPDATE**

---

The report by the Auditor General was published on 10 December 2015. It provides an update on progress in implementing the financial measures in the Scotland Act 2012 since the Auditor General's previous report in December 2014.

Key messages from the report are:

- Revenue Scotland successfully implemented the two devolved taxes on time. The IT system and people needed to collect and manage the taxes were in place by the time the taxes were introduced. It cost £5.5 million to implement the devolved taxes, £1.2 million more than originally estimated, owing mainly to the need for additional staff in the set-up phase. Revenue Scotland is now refining its systems and processes, and is applying lessons learned from implementing the two devolved taxes in preparation for further devolved taxes.
- The Scottish Government and HMRC are working well together in preparing for the introduction of the Scottish rate of income tax in April 2016. The estimated cost range of setting up the Scottish rate of income tax has decreased by £10 million, to between £30 million and £35 million.
- The Scottish Government established its Fiscal Capability 2015 Programme to oversee the introduction of the new financial powers in the Scotland Act 2012. It has made good progress in modifying its existing arrangements to accommodate the new powers. Some arrangements to manage the powers beyond 2015/16 are still being developed, including longer-term arrangements for capital borrowing and accounting arrangements for the devolved taxes and capital borrowing. This is a reasonable approach, given that the fiscal framework is yet to be agreed with the UK Government. These are important elements of sound financial management that will need to be fully developed quickly following agreement of the framework.

At the time of reporting, the Scottish and UK Governments had yet to agree the terms of the block grant adjustment for the devolved taxes after 2015/16, which is highlighted in the report's key messages. Since then, they have agreed a

provisional one-year adjustment for 2016/17, but are still to agree a permanent block grant adjustment mechanism as part of the fiscal framework.

The Auditor General's report makes two recommendations to the Scottish Government about progressing its strategy for capital borrowing and arrangements for reporting on devolved tax receipts and capital borrowing.

Audit Scotland will consider progress in these areas and how the Scottish Government develops its financial management and reporting more generally to reflect increasing financial devolution as part of its ongoing work programme.

### Public Audit Committee Members Bulletin: 27 January 2016

The following table details new documents laid or published which fall within the general remit of the Committee. Except in relation to reports from the Auditor General for Scotland, there is no requirement for the Committee to consider these documents, however Standing Orders provide for the Committee to consider any such documents, if it so decides.

#### Forthcoming AGS reports

Title	Anticipated publication date
Changing models of health and social care <i>(j)</i>	March 2016
Maintaining Scotland's roads: a follow-up audit	June 2016
Audit of higher education in Scotland	June 2016
Supporting Scotland's economic growth: The role of the economic development agencies	Summer 2016

*(j) Joint AGS/Accounts Commission report*

#### Forthcoming Accounts Commission reports (for information)

Title	Anticipated publication date
Social work in Scotland	Summer 2016
An overview of local government in Scotland 2016	March 2016