



HM Revenue
& Customs

Jim Harra
HMRC Executive Committee

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1 March 2018

Dear Ms Marra

Thank you for your letter of 2 February asking for further information following evidence from Amyas Morse, Comptroller and Auditor General to your Committee in January.

Given the Scottish Government's proposals in the 2018-19 Draft Budget to alter the number of income tax bands, what scope is there for people in higher income groups to avoid paying higher rates of income tax?

The increase in the number of tax bands does not alter the range of ways in which Scottish taxpayers might seek to pay less tax than is correctly due. In broad terms, the greater the divergence between the UK and Scottish regimes, the greater the risk that taxpayers will not declare the correct status as a Scottish or UK taxpayer - the 1 percentage point differential in UK and Scottish rates may therefore create an incentive for some taxpayers to be non-compliant. HMRC's specific plans to address non-compliant activity in 2018/19 are currently being prepared and will be shared with the Scottish Government later in this year.

How could the Scottish Government's tax proposals alter the administrative costs of collecting taxes in Scotland?

We expect costs to be in line with the estimated range we have previously stated - a significant divergence between the rates and bands that apply in Scotland and those that apply to the rest of the UK may lead to an increase in costs of up to £5m. Work on the costings of the tax proposals contained in the budget is ongoing. I hope though it will be of use to you and your colleagues on the committee if I provide further detail on what this extra cost may relate to.

HMRC administrative costs may arise in a number of areas, particularly: changes to processes, contact from customers and compliance management. Taking these in turn, in the context of the changes to Scottish income tax agreed by the Scottish Parliament for 2018/19:

- Process changes – while the majority of HMRC systems have already been amended to accommodate Scottish income tax powers, the new rate bands agreed by the Scottish Parliament will entail additional changes to processes and therefore additional cost. An example of this would be the PAYE process where the new rate bands require changes to Scottish tax codes to ensure the correct tax continues to be collected from Scottish taxpayers.
- Customer contact – the divergence in the 2017/18 Higher Rate Thresholds had negligible impact on customer contact levels. The more significant changes agreed for 2018/19 may, however, cause contact from Scottish taxpayers to rise, although we would not expect this to be significant.
- Compliance – the rates and thresholds set for 2018/19 will need to be reflected in HMRC's compliance plans, and we are evaluating the form or extent of activity which may be required.

Does self-reporting on residency potentially enable people to undertake tax planning in a way that enables them to avoid paying a higher rate of income tax?

It is possible that customers could contact HMRC to change their address seeking to either claim not to be a Scottish taxpayer or indeed, as the tax is lower for some, claiming to be a Scottish taxpayer. There is a range of activity that HMRC undertakes and will continue to undertake to assess and address this risk – for example:

- As part of its administration of the tax system HMRC has access to and receives an extensive range of data, including address data, which is used to inform and direct compliance activity.
- We regularly compare our address data against third party address data to identify potential instances of inaccurate addresses – whether through deliberate non-compliant behaviour or mere customer oversight.
- For all individuals, whether in Self-Assessment or PAYE, HMRC will continue to monitor cross-border migration trends to identify possible evidence of customer behavioural response and also validate the accuracy of reported moves and the completeness of its address data.
- For Self-Assessment customers there is a box to check for the address status and this is monitored. It is an offence, potentially liable to criminal prosecution, to knowingly submit a tax return that is incorrect.
- HMRC has dedicated compliance resource focused on High Net Worth and Affluent individuals as well as employer compliance work focused on employed taxpayers.

Are your IT systems sufficiently flexible to cope with any further changes that might be made to Scottish income tax bands?

HMRC systems can accommodate the full extent of the income tax powers devolved to the Scottish Government.

HMRC has adapted its standard risk model to cover Scottish-specific tax risks. Do you plan to revisit the risk model to account for the proposed changes to the Scottish tax system?

The Service Level Agreement between HMRC and the Scottish Government for the operation of Scottish income tax commits us to an annual review of compliance.

HMRC will annually assess the risk of individuals seeking to avoid or evade paying the due amount of tax through misleading HMRC with incorrect address details and devise, in discussion with the Scottish Government, a plan of direct 'respond' compliance activity to address such behaviour.

In addition, HMRC will continue to assess risk and undertake compliance activity into the wider, generic tax affairs of Scottish taxpayers, in the same manner as it does now, as part of its administration of the UK income tax system as a whole. HMRC will apply risk based

compliance activity to the collection of Scottish income tax in the same way as is applied to the collection of income tax from taxpayers in the rest of the UK. The Scottish Government will not be recharged for this activity.

We understand that changing the law to require people to notify HMRC of a change in address would be a reserved issue. However, how could such an approach impact on HMRC's systems for collecting taxes and identifying Scottish taxpayers?

In making such a decision a number of factors would need to be considered, including balancing the fiscal benefits of such a mandatory regime against the administrative costs of its introduction and policing.

I hope this response is helpful.

A handwritten signature in black ink, appearing to read 'HARRA', written in a cursive style.

JIM HARRA
Deputy CEO and Second Permanent Secretary