

From: Michael Boughey
Deputy Director
Large Scale Platforms
DWP Group

To: Aidan Grisewood
Deputy Director
Fiscal Responsibility Division
Scottish Government
Area 3D North
Victoria Quay, Edinburgh
EH6 6QQ

Date: 1 December 2016

Scotland Acts 2012 and 2016

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

Dear Aidan

Thank you for your letter of 1 December which included an Annex with an agreed updated version of the arrangements we made last year, under which our organisations worked together to ensure that value for money was achieved as DWP made ready for the implementation of the Scottish Rate of Income Tax (SRIT) from April 2016.

The arrangements as referenced in the original Annex applied only to the implementation of SRIT, as introduced by the Scotland Act 2012. Therefore the attached Annex has been updated and amended, to ensure it covers not only the work necessary to complete the full implementation of SRIT including Tax Regime changes, but also the implementation of the further income tax powers devolved to the Scottish Parliament by the Scotland Act 2016. This will ensure that DWP systems can continue to recognise and process information on Scottish taxpayers in the same way that they currently recognise and process UK taxpayers.

I therefore formally provide agreement to the new version of the arrangements proposed in the Annex of this letter. It will continue to provide a transparent framework under which our organisations will work together to ensure that value for money is achieved as DWP make the changes necessary both to complete the implementation of SRIT, and also the further income tax powers contained in the Scotland Act 2016.

DWP will contribute to the annual update reports prepared by the UK Government for the UK Parliament as set out in the Scotland Acts of 2012 and 2016 respectively.

Yours sincerely

Michael Boughey

Telephone 01925 845587

Copy List:

Mayank Prakash

Richard Cornish

ANNEX TO THE EXCHANGE OF LETTERS BETWEEN THE SCOTTISH GOVERNMENT AND THE DEPARTMENT OF WORK AND PENSIONS DATED 01 December 2016

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

These arrangements update and replace those agreed in the Exchange of Letters between the Scottish Government (SG) and the Department of Work and Pensions (DWP) dated 19 November and 1 December 2015 for the Scottish rate of income tax (SRIT) as provided for by the Scotland Act 2012. Under the previous arrangements, DWP made the changes necessary to allow its systems and processes to recognise SRIT when it was introduced on 6 April 2016. This updated version sets out the continuing arrangements for the work that DWP require to do to complete its implementation of SRIT and the additional work now required to implement the Scottish income tax powers provided for by the Scotland Act 2016.

Introduction

1. The Scottish rate of income tax (SRIT), provided for by the Scotland Act 2012, was set for the first time for tax year 2016/17 by a Scottish Rate Resolution passed by the Scottish Parliament on the 11 February 2016. The Scotland Act 2016 provides for the further devolution of powers for the Scottish Parliament to set all income tax rates and bands. The Fiscal Framework agreed between the UK and Scottish Governments sets out that these powers will be available to the Scottish Parliament from 2017/18. SRIT and Scottish Income Tax are not fully devolved taxes. They form part of the UK income tax system and are 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 and, subsequently, Scottish income tax has consequential impacts for the Department of Work and Pensions (DWP). DWP requires, therefore, to continue to ensure that its systems and processes can accommodate SRIT and also to ensure that they are ready to accommodate Scottish income tax from April 2017.
3. From tax year 2017/18 Scottish Ministers will be responsible for proposing Scottish income tax rates and bands 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 both SRIT and Scottish income tax 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 and Scottish income tax. The arrangements in place between the Scottish Government (SG) and HMRC for setting up and operating SRIT and Scottish income tax 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') gave the Scottish Parliament the power to set a Scottish rate of income tax (SRIT) to apply to Scottish taxpayers. SRIT commenced on the 6 April 2016 for tax year 2016/17. The Scottish Parliament set a rate of 10p for 2016/17 which is added to each of the main UK income tax rates after ten pence in the pound is been deducted. The 2012 Act repeals the provisions for the Scottish Variable Rate (SVR) with effect from the date SRIT began. It is administered by HMRC as part of the UK-wide income tax system and applied to non-savings and non-dividend income.
5. SRIT will cease to operate at the point at which the Scottish income tax powers under the Scotland Act 2016 are applied from tax year 2017/18 as provided for in the Fiscal Framework agreement

Scottish income tax

6. The Scotland Act 1998 as amended by the Scotland Act 2016 gives the Scottish Parliament the power to set all income tax rates and bands. The Personal Allowance will remain reserved and as such continue to be set by the UK Government. As with SRIT, Scottish income tax will be administered by HMRC as part of the UK wide tax system and applied to all non-savings, non-dividend income. Scottish income tax rates and bands will be set each year through a resolution passed by the Scottish Parliament on the basis of a proposal made by Scottish Ministers. From 2017/18 all income tax receipts on non-savings, non-dividend income will accrue to the Scottish Government.

Purpose of this annex

7. This Annex sets out the arrangements agreed between the SG and DWP for ensuring DWP administered taxable benefits and associated IT systems continue to recognise and interact with SRIT and from 2017/18 onwards Scottish income tax 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 and Scottish income tax 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.
8. 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;
 - The agreement between the Scottish Government and the United Kingdom Government on the Scottish Government's fiscal framework (the Fiscal Framework);
 - 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

9. This Annex and the arrangements set out within came into effect on the date it was accepted by DWP and SG in their Exchange of Letters of 01 December 2016. It updates and replaces the previous Annex and arrangements set out in the Exchange of Letters of 19 November and 1 December 2015 between DWP and SG. It has no expiry date but will cease to have effect if Scottish income tax 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

10. 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 both the completion of the implementation of SRIT and the timely introduction and implementation of Scottish income tax. 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.

11. 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 Digital Workplace and Technology Platforms.

12. 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), or any changes affecting the Part 3 provisions, 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. DWP will contribute to the UK report. The Fiscal Framework agreement reiterates that in line with the Section 33 provisions of the 2012 Act that both Governments will also separately prepare and publish a similar type of report covering functions and duties devolved under Scotland Act 2016. These reports are also to be provided to the UK and Scottish Parliaments and DWP will contribute to sections on Scottish income tax in the UK reports.

Roles and responsibilities of DWP and SG

13. 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 and the Scottish income tax provisions in Scotland Act 2016. The process will take an inter-governmental approach to quality assurance, reviewing progress against milestones and ensuring value for money.

14. The SG will be represented within DWP's internal governance arrangements for implementing SRIT and introduction of Scottish income tax at both project and programme level. The SG may also request that DWP commission an external assurance review at the SG's expense.

15. 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.
16. DWP will develop and test the IT and administrative systems for compliance with Scottish income Tax in consultation with HMRC and the SG.
17. DWP will invoice SG for agreed items of expenditure as set out in paragraph 35 below.
18. SG will make payment to DWP for amounts invoiced for agreed items of expenditure as set out in paragraph 33 below.
19. DWP will have no role in relation to determining an individual's tax liability nor for the publicity of SRIT or Scottish income tax other than ensuring, where appropriate, customer communications reflect the Scottish rate and - from April 2017 - Scottish rates and bands.

DWP IT and Administrative impacts of SRIT and Scottish Income Tax Implementation

20. DWP will remain responsible for ensuring that the correct IT and administrative systems are in place to support SRIT and the timely introduction of Scottish income tax for tax year 2017/18.
21. DWP will keep the SG informed of, and will consult with the SG on plans, timetables, estimate 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.
22. DWP will upgrade and test all IT systems for all areas of DWP business that will be impacted by SRIT and Scottish income tax. This will be done through contracted IT suppliers and in accordance with its normal IT development practice.
23. 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.
24. The SG will have an opportunity to review plans for IT testing and the results of such tests.
25. DWP will develop non IT systems for all areas of DWP business that will be impacted by SRIT and Scottish income tax. This will be done in accordance with normal DWP practice.
26. A breakdown of the expected costs and activities for both IT system and non IT system changes after will be shared with the SG before such costs are incurred.
27. 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

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

Funding

29. DWP will undertake work to ensure the current social security system recognises Scottish taxpayers and that its respective IT systems interface with HMRC Scottish income tax systems/platforms for SRIT and Scottish income tax purposes. In undertaking this work, DWP will review changes made in 2015-16 for the implementation of SRIT, to extract value for money, where possible, from this earlier investment.

30. 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.

31. The SG will meet costs which it is satisfied have wholly and necessarily been incurred as a result of the introduction of SRIT or Scottish income tax.

32. Once the changes are made to DWP's IT systems to recognise SRIT as introduced in the Scotland Act 2012 and Scottish income tax as introduced by Scotland Act 2016, there will be no additional annual expenditure to maintain these changes.

33. 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 relating to staff guidance and customer forms and letters required as a result of the introduction of SRIT or Scottish income tax.
- 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 or Scottish income tax 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 or Scottish income tax.
- Supplier issues covered under DWP contract warranties.
- The SG should not pay for any consequence of cost incurred by the DWP business invoking manual processes due to supplier issues. This could for example be additional changes to Letters and Guidance.
- Costs involving changes to the IT systems where aspects of SRIT or Scottish income tax cannot reasonably be costed separately.

34. Where a dispute arises over a payment in relation to matters set out above it will be dealt with under the dispute resolution process as set out in paragraph 37.

Invoicing

35. 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.

36. 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

37. Where a dispute arises over a payment in relation to matters set out in this above, it will be discussed at the DWP Digital Workplace and Technology Platform's Senior Leadership Team 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 Digital Workplace & Technology Platforms or successor Director. If agreement is not reached between these Directors, then the dispute resolution section of the Fiscal Framework agreement will have effect.

Information sharing

38. 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 and paragraph 107 of the Fiscal Framework agreement. When available the Scottish Government will also provide DWP with information with regard to notifications of tax rates and rate changes.

Limitations

39. DWP operates within the legal constraints of customer confidentiality as set out in the Data Protection Act 1998 and Social Security Administration Act 1992.