Clarifying the Scope of the Scottish Rate of Income Tax
Consultation on draft legislation – HM Revenue & Customs (HMRC) Technical Note
Response from the Low Incomes Tax Reform Group (LITRG)

1 Introduction

1.1 We welcome the opportunity to comment on the above Technical Note and draft legislation, issued in December 2014 by HMRC.

1.2 This Technical Note, together with the previous Technical Note issued in May 2012, appears to have dealt with all the current issues; inevitably, however, further issues will arise, in particular when the Scottish Rate of Income Tax (SRIT) comes into force in April 2016. It is essential that HMRC have a mechanism in place to enable issues to be raised, to solve them and to issue guidance to stakeholders swiftly. We would like to receive reassurance from HMRC that they intend to put in place such a mechanism. This should also include appropriate liaison with Revenue Scotland and we would like to see HMRC retain a policy team in respect of the SRIT, to manage its continuing evolution.

1.3 We make some comments on the Technical Note and then consider the draft legislation. We have not included an Executive Summary, therefore.

2 About Us

2.1 The Low Incomes Tax Reform Group (LITRG) is an initiative of the Chartered Institute of Taxation (CIOT) to give a voice to the unrepresented. Since 1998 LITRG has been working to improve the policy and processes of the tax, tax credits and associated welfare systems for the benefit of those on low incomes. Everything we do is aimed at improving the tax and benefits experience of low income workers, pensioners, migrants, students, disabled people and carers.

2.2 LITRG works extensively with HM Revenue & Customs (HMRC) and other government departments, commenting on proposals and putting forward our own ideas for improving the system. Too often the tax and related welfare laws and administrative systems are not designed with the low-income user in mind and this often makes life difficult for those we try to help.

2.3 The CIOT is a charity and the leading professional body in the United Kingdom concerned solely with taxation. The CIOT's primary purpose is to promote education and study of the administration and practice of taxation. One of the key aims is to achieve a better, more efficient, tax system for all affected by it – taxpayers, advisers and the authorities.

3 Technical Note

3.1 *Real Estate Investment Trusts (REITs), Property Authorised Investment Funds (PAIFs) and certain types of annual payments*

3.1.1 We have nothing to add to the response submitted by our CIOT colleagues in respect of REITs, PAIFs and certain types of annual payments, except for the point below concerning guidance.

3.1.2 There will need to be clear guidance for Scottish taxpayers that income of these types is subject to the Scottish rate of income tax, as it is not savings or dividend income, but non-savings income. In addition, it will need to be made clear that their final income tax liability may differ from the tax deducted at source – this is particularly important for basic rate taxpayers, who might expect the deductions at source to be their final liability in relation to that income.[1]

3.2 *Payments from Interest in Possession Trusts and deceased estates*

3.2.1 The original proposal in respect of such payments was for deductions by trustees and personal representatives to continue to be made at the UK basic rate and for the income to be taxed at UK rates of income tax in the hands of a Scottish taxpayer beneficiary.[2]

3.2.2 We note the decision to amend the proposal such that income from interest in possession trusts and deceased estates will be taxed at Scottish rates of income tax when arising to

[1] If the SRIT does not diverge from the UK rate, this situation will not arise (although the taxpayer's final overall tax liability may differ for other reasons). Where the SRIT and UK rate do diverge, such clarification will be essential, particularly for the unrepresented taxpayer.

[2] Clarifying the Scope of the Scottish Rate of Income Tax, HM Revenue & Customs Technical Note, May 2012.

Scottish taxpayer beneficiaries.[3] This is likely to make completion of a self assessment tax return simpler from a mechanical point of view than the original proposal. It is not clear from the Technical Note whether deductions by trustees and personal representatives will continue to be made at the UK basic rate. We assume that this will be the case, however.

3.2.3 We do have a concern that this change will mean that some basic rate taxpayers will be forced into the self assessment system, or will face complex adjustments to their PAYE code, should the UK and Scottish rates diverge.[4] If the Scottish rate is higher than the UK rate, the unrepresented Scottish taxpayer might face an unexpected and unwelcome bill. This is a particular worry for individuals who are unrepresented and are on a low income. In addition, it will undoubtedly prove administratively burdensome to HMRC – unrepresented taxpayers are unlikely to understand the position, and yet the onus will be on them to notify HMRC that they need to enter the self assessment system to declare the income on which UK tax has already been deducted so that they can pay the extra Scottish tax. In addition, the cost of issuing a self assessment tax return to affected Scottish rate taxpayers to collect the extra few pence will probably be disproportionate to the amount of revenue collected.

3.2.4 In view of these concerns, clear guidance will be essential, particularly for Scottish taxpayer beneficiaries, but also for trustees and personal representatives, who are likely to receive queries from beneficiaries on this topic. It will also be necessary to ensure communications reach those affected.

3.2.5 A possible solution might be to have a franking system whereby any such non-savings income that has suffered deduction of tax at the UK rate is deemed already to have been fully taxed at the Scottish rate. This would mean that the basic rate Scottish taxpayer 'loses out' if the Scottish rate is lower than the UK rate, but at least they will not suffer the inconvenience of being pursued for more tax if the Scottish rate is higher, whether through PAYE or under self assessment. This would also save a lot of work for HMRC for what, in most cases, would be relatively small amounts of tax.

3.3 ***PAYE Amendments: information for Scottish taxpayers***

3.3.1 We welcome the confirmation in the Technical Note that details of the Scottish rate will be shown separately in HMRC's Tax Calculator, annual Tax Summary and the annual statement of income tax liability (P60). It is essential that Scottish taxpayers receive the information that will enable them to calculate and understand their income tax liability, and also to make any appropriate claims for tax relief. Many Scottish taxpayers will probably expect to see information concerning the Scottish rate on their payslips, and the provision of information

[3] It is not clear from the Technical Note, but we have assumed in making our comment that the Scottish rates will only apply to non-savings income, such as property income, from interest in possession trusts and deceased estates in the hands of Scottish taxpayer beneficiaries.

[4] These issues were identified in the original Technical Note: para. 48 ff., Clarifying the Scope of the Scottish Rate of Income Tax, HM Revenue & Customs Technical Note, May 2012.

about the Scottish rate paid will be an important part of the communication around the SRIT.

3.3.2 We note that not all employees receive a form P60, for example if their employment has ceased prior to the end of the tax year on 5 April. For such employees, we think it would be appropriate for information on the Scottish rate to be included on form P45. In addition, when an employee dies, it is likely that either a P45 or payslip will be issued, but not a P60. If information on the Scottish rate is not readily available it could delay wrapping up the estate, causing stress to the bereaved. In the interests of transparency and provision of relevant information to all taxpayers, we therefore recommend that information on the Scottish rate be included on form P45 (and the new leaver statement in due course).

3.3.3 Some employees, engaged on a more casual basis, may receive neither a form P60 nor a form P45 – they may simply receive a payslip on the odd occasion when they have carried out work for the employer. Such employees would be reliant on the Tax Calculator and annual Tax Summary to demonstrate their position, and these sources of information may either not be acceptable or adequate for some purposes.

3.3.4 Ideally, we would like to see information on the Scottish rate included on payslips. It should be possible to have the details on monthly/weekly payslips, as the information will have been calculated for the purposes of PAYE, and will presumably show on a feed for PAYE Real Time Information (RTI) purposes.

3.3.5 We recognise, however, the additional burdens that employers and pension providers would face if there were a requirement to provide information on the Scottish rate in individual payslips. In particular, we understand that such a requirement would mean that payslips need to be redesigned – this process takes a lot of time, possibly several months. We do not wish to see a sudden, last-minute decision to require Scottish rate information to be shown on payslips, therefore. If a decision is made that the information should be included on payslips, an appropriate timescale should be allowed for employers, pension providers and payroll software houses to act on this – and they should be consulted as to what that is. In addition, the cost of redesigning payslips, for smaller employers in particular, should be taken into account in coming to any decision to go down this route.

3.3.6 We think it is important that there is transparent and full provision of information to taxpayers, so that they can understand their tax liability and tax position. In light of this, we recommend that there should also be a requirement to show the Scottish rate separately on form P45 and the payslip (subject to our comments above), in addition to the requirements proposed in the Technical Note.

4 Draft Legislation

4.1 *The Scottish Rate of Income Tax (Consequential Amendments) Order 2015*

4.1.1 We have no comments.

4.2 *The Income Tax (Pay As You Earn) (Amendment) Regulations 2015*

4.2.1 We have no comments, subject to our points at paragraph 3.3.1 ff. above.

LITRG
27 January 2015