Chartered Institute of Taxation
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Low Incomes Tax Reform Group
A voice for the unrepresented
20th Anniversary

Clarifying the Scope of the Welsh Rates of Income Tax

Consultation on draft legislation- HM Revenue & Customs (HMRC) Technical Note
Joint Response from the Low Incomes Tax Reform Group (LITRG) and Chartered Institute of Taxation (CIOT)

1. Introduction

1.1. We welcome the opportunity to comment on the above Technical Note and draft legislation regarding the Welsh Rates of Income Tax (WRIT), issued in October 2018 by HMRC, although we note there is a very short response period of less than two weeks, which is unhelpful.

1.2. This Technical Note appears to have dealt with concerns raised previously[1] in relation to the introduction of the Scottish Rate of Income Tax (SRIT) which are relevant to the partial devolution of income tax to Wales from April 2019. HMRC should use the experience they have gained, and continue to acquire, from the introduction and application of the SRIT and Scottish Income Tax to ensure that the introduction of the WRIT is as smooth as possible with limited problems arising.

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[1] See documents relating to the Scottish Rate of Income Tax on GOV.UK

2012:http://webarchive.nationalarchives.gov.uk/20140603114240/http:/www.hmrc.gov.uk/news/technote-scot-taxrate.pdf

2014: https://www.gov.uk/government/publications/clarifying-the-scope-of-the-scottish-rate-of-income-tax-technical-note

2016: https://www.gov.uk/government/publications/clarifying-the-scope-of-scottish-income-tax-powers

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1.3. However, inevitably, further issues will arise when the WRIT are introduced and it is essential that HMRC have mechanisms in place to enable issues to be raised, to solve them and to swiftly issue guidance to stakeholders, including the Welsh Revenue Authority (WRA). We would like to receive reassurance from HMRC that they intend to put in place such mechanisms and confirmation that HMRC will retain a policy team in respect of the WRIT, to manage its continuing evolution.

1.4. We make some comments on the Technical Note and then consider the draft legislation. Some of our comments may not be relevant, or as urgent now, while the WRIT are planned to be the same as the UK tax rates, but will become more acute if the WRIT diverge from the UK tax rates.

2. About Us

2.1. The Low Incomes Tax Reform Group (LITRG) is an initiative of the Chartered Institute of Taxation 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 Chartered Institute of Taxation (CIOT) is the leading professional body in the United Kingdom concerned solely with taxation. The CIOT is an educational charity, promoting education and study of the administration and practice of taxation. One of our key aims is to work for a better, more efficient, tax system for all affected by it – taxpayers, their advisers and the authorities. The CIOT's work covers all aspects of taxation, including direct and indirect taxes and duties.

2.4. The CIOT draws on our members' experience in private practice, commerce and industry, government and academia to improve tax administration and propose and explain how tax policy objectives can most effectively be achieved. We also link to, and draw on, similar leading professional tax bodies in other countries. The CIOT's comments and recommendations on tax issues are made in line with our charitable objectives: we are politically neutral in our work.

2.5. The CIOT's 18,000 members have the practising title of 'Chartered Tax Adviser' and the designatory letters 'CTA', to represent the leading tax.

3. Technical Note

3.1. ***General comments on guidance and communication***

3.1.1 Taxpayers must understand their tax position and whether or not they are Welsh taxpayers. There must be comprehensive guidance available for taxpayers; this guidance must be accessible and it must be included on the GOV.UK website. We also think it should either be included on or accessible through the WRA website, and it should be linked to the Welsh government website. The recently issued Welsh taxpayer technical guidance should be accessible via the WRA website. Although the WRA will not be administrating the WRIT, it should be anticipated that a number of taxpayers with questions or concerns about the WRIT will contact the WRA in preference to HMRC. We understand from our work with Revenue Scotland and the Scottish Government's Fiscal Unit that both of these organisations have received queries from Scottish taxpayers about Scottish Income Tax and the SRIT.

3.1.2. This guidance should cover the appeal process on the income tax status of a taxpayer. For many taxpayers their tax residence status will be easily identified. However, undoubtedly there will be some taxpayers where there may be additional complexities and potential disagreement regarding whether or not they are Welsh taxpayers. For example, we understand that there are a small number of properties which straddle the Welsh-English border and that HMRC are currently considering the tax status of the occupants of these properties.[2]

3.1.3. There needs to be clear guidance, preferably with examples, to assist Welsh taxpayers with understanding their tax position and tax responsibilities when there are more complex tax situations. Examples include claiming tax relief for charitable donations if a higher rate or additional rate Welsh taxpayer, trust income received by Welsh beneficiaries which will be subject to the WRIT, understanding the tax position where a personal service company (PSC) is used (that is, when IR35 applies), and understanding the order of set-off of allowances against different sources of income.

3.1.4. The guidance must also be included in the tax return notes provided to assist when completing self assessment tax returns and the 'help' functions when using the HMRC online system to prepare tax returns. It would be helpful to have confirmation that the HMRC online software, which many unrepresented taxpayers rely on and use, will be able to work correctly with these changes, especially following the problems when the dividend allowance and personal savings allowance were introduced. We also understand that there are a few filing exclusions for the 2017/18 tax year that relate to Scottish taxpayers specifically. It would be helpful to know that HMRC intend to resolve these for the 2018/19 tax year for Scottish Income Tax, and in respect of the WRIT for the 2019/20 tax year. HMRC should be able to produce online self assessment return and calculation processes that match the legislation. If they cannot then it must bring into question whether the tax system is too complicated to be understandable.

3.1.5. Guidance must be available for employers to understand what these changes mean and how to implement them. Many small businesses will not have a separate payroll department or

[2] We understand the number of such properties is approximately 30.

be able to afford professional support. However, their employees will often expect their employer to answer questions regarding individual payslips and explain deductions made through the PAYE system. Although there has been communication regarding the introduction of the 'C' PAYE code, there needs to be step-by-step guidance available to assist these employers to work alongside their employees to ensure their individual tax position is correct. For example, guidance is needed to explain the importance of having an accurate address for each employee, what an employee should do if they do not understand or disagree with their tax residence status, what happens if an employee moves from Wales to England (or vice versa) during a tax year and an understanding of how the Construction Industry Scheme and IR35 will work.

3.1.6. Effective publicity and communications will be key to ensuring the smooth introduction and operation of the WRIT. Publicity for the introduction of the WRIT has, in our view, yet to start in earnest. In addition, it is starting from a low base of understanding; a recent survey[3] looking at the experience of Scottish taxpayers amply demonstrates the poor awareness and understanding of the Scottish Income Tax two years after it was introduced, which shows that the task of effective communication should not be underestimated. There are also misconceptions that need to be overcome in a relatively short period of time when there are other important financial announcements which may compete for taxpayers' attentions such as plans for Brexit.

3.1.7. Part of publicising the WRIT involves producing clear, accurate and comprehensive guidance for different groups which provides answers to the key questions that individuals will have. In particular, it is important that the guidance includes details of taxpayers' responsibilities, such as what they should do when they receive a notification letter or coding notice indicating that they are a Welsh taxpayer, or what they should do if they think they are a Welsh taxpayer and do not receive such a notice. We have a concern about the lack of awareness of which tax authority is responsible for the WRIT. We believe that it is essential that the publicity surrounding the WRIT makes it abundantly clear that the WRIT will be administered and collected by HMRC.

3.2. Pensions Tax Relief

3.2.1. We look forward to receiving confirmation from HMRC regarding the timetable on their work with relevant pension providers to identify and differentiate Welsh taxpayers so that the correct Relief at Source claims are made.

3.2.2. The technical note explains Welsh taxpayers will be identified by the January before the tax year starts and this information will be passed onto the pension providers. It would be useful for guidance to be made available to both pension providers and their pension recipients about what to do if their tax residence status changes. For example, any mid-year changes

[3] See the Scottish Taxes Policy Forum paper: https://www.tax.org.uk/media-centre/press-releases/press-release-new-poll-discovers-more-four-fifths-scots-lack

which will affect whether or not a pension recipient is a Welsh taxpayer, will potentially have to be dealt with at the end of the tax year either through self assessment or the PAYE system.

3.3. ***Trusts***

3.3.1. We understand that changing the tax resident status for trust and estates would increase complexity in the trust tax system. However, it must be made clear to Welsh taxpayers who are trust beneficiaries that their income from the trust will be subject to the WRIT. This could cause confusion as although the income may have been classed as savings income in the trust, it will become non-savings income for the beneficiaries. Clear guidance with the use of examples should be provided to help Welsh taxpayers understand their tax position.

3.4. ***Other income tax issues***

3.4.1. It is important not to consider income tax in isolation; in particular, interactions with tax credits and benefits can have a significant impact on the living standards of low income individuals. For example, a reduction in the rate of income tax may not be the most effective way of helping people on low incomes because of the interaction with means-tested benefits that are based on net income, as they will not benefit from their increased net earnings level to the same extent as someone not in receipt of a means-tested benefit. Universal credit, for example, will be reduced if after-tax income increases. Indeed, when considered alongside additional 'passported' benefits, such as free school meals, the combination of increased net pay and reduced means-tested benefits could lift an individual outside the entitlement threshold which passports them to these additional aspects of support.

3.4.2. Other effects of changes to the tax system must also be considered. For example, the landlords finance cost restriction will include the WRIT when being calculated, and while the tax credits regulations have been amended to ensure that tax credit claimants will not be affected by this restriction, HMRC must consider and provide guidance on how this restriction may affect child maintenance payments, student loans and the High Income Child Benefit Charge.

3.5. ***Real Estate Investment Trusts and Property Authorised Investment Funds***

3.5.1. There will need to be clear guidance for Welsh taxpayers explaining that income of these types is subject to the WRIT, 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. If the WRIT do 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 WRIT and UK rate do diverge, such clarification will be essential, particularly for the unrepresented taxpayer.

3.5.2. Guidance should be provided about whether these Welsh taxpayers will need to complete a self assessment tax return if they do not already do so or whether any additional income tax due can be paid through an adjustment to their PAYE code or through a simple assessment.

3.6. **PAYE amendments**

3.6.1. We welcome the confirmation in the Technical Note that details of the Welsh rate will be shown separately in HMRC's Tax Calculator and annual Tax Summary. It is essential that Welsh 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.

3.6.2. Ideally, we would like to see information about the Welsh rate included on both the Form P60 (the form provided to employees showing their gross salary and income tax paid during the tax year) and also on payslips[4]. This will assist with Welsh taxpayers' understanding of their tax deductions and the provision of information about the Welsh rate paid will be an important part of the communication around the WRIT. 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.

3.6.3. We recognise, however, the additional burdens that employers and pension providers would face if there were a requirement to provide information on the Welsh rate on individual payslips. In particular, we understand that such a requirement would mean that payslips need to be redesigned - this process takes a significant period of time. 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.

3.6.4. We believe 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 Welsh rate separately on form P45 and the payslip (subject to our comments above), in addition to the requirements proposed in the Technical Note.

4 The Devolved Income Tax Rates (Consequential Amendments) Order 2018

4.1 We have no comments.

[4] Currently there are no requirements to show Scottish Income Tax separately on payslips, or forms P45 and P60. Our comments at paragraphs 3.6.2, 3.6.3 and 3.6.4 should also apply to Scottish Income Tax.

5 The Income Tax (Pay As You Earn) (Amendment No. 2) Regulations 2018

5.1 We have no comments.

LITRG and CIOT
5 November 2018