



National Audit Office



# Administration of Welsh rates of income tax 2020-21

HM Revenue & Customs

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**REPORT**

**by the Comptroller  
and Auditor General**

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**SESSION 2021-22  
21 JANUARY 2022  
HC 1014**

## Key facts

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**1.3m**

Welsh taxpayers in 2019-20

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**£2,041m**

Welsh rates of income tax  
revenue in 2019-20

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**£2,110m**

HM Revenue & Customs'  
estimate of the Welsh rates of  
income tax revenue in 2020-21

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**£0.7 million** Costs of administering Welsh income tax in 2020-21

# Summary

## Introduction

### Welsh income tax

**1** The Wales Act 2016 gave the Senedd full power to determine the rates (excluding the personal allowance) paid by Welsh taxpayers on all non-savings, non-dividend income, from 6 April 2017. The Welsh Government receives all income tax revenue generated from non-savings, non-dividend income under Welsh income tax policy.

**2** From April 2019, the United Kingdom (UK) basic, higher and additional income tax rates were reduced by 10 percentage points and the Welsh Parliament had the power to apply Welsh rates. The sum of the reduced UK rates and the new Welsh rates determines the overall rate of tax paid by Welsh taxpayers (**Figure 1** overleaf). For 2020-21, the Welsh Parliament set the Welsh rates of income tax at 10% across all bands, effectively matching the UK rates at 20% (basic rate), 40% (higher rate) and 45% (additional rate).

### Roles and responsibilities

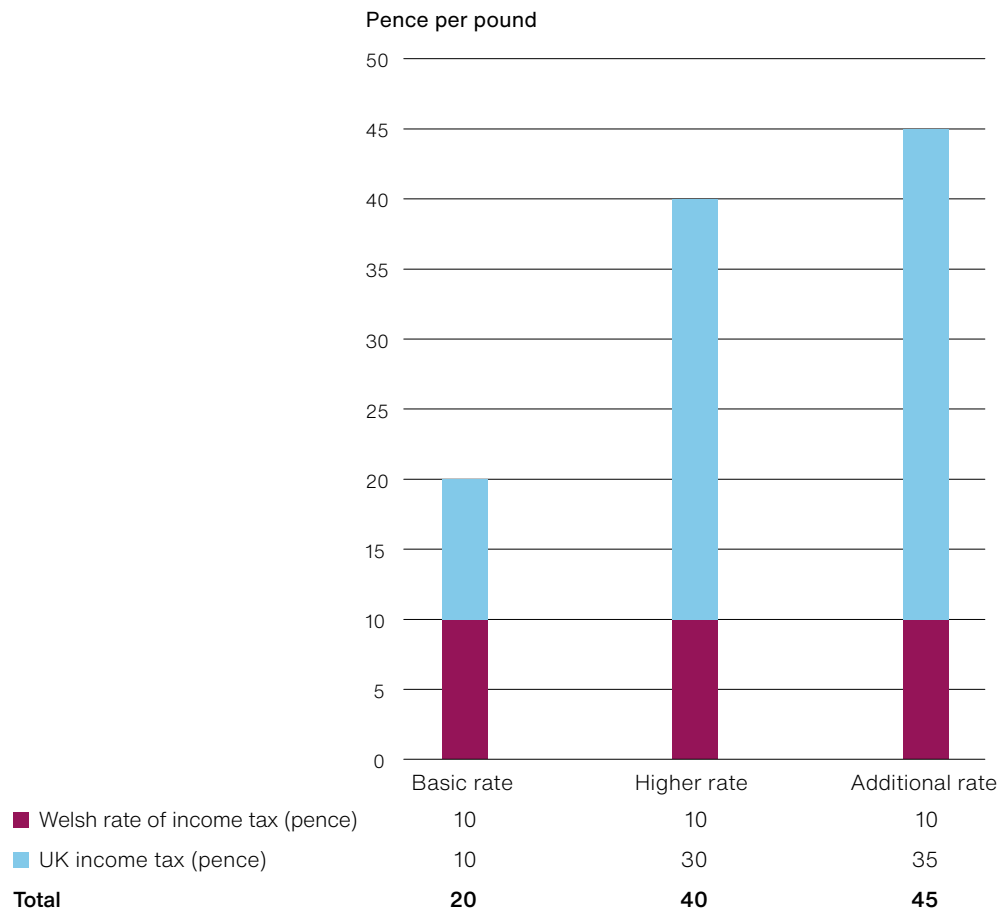
**3** HM Revenue & Customs (HMRC) administers and collects Welsh income tax as part of the UK tax system. HMRC identifies taxpayers living in Wales by applying a 'flag' in its systems that indicates they are subject to Welsh income tax rates. HM Treasury is responsible for paying Welsh income tax to the Welsh Government.

**4** Following the end of each tax year, HMRC produces a provisional estimate of Welsh income tax revenue for that year. The final outturn is calculated the following year once HMRC receives further information from taxpayers and employers. This report covers the final outturn for 2019-20 and the provisional outturn for 2020-21. HMRC expects to publish the outturn for 2020-21 in its 2021-22 Annual Report and Accounts.

**Figure 1**

Welsh rates of income tax for 2020-21

The UK rates of income tax are effectively reduced by 10p per £1 and replaced with the Welsh rates of income tax



**Notes**

- 1 For each tax band (basic, higher and additional), the UK government reduces the amount of tax it will collect by 10 pence per £1 and the Welsh Government sets the Welsh rate of income tax to be added to the UK rates of tax.
- 2 For 2020-21, the Welsh Government set each Welsh rate of income tax at 10 pence, meaning that Welsh taxpayers pay an amount of tax equivalent to the UK rate for each tax band.

Source: The Welsh Government

**5** The Government of Wales Act 2006, as amended by the Wales Act 2014, requires the Comptroller and Auditor General (C&AG) to prepare a report for each financial year on:

- the adequacy of any of HMRC's rules and procedures put in place, in consequence of the Welsh 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 that is attributable to a Welsh rate resolution; and
- the accuracy and fairness of amounts reimbursed to HMRC as administrative expenses.

**6** This report considers:

- HMRC's calculation of the 2019-20 income tax revenue for Wales, the 'outturn', and assurance on the correctness of amounts brought to account (Part One);
- HMRC's estimate of the 2020-21 income tax revenue for Wales and our view on the estimate methodology (Part One);
- key controls operated by HMRC to assess and collect income tax (Part Two);
- HMRC's approach to assessing and mitigating the risk of non-compliance with Welsh tax requirements (Part Two); and
- the cost of administering Welsh income tax. We provide assurance on the accuracy and fairness of these amounts in the context of costs incurred by HMRC (Part Three).

**7** Appendix One sets out our audit approach and methodology.

## **Key findings**

Welsh income tax 2019-20 final outturn and 2020-21 estimate

**8** **HMRC calculated the final outturn for 2019-20 as £2,041 million, representing amounts collected under Welsh income tax policy.** HMRC's estimate of Wales's 2019-20 income tax revenue, published in September 2020, was £2,008 million, meaning the actual outturn was £33 million higher than HMRC had originally estimated. We examined the methodology to calculate the actual outturn, which necessarily includes remaining areas of estimation. In these areas, we evaluated the basis of HMRC's estimate including relevant assumptions and available data. Based on that audit work, we concluded the Welsh income tax revenue outturn for 2019-20 is fairly stated (paragraphs 1.2 to 1.16).

**9 HMRC has estimated Welsh income tax revenue for 2020-21 as £2,110 million.**

This represents an increase of £69 million (3.4%) against the 2019-20 outturn. Despite the impact of public health restrictions arising from COVID-19 on the economy and HMRC compliance activity, income tax revenues remained stable because growth in wages and salaries was stronger than anticipated. HMRC expects to calculate the finalised 2020-21 income tax outturn attributable to Wales in 2022. The estimate HMRC produces is solely for financial reporting purposes in its annual accounts and does not affect the amount of revenue ultimately received by the Welsh Government (paragraphs 1.17 to 1.21).

**10 The impact of COVID-19 on both the economy and individual taxpayers increases the level of uncertainty in HMRC's estimate of Welsh income tax revenue in 2020-21.**

HMRC identified the collectability of tax revenues as the key source of uncertainty and took account of this as part of its normal calibration to outturn adjustment. We consider the approach adopted by HMRC to estimating the impact of COVID-19 on Welsh income tax revenue in 2020-21 to be reasonable (paragraph 1.22).

Administration of Welsh rates of income tax

**11 HMRC has adequate rules and procedures in place to ensure the proper assessment and collection of Welsh income tax and those rules are being complied with.** Our work on Welsh income tax matters builds on our wider assessment of HMRC's rules and procedures, completed as part of our annual audit of HMRC. As part of that audit, we concluded that HMRC framed adequate regulations and procedures to secure an effective check on the assessment, collection and proper allocation of revenue, and that they are being duly carried out (paragraph 2.2 to 2.13).

**12 Maintaining an accurate and complete record of the addresses of Welsh taxpayers to correctly determine residency remains the key challenge in administering the system.** HMRC relies on taxpayers notifying it of a change of address, although there is no legal requirement for them to do so. We found that there had been an increase in the number of missing Welsh postcodes identified by HMRC's address cleansing work, with 30,473 identified compared to 17,371 when we last reported. This continues to represent a small proportion (around 2%) of the overall taxpayer population with HMRC having investigated and updated all identified cases where individuals were either employed or receiving a pension (paragraph 2.14 to 2.24).

**13 HMRC continues to assess the risk of non-compliance in relation to Welsh income tax as low because there is no divergence between Welsh tax rates and the rest of the UK.** In 2020-21, HMRC produced a Welsh Strategic Picture of Risk (SPR). It considers the main areas of risk to Welsh income tax to be the same as those compliance risks which are tackled at the whole-of-UK level. There are no risks identified in the Welsh SPR specific to Wales (paragraphs 2.25 to 2.26).

**14 HMRC calculated a compliance yield of £100 million relating to Wales for 2019-20, the most recent data available.** HMRC measures the effectiveness of its enforcement and compliance activities through compliance yield: its estimate of the additional revenues that HMRC considers it has generated, and the revenue losses it has prevented. HMRC also estimates the Welsh share of net losses was £280 million. These figures are calculated based on a proportion of the UK figure, rather than using Welsh-specific data to quantify the risks. HMRC does not consider geographical variations in the level of compliance risk, or the relative success of compliance activity in Wales compared with the rest of the UK (paragraphs 2.26 to 2.27).

**15 HMRC has limited performance data available about its compliance activities in Wales.** Unlike its income tax system which flags residents as Welsh, HMRC's compliance system cannot readily identify people living in Wales. HMRC therefore cannot easily track and monitor compliance activity in Wales and this affects its ability to collect performance data about the extent of Welsh non-compliance (paragraph 2.29).

**16 COVID-19 has continued to have an impact on HMRC's compliance and debt management activities.** Across the UK, there were 29% fewer civil compliance cases opened and 26% fewer cases closed in 2020-21 than in 2019-20, which reduces the level of tax receipts that HMRC has collected through its compliance activities. Our recent report *Managing tax debt through the pandemic* found that the debt balance for income tax across the UK increased from £11 billion at the end of 2019-20 to more than £16 billion at the end of 2020-21. An analysis of income tax debt attributable to Wales is not currently available (paragraph 2.30 to 2.33).

## Costs

**17 In 2020-21 HMRC incurred and recharged £0.7 million of costs to the Welsh Government for the cost of implementing and administering Welsh income tax.**

We examined HMRC's method for estimating the costs of implementing, collecting and administering Welsh income tax for the year ended 31 March 2021. Based on our audit work, we have concluded that the amount paid by the Welsh Government was accurate and fair in the context of the agreement between HMRC and the Welsh Government. The 2020-21 costs were lower than in 2019-20, largely because the costs of implementing the Welsh Income Tax Project reduced by £1.2 million. In 2019-20 HMRC recharged costs of £2 million, comprising £1.4 million of implementation costs and £0.6 million of operating costs (paragraph 3.4 to 3.5 and Figure 8).