



National Audit Office



REPORT

# Administration of Scottish income tax 2021-22

HM Revenue & Customs

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SESSION 2022-23  
12 JANUARY 2023  
HC 1022

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## Key facts

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**2.5mn**

Scottish taxpayers in 2020-21

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**£11.95bn**

Scottish income tax revenue  
in 2020-21

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**£13.30bn**

HM Revenue & Customs'  
estimate of Scottish income  
tax revenue in 2021-22

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**£0.6 million** costs of administering Scottish income tax in 2021-22

# Summary

## Introduction

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

**2** The Scottish Parliament sets income tax rates in Scotland using the five-band system first introduced in 2018-19. There are three tax bands in the rest of the UK. For 2021-22, the top rate tax band in Scotland stayed at £150,000. All other tax bands increased by between approximately 0.5% and 0.6%, similar to the increases for the rest of the UK (see **Figure 1**). The personal allowance, set by the UK government, increased from £12,500 in 2020-21 to £12,570 in 2021-22.

## Figure 1

Income tax rates and bands in Scotland and the rest of the UK for 2021-22

There are five tax bands above the personal allowance in Scotland compared with three in the rest of the UK

Band	Income tax rates in Scotland		Income tax rates in the rest of the UK	
	Taxable income (£)	Tax rate (%)	Taxable income (£)	Tax rate (%)
Personal allowance <sup>1</sup>	Up to 12,570	0	Up to 12,570	0
Starter rate	12,571 to 14,667	19	-	-
Basic rate	14,668 to 25,296	20	12,571 to 50,270	20
Intermediate rate	25,297 to 43,662	21	-	-
Higher rate	43,663 to 150,000	41	50,271 to 150,000	40
Top rate <sup>2</sup>	More than 150,000	46	More than 150,000	45

### Notes

- 1 A taxpayer's personal allowance is reduced by £1 for every £2 of net income above £100,000.
- 2 This is known as the additional rate in the rest of the UK.

Source: HM Revenue & Customs, *Income Tax rates and Personal Allowances*, available at: [www.gov.uk/income-tax-rates/previous-tax-years](http://www.gov.uk/income-tax-rates/previous-tax-years), accessed October 2022 and HM Revenue & Customs, *Income Tax in Scotland*, available at: [www.gov.uk/scottish-income-tax/2021-to-2022-tax-year](http://www.gov.uk/scottish-income-tax/2021-to-2022-tax-year), accessed October 2022.

**3** HM Revenue & Customs (HMRC) administers and collects Scottish income tax as part of the UK tax system. HMRC identifies taxpayers living in Scotland by applying a 'flag' in its systems that indicates they are subject to Scottish income tax rates and thresholds. HMRC has calculated that there were 2.5 million Scottish taxpayers in 2020-21. HM Treasury is responsible for paying Scottish income tax to the Scottish Government.

**4** Following the end of each tax year, HMRC produces a provisional estimate of Scottish 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 2020-21 and the provisional estimate for 2021-22. HMRC expects to publish the outturn for 2021-22 in its 2022-23 Annual Report and Accounts.

**5** Section 80HA of the Scotland Act 1998, as amended by the Finance Act 2014 and the Scotland Act 2016, requires the Comptroller and Auditor General (C&AG) to prepare a report for each financial year on:

- the adequacy of HMRC's rules and procedures, in consequence of the Scottish rate provisions, to ensure the proper assessment and collection of income tax charged at rates determined by those provisions;
- whether these rules and procedures are being complied with;
- the correctness of sums brought to account by HMRC which relate to income tax attributable to a Scottish rate resolution; and
- the accuracy and fairness of amounts reimbursed to HMRC as administrative expenses.

**6** This report assesses:

- HMRC's calculation of the 2020-21 income tax revenue for Scotland, the 'outturn', and assurance on the correctness of amounts brought to account (Part One);
- HMRC's estimate of the 2021-22 income tax revenue for Scotland 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 Scottish tax requirements (Part Two); and
- the cost of administering Scottish income tax. We provide assurance on the accuracy and fairness of these amounts in the context of costs incurred by HMRC (Part Three).

**7** In December 2022, the Scottish Government announced that the top rate of income tax will increase from 46% to 47% and that the higher rate of income tax will increase from 41% to 42%. This will come into effect on 6 April 2023 to cover the 2023-24 tax year. The level at which taxpayers will pay the top rate of income tax will reduce from £150,000 to £125,140 for taxpayers in both Scotland and the rest of the UK. We will consider the impact of these changes in future reports.

**8** Appendix One sets out our audit evidence base.

## Key findings

### Scottish income tax 2020-21 final outturn and 2021-22 estimate

**9 HMRC calculated the final outturn for 2020-21 as £11,948 million, representing amounts collected under Scottish income tax policy.** HMRC's estimate of 2020-21 Scottish income tax revenue, published in November 2021, was £12,035 million, meaning the actual outturn was £87 million (0.7%) lower than HMRC had originally estimated. We examined the methodology for the calculation of the actual outturn, which necessarily includes some remaining areas of estimation, for instance where returns from taxpayers had not yet been received. In these areas, we have evaluated the basis of HMRC's estimate, including the relevant assumptions and available data. Based on that audit work, we have concluded that the Scottish income tax revenue outturn for 2020-21 is fairly stated (paragraphs 1.2 to 1.16).

**10 HMRC has estimated Scottish income tax revenue for 2021-22 as £13,295 million.** This represents an increase of £1,347 million (11.3%) compared with the 2020-21 outturn. Income tax for the whole of the UK increased by 13.2% in 2021-22. The increases in UK and estimated Scottish income tax revenues reflect the recovery of the economy after the acute phase of the COVID-19 pandemic had ended. HMRC expects to calculate the finalised 2021-22 income tax outturn attributable to Scotland in 2023. 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 Scottish Government (paragraphs 1.17 to 1.22).

**11 External factors have increased the level of uncertainty in HMRC's estimate of Scottish income tax revenue for 2021-22.** HMRC identified the key source of uncertainty as the accuracy with which it can estimate Scotland's share of UK income tax liabilities, particularly since this estimate relies on survey data from 2019-20. External factors outside its direct control, such as the wave of the Omicron variant of COVID-19 that developed during the year and the impact of the Ukraine conflict on taxpayers' ability to meet their tax liabilities, have introduced further uncertainty to the estimate. We consider the approach adopted by HMRC to estimating the impact of these areas of uncertainty on Scottish income tax revenue in 2021-22 to be reasonable (paragraph 1.23).

## Administration of Scottish income tax

**12 HMRC has adequate rules and procedures in place to ensure the proper assessment and collection of Scottish income tax and those rules are being complied with.** Our work on Scottish 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 had framed adequate regulations and procedures to secure an effective check on the assessment, collection and proper allocation of revenue, and that these regulations and procedures are being duly carried out (paragraphs 2.2 to 2.14).

**13 Maintaining an accurate and complete record of the addresses of Scottish taxpayers 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 a reduction in the number of Scottish postcodes identified by HMRC's address-cleansing work as either missing or invalid, with 1% (25,488) of the overall taxpayer population identified as either missing or invalid in June 2021 compared with 2% (61,213) in September 2020. HMRC has investigated and updated those cases where individuals were either employed or receiving a pension (paragraphs 2.16 to 2.25 and Figure 8).

**14 The divergence between the tax regimes in Scotland and the rest of the UK in 2021-22 remained broadly the same as in 2020-21.** As in previous years, the amount of income tax paid in Scotland diverges the most in percentage terms from the rest of the UK for those earning around £50,000, although the percentage difference paid by taxpayers at that level did reduce slightly in 2021-22. HMRC continues to assess the risk of a Scottish taxpayer manipulating their address to minimise their tax liability. HMRC has not identified any significant or widespread instances of taxpayers changing their address to obtain a tax advantage (paragraphs 2.29, 2.38 to 2.41 and Figure 9).

**15 HMRC continues to assess as 'low' the risk of non-compliance as a result of divergence between Scottish income tax and rest of the UK.** In 2021-22, HMRC produced a Scottish Strategic Picture of Risk (SPR). It considers the main areas of risk to Scottish income tax to be the same as those compliance risks which are assessed at the whole-of-UK level. There are no risks identified in the Scottish SPR which are specific to Scotland as HMRC assesses that compliance risk in Scotland is consistent with the rest of the UK. There is a risk that this current position may not be sustainable in the longer term, particularly if further divergence of tax policy occurs. The Scottish Government did not ask HMRC to undertake any specific compliance activity in 2021-22, in addition to the work undertaken as part of its UK-wide compliance approach (paragraphs 2.28 to 2.30 and 2.38).

**16 HMRC calculated a compliance yield of £280 million relating to Scotland for 2020-21, the most recent data available.** HMRC measures the effectiveness of its enforcement and compliance activities through compliance yield: its estimate of the additional revenues it has generated through its compliance work, and the revenue losses it has prevented. HMRC also estimated that Scotland's share of net losses was £970 million. HMRC calculates these figures as a proportion of the equivalent UK figure, rather than using Scotland-specific data to quantify the risks. HMRC does not consider or report on geographical variations in the level of compliance risk, or the relative success of compliance activity in Scotland compared with the rest of the UK (paragraph 2.31).

**17 HMRC has limited performance data available about its compliance activities in Scotland.** Unlike its income tax system which flags residents as Scottish, HMRC's compliance system cannot readily identify people living in Scotland. HMRC therefore cannot easily track and monitor compliance activity in Scotland and this affects its ability to collect performance data about the extent of Scottish non-compliance (paragraph 2.33).

**18 COVID-19 continued to have an impact on HMRC's compliance activities during 2021-22.** Across the UK, the number of compliance cases opened and closed in 2021-22 was higher than in 2020-21 but 27% lower than in 2019-20 before the pandemic. The ability to conduct face-to-face enquiries and the need to re-deploy compliance staff to support other COVID-19 measures also affected its compliance activity during the year. HMRC's yield from its tax compliance activities for the whole of the UK was £30.8 billion in 2021-22, up 1.1% compared with 2020-21 but lower than the £36.9 billion reported in 2019-20. It will take some time to understand fully the impact of the pandemic on tax compliance and yield (paragraphs 2.34 and 2.35).

**19 Tax debt has reduced since 2021 but remains higher than pre-pandemic levels.** HMRC's debt balance is affected by external factors that have an impact on taxpayers' ability to pay their tax liabilities, including current inflationary pressures and increases in the cost of living. At 31 March 2022, total tax debt for the UK was £41.6 billion, 86% (£19.2 billion) higher than the level of debt reported at 31 March 2020, before the impact of the COVID-19 pandemic. HMRC expects the level of tax debt to fall more slowly than it initially anticipated. HMRC estimated Scottish taxpayers' total tax debt to be £2.0 billion as at 31 December 2021, 5.7% of UK tax debt at that time.<sup>1</sup> Some £0.9 billion of this was attributed to debts from Pay As You Earn (PAYE) and Self Assessment income tax. HMRC calculated this estimate in response to a question from the Scottish Public Audit Committee, with no equivalent figure being available at 31 March 2022 (paragraphs 2.36 and 2.37).

<sup>1</sup> Figures provided by HMRC to the Convener of the Scottish Public Audit Committee in June 2022. Figures do not sum to the total debt balance of £39.5 billion at that time because they exclude non-UK debts where the country cannot be identified. We have not audited these figures.

## Costs

**20 In 2021-22 HMRC incurred and recharged £0.6 million to the Scottish Government for the cost of administering Scottish income tax.** We examined HMRC's method for estimating the costs of collecting and administering Scottish income tax for the year ended 31 March 2022. Based on our audit work, we have concluded that the amount paid by the Scottish Government was accurate and fair in the context of the agreement between HMRC and the Scottish Government (paragraphs 3.4 and 3.5 and Figure 10).