



Submission to the Scottish Government

The Role of Income Tax in Scotland's Budget

4 December 2017

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About ICAS

1. The following submission has been prepared by the ICAS Tax Board. The ICAS Tax Board, with its five technical Committees, is responsible for putting forward the views of the ICAS tax community, which consists of Chartered Accountants and ICAS Tax Professionals working across the UK and beyond, and it does this with the active input and support of over 60 board and committee members. The Institute of Chartered Accountants of Scotland ('ICAS') is the world's oldest professional body of accountants and we represent over 21,000 members working across the UK and internationally. Our members work in all fields, predominantly across the private and not for profit sectors.
2. With approximately half our members based in Scotland, we have had extensive dealings with the new devolved tax powers. ICAS has contributed the experience of its members and their technical expertise in the development and implementation of the two existing devolved taxes, Land and Buildings Transaction Tax (LBTT) and Scottish Landfill Tax (SLfT), in the development of the proposed Air Departure Tax, and the establishment of the tax authority Revenue Scotland. ICAS has also contributed to the development of both Scottish Rate of Income Tax and the Scotland Act 2016 income tax rates and bands.
3. ICAS has a public interest remit, a duty to act not solely for its members but for the wider good. From a public interest perspective, our role is to share insights from ICAS members into the many complex issues and decisions involved in tax and financial system design, and to point out operational practicalities. Therefore, we have focused on the operational aspects of Scottish income tax, which is where the expertise of the Tax Board and the Scottish Taxes Committee rests.
4. As a matter of policy, ICAS does not comment on the rates of any tax.

General comments

5. ICAS welcomes the discussion paper 'The Role of Income Tax in Scotland's Budget', published by the Scottish Government in November 2017. It offers a refreshingly transparent view of the analysis and possible approaches to setting income tax rates and bands for 2018/19. ICAS representatives were also pleased to be invited to participate in round table discussions about the paper.
6. The paper 'The role of Income Tax in Scotland's Budget' provides four alternative approaches to setting the income tax rates and bands for 2018/19. There are practical and administrative matters to consider in the discussion, a number of which have already been identified and discussed in the paper.
7. ICAS has outlined its views regarding the operational opportunities and constraints around the exercise of the devolved tax powers, including income tax, in chapter 2 of the Fraser of Allender publication 'Scotland's Budget Report 2017'.
<https://www.sbs.strath.ac.uk/economics/fraser/20170926/Scotlands-Budget-2017.pdf> . This submission expands on our earlier views.
8. Scottish income tax cannot be considered in isolation because the powers are only partly devolved. The tax is intricately interwoven with UK taxes, and the Scottish Parliament has only a limited number of pieces of the jigsaw.
9. Behavioural responses by taxpayers may limit some options; however, behavioural repercussions may not limit the Scottish Government's choices if the policies are considered attractive by the electorate. It will also be necessary for the electorate to trust that policy objectives are achievable and will be achieved – that a better economy, desired redistribution, or better public services will result from additional taxation.
10. A key element of tax policy should be, where possible, to enhance and support the economy: at the very least, measures should not add to the complexity of doing business in Scotland and should not put Scottish business at a competitive disadvantage.
11. A five-year roadmap to set out the objectives of Scottish tax policy would be helpful: this should set out policy objectives and provide clarity of purpose, and tie in with the Scottish Fiscal Framework.

Transparency of data and the link between Scottish tax receipts and the operation of the Fiscal Framework will be crucial if the public are to maintain faith in the process.

12. Administrative responsibility for Scottish income tax remains with HMRC but the Scottish Government pays HMRC for costs of collection and significant variations to the income tax rates and bands may cost more to collect. However, it needs to be remembered that much of the collection of income tax, through PAYE, is done by employers.
13. When additional rate bands are introduced, care is required with the administrative side. Much is made of digital processes enabling the implementation of more detailed provisions but some words of caution:
 - For changes to payroll software, to process 'S' codes through PAYE, the software houses require specific details as early as possible. The shorter the notice, the more expensive to change and the more scope for mistakes.
 - With self-assessment software HMRC is already having difficulties this year and there are many exceptions to online filing so that these have to be submitted on paper. The system is already too complicated around income tax and, in particular, with savings income.
 - Administrative ease is desirable but digital ease should not mask complexity of tax raising powers because this compromises accountability.
 - Pension providers and payroll software providers will require enough time to adapt their systems to include the new provisions and pensions tax relief as appropriate.
14. Where additional rates and bands are introduced, the interactions between Scottish income tax and other reserved UK taxes should be considered.
 - For example, the 'basic rate' should be specified (section 80C, Scotland Act 1998 as amended by Scotland Act 2016). Whatever the basic rate is determined to be will impact on reliefs such as marriage allowance, gift aid (discussed below) and pension contributions.
 - It should also be noted that with regard to pension contributions, higher and additional rate taxpayers can claim tax relief at their marginal rate of tax.
15. When introducing new rates and bands, the effective rate of tax at each point should be considered to ensure that there is no adverse consequence. Potential areas to consider are where child benefit is withdrawn, the point where the personal allowance is withdrawn and the marriage allowance. Care may need to be taken so as not to exacerbate existing kinks or to create more. It may be difficult to reconcile a more progressive system of rates and bands with existing kinks and reserved matters.
16. While Holyrood has the power to set income tax rates and bands, the UK Government retains control over the personal allowance and all tax reliefs, including Gift Aid.
17. How could different income tax rates in different parts of the UK impact on the Gift Aid system? At present, charities (and Community Amateur Sports Clubs) can claim Gift Aid at the UK basic rate of income tax: this creates a link between the tax paid by the donor and the Gift Aid claimed by the charity. If this policy continues once the Scottish basic rate varies from the rest of the UK, this link will be weakened. However, maintaining the link is also challenging as it means that all UK charities would need to know whether a donor was a Scottish or rest of the UK taxpayer with the administrative and potentially behavioural consequences that would entail: this is therefore an issue relevant to charities across the UK and likewise tax paying donors.
18. HMRC has published three technical notes on clarifying the scope of Scottish income tax powers which refer to its policy on Gift Aid. The most recent technical note was published in [December 2016](#): this note confirms the position set out in the two earlier technical notes published in December 2014 and May 2012. The technical note published in [December 2014](#) sets out the position in more detail than the December 2016 technical note.
19. If rates and bands diverge as expected, the UK Government will need to determine whether and for how long its current position is sustainable. If the current position is considered unsustainable an alternative policy accompanied by appropriate administrative arrangements would need to be implemented. If both bands as well as rates diverge, a question may arise over the band in which the basic rate of income tax in Scotland resides.

20. More broadly, there is a need for sound financial processes that provide useful and meaningful financial information. Such financial information is needed to allow a better understanding of tax policy and collection, how it has been used to support public finances, and to enable taxpayers to hold decision makers to account. An important part of this is being able to analyse devolved revenues against budget to assess whether policy decisions have achieved their intended effect.