SCOTTISH RATE OF INCOME TAX: DEPARTMENT OF WORK AND PENSIONS IMPLEMENTATION COSTS – EXCHANGE OF LETTERS

As you are aware, under the settlement for the Scotland Act 2012, it was agreed that the Scottish Government would pay the costs incurred as a result of implementing and administering the financial provisions. In respect of the Scottish Rate of Income Tax (SRIT) provisions, the main costs are attributable to work that HMRC is doing as the body responsible for the collection and management of SRIT as part of the UK income tax system. Edward Troup, HMRC’s Second Permanent Secretary and Additional Accountable Officer for the SRIT appeared before the Finance Committee on 28 October. He confirmed the estimates for implementation remain between £30m - £35m, as reported in the UK Government’s *Third Annual Report on the Implementation and Operation of Part 3 (Financial Provisions) of the Scotland Act 2012* in March this year, as well as providing an update on potential running costs.

The UK Government’s March report identified that the Department of Work and Pensions (DWP) was also making changes to its systems to reflect the introduction of SRIT. DWP need to make changes to ensure that its systems recognise and process information on Scottish taxpayers from April 2016 in the way they currently do for UK taxpayers. At this time, DWP estimates the implementation costs associated with this work to be £1.8m, with no ongoing running costs.

My officials have worked with DWP’s SRIT Project Team to: understand the work being done by DWP to ensure that DWP is compliant with SRIT; identify the changes that are being incurred wholly and necessarily as a result of SRIT’s introduction and their associated costs; and, agree appropriate governance arrangements to allow the Scottish Government to work with DWP to scrutinise these costs and achieve value for money.
I enclose a copy of the exchange of letters between officials within the Scottish Government and DWP agreeing the arrangements under which our organisations will work together and make the changes necessary to ensure a smooth implementation of SRIT from April 2016. These arrangements, while taking into account the different role and estimated implementation costs of DWP, are closely modelled on the Memorandum of Understanding in place for SRIT between the Scottish Government and HMRC.

The arrangements apply only to the implementation of the Scottish income tax powers introduced under the Scotland Act 2012 and, therefore, will be reviewed or replaced at such time as any further income tax powers are devolved to the Scottish Parliament.

I am writing in similar terms to the Conveners of the Finance and Public Audit Committees.

JOHN SWINNEY

Encl. Exchange of letters on the Arrangements between the Scottish Government and the Department of Work and Pensions for the Scottish Rate of Income Tax
Dear Michael


Thank you for your helpful letter of 16 October confirming that you are now responsible for the delivery and implementation of SRIT within DWP.

In March, the UK Government identified, in its Third Annual Report on the Implementation and Operation of Part 3 (Financial Provisions) of the Scotland Act 2012, that DWP was making changes to its systems to reflect the introduction of SRIT. The Scottish Government understands that these are changes that will ensure that DWP systems can continue to recognise and process information on Scottish taxpayers from April 2016.

Under the settlement for the Scotland Act 2012, it was agreed that the Scottish Government pay the costs incurred as a result of implementing the financial provisions of the Scotland Act 2012.

Scottish Government officials have, therefore, been working with DWP’s SRIT Project Team to: understand the work being done by DWP to ensure that DWP is compliant with SRIT; to identify the changes that are being incurred wholly and necessarily as a result of SRIT’s introduction and their associated costs; and, to agree appropriate governance arrangements to allow the Scottish Government to work with DWP to scrutinise these costs to achieve value for money.

I now seek your formal agreement to the arrangements proposed in the Annex of this letter which will provide the transparent framework under which our organisations will continue to work together to ensure that value for money is achieved as DWP make the changes necessary to ensure a smooth implementation of SRIT from April 2016.

Victoria Quay, Edinburgh EH6 6QQ
www.gov.scot
These arrangements apply only to the implementation of the Scottish rate of income tax powers introduced under the Scotland Act 2012 and, therefore, will be reviewed or replaced at such time as any further income tax powers are devolved to the Scottish Parliament.

A copy of these arrangements will be provided to the Scottish Parliament’s Finance and Public Audit Committees.

Yours sincerely

[Signature]

SEAN NEILL
Deputy Director

Encl. ANNEX: Arrangements between the Scottish Government and the Department of Work and Pensions for the Scottish Rate of Income Tax (5 pages)
From: Michael Boughey  
Deputy Director  
Technology Platforms  
DWP Technology  

To: Sean Neill  
Deputy Director  
Scottish Government  
Area 2F South  
Victoria Quay  
Edinburgh  
EH6 6QQ  

Date: 1st December 2015  

Scottish Rate of Income Tax (SRIT)  
Arrangements between the  
Scottish Government and the Department for Work and Pensions (DWP)  

Dear Sean,  

Thank you for your letter of the 19 November 2015, which included an Annex with proposed arrangements between the Scottish Government and the Department for Work and Pensions for the Scottish Rate of Income Tax.  

I formally provide agreement to the arrangements proposed in the Annex, which will provide the transparent framework under which our organisations will continue to work together to ensure that value for money is achieved as DWP make the changes necessary to ensure a smooth implementation of SRIT from April 2016.  

I also fully agree that the arrangements only apply to the implementation of the Scottish Rate of Income Tax powers introduced under the Scotland Act 2012 and therefore, that they will be reviewed or replaced at such time as any further Income Tax powers are devolved to the Scottish Parliament.  

Yours sincerely  

Michael Boughey  
Telephone: 04925 845587  

Copy List:  
Ray Long  
Steve Faill  
Una Wiatrek  
Richard Cornish  
James Pike  
Simon Boniwell

Arrangements between the Scottish Government and the Department of Work and Pensions for the Scottish Rate of Income Tax

Introduction

1. The Scottish rate of income tax (SRIT) will be set, each year, through a Resolution passed by the Scottish Parliament on the basis of a proposal made by Scottish Ministers. SRIT is not a devolved tax. It forms part of the UK income tax system and will be administered along with the rest of the income tax system by Her Majesty’s Revenue and Customs (HMRC).

2. As certain aspects of the current tax and benefit systems are inter-dependent, the introduction of SRIT has consequential impacts for the Department of Work and Pensions (DWP). DWP requires, therefore, to ensure that its systems and processes are ready to recognise SRIT when it is introduced from April 2016.

3. Scottish Ministers will be responsible for proposing the tax rate but not for any other element of the tax nor for its administration. However the Scottish Government’s (SG’s) budget will bear the agreed costs of setting up and operating SRIT and will benefit from revenue collected. This Annex sets out arrangements for the SG to meet the costs of changes to DWP administrative and IT systems made necessary by the introduction of SRIT. The arrangements in place between the Scottish Government (SG) and HMRC for setting up and operating SRIT are covered by a separate Memorandum of Understanding.

Scottish rate of income tax

4. The Scotland Act 1998 as amended by the Scotland Act 2012 (‘the 2012 Act’) gives the Scottish Parliament the power to set a Scottish rate of income tax (SRIT) to be charged on Scottish taxpayers. It will be administered by HMRC as part of the UK wide tax system and applied to non-savings income. The Scottish Parliament will be able to set a rate of SRIT from zero to any number of pence or half pence in the pound. The rate will be added to each of the main UK rate bands after ten pence in the pound has been deducted from each rate. The 2012 Act repeals the provisions for the Scottish Variable Rate with effect from the date SRIT begins. SRIT will be set each year through a resolution passed by the Scottish Parliament on the basis of a proposal made by Scottish Ministers.

Purpose of this annex

5. This Annex sets out the arrangements agreed between the SG and DWP for ensuring DWP administered taxable benefits and associated IT systems recognise and interact with SRIT in order that benefit recipients who are Scottish taxpayers continue to receive the correct amount of benefits and that the correct tax information is recorded for HMRC purposes. It sets the respective responsibilities of the SG and DWP in relation to these aspects of SRIT implementation and provides a framework for inter-Government work on this issue. It has no formal legal force, nevertheless both Governments expect it to be followed.
6. These arrangements reflect:
   - The Memorandum of Understanding and Supplementary Agreements between the United Kingdom Government, The Scottish Ministers, the Welsh Ministers and Northern Ireland Executive Committee;
   - Cabinet Office Devolution guidance notes; and
   - HM Treasury’s statement of funding policy, “Funding the Scottish Parliament, National Assembly of Wales and Northern Ireland Assembly”.

**Date and Timing**

7. This Annex and arrangements described within it come into effect when the last of the parties’ to signify their acceptance of those arrangements through an exchange of letters signifies acceptance. It has no expiry date but will cease to have effect if SRIT is repealed. The arrangements may be brought to an end by agreement between DWP and SG and will be reviewed at the request of either party.

**Senior responsible officers and Parliamentary reporting**

8. The DWP Permanent Secretary is the Accounting Officer with overall responsibility for ensuring that the correct IT and administrative systems are in place within DWP to support the timely introduction of SRIT. Scottish Parliamentary Committees may request that DWP provides a senior official to give evidence, and DWP will consider these requests in line with Cabinet Office guidance on officials’ attendance at such Committees. The senior officials with responsibility for matters covered by this Annex are the Deputy Director, Fiscal Responsibility for the Scottish Government and the nominated Deputy Director DWP Technology Platforms.

9. Section 33 of the 2012 Act lays a duty on the Secretary of State to make a report each year until 2020 at the earliest on the implementation and operation of Part 3 of the 2012 Act (Finance) which will include a report on the implementation and operation of SRIT. This report must be laid in each House of Parliament and sent to Scottish Ministers who must lay a copy before the Scottish Parliament. Scottish Ministers are similarly required to make a report each year to the Scottish Parliament, which in turn is sent to the UK Government and laid before the Westminster Parliament. These reports must include a report on progress with implementing and operating the financial provisions in the 2012 Act and DWP will contribute to the UK report.

**Roles and responsibilities of DWP and SG**

10. DWP will continue to have in place appropriate governance arrangements to ensure DWP IT systems, relevant staff guidance, customer forms and letters comply with SRIT provisions in the Scotland Act 2012. The process will take an inter-governmental approach to quality assurance, reviewing progress against milestones and ensuring value for money.

11. The SG will be represented within DWP’s internal governance arrangements for implementing SRIT at both project and programme level. The SG may also request that DWP commission an external assurance review at the SG’s expense.
12. DWP will make the necessary changes to benefit IT platforms which interface with the UK tax systems to enable them to recognise the new Scottish tax code. At the same time and where appropriate, staff guidance and customer forms and letters will be amended accordingly.

13. DWP will develop and test the IT and administration of SRIT in consultation with HMRC and the SG.

14. DWP will invoice SG for agreed items of expenditure as set out in paragraph 30 below.

15. SG will make payment to DWP for amounts invoiced for agreed items of expenditure as set out in para 30 below.

16. DWP will have no role in relation to determining an individual’s tax liability nor for the publicity of SRIT other than ensuring, where appropriate, customer communications reflect the Scottish rate.

**DWP IT and Administrative impacts of SRIT Implementation**

17. DWP will remain responsible for ensuring that the correct IT and administrative systems are in place to support the timely introduction of SRIT.

18. DWP will keep the SG informed of, and will consult with the SG on plans, timetables, estimated costs, risks and progress. Where there are options for developing and amending such systems, DWP will discuss these, together with the cost, risk, efficiency, effectiveness or customer impact factors, with the SG before an option is selected.

19. DWP will upgrade and test all IT systems for all areas of DWP business that will impacted by SRIT. This will be done through contracted IT suppliers and in accordance with its normal IT development practice.

20. The cost and functionality of each part of the IT system will be notified to the SG, subject to any confidentiality rules in prevailing DWP contracts.

21. The SG will have an opportunity to review plans for IT testing and the results of such tests.

22. DWP will develop non IT systems for all areas of DWP business that will impacted by SRIT. This will be done in accordance with normal DWP practice.

23. A breakdown of the expected costs and activities for both IT system and non IT system changes will be shared with the SG before such costs are incurred.

24. DWP and the SG will scrutinise the IT and non IT System costs with a view to ensuring value for money. Where the SG have any concerns about the cost of a particular item that joint discussions cannot resolve, the SG – or DWP on behalf of the SG – may request an independent assessment of the estimated costs in question. All associated costs of the independent assessment will be met by the SG. Any contracts and costs finalised after this Annex takes effect, will be discussed and agreed with the SG in advance.
Continuing operations

25. After IT changes have been made to deliver SRIT, DWP will maintain its IT and administrative systems so that SRIT continues to operate effectively in respect of the administration of benefits.

Funding

26. DWP will test existing infrastructure put in place pre-1998 in preparation for Scottish Variable Rate of Tax to extract value for money from this earlier investment, but also needs to undertake new work to cover benefits and IT systems that have been developed and come on-line in the intervening time to ensure the current social security system will recognise Scottish taxpayers and that the respective IT systems interface with HMRC SRIT systems.

27. Where DWP charges for its services, it does so (following HM Treasury policy) at the full economic cost of providing the service seeking to make clear the breakdown of the calculation. Full economic cost is based on the average salary cost for the relevant grade plus per capita overheads such as superannuation. Where costs are under contract by third parties including DWP’s IT supplier, these will be charged at cost.

28. The SG will meet costs which it is satisfied have wholly and necessarily been incurred as a result of the introduction of SRIT.

29. Once the changes are made to DWP’s IT systems to recognise SRIT as introduced in the Scotland Act 2012, there will be no additional annual expenditure to maintain these changes.

30. Costs will be borne by the SG and DWP as set out below:

Costs borne by SG – DWP will invoice and the SG will pay for:
- Capital and project costs of making IT changes to DWP IT systems and ancillary costs (i.e. non-IT) relating to staff guidance and customer forms and letters required as a result of the introduction of SRIT.
- If suppliers consume more time and materials than agreed estimates, DWP will discuss with SG with the expectation that SG will meet costs if these increases have been incurred wholly and necessarily as a result of the introduction of SRIT and not as a result of error on the part of suppliers.

Costs borne by DWP – DWP will not charge for:
- Cost of changes to DWP IT systems where no specific provision needs to be made for SRIT.
- Supplier issues covered under DWP contract warranties.
- If a supplier fails to deliver, the SG should not pay for any consequence of costs incurred by the DWP Business invoking manual processes due to supplier issues. For example additional changes to Letters and Guidance.
- Costs involving changes to the IT systems where aspects of SRIT cannot reasonably be costed separately.
Invoicing
31. DWP will invoice SG for costs quarterly in arrears. SG will make payment to DWP within 30 days of the invoice date, or within 30 days of receipt of the invoice if there is a delay of more than 5 days between invoice date and date of receipt.

32. Separate arrangements may be agreed between DWP and the SG for Quarter 4 payments to ensure that payments are made in the appropriate financial year.

Dispute resolution
33. Where a dispute arises over a payment in relation to matters set out in this above, it will be discussed at the DWP Technology Platforms Functional Board or its successor at which the Scottish Government is represented. If agreement is not reached between DWP and SG the matter will be escalated to the SG’s Director of Financial Strategy and DWP’s Director of Technology Platforms or successor Director.

Information sharing
34. DWP will provide SG with information that will enable Scottish Ministers and officials to discharge their duties in respect of Parliamentary accountability. This includes information in relation to the reporting requirements of Section 33 of the 2012 Act.

Limitations
35. DWP operates within the legal constraints of customer confidentiality, the Data Protection Act 1998 and Social Security Administration Act 1992.