



The Scottish Parliament
Pàrlamaid na h-Alba

Official Report

PUBLIC AUDIT COMMITTEE

Thursday 22 November 2012

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**PUBLIC AUDIT COMMITTEE
17th Meeting 2012, Session 4**

CONVENER

*Iain Gray (East Lothian) (Lab)

DEPUTY CONVENER

*Mary Scanlon (Highlands and Islands) (Con)

COMMITTEE MEMBERS

*Colin Beattie (Midlothian North and Musselburgh) (SNP)

*Willie Coffey (Kilmarnock and Irvine Valley) (SNP)

*James Dornan (Glasgow Cathcart) (SNP)

*Mark Griffin (Central Scotland) (Lab)

*Colin Keir (Edinburgh Western) (SNP)

*Tavish Scott (Shetland Islands) (LD)

*Sandra White (Glasgow Kelvin) (SNP)

*attended

THE FOLLOWING ALSO PARTICIPATED:

Alistair Brown (Scottish Government)

Russell Frith (Audit Scotland)

Caroline Gardner (Auditor General for Scotland)

Jonathan Sewell (Scottish Government)

Mark Taylor (Audit Scotland)

CLERK TO THE COMMITTEE

Roz Thomson

LOCATION

Committee Room 1

Scottish Parliament

Public Audit Committee

Thursday 22 November 2012

[The Convener *opened the meeting at 09:30*]

Scotland Act 2012

The Convener (Iain Gray): Welcome to our 17th meeting in 2012. I ask everyone to ensure that their phone is off. We have semi-apologies from Mr Scott, who has to leave to go to the Referendum (Scotland) Bill Committee at some point.

Tavish Scott (Shetland Islands) (LD): When is an apology not an apology?

The Convener: He apologises sincerely.

This morning, we have two panels of witnesses on the single topic of the Scotland Act 2012, after which we will consider our approach to the topic. Does the committee agree to take that item in private?

Members *indicated agreement.*

09:31

The Convener: Our first panel of witnesses are from Audit Scotland. We have the Auditor General for Scotland, who is accompanied by Mark Taylor, assistant director of the audit services group, and Russell Frith, the assistant auditor general. I invite the Auditor General to make some introductory remarks.

Caroline Gardner (Auditor General for Scotland): The Scotland Act 2012 makes significant changes to Scotland's public finances. We are grateful for the opportunity to discuss the audit implications of those changes with the committee at this early stage. My colleagues are Russell Frith, who is responsible for audit policy and quality in Audit Scotland, and Mark Taylor, who leads the annual audit of the Scottish Government. I will rely on them to help me answer any questions that the committee might have on the financial implications of the 2012 act.

The financial provisions cover new borrowing powers and devolved taxes as well as the Scottish rate of income tax. We think that the devolved taxes are relatively straightforward. They will be set by the Scottish Parliament and collected by revenue Scotland and bodies such as Registers of Scotland and the Scottish Environment Protection Agency. There will be a one-off adjustment to the block grant, and the revenue that is raised by the devolved taxes will be audited through the usual

arrangements for auditing revenue Scotland, once it is formally established, and through the existing audits of the Scottish Government, SEPA and Registers of Scotland.

The Scottish rate of income tax is different, in that it will lead to an adjustment to the amount of money that is transferred from Westminster to Scotland each year. As the committee heard yesterday, it will be collected by Her Majesty's Revenue and Customs as part of its responsibilities for collecting income tax across the United Kingdom. Audit Scotland has not been involved in auditing the amount of the Scottish block grant that is transferred from Westminster, which has been heavily influenced by the application of the Barnett formula and formalised by the annual Westminster budget and appropriation acts. The introduction of the Scottish rate of income tax brings added complexity and volatility to the amount of money that is available to the Scottish Government each year.

The Scottish rate of income tax will be set by the Scottish Parliament, but it will be administered and collected by HMRC as part of its wider responsibilities for income tax. As the committee heard yesterday, HMRC is audited by the National Audit Office. Audit Scotland's powers and responsibilities do not include access to HMRC. The Scottish rate of income tax revenue will be only a small part of HMRC's work, although it is of course much more significant to Scotland.

My concern is to help ensure that the Scottish Parliament receives appropriate levels of assurance about the operation of the Scottish rate of income tax and the resulting adjustments to the amount of block grant that is received in Scotland. For us, the main audit issues fall into five categories: first, accounting accountability and regularity; secondly, financial management; thirdly, project management; fourthly, the set-up and running costs that are involved; and, fifthly, tax collection and the impact on the block grant.

We think that the first four issues will be relatively straightforward from an audit perspective once the arrangements have been finalised. We can contribute to the overall assurance in those areas by reviewing the assurance and control mechanisms that the Scottish Government puts in place with HMRC through the draft memorandum of understanding and by commenting on the level of assurance that is received from HMRC and the NAO. We can also audit any expenditure that the Scottish Government incurs during the set-up phase, as part of the audit of the Scottish Government's accounts. We can also, to an extent, audit the set-up and running costs that are incurred by HMRC, assuming that those are invoiced to the Government in line with the memorandum of understanding.

That said, the collection of the Scottish rate of income tax and its impact on the block grant are new areas for us all, and there must be clear and transparent reporting arrangements.

We are grateful for this opportunity to discuss the audit implications of the changes with the Public Audit Committee as the accountability and audit arrangements take shape, and we will do our best to answer the committee's questions.

The Convener: Thank you very much.

I will kick off the questioning. As you know, we took evidence yesterday from Mr Morse, your equivalent in the National Audit Office, who I thought implied that the arrangements as described did not—how can I put it?—require HMRC to provide detailed enough information on the on-going collection of the Scottish rate of income tax. What is your sense of that?

Caroline Gardner: Our view is that the issue is not yet clear enough. Like you, we have had the opportunity to see the memorandum of understanding, which contains provision for the income and expenditure related to SRIT to be included in HMRC's accounts. However, we are not clear about the level of detail that will have to be set out in those accounts and, in turn, the level of audit coverage that my NAO counterpart will be required to provide and therefore the assurances that the Scottish Parliament can have in that respect. We think that that is a developmental issue—as I said in my opening remarks, the situation is new to all of us—but our view is that it is important to be clear about the detail and for the detail to be sufficient for the Scottish Parliament to have assurance. That probably means that the detail will have to be at a higher level than is necessary for assurances with regard to HMRC's collection of income tax across the United Kingdom.

The Convener: As Auditor General, you have a statutory basis for your work. Yesterday, Mr Morse seemed to imply that he felt that he needed a stronger statutory basis for auditing the collection of the Scottish rate of income tax. What is your view on that?

Caroline Gardner: Again, the area is developing. At the moment, Amyas Morse's powers as Comptroller and Auditor General for auditing HMRC and reporting to the UK Parliament are very clear. However, it is not clear on what basis he will report to or produce a report for consideration by the Scottish Parliament.

Equally, although there is a long history of close working between the NAO and Audit Scotland, which we would expect to continue when the Scottish rate of income tax is introduced, it is not clear on what basis I could report to the Scottish Parliament on a report produced by the

Westminster Comptroller and Auditor General. There needs to be a bit of fine tuning of the audit powers rather than the tax collection and setting powers.

The Convener: Mr Morse made what seemed to me to be the curious suggestion that he could carry out the audit but that you as Auditor General for Scotland could report to the Scottish Parliament. What is your view on that?

Caroline Gardner: We are all grappling with the implications of a new way of collecting tax. After all, we are talking about a shared income tax base with receipts that will be shared between the UK and Scottish Parliaments. We have not been in such a position before and are working through how that might work in practice. It is very clear that the NAO is and will continue to be the auditor of HMRC; it is willing to do additional work to audit whatever method of accounting for the Scottish rate of income tax is agreed, and that is the right route for providing professional coverage of the revenue and expenditure involved. However, we have not yet worked through how that will be reported to the Scottish Parliament as opposed to the UK Parliament. We are both committed to working together to make that happen, but there is as yet no statutory underpinning and we need to think about what will be most effective with regard to the work involved and in providing assurance to the Scottish Parliament in ways that are clear cut and maintain the right accountability.

Mary Scanlon (Highlands and Islands) (Con): I will pursue the question that I asked yesterday. I got the impression from the witnesses yesterday that they were very keen to work together, listen to what we had to say, and make sure that what is right for Scotland happens—I hope that that will be the case.

I certainly do not want a lot of duplication of effort, as I do not think that that would be helpful. However, at the outset, where can we have a positive and constructive input into overseeing the collection of stats? What level of detail and information do you think that we need from HMRC? I refer to the examples that I gave yesterday. Would you expect—I think that you have mentioned this already—a progress report on the setting up of the system and its costs? Do you think that information on Scottish taxpayer compliance levels would be essential? Do you expect that there will be reporting on customer service performance in relation to Scottish taxpayer queries, HMRC's performance in collecting Scottish taxes and things such as the level of errors, fraud and write-offs among Scottish taxpayers? At the outset, it would be very helpful if you would tell us exactly what you think would be in Scotland's best interests, to provide the

appropriate level of assurance that you mentioned in your introductory remarks.

Caroline Gardner: There are two strands to that, which are worth separating out. The first is the requirement in HMRC's accounts in relation to how the Scottish rate of income tax is covered. Helpfully, the memorandum of understanding is clear that income and expenditure associated with the SRIT will be recorded in HMRC's accounts. It does not yet specify what the level of detail will be, and we think that it would be helpful to make sure that the level of detail is appropriate. Perhaps there should be a separate statement in HMRC's accounts that would be the focus of the NAO's audit and of any assurance provided to the Scottish Parliament.

The second strand is performance information, which you as a Parliament may want HMRC to report. There are a range of options there. You heard yesterday that most of that performance information would be information that HMRC already reports about income tax collection.

Mary Scanlon: Is that UK-wide information?

Caroline Gardner: Yes. If you want to add new elements of performance information to that, there might be a cost implication. It seems to us that now is the right time to be discussing what additional information is needed by the Scottish Parliament, to build that in at this stage and make sure that the costs and benefits of providing that information are clearly understood.

Mary Scanlon: There seems to be a ballpark figure for the Scottish rate of income tax. What do you think would be the appropriate level of detail that would benefit the work of this Parliament and what would be the appropriate performance information? I mentioned compliance, fraud, write-offs and so on. I am really just asking for a steer on what, under those two headings, you think would be important at this stage.

Caroline Gardner: That is a decision for the Parliament, but I think that there is absolute value in the Parliament having a clear picture of compliance collection rates in Scotland and the variation that might exist between those and the rates in the remainder of the UK's income-tax base. Beyond that, there is an important discussion to be had about the trade-off between costs and benefits that always comes into account. Russell Frith may want to add to that.

Russell Frith (Audit Scotland): Caroline Gardner is absolutely right. Some things that Mary Scanlon mentioned, such as performance in collecting the Scottish tax and the level of write-offs, absolutely should be things that are readily and separately identified for Scotland. There is a discussion to be had on some of the other things, such as the level of customer service

performance. As I think that you heard yesterday, HMRC operates a lot of its call centres and the like on a UK basis, so it would be probably quite difficult to extract that type of information separately.

Mary Scanlon: That is very helpful. Thank you.

Mark Griffin (Central Scotland) (Lab): The block grant given to Scotland will be determined by the Office for Budget Responsibility and its forecasts, and it will then be reconciled with actual receipts. Will the data for the overall picture of the collection of the Scottish rate of income tax have to be gathered, to allow that reconciliation to take place?

09:45

Caroline Gardner: The information on the absolute level collected certainly will be. The question is whether there are differences in compliance levels in relation to outstanding tax—levels of bad debt—between Scottish taxpayers and rest-of-UK taxpayers that the committee may want to explore. They would not have a direct impact on the revenue in the year or on the reconciliation that was carried out, but they might be of interest to the Parliament in the context of the wider question of how the Scottish rate of income tax was being administered on its behalf by HMRC.

Mark Griffin: Do you think that it is appropriate that there could be an impact on the Scottish budget as a result of variances in collection performance between Scotland and the rest of the UK? HMRC does not have a line of accountability to this Parliament, which would be affected by such a difference in collection rates, so we would not be able to challenge the existence of differences in performance across the UK.

Caroline Gardner: I think that we heard yesterday from Mr Troup that the collection of the Scottish rate of income tax would be no different from the collection of income tax across the piece. Therefore, all of us would expect there to be no difference between collection or compliance levels for Scottish rate payers and collection or compliance levels for all other income tax payers. It would start to get interesting if there were a situation in which Scotland had tax rates that were different from those in the rest of the UK, which would mean that there might be different incentives for people to avoid or evade tax payment. Questions might also arise to do with the identification of Scottish taxpayers and the challenges that may come up as that develops. That is one reason why having the information is useful, although I suspect that, certainly in the transitional period, there is not a great likelihood that anything that is done by HMRC would affect

the levels of income that are available to Scotland during that period.

Mark Griffin: Yes, I think that you are right. As long as the rate of income tax in Scotland stays the same as the rate in the rest of the UK, there will not be issues, but if it is varied, there will be issues with collection. The question remains. If the rate is ever changed, is it an issue that HMRC does not have a direct line of accountability to the Parliament?

Caroline Gardner: That is why getting the reporting and accountability arrangements clear and agreed now is so important. Getting that done in advance of any potential problems arising is obviously preferable to trying to sort things out once there is a concern that needs to be addressed. We are dealing with a shared tax base, but different proportions of the tax revenues will come to the Scottish Parliament and to the UK Parliament. That is a new situation for all of us. The arrangements that are set out in the memorandum of understanding take us a long way towards resolving the issue, but there are a couple of things that could do with further agreement at this stage of the development of the new system.

Sandra White (Glasgow Kelvin) (SNP): Good morning. One of the questions that I asked yesterday was about the set-up costs of between £40 million and £45 million. Of that, £10 million will go into information technology. Audit Scotland produced a report on information and communication technology contracts, with which we have had a number of problems. The Scottish Government and the Scottish Parliament will be paying that money. What role will Audit Scotland have when the £10 million ICT contract is put out? When we asked what the remaining £35 million would be spent on, we were told that it would be spent on advertising, mailmerges, postage and so on. What input will Audit Scotland have in looking at that and ensuring that the Scottish Government gets value for money?

Caroline Gardner: The set-up and running costs are one of the areas in which the memorandum of understanding is very helpful in moving us on. I ask Mark Taylor to talk you through our current thinking in that area.

Mark Taylor (Audit Scotland): Our current thinking is that there are a number of options for how deep we can go in relation to those issues, some of which are straightforward from an audit perspective and some of which need further development of audit arrangements, as Caroline Gardner described.

At a simplistic level, we are talking about expenditure that goes through the Scottish Government accounts and which is subject to audit as part of those accounts, and we will

certainly look to audit it. Similarly, we will certainly look at the Scottish Government's arrangements for ensuring value for money, the provision of the right information, the right reporting and the right project management in those areas. Again, we would expect to do that as part of the audit.

Beyond that, we are looking at the opportunities for discussing with the National Audit Office how we can work with it to look in a bit more detail at available data and information on the basis of costing and charging. The challenge is that the circumstance is unique—there are no benchmarks and there is no competition with which we can make an absolute comparison on value-for-money grounds. However, in circumstances that we are used to in a number of areas, the issue is the arrangements that are set up and our ability to understand and audit them.

Sandra White: Caroline Gardner mentioned reporting on progress. We have a timescale, but we do not know when the contracts will be put out and we do not know how the money will be spent. Will Audit Scotland report on progress with that to the committee?

Mark Taylor: As part of the Scottish Government audit, we already have oversight of the progress that the Scottish Government and its partners are making to address the issue. We report to them on that progress. From that work arises the opportunity for us to report to the Parliament through a number of vehicles, when that would be appropriate and when there are issues to bring to members' attention. We will keep that under review and discussion with the Auditor General.

Colin Beattie (Midlothian North and Musselburgh) (SNP): Revenue Scotland has been mentioned briefly. Will you confirm whether Audit Scotland will audit the two taxes that revenue Scotland will collect?

Caroline Gardner: We do not yet know the detailed arrangements for collecting the devolved taxes. We know that revenue Scotland will be set up to oversee collection and that it will work closely with Registers of Scotland and the Scottish Environment Protection Agency. It is clear that, under my powers in the Public Finance and Accountability (Scotland) Act 2000, we will be able to appoint auditors to revenue Scotland, as we do to the two existing bodies, and that we will be able to audit the set-up and collection of taxes under those arrangements.

Colin Beattie: Perhaps we will get a rebate from the National Audit Office, as it will not have to audit that part of the business.

When I asked questions yesterday, it became clear that the Scottish accounting officer is not a

statutory post. Does that have significant implications for reporting to the Parliament?

Caroline Gardner: The issue is that the accounting officer comes under the UK legislation and has a reporting line to the UK Parliament, but not to the Scottish Parliament. The memorandum makes it clear that the Scottish Parliament and its committees can invite the additional accounting officer to give evidence and that the additional accounting officer will respond to such invitations, but there is no power to compel, and the officer will not have a direct accounting line to this Parliament in the way that Scottish accountable officers are accountable to it.

That position is an inevitable consequence of the shared income tax base with which we are working. However, the opportunity exists to clarify further in the agreements that are put in place how the arrangements will work and particularly what will happen in the event of disagreement, if that ever occurs.

Colin Beattie: To be absolutely clear, that means that, although the committee could ask the officer to give evidence, they would not be required to come and give evidence.

Caroline Gardner: It is clear in the memorandum that the committee will have the power to ask the officer to give evidence and they would be expected to respond, but there will not be a direct accountability relationship in the way that Scottish accountable officers are required to give evidence to the Scottish Parliament.

Colin Beattie: Yesterday, I asked questions about the £45 million cost of setting up the system. For the first time, I heard that £10 million of that would be IT costs. Do we know anything about the breakdown of the £45 million? I do not know whether Audit Scotland has been involved in that.

Caroline Gardner: At this stage, I do not think that we know much about that. All of us are working with the high-level estimates that were produced during the passage of the bill that became the Scotland Act 2012 earlier this year. Detailed planning started this calendar year to take that forward. Does Mark Taylor want to add to that?

Mark Taylor: I confirm that we have no great insight into the breakdown in detail. It was said yesterday that the figure is a high-level estimate, and the expenditure will have a number of components. We recognise that we would expect money to be spent on such things, but we have no information to share with the committee about the detailed amounts that are allocated to each aspect.

Colin Beattie: It seems that when it comes down to it, you do not have much information on

an awful lot of things to do with the arrangement that is being set up. I know that it is early days.

There is concern in the committee and elsewhere about the interface between Audit Scotland, HMRC and the NAO. I do not know what your relationship with HMRC and the NAO has been, but I hope that you are taking a proactive approach to engagement with those bodies, so that you can agree on a *modus operandi*. I do not know whether the Scottish Government has expressed a view on your involvement, other than in the memorandum of understanding.

Caroline Gardner: At this stage we are engaging closely with the National Audit Office and the Scottish Government, to understand how their thinking is developing and to play in our views about what is needed to ensure that the Scottish Parliament has the assurance that it needs.

We have not had direct contact with HMRC, because there is no statutory basis for our having such contact, but I am comfortable that our working relationship with the National Audit Office is close enough that we are not missing important factors. That is the next stage in developing the accounting and audit arrangements for the new powers, in line with the wider discussions that you are having.

Willie Coffey (Kilmarnock and Irvine Valley) (SNP): The Auditor General is being incredibly diplomatic, as ever. The memorandum of understanding does not give Audit Scotland the place in the process that I think we require it to have. I get the sense that Audit Scotland is being treated as an interested third party. However, its importance to the Scottish Parliament and the Scottish Government is such that its role should be far more clearly defined in the memorandum of understanding. Currently, the roles and relationships are not set out clearly and strongly enough. That is reflected in the many unknowns and questions about the lines of accountability for what is the principal body that does such work on our behalf. I do not know what members think, but that is certainly my view.

We have talked about set-up and administrative costs, and the Office for Budget Responsibility will make the first estimate of the reduction in the block grant. Will there be agreement on that, or will the OBR just make the decision? In such circumstances, it is important that there is agreement to proceed. The last thing that we want is disagreement between the two Governments on the set-up and running costs for the system and then on the reduction in the block grant, which could have a significant effect on the Scottish budget. In the absence of clarity at this stage, can we press for agreement to be reached, as

opposed to a decision being made by our UK partners?

I want to talk about the outcome of the referendum, whether it is a yes or a no. This is not a political point; it is a point for an auditor. There is a responsibility on both Governments to prepare the ground for both outcomes. The last thing that we want is for there to be a sense that money has been wasted. It is incumbent on the systems on both sides of the border to prepare for both outcomes, so that the public can be assured that money has not been wasted.

I do not know what the OBR's initial assessment will be. It could be £1 billion—none of us knows. Do you have an idea, Auditor General? It is important that we begin to discuss the issue, so that clarity can be brought to the table and there can be proper planning and decisions.

10:00

Caroline Gardner: You made a lot of points, and I will try to touch on each one. First, on audit powers, we think that the area needs further clarification in the memorandum of understanding. Work on that is developing well, but the two powers that could do with being clarified are, first, the level of detail required in HMRC's accounts on the Scottish rate of income tax and the revenue and costs that are associated with it and, secondly, the audit responsibilities of the NAO and Audit Scotland in relation to the two Parliaments who have an interest in the matter. It is early days, but further development could be useful in those areas.

You are absolutely right that there are two dimensions to the grant adjustment, and we must not lose sight of either of them. The first is the Scottish rate of income tax and the amount collected through it as we move through the transitional period into the steady state. The second is the impact of the OBR forecast, particularly in the transitional period. I do not have a view on the OBR forecast, and it is not something on which we would have a view, but the Parliament has a role in looking at how that will operate. The understanding between the Scottish Government and the OBR about how the process will work and any mechanisms that are in place for dealing with concerns about it is not covered by the memorandum of understanding, which is about the SRIT element of the adjustments, but it is also important.

Your fourth point was about the referendum in 2014 and the potential for further significant change on the back of that. I do not think that I can add anything to what Mr Troup said yesterday. We are preparing for something that is in legislation and that is coming. We have a significant

professional interest in ensuring that the arrangements are put in place and that we use the transitional period between now and 2016 to do that as well as possible. If further change takes place after that, that work will stand us all in good stead. However, for now, we need to prepare for what is currently in legislation.

Willie Coffey: Do we know when the OBR will make its assessment of the first cut to the block grant? When will that be in relation to the referendum outcome? Will it be after it?

Caroline Gardner: I think that it would have to be after it, in relation to anything other than what is currently in the Scotland Act 2012 and the framework that we are now working within.

Willie Coffey: Is discussion going on to agree what the cut will be, or is the OBR going to make the decision?

Caroline Gardner: The OBR has issued a paper on forecasting Scotland's taxes, but your question would be better directed to the Scottish Government panel that will be before you after this one.

Willie Coffey: I will do that. Thank you.

The Convener: Mrs Scanlon has a short follow-up question.

Mary Scanlon: It is a supplementary to Colin Beattie's and Willie Coffey's questions.

I hear what you are saying, Auditor General, about the level of detail and I heard what was said yesterday about the willingness to work together. I certainly would not like anyone to think that Audit Scotland is totally excluded and that we are not talking to you—that is not my impression. You said that you have been engaging with HMRC and the NAO and that you have very good relationships with them. Did you have any direct or indirect role in drafting the memorandum of understanding? Are there any aspects of the memorandum of understanding that you feel are inappropriate, unacceptable or unhelpful in the context of future good working relations?

Caroline Gardner: Our engagement has been with the NAO and the Scottish Government rather than with HMRC, and we have had a lot of discussion with both of them about the broad questions and the issues in the memorandum of understanding. The Scottish Government has invited our comments on the draft as it stands and we are happy to give it our detailed comments.

It is fair to say that there are no areas of the memorandum that we think are unhelpful or pointing in the wrong direction. The one set of comments that we will discuss with the Scottish Government is about the value of putting more flesh on the bones and the level of detail that is

required in HMRC's accounts and the audit arrangements.

James Dornan (Glasgow Cathcart) (SNP): We have talked a lot about the relationship between Audit Scotland, HMRC and the NAO. I agree with what Mary Scanlon said. Yesterday, Mr Morse made it clear that he would consult Audit Scotland and have a close working relationship with you. I also thought that he made it clear that the eventual decision will be in his lap and that whatever he decides is the outcome is the way that things will be. Given the importance of that to the block grant—and, therefore, Parliament's ability to do its job—how are you moving forward in your relationship with HMRC and the NAO, in particular? Do you have a timetable for reporting back to the committee and the Parliament what the outcome will be? Do you have a preferred outlook on how the process will finish?

Caroline Gardner: That is an interesting question. I took a slightly different view of what Amyas Morse said yesterday. First, it is unarguable that the responsibility and the statutory power to order HMRC lie with the National Audit Office, and that will not change. HMRC is a very big UK Government department and the NAO audits it. Further to that, however, the NAO is very willing to talk about a range of options for ensuring that the Scottish Parliament gets the assurance that it needs, including by working closely with us and potentially, over time, transferring some of the responsibilities for either doing the audit work or, more likely, reporting on how it works. How that would happen is still up for discussion.

We do not have a detailed plan for what needs to be in place by when, other than the annual cycles that we both have, which will determine by when we have to complete the audits and report to our respective Parliaments on the HMRC preparations, the Scottish Government preparations and how those are interacting. In many ways, we are keen for the memorandum of understanding and any other agreements that are required to make it as clear as possible what we both need to audit in exercising our responsibilities. It is worth being clear that, given the lead time for the Scottish rate of income tax, we are pretty well placed, but I am keen that we use the available time to pin down the things that matter before there is a live Scottish rate of income tax on which we need to give assurances to our respective Parliaments.

James Dornan: I appreciate what you have said. As I said, Mr Morse made it clear that he is willing to work closely with you. I was interested to hear you say that you feel that Audit Scotland might well have a place in auditing, as I did not get that impression from Mr Morse yesterday. I got the impression that, as you say, there is a statutory

responsibility and that, beyond that, information will be passed to you in some form, either through joint working or through a simple passing on of information.

Caroline Gardner: That is certainly the current statutory position. It came across clearly yesterday and I recognise it absolutely as being the status quo. What I heard from Amyas Morse was a real recognition, first, of the Scottish Parliament's interest in the Scottish rate of income tax as a significant part of the expenditure that you have available for public services in Scotland and, secondly, that things will continue to evolve. I think that at one point he used a vivid phrase about letting the dog see the rabbit, and I think that there is a recognition in there that the existing arrangements probably need to be developed a bit further to give you confidence that the Scottish Parliament's interests are being taken care of as part of the new tax collection arrangements.

I ask Mark Taylor to talk you through some of our existing ways of working with the NAO on a range of related, although not identical, sets of expenditure and what some of the options might be in the medium term—I stress that—as all of this evolves.

Mark Taylor: To pick up on the first point, it is worth while emphasising that we have pre-existing arrangements with the National Audit Office across a range of detailed audit work, and we work together to reach common outcomes. The committee will be familiar, as the previous committee was, with one of the strongest examples of that, which is around European funding and our work together with colleagues in the National Audit Office, and indeed the audit institutions of the rest of the UK, towards a single report and a single opinion on European funding issues. We have similar arrangements for the work to build up whole-of-Government accounts at a UK level, some work on forestry and work in a number of other areas.

The fact that we have those working relationships helps to illustrate where we might get to. We need to distinguish between who does the detailed work and has access to the information and evidence and how judgments are formed from that. We find it difficult to envisage a situation in which we would not in some way work in partnership with the National Audit Office on things such as how control systems work and the detail of the arrangements that are in place at HMRC. The NAO has the evidence on that and the understanding of it, and it would be an inefficient audit process if we did not try to make something of that. Even in the case of some of the more extreme examples—if I can use that phrase—of our involvement, we would look to use such information.

Broadly, a number of models are available to us, and Amyas Morse indicated yesterday his willingness to talk about those, subject to the underpinning in the agreement. The models involve different degrees of our involvement in undertaking work and making judgments, but under each of the models we would be keen to work in partnership with the National Audit Office and reliant on that to reach those judgments. Ultimately, as Amyas Morse said yesterday, that might involve the Auditor General making reports that are based on information that we have shared and gathered with the National Audit Office. We are not there yet, but that might be one outcome of the journey.

Tavish Scott: First, I apologise for having to leave earlier to attend a meeting of the Referendum (Scotland) Bill Committee, which was, though, commendably brief.

I will follow on from Mr Dornan's and Mr Coffey's thoughtful questions. First, on the OBR, given the Cabinet Secretary for Finance, Employment and Sustainable Growth's answer to a question last week in Parliament, my understanding is that the Scottish Government is investigating a MacOBR, as it were, though there will no doubt be a much more elegant title for it. Is Audit Scotland involved in that work? Is it too early yet to understand how that will play into the whole audit architecture, as it were, that we envisage arriving in the next few years?

Caroline Gardner: I will ask Mark Taylor to pick up on the detail of that, because as part of his audit of the Scottish Government he is very close to the overall preparations that the Government is making for implementation of the Scotland Act 2012.

Mark Taylor: On the broad question, I would start by distinguishing between the role that the OBR would play in a Scottish version of the OBR and the role of audit, because those are different things and I would therefore not anticipate that there would immediately be a role for audit. The question about the OBR is a valid one to which the Scottish Government is paying attention.

From our perspective, we would want to see some vehicle to consider and establish arrangements for forecasting and understanding what the impact on the economy is likely to be, and arrangements for the interplay between financial management and management of the economy, as well as a vehicle for doing that. As for what the preferred option for that would be, ultimately that will be a policy decision about how best to do it. However, certainly as we continue to talk to the Scottish Government and keep an eye on its progress, we will look to ensure that the capacity to do those sorts of things is built into its arrangements.

Tavish Scott: Thank you. My second point is on the answers that you gave Mr Dornan on the emerging relationship with the National Audit Office. We cannot have auditors auditing the auditors is what I guess you are driving at in that regard. Would that description be fair? The principle here is that there should be a proper audit of Government and public expenditure, and the principle should be the same in respect of tax. However, it is not your job or their job to audit one another, is it? We need to be clear about who is doing the auditing and then what the role is of the respective other part of the architecture.

Caroline Gardner: The latter point is spot on. The broad point is that there are all sorts of instances right across society and the economy where auditors place reliance on each other's work, for very good reasons, because there is no point in us all duplicating the same things. That is a good example that can work in this case to support the interests of both the UK Parliament and the Scottish Parliament. However, there is a bit more work to do to flesh out how that would work in practice.

Tavish Scott: Thank you. In that context, is Ms Scanlon's point correct in that Audit Scotland has a clear understanding of how that needs to work and what the lines of communication should be to allow it to occur? Or is it still too early to know precisely what the architecture—to use that word again—will look like?

Caroline Gardner: It is too early, partly because it is not yet clear what in fact any of us will be auditing. First, there is the question about what HMRC is required to account for in relation to the SRIT, which builds a little bit on the provisions in the draft memorandum of understanding. Then there is a discussion to be had between us and the NAO around what audit work is needed to audit that, what assurance is required by both Parliaments and what the right reporting lines are to cover that.

Tavish Scott: Great. Thank you.

The Convener: Mr Dornan has a follow-up question.

James Dornan: Further to Tavish Scott's point, the issue is not so much about who is auditing, because we trust that the NAO will do the job properly, but about reporting back to Parliament. Audit Scotland reports back to Parliament, so it is about the NAO's journey between getting the information and being able to report back on it to Parliament. That is the point that I was trying to make earlier.

Caroline Gardner: For the record, I absolutely recognise that. It is very clear to all of us in the NAO and Audit Scotland that both Parliaments have a real interest in the matter and that both

Parliaments need to have that interest satisfied. I think that we can fulfil those interests by working together in the way that I just outlined, but we do not yet have the detailed arrangements in place as a blueprint for how it would work. That is work that is still to follow.

The Convener: Thanks. I just want to round up and check my understanding of that exchange, then I will ask a question that follows on from it. What you are saying, Auditor General, is that there is no doubt that only the NAO has statutory access to HMRC to extract the necessary data and information but that, in your view, once that data has been extracted, it would be entirely possible and in line with the way in which you already work with the NAO for you to work with it to process the data and form a judgment from it. Is that right?

Caroline Gardner: Broadly, yes.

The Convener: My question then is: where would that agreement be assured? Would it be in the memorandum of understanding, or would you simply have an informal agreement with the NAO, as happens for forestry and the other areas to which Mr Taylor referred?

Caroline Gardner: I think that there would be real value in setting things out clearly in a document that was agreed between the parties. That could be done in the memorandum of understanding or in a side document related to it. There is the related minor issue of the statutory basis for both of us to do those reports in future to our respective Parliaments. However, I do not have a strong preference for where the agreement sits; the important thing is getting the clarity at this point in time rather than which particular document it sits in.

The Convener: Thank you very much indeed. That is very helpful.

I will suspend the meeting for five minutes for a change of witnesses and for the relief of the committee.

10:15

Meeting suspended.

10:22

On resuming—

The Convener: I welcome to the meeting our second panel: Alistair Brown, deputy director, and Jonathan Sewell, principal policy analyst, both from the Scottish Government's finance directorate.

Mr Brown, do you wish to make some opening remarks?

Alistair Brown (Scottish Government): With your permission, convener.

The committee might find it helpful to have a little background on our role. I am responsible for the Scottish Government's overall programme of work to implement the Scotland Act 2012's financial provisions in so far as the Scottish Government is responsible for them. Those provisions include the devolved taxes, the borrowing powers and our elements of the Scottish rate of income tax. We are working very closely with HMRC on preparing for the introduction of the Scottish rate of income tax; indeed, Jonathan Sewell has been particularly closely involved and sits on HMRC's project board, which is planning for the development and introduction of the Scottish rate.

With regard to the Scottish rate, we are obviously working within the detailed provisions in sections 25 and 26 of the 2012 act. I should point out that when we talk about estimated costs, I mean the estimates that the UK Government published back in November 2010 when the original Scotland Bill was introduced. As the committee has heard, the estimate for introducing the Scottish rate was—and remains—between £40 million and £45 million and between £4 million and £4.5 million a year from 2016 onwards for its operation.

As officials working in this area, we are aiming to ensure that there is a reliable system for collecting all the Scottish rate of income tax that is due; that we provide a good service to Scottish taxpayers; and that we do both at the lowest cost achievable, consistent with accurate and reliable tax collection and a good service.

We are also interested in and want to ensure the provision of adequate assurance and relevant information about the Scottish rate to this committee and to the Scottish Parliament. We are seeking to achieve that by working with HMRC at official level. As I said, Jonathan Sewell is a member of the project board, and I sit on a programme board that looks across all of the financial elements in the 2012 act. As members of the programme and project boards, we receive papers and proposed timescales and cost estimates, and we have the opportunity to ask questions about those and probe HMRC. The arrangements for doing that are under preparation but they are set out in the draft memorandum of understanding, of which the committee is aware.

Our key aim, as far as the set-up phase is concerned, is to continue to ensure that robust arrangements are in place for identifying all Scottish taxpayers and for keeping that database up to date—that is absolutely essential.

We aim to scrutinise costs to ensure that we understand HMRC's estimates and how they are composed, and any options for reducing those costs or for seeking additional features, which may cost more. All of that is within our scope.

We need also to understand what information will be available to us from HMRC's systems about Scottish taxpayers and the tax that they pay.

That is all in the set-up phase. All being well, from April 2016 we move into the operational phase of the Scottish rate. Our key aims there are to be able to monitor tax receipts; and to understand compliance activity that takes place in relation to the Scottish rate and any risks in respect of tax compliance and tax collection.

We will want to be able to track service levels available to Scottish taxpayers and obtain management information about the operation of the tax, all enabling us to track performance and service standards. One final point about the Scottish rate is that everything that we do and that HMRC does must be robust enough to stand the weight of the Parliament deciding to vary the Scottish rate, if it chooses to do so, away from 10p.

We are also involved in the work that was discussed earlier, on forecasting receipts from the Scottish rate, and in the work with HM Treasury on calculating the block grant adjustment. That all falls within our team's work.

I hope that the committee finds that helpful.

Mary Scanlon: I will be boringly predictable and ask the same questions that I asked earlier today and yesterday. It is about getting clarity now, and about the level of detail that it is reasonable, or unreasonable, to ask HMRC for. I have my little list here.

For example, is it reasonable to ask for progress on the set-up costs? Is it reasonable to ask specifically for tax compliance levels in Scotland and about performance in collecting Scottish taxes? Is it reasonable to ask for the level of error, fraud and write-offs among Scottish taxpayers?

We have been told that customer service performance is more at the UK level, so perhaps it is not entirely reasonable to ask about that. However, is it reasonable to ask HMRC about those four issues—set-up, compliance levels, performance and write-offs—in order to ensure that auditing and scrutiny arrangements are acceptable in future?

10:30

Alistair Brown: What I can certainly say to Ms Scanlon is that those are highly relevant questions. They all bear on the task of setting up a

system and collecting a Scottish rate of income tax.

To refer briefly to each question, the costs of set-up and progress on estimating those costs are key issues. In section 33 of the Scotland Act 2012, there is a requirement on both Governments to report to both Parliaments. That is shorthand, but the section lays the obligation of statutory annual reporting on progress with implementing part 3 of the act, which contains the financial provisions. Therefore, at least there is a statutory requirement that progress should be reported to the Parliament annually, and it would be safe for the committee to assume that the progress report would include estimates of costs and, in due course, costs incurred.

On the compliance effort, performance, errors, fraud and write-offs, the questions clearly relate to the period after 2016, when the Scottish rate would be collected. As I said, those questions are highly relevant. Detailed information on those matters is not yet available at this stage, but we would expect to follow up those issues with HMRC as the project progresses.

Mary Scanlon: I have two supplementary questions.

First, you said that my questions were highly relevant. Are there other highly relevant pieces of information that we should be asking for at this stage?

Secondly, given that Jonathan Sewell is on the project board at HMRC, is it wiser to ask for the level of detail while the systems are being set up in the next couple of years, rather than asking for them later on, when there could be a significant change and perhaps a significant increase in the cost of the system?

Alistair Brown: I will deal with the second question first.

I very much agree that it is sensible and wise to signal well in advance what management or accounting information we would find it helpful to have so that computer systems, for example, can be designed from the beginning to produce it. That is likely to be cheaper than it would otherwise be and provision would be much easier.

Your first question was whether there are other areas of information that it would be sensible to ask about. That gets us into quite detailed territory on tax and how it works. Once the tax is up and running, there will certainly be information that we will be interested in that is not directly related to the tax itself. Information about tax that has been collected and trends on tax collected over time gives, for example, an insight into the economy's performance. That is the kind of information that we will want to discuss with HMRC officials. We

will want to discuss having that fine-grained information available to us.

Mary Scanlon: That is about looking at the complete revenue figure and identifying trends rather than looking at the information that is required within the HMRC accounting process.

Alistair Brown: Yes, and it would relate to the aggregate of tax collected rather than to specific issues to do with compliance, errors or fraud.

Mary Scanlon: That is more on a macro level than a micro level.

Alistair Brown: You could say that.

Mary Scanlon: I think that you answered the question about the information technology systems. I do not know whether Jonathan Sewell needs to go into that.

Jonathan Sewell (Scottish Government): It is fair to say that, given the interest that the committee has shown in that matter, I will certainly bring it up and look at where in the process we need to address it. We are still at a very early stage in the project.

James Dornan: I have a couple of questions that are—I hope—connected. What role does the Scottish Government envisage Audit Scotland playing in relation to the Scottish rate of income tax? How will the Scottish Parliament be kept informed of any key decisions or significant changes to existing expectations in relation to the cost, timing or quality of the systems, aside from in the annual implementation report?

Alistair Brown: On your first point, Audit Scotland's role is under discussion with Audit Scotland. The committee's hearings yesterday and today have moved consideration of the issues forward. As Caroline Gardner said, there are important points to be discussed between Audit Scotland and the National Audit Office. The two are accustomed to working together, but not on the collection of tax. They are discussing the audit arrangements and Audit Scotland's role, and those discussions will develop further. The Scottish Government would defer to the Auditor General's view on the best arrangements. However, we want a high standard of assurance on which this committee can rely, and on which we can rely. We are at one on that.

Your second question was about arrangements for keeping the committee and the Parliament informed about progress on the Scottish rate project. In response to Ms Scanlon, I mentioned the statutory annual report. Obviously, it is for the committee to consider whether an annual report is adequate or whether it wants something more frequently. I am sure that Mr Swinney and officials will want to respond as best they can to requests for additional information.

James Dornan: I want to follow up on an issue that I raised with the Auditor General. Do you have any idea of the timeline for formalising the audit arrangements?

Alistair Brown: You would be taking me out of my area of knowledge if I tried to answer that. We will work closely with Caroline Gardner and her colleagues in the coming months to further refine the audit arrangements and the nature of the agreement that should exist between Audit Scotland and the National Audit Office. The obvious point is that the auditors—the NAO and Audit Scotland—are independent of Government, so we cannot tell them what to do, although we can certainly discuss with them what they plan to do.

James Dornan: Will there be a latest date by which the arrangement will need to be in place for everybody to feel comfortable about it? I add that I am not looking for the date.

Alistair Brown: From a purely technical point of view, the two sets of auditors will need to reach agreement before they finalise their audit plans for the first year in which the Scottish rate operates, but that is still some way in the future. I would think that, for other reasons, the two sets of auditors would want to have a written agreement—no, I will not anticipate what they arrive at. For other reasons, the two sets of auditors would want to have an agreement some time in advance of 2015, which is the year before the Scottish rate comes in.

Colin Beattie: One issue that arose at our meeting yesterday and that I raised with Audit Scotland earlier is that there seems to be little detail on the estimated £45 million cost. It seems to be a notional figure. Yesterday, we heard for the first time that £10 million is for IT and the rest of it is for various other things. There was a lack of clarity when I asked about the extent to which performance reporting costs and so on are incorporated. Does the Scottish Government have a breakdown of the figure?

Alistair Brown: The figures that we have are simply those that the UK Government published alongside the Scotland Bill in November 2010. As I said in my opening remarks, that estimate is now quite old, but it has not yet been updated. As Jonathan Sewell said, the project to introduce the Scottish rate of income tax is in its early stages. It is at the planning stage. One stream of work in the project is to develop more refined and accurate estimates of cost although, inevitably, the work of refining the cost estimates depends on the progress of the planning work. I should add that we are dependent on HMRC developing the cost estimates.

By the time that the first statutory annual progress report under section 33 of the Scotland Act 2012 is produced—which will be no later than the first anniversary of the enactment of the act, which will be in May 2013—we should see some development of the cost estimates. That is what I would expect.

Colin Beattie: The cost estimates that we have seen so far are purely those from the UK Government. Does the Scottish Government have any estimates for the costs that are being incurred, notionally or actually, on its side?

Alistair Brown: Are you referring to costs within the Scottish Government, as opposed to the costs incurred by HMRC that we will have to pay?

Colin Beattie: Yes.

Alistair Brown: The costs that we envisage in relation to the SRIT are the costs for people like Jonathan Sewell and me who must spend part of our time on the issue either sitting at our desks or travelling to London to attend project board meetings and the like. Those costs will be absorbed within the overall administration cost and will be subject to the controls that apply to that.

Colin Beattie: I have been asking about the role of the Scottish accounting officer, which is not a statutory post and so does not quite equate to what we know as an accountable officer. Do you envisage any difficulties because of that difference?

Alistair Brown: Are you referring to the additional accounting officer, Edward Troup, who appeared before the committee yesterday?

Colin Beattie: Yes.

Alistair Brown: As Caroline Gardner helpfully clarified earlier this morning, Edward Troup is appointed by HMRC's principal accounting officer, Lin Homer, whose formal accounting responsibilities are to the UK Parliament. As Caroline Gardner pointed out, what HMRC and the UK Government are saying is that, when asked to do so, Mr Troup will attend meetings of the Scottish Parliament and its committees and will answer questions. However, it is absolutely correct to say that there is no formal or statutory reporting line from Mr Troup to the committee.

Colin Beattie: Do you envisage that any difficulties or issues will be caused by that?

Alistair Brown: Provided that the work required to develop the Scottish rate of income tax project moves smoothly and that the tax itself, once operational, does not give rise to any major or unforeseen difficulties, I expect that the arrangements that have been set out should work and should work well. The committee will have its own view on its conversation with Mr Troup

yesterday. Difficulties tend to arise when things go wrong, and part of our job is to do our best to ensure that things do not go wrong.

Colin Beattie: The committee has recently taken evidence on information and communication technology projects, many of which have not gone particularly well. I assume that, certainly from the point of view of the Scottish Government's participation, those lessons have been learned and will be put to good use.

Alistair Brown: That is a very good point, which, as a public official, I strongly agree with. We followed with interest both the Audit Scotland work on ICT projects and the committee's hearings on that subject. What I can say that may be helpful is that, while the responsibility for developing the IT elements of the Scottish rate project lies with HMRC, we will be able to look at papers relating to the planning, commissioning and undertaking of that work. If we wish to do so, we will be able to ask our ICT colleagues in the Scottish Government to cast their eye over those papers, offer comments and help us to challenge or to probe. Perhaps Jonathan Sewell will be able to add something more on that.

Jonathan Sewell: I think that it is true that we will have full access to all the documentation of the project, so we can share any technical specifications with our procurement experts. There is an official dispute process for the IT costs, so issues can be taken to an external arbitrator to establish what the true costs are if there is any doubt.

10:45

The Convener: Mr Dornan, do you have a direct supplementary to the previous question?

James Dornan: I want to come back to something that Colin Beattie mentioned earlier, convener. We have a rough estimate of £40 million to £45 million for the cost of introducing the Scottish rate but, as has been said, it is kind of out of date. The Scottish Government has said that it will be responsible for any reasonable costs, but what if it decides that the costs are not reasonable? Who decides whether the costs are reasonable and what will happen after that?

Alistair Brown: In the case of a dispute over whether a cost is reasonable, Jonathan Sewell has made it clear that, with regard to the IT element, the draft memorandum of understanding sets out a process whereby we can commission a third party to check the IT costs quoted by HMRC's contractual partner. As a result, we have the opportunity to establish reasonableness in that respect. As for the balance of the cost that is non-IT, which amounts to £30 million, we as officials will look very carefully at cost estimates and break

them down—or ask HMRC to break them down—into items and rates to allow us to judge whether the proposal is reasonable. In the event that no agreement is reached between us and our HMRC colleagues at official level, the draft memorandum sets out an escalation process in which the issue can be discussed by ministers of the Scottish and UK Governments and a resolution reached at that level.

The Convener: Do you have a follow-up question, Ms White?

Sandra White: Yes, convener. Although paragraph 2.2 of the draft memorandum refers, as Mr Brown has suggested, to “independent assessment”, it also mentions the “additional cost” of such assessment. Who will pay for bringing in independent assessors if there is a dispute? Will it be the Scottish Government?

Alistair Brown: If we sought an independent assessment of costs, it would be at our initiative and HMRC would expect the Scottish Government to meet the cost. I refer Ms White to the second bullet point in paragraph 4.2 of the draft MOU, which refers to the

“Cost of any independent assessment”.

I understand from HMRC colleagues that these costs are not hugely high. They are measured in thousands of pounds, not tens of thousands.

Sandra White: I wanted to clarify that point, although I note that as the Audit Scotland report on IT contracts has made clear such assessments have sometimes cost not thousands of pounds but millions of pounds. I am not saying that that will happen, but my point is that, as the memorandum of understanding makes clear, if we are not happy with something or think that something untoward has been done or that there has been a mistake, the Scottish Government and the taxpayers of Scotland will have to pay for an independent assessment of the matter.

Alistair Brown: Just to be clear, I should point out that paragraph 2.2 and the second bullet point of paragraph 4.2 refer to the costs of bringing in an independent party to review the cost estimate that has been provided by HMRC or its supplier. In other words, if we felt that the cost was too high, we could have it reviewed. It would be a desk review by IT experts and, under these provisions, we would pay for their time.

Sandra White: We would still have to bear the costs of that. Moreover, if the IT system was found wanting, the Scottish Government would need to pay again.

The Convener: I think that Mr Brown has answered the question, Ms White.

Mark Griffin: Paragraph 6.3 of the memorandum of understanding states:

“Once SRIT becomes operational, HMRC will provide information to”

the Scottish Government

“in a form and at a frequency to be agreed throughout the ... year”

in relation to compliance, performance and so on. Is the format of that paragraph appropriate or should the memorandum of understanding set out in advance the form in which the information should be provided?

Alistair Brown: Are you asking whether we should set out in, say, an annex the precise information that will be required?

Mark Griffin: Yes.

Alistair Brown: That is a reasonable point. We have seen the draft memorandum of understanding as providing a framework within which a number of pieces of work will be undertaken over time. That is our and HMRC’s understanding of the task. From the point of view of flexibility and being able to respond to developing understanding and appreciation of what the requirements might be, I would prefer the memorandum to be maintained as a framework with scope for agreement to be reached on individual elements of the work within it. Nevertheless, I take the point and recognise that the committee may have a view on that.

Mark Griffin: The form of information will be important in allowing the Government to analyse compliance and performance. I do not know whether you heard my earlier question. I think that we have an issue with the accountability of HMRC to this Parliament. If its performance is lacking, that impacts on our budget. What would the Scottish Government’s position be if HMRC’s performance in collecting income tax was worse in Scotland than in the rest of the UK?

Alistair Brown: To some extent, that is a hypothetical question, so we must project our minds forward to when the tax is in operation. The first point to make, in agreeing with you, is that it will be important for us to have sufficient information about the operation of the Scottish rate to enable us to judge how well it is being implemented and how well the tax is being collected. Your substantive question was about what would happen if we thought that HMRC was not abiding by the provisions in the draft memorandum, which state that its compliance activity will be comparable, pound for pound. If the situation arose, that would be a matter for discussion with HMRC and would need plans for rectification.

Mark Griffin: I note from your previous answer that there is a dispute resolution provision in the paragraph relating to the set-up costs. Would it not be appropriate to include dispute resolution in paragraph 6, to cover the scenario that we have just talked about?

Alistair Brown: Excuse me while I remind myself what paragraph 4.6 says about dispute resolution.

You are right to point out that that paragraph relates to the set-up project for establishing the Scottish rate and does not refer to the on-going arrangements for running the tax. You make a fair point, and we will look into that. You must bear it in mind that this is a draft memorandum and we are all engaged in examining it and making sure that it is complete. We would be happy to look further at the issue that you have raised.

Mark Griffin: Thank you.

Tavish Scott: I would like to lead you back briefly to the evidence on IT that HMRC gave to the committee yesterday. I presume that you are familiar with HMRC's evidence on its confidence in its ability to run a successful IT system, its existing record and how that might compare with things that have gone wrong in a UK or, indeed, a Scottish sense. I take it that you are comfortable with the evidence that HMRC led yesterday.

Alistair Brown: As far as I am aware, it was factually accurate.

Tavish Scott: Quite. Thank you. I want to ask about reporting to this Parliament by the Scottish Government, which you mentioned earlier. Your helpful written submission to the committee mentions section 33 of the 2012 act, but I cannot find anything specific in the memorandum that relates to how the Scottish Government will report to the Parliament in any other way than through the annual report, which you correctly identified earlier. Is it your contention that it is up to us to make the case for what information we would like, how regularly we would like to receive it and so on?

Alistair Brown: Yes. The memorandum of understanding is a non-statutory agreement between the Scottish Government and HMRC concerning the framework to be placed around the development and operation of the Scottish rate, so it does not govern the kind of information that the committee or the Parliament as a whole would wish to see from us. We would want to respond to whatever requirements the Public Audit Committee might have, as we do in other contexts. I can think of several issues on which we are committed to providing half-yearly reports or copies of key documents to the committee. If you identified issues of that kind, we would want to respond as helpfully as we could.

Tavish Scott: Indeed. However, we are in new territory and this is the first opportunity that the committee, and indeed the Parliament, has to set out mechanisms to ensure adequate and appropriate scrutiny of Government—in this context, both HMRC and the Scottish Government. We need to know how best to design those mechanisms, so that they are not an onerous obligation on either side but so that adequate scrutiny is ensured. Do you accept that?

Alistair Brown: Yes, indeed. The committee might want to take the view of Audit Scotland on that issue, given its recent and highly relevant work on ICT projects in general.

Tavish Scott: Thank you. That brings me to my second point, which is the split, as it were, between the audit functions of compliance and the other areas that Mark Griffin mentioned, and the management information that—as you mentioned earlier—the Government wants to gain from the collection of the tax and what that means, economically. There is a difference between those areas of information. The second area would probably be for the Economy, Energy and Tourism Committee, rather than this committee, but that is not my point. My point is, how do we put in place mechanisms so that the information that the Scottish Government wishes to get from HMRC is also available to the Scottish Parliament?

Alistair Brown: One answer to your question is that if the information were available to the Scottish Government, it would obviously be available on request to the Public Audit Committee. It is worth saying that that would exclude any information from which individual taxpayers could be identified, although I do not think that anybody is thinking of that.

The Scottish Government will need information to satisfy itself that HMRC is collecting the right amount of tax, compliance work is being undertaken appropriately, arrears are being followed up and so on, and those are all issues on which we will need to derive comfort. We, too, will be looking at the audit work of the National Audit Office on the Scottish rate; we heard the Auditor General's comments on that.

As well as the UK Parliament and the Scottish Parliament deriving some assurance from HMRC's audit, we will be very interested in it. We will continue to work with HMRC officials to ensure that we understand the significance of its compliance and collection work.

Tavish Scott: That means that we will not have a recurrence of the situation that happened with the Scottish variable rate, when Parliament was not told that a very significant change had been made. From a parliamentary point of view, that was obviously a bit of a concern.

Alistair Brown: I am sure that Mr Swinney and his officials—including me—would be anxious to ensure that that did not recur.

Tavish Scott: That is very helpful. Thank you.

Jonathan Sewell: As part of the implementation project, HMRC colleagues are paying a great deal of attention to our deadlines and requirements for reporting to parliamentary committees. Although the project is at an early stage, that conversation is definitely taking place.

Willie Coffey: Having heard the conversations over the past period on the set-up costs and running costs, it seems that Scotland is being asked to sign a blank cheque. We do not know how much we will ultimately pay and we do not know when we will know that. That seems a precarious arrangement to have when we set out on this course of action.

Regarding the OBR issue and first assessment for the cut in block grant, is there any indication of what the value of that might be? From my reading, there is no agreement to reconcile any error in that assessment. If the suggestion is that in the event of an underestimate or overestimate the parties will take the benefit or the risk, it seems to me that an error would have a much more significant impact on the Scottish budget than on the UK Government. Why is there no agreement to reconcile the forecast with the actual receipts, perhaps in the following year?

Is there an indication of the value of the first cut? What are the Scottish Government's thoughts on agreeing on the value and on the possibility of reconciliation?

11:00

Alistair Brown: I will do my best to answer your questions. The OBR, which is independent of the UK Government, although it was set up by it, exists largely to produce economic and fiscal forecasts of the UK economy. The OBR produced—I think on 21 March this year—its first estimate of the tax receipts that would flow from the taxes that were set out in the Scotland Bill.

There is therefore a published report from the OBR that estimates receipts from the Scottish rate, assuming a 10p in the pound rate. It also estimates receipts from stamp duty land tax and the landfill tax in Scotland, which are being devolved and from the aggregates levy. The committee will want to be aware of that publication. I do not have a copy with me, but my recollection is that the OBR estimated the total take from the Scottish rate of income tax, if it were in place now, at £4.5 billion, which implies that a 1p rate would yield £450 million. Is that your recollection, Jonathan?

The Convener: The forecast for 2012-13 was £4.417 billion.

Alistair Brown: Thank you. The OBR also produced forward projections to 2016-17, and I think that the figure got to about £5.6 billion.

The Convener: It is £5.633 billion.

Alistair Brown: Thank you. Does that help to answer your question, Mr Coffey?

Willie Coffey: It takes us along the way, but let us imagine that there is a 1 per cent error in the forecast for 2012-13. That means that actual receipts would be £45 million shy of the line, from one side or the other, which could have a significant effect on what the Scottish Government could do. I do not understand why there is no agreement to reconcile. That could be done the following year, so that the figures balanced.

Alistair Brown: The arrangement for striking the block grant adjustment and then adjusting the adjustment is set out in the command paper, "Strengthening Scotland's Future", which was published in November 2010. In that paper, the arrangements for reconciling and adjusting the block grant adjustment are described in some—although not full—detail. We are working with Treasury officials on the detail of that and we will bring the work back to ministers for agreement in due course.

We envisage that the block grant adjustment for the first year will be struck on the basis of a projection, because of course there will be no actual outturn before the year begins. We will then allow the financial year to run. Actual receipts from the Scottish rate of income tax will not all be received in the year in question, because, for example, a self-assessment taxpayer does not fill in a tax return or pay the tax until up to 10 months after the end of the year to which the payment relates. Therefore, towards the end of year 2, we should have a reasonably accurate figure of the actual receipts. The proposition as set out in the UK Government's command paper is that the actual figure will then be compared with the forecast and a reconciliation will be carried out. By then it will be nearly three years after the beginning of the first year, and at that point there will be a further adjustment to the block grant adjustment, to take account of the reconciliation from year 1.

It is fairly complicated stuff, but it is accepted that, because of the difficulty of projecting receipts from the Scottish rate of income tax, there must be a form of reconciliation, at a point when that can be done accurately.

Willie Coffey: That is more encouraging than I had anticipated.

Tavish Scott: I have a small supplementary that follows on from Mr Coffey's question. The reconciliation that Mr Brown has eloquently described would go hand in hand with the year-on-year reconciliations that happen in Government accounting anyway, because of end-year flexibility. I well remember those from my time as a minister—it was agonising at the time. Is it fair to say that there is always uncertainty at the end of every financial year and that the new measures just add another degree of that?

Alistair Brown: Yes. The reconciliations and end-year flexibility to which you refer are to do with spending money, and the reconciliation that I attempted to explain is to do with income. It is good to keep the two distinct in our minds, but you are right to draw attention to the fact that there will be a degree of uncertainty in future once the taxes are established. There will be some volatility and uncertainty about the size of the Scottish block.

The Convener: Ms Scanlon has a supplementary question.

Mary Scanlon: I just want some clarity on an issue that I raised earlier. My understanding was that the basic system has been agreed between the Scottish Government and HMRC. The list that I gave earlier was of what I understood to be optional extras, such as work on performance, compliance and write-offs of tax. I apologise, because I should have read the Government's written submission before I asked the question and I am now slightly confused. On page 2, the second last paragraph, which is on compliance, states:

"HMRC will, once the SRIT system is up and running, conduct risk analysis and assessment, and compliance and anti-avoidance activity, on individuals"

in relation to Scottish taxpayers and others. Is that work included in what has already been agreed? My earlier question was about the level of detail that we need and what we should ask for. I apologise, because it seems that what I asked about has already been agreed, or am I confusing myself?

Alistair Brown: I simply flag up the distinction between the work that will be done, and which would have to be done by any competent tax authority—the business of compliance work, assurance, analysis and assessment, as set out in the passage that you read out—and the information that will be available to us about that as it applies to Scottish taxpayers. When we talk about the information that we would seek in order to satisfy ourselves that the work has been done, that gets down to a level of detail that we have not yet reached.

Mary Scanlon: We are asking about what information we need for Scotland to ensure that

we understand compliance, performance, write-offs and so on. My point is that the Scottish Government's submission is clear that, on compliance,

"HMRC will ... conduct risk analysis"

and so on. If HMRC is going to do that, and that will be unique to Scotland, it should be easy to give us the information. My point is that, on the issue that I asked about earlier, it now appears that that work is included in what has already been agreed, rather than an optional extra that we have to pay for.

Alistair Brown: It would be very easy to say yes. There is absolutely no doubt in my mind that the work must be done and that it will be done, as it states in the paragraph that you quoted.

Mary Scanlon: It says that it "will" be done.

Alistair Brown: Yes. Some of the work will be simply a continuation by HMRC of the compliance and assurance work on income tax that it does across the UK. However, some of that will be specific to Scotland, for example, in so far as it relates to the status of Scottish taxpayers. That is specific to Scotland. HMRC must and will conduct compliance and assurance work on that. As an example, it wants to check a sample of Scottish taxpayers every year to ensure that they remain Scottish taxpayers and that they are properly coded as such. That is an example of assurance work that will be specific to Scotland.

Mary Scanlon: My point is just that, according to your written submission, on compliance, the process seems to be further down the line than I had previously understood to be the case.

Alistair Brown: If I had had my wits about me, I would have drawn the committee's attention to that paragraph.

Mary Scanlon: If I had had my wits about me, I would have read it before I asked the question.

The Convener: If I had had my wits about me as convener, we would have finished 10 minutes ago.

We need to draw this session to a close. I thank Mr Sewell and Mr Brown.

11:10

Meeting continued in private until 11:27.

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