

TAX ADMINISTRATION AND CONSTITUTIONAL CHANGE IN SCOTLAND

Introduction

In this, the 10th year of the Scottish Parliament, a number of Constitutional alternatives for Scotland are now proposed, including the recommendations of the Commission on Scottish Devolution (the Calman Commission), full fiscal autonomy (referred to as “devolution max” in the Scottish Government’s *Fiscal Autonomy in Scotland* paper) and indeed complete separation from the United Kingdom.

This paper, prepared in consultation with HM Revenue and Customs and HM Treasury, considers some of the implications of these alternatives on the tax administration system in Scotland and what they would mean to real people and businesses in Scotland.

The main findings are:

- As part of the unified UK tax system, there is no need for Scottish businesses, individuals or HMRC to divide tax liability between Scotland and the rest of the UK in relation to any UK taxes.
- The Scotland Office estimate that **the tax compliance costs for Scottish business could double to more than £1bn** if a separate Scottish tax system was introduced, as would be necessary under fiscal autonomy or separation.
- Companies such as retail multiples purchasing, processing and selling goods across both jurisdictions would need to: comply with two different sets of rules for each tax collected and remitted to each administration; and establish the proportions of profits liable for Corporation Tax in each jurisdiction. Potentially, the compliance burden for cross border businesses would be duplicated for each tax.
- It is not possible to estimate the costs of creating and operating a separate Scottish Tax system as nothing is known of what taxes would apply and what the operational rules would be. By way of comparison, HMRC’s annual administrative costs are c. £4 billion. It is not clear if the ongoing operational costs of a separate system would be radically less than these running costs.
- One way of reducing some of the compliance cost to business of fiscal autonomy or separation would be to move away from a PAYE system and require individuals to self assess their own tax bills. This would be abandoning a key feature giving the UK tax system an advantage over many others in the developed world.
- The burden of complying with a separate tax system would fall disproportionately on business because, in addition to their own tax liabilities, they are responsible for withholding tax due from remuneration paid to their employees. It is estimated that 65% of Scotland’s exports are to the rest of the UK.
- No estimates exist of the rates of taxes that might be needed in Scotland under full fiscal autonomy or separation from the rest of the United Kingdom. The response to any divergence in tax rates in Scotland compared to the rest of the UK is not known. Scotland’s long term fiscal position, allied to the creation of new administrative costs, suggest that lower taxes are unlikely to be affordable

EXECUTIVE SUMMARY

Fiscal Autonomy and separation from the United Kingdom would require the creation of separate tax collection arrangements in Scotland with separate rules and rates.

HMRC is not structured to operate the UK tax system separately for Scotland and at present its role is legally confined to operating the UK tax system.

It is not possible to estimate the costs of creating and operating a separate Scottish Tax system as nothing is known of what taxes would apply and what the operational rules would be. By way of comparison, HMRC's annual administrative costs are c. £4 billion.

Business makes the physical payment for taxes that are additional to their own liability, so the burden of complying with a separate tax system falls disproportionately on business and on SMEs in particular.

PWC/World Bank research shows the UK tax system to be one of the easiest for business to comply with, ranking 16th out of 181 countries. Even so, the Scotland Office estimates that tax compliance costs to business in Scotland could be around £505 million per year.

Fiscal Autonomy or separation would have a significant impact on the tax compliance costs for Scottish businesses trading with the rest of the UK as they would have to comply with two tax administrations (UK and Scotland) and segregate Scottish transactions from those with the rest of the UK. Under these circumstances, total business tax compliance costs in Scotland would double, or more, and exceed £1 billion/year.

One way of reducing some of the compliance costs to business of fiscal autonomy or separation would be to move away from a PAYE system and require individuals to self assess their own income tax bills. This would abandon a feature that gives the UK tax system an advantage over many others in the developed world.

The KPMG "*Administrative Burdens: HMRC Measurement Project*" lists the specific elements of tax compliance that create the greatest burden on business. Of these, the top five are:

- 1. Issuing VAT invoices;**
- 2. Submission of quarterly VAT return;**
- 3. Income Tax return for self employed;**
- 4. Submission of customs declarations;**
- 5. Self Assessment of profits for the corporation tax return.**

TAXATION - ADMINISTRATIVE AND COMPLIANCE COSTS

Administrative and Compliance Costs have only recently been brought into mainstream academic analysis of tax systems. Administration costs refer to the costs to Government of establishing and operating all aspects of the tax system. Compliance costs are incurred by tax payers (both individuals and businesses) in complying with their tax obligations- they are not the same as the actual taxes paid. By way of example, under the UK system, a company would incur tax compliance costs by calculating and remitting to HMRC both its own tax liabilities and the cost of deducting income taxes etc from salaries and wages paid to its employees through the PAYE system.

THE UK TAX SYSTEM

Public Services and Taxation in the UK and Scotland

Most taxes in the UK are collected by HM Customs and Revenue (HMRC) with receipts accruing to the UK Consolidated Fund. Central government spending is determined by the allocation of budgets to individual government departments which have no linkages to where revenues were raised.

The budget available to the Scottish Parliament is part of this process in that the UK Government, via the Secretary of State for Scotland, transfers monies to the Scottish Consolidated Fund. The Scottish Parliament and Ministers then spend this money as they wish in order to deliver the public services devolved to the Scottish Parliament. These payments from the UK Government are sometimes known as the block grant, with year on year changes to the Departmental Expenditure Limit (DEL) calculated by the Barnett formula¹. Hence, the budget of the Scottish Parliament does not directly relate to Scottish tax receipts, aside from Non Domestic Rates and the effect of the unused tax varying power (the Scottish Variable Rate of +/- 3p).

The Scottish Government's *Government Expenditure and Revenue in Scotland* (GERS) publication estimates the taxes raised in Scotland and the totality of expenditure, both by the Scottish Parliament, and also by the UK Government both in and on behalf of Scotland. The nature of both the taxation and expenditure systems requires much of this information to be estimated as in particular most of the taxes, but also elements of UK Government expenditure, are not ascribed on a geographical basis. Over time, GERS suggests that the totality of public expenditure in and on behalf of Scotland exceeds the total of taxes raised. Offshore oil and gas taxation receipts are treated as assets of the UK as a whole, but if a geographical share of North Sea revenues is attributed to Scotland, a substantial deficit remains, estimated at £20 billion since 1980/81.

Tax Administration in the UK

HM Revenue and Customs (HMRC) is a non Ministerial Government Department formed on the 18 April 2005, following the merger of the Inland Revenue and HM Customs and Excise Departments.

HMRC collects and administers direct and indirect taxes, as well as paying and administering Child Benefits, Child Trust Fund payments, Child Tax Credits, Working Tax Credits and the Health in Pregnancy Grant. It is also responsible for the enforcement of the National Minimum Wage on behalf of the Department for Business Innovation and Skills. Its

¹ The allocated Departmental Expenditure Limit (DEL) is presently worth around £30 billion annually. Additionally, UK Government funds demand led expenditure devolved to Scotland- the Annual Managed Expenditure (AME) budget.

overall administration budget is around £4billion per year. In 2008/9, the total of taxes collected by HMRC amounted to £435.7 billion and it distributed around £35 billion in social protection payments.

HMRC employs around 85,000 people and has more than 300 offices and processing facilities across the whole of the United Kingdom including large centres in Bathgate, Cumbernauld, East Kilbride and Dundee who deal with diverse issues such as debt management and Tax Credits. In keeping with the nature of the UK's taxation and expenditure system, HMRC is structured around individual taxes and benefits, and not around supporting, say, VAT payments for one particular devolved country or region of England. This corporate structure enables HMRC to develop and concentrate specialism in particular taxes (the operation and administration of a number of taxes and the engagement with those liable often involves a high level of specialist knowledge- for example in relation to financial services) but not duplicating operations and creating administrative inefficiencies by having, say, a specialist VAT team in each devolved country and all 9 Government Office regions of England. In practice, this means that those who live, work or run businesses work in Scotland could have their tax affairs dealt with in a completely different part of the UK, and equally, many tax payers in England, Wales and Northern Ireland will have an element of their affairs managed from HMRC in Scotland.

What are the UK Taxes?

HM Revenue & Customs (HMRC) is responsible for administering the taxes set out in Table 1, below. This is from the Scottish Executive's GERS publication, and shows estimates of Scottish and the actual, out-turn, UK receipts for these taxes for 2007 - 08.

	(£ million)	UK	Scotland
Income tax		151,746	11,244
Corporation tax (excl North Sea)		40,017	3,465
Capital gains tax		5,267	299
Other taxes on income and wealth		2,764	244
National insurance contributions		95,510	7,766
VAT		89,878	7,972
Fuel duties		24,905	2,074
Stamp duties		14,123	908
Tobacco duties		8,031	923
Alcohol duties		8,215	718
Betting and gaming and duties		961	103
Air passenger duty		1,949	164
Insurance premium tax		2,311	195
Landfill tax		898	83
Climate change levy		705	65
Aggregates levy		340	52
Inheritance tax		3,890	269
UK Continental Shelf Taxes:			
Petroleum revenue Tax		1,680	
North Sea Corporation Tax		6,095	

Source: Scottish Government Government Expenditure & Revenue in Scotland

Table 1: Taxes Administered by HMRC- actual UK and estimated Scottish receipts 2007-08

Who Pays and What are the Compliance Costs?

Businesses are responsible for remitting to HMRC the majority of taxes in the UK. The IFS estimates that 92% of all HMRC operated taxes and 88% of all UK tax receipts were remitted by business in the UK in 2006-07.

The most recent quantification of the compliance costs placed on business by the UK tax system was completed by KPMG in 2006 in their “*Administrative Burdens: HMRC Measurement Project*”. This estimated that the total administrative cost imposed on businesses by the UK tax system was £5.1 billion per annum- see table 2 below. This figures was relatively low internationally, and since 2006 the Government has implemented or committed to measures that further reduce the burden by £540 million per annum.

Applying Scotland's proportionate share of the population of each size of business² allows an estimate of the total tax compliance costs in Scotland to be constructed, also depicted in Table 2 below.

Size of business (no employees)	0	1 – 9	10 - 49	50 - 249	250 +	TOTAL
UK Compliance Cost for HMRC taxes (£ million)	1,216	1,952	925	364	642	5,100
Scotland Compliance Cost for HMRC taxes (£ million)	70	150.5	73.9	38	173.9	506.4

Source: KPMG *Administrative Burdens: HMRC Measurement Project*, Scotland Office estimates

Table 2: Compliance costs of the tax System to Business in UK and Scotland

Independent analysis conducted by PriceWaterhouseCoopers and the World Bank suggests that the UK system is operationally one of the best in the developed world. In their 2009 “Paying Taxes” survey, the UK is ranked 16th out of 181 countries for “ease of paying taxes”, the highest placed of the G7 countries and - considerably above the United States (ranking = 46th), Canada (ranking = 28th), France (ranking = 66th) and Germany (ranking = 80th). Of the EU countries, only Ireland (= 6th), Denmark (= 13th) and Luxembourg (= 14th) had a higher ranking than the UK.

The same analysis also indicates that the overall tax rate for business in the UK is globally very competitive. PriceWaterhouseCoopers and the World Bank estimated that the total tax rate on business in the UK is 35.3% of taxable profits, lower than the US (42.3%), Canada (45.4%), France (65.4%) and Germany (50.5%).

² Data from Scottish Government's annual Scottish Economic Statistics publication

CONSTITUTIONAL ALTERNATIVES AND TAXES IN SCOTLAND

The choices considered are the status quo, the recommendations of the Commission on Scottish Devolution of June 2009 and those cited by the Scottish Government in their "*Fiscal Autonomy*" paper of January 2009.

The Status Quo

As stated above, central government taxes operate on a UK wide basis and are collected by HMRC. The Scottish Parliament does have a tax varying power, which enables it to vary the basic rate of income tax for Scottish taxpayers by 3p. The Scotland Act then provides for the additional administration costs incurred to be reimbursed from the Scottish budget.

As Scotland is part of the unified UK tax system, there is no need for businesses, individuals or HMRC to incur administrative or compliance costs for separate calculations or reporting of their tax liability in respect of income arising within Scotland and the rest of the UK.

The exception to this is in relation to the Scottish Variable Rate. The administrative consequences of this are that HMRC needs to maintain a record of all Scottish taxpayers, and if invoked, append an indicator (probably an "S") to the tax codes of those deemed to be resident in Scotland. Hence, if the SVR were to be invoked, there would be some administrative cost to HMRC which, in accordance with the Scotland Act and the agreed principles for funding devolution, would be met from the Scottish rather than HMRC budget. The extra field in employees' tax codes and the associated additional calculation would be associated with some additional compliance costs in relation to the PAYE system. There would be additional administrative costs in adapting the Income Tax self assessment regime to identify and record Scottish taxpayers. The overall administrative cost would be predicated on the level of compliance activity deemed necessary in respect of the SVR.

Tax Assignment

Tax assignment would involve the UK Government retaining control over defining the tax base and rates, but some or all of the taxes paid in Scotland would be earmarked or assigned to the budget of the Scottish Parliament. Both the Commission on Scottish Devolution and the Scottish Government's *Fiscal Autonomy* paper identified but largely rejected the assignment of taxes as an alternative means of financing the Scottish Budget.

The administration of any system of tax assignment is dependent on how the Scottish yields would be derived. As cited above, exact figures for the yield of UK taxes raised in Scotland are not available- the best information we have at present is in the GERS publication. A system of tax assignment dependent on the calculation of actual Scottish tax receipts would be administratively complex, potentially imposing significant compliance costs to any business or individual operating both in Scotland and the rest of the UK. For example, a means of defining how much of a company's Corporation Tax liability attributed to its operations in Scotland and how much relates to activity in the rest of the UK would be needed. The only realistic way of reducing these administrative and compliance costs would be for a system of tax assignment to operate on the basis of agreed formulae to estimate the taxes raised in Scotland, rather than the actual amounts.

Enhanced Devolution / Recommendations from the Commission on Scottish Devolution

Fiscal Autonomy in Scotland then suggests a system of what it terms "enhanced devolution". Rather than considering the speculative model therein, the Commission on Scottish Devolution's taxation recommendations are addressed. These are:

- the Scottish Variable Rate of income tax should be replaced by a new Scottish rate of income tax, collected by HMRC, which should apply to the basic and higher rates of income tax.
- the basic and higher rates of income tax levied by the UK Government in Scotland should be reduced by 10 pence in the pound, and the block grant from the UK to the Scottish Parliament should be reduced accordingly.
- Half of the income tax on savings and distributions should be assigned to the Scottish Parliament's Budget.
- The structure of the income tax system, including the bands, allowances and thresholds should remain entirely the responsibility of the UK Parliament.
- Stamp Duty Land Tax, Aggregates Levy, Landfill Tax and Air Passenger Duty should be devolved to the Scottish Parliament
- The Scottish Parliament should be given a power to legislate with the agreement of the UK Parliament to introduce specified new taxes that apply across Scotland.

The Commission on Scottish Devolution's final report was predicated on their perceived need to retain the current unified UK tax system, the Commission felt this was necessary in order to avoid impeding the constant trade in goods, capital and services with the rest of the UK. Additionally, the Commission envisaged that their primary recommendation on income tax could operate by exploiting systems already created to support the existing (unused) Scottish Variable Rate, although if this is the case, it would need to be extended beyond the basic rate of income tax. At the time of writing, detailed analysis is underway within Government in furtherance of the commitment to assess, and explore how to implement, these proposals³.

The Commission also selected four relatively minor taxes they considered suitable for devolution on the grounds that they considered them to relate to taxes on fixed, immobile bases for which the Scottish liability was, they felt, already to some extent determined (as for SDLT and partially for APD, Aggregates Levy and Landfill Tax). This would result, according to Calman, in any compliance and administrative costs associated with having a separate Scottish system largely already being met. The detailed assessment by Government of how to implement the Calman Commission's proposals will extend to these recommendations and the extent to which their analysis was accurate will be determined.

The Calman Commission also recommended assigning a share of income tax on savings and distributions, which the Commission portrayed as a pragmatic alternative to applying a separate Scottish income tax. The section above describes some of the administrative issues around tax assignment, but this again falls within the scope of the ongoing work within Government to assess, and explore how to implement, these proposals.

Devolution Max/ Full Fiscal Autonomy within the United Kingdom Independence and separation from the United Kingdom

Fiscal Autonomy in Scotland proposes two further constitutional forms: (full) Fiscal Autonomy within the United Kingdom and independence or separation from the United Kingdom. Common to both is that all taxes would be devolved to the Scottish Parliament. That is to say, the Scottish Parliament would need to firstly decide which bases it wished to tax, what the rules would be and what the rates would be. It would be responsible for the collection and the entire administration of these taxes.

³ Refer to Secretary of State for Scotland's written Ministerial Statement to the House of Commons of 15.06/2009

An inherent feature of full fiscal autonomy and separation is that the tax liability of businesses and individuals relating to activities in Scotland needs to be completely segregated from those pertaining to any activity elsewhere in the UK. From an administrative perspective, this would require new Scottish systems to be created and operated, the total cost of which would be dependent on the taxes chosen by the Scottish Parliament. Even if an identical tax regime was chosen to apply in Scotland, the structure of HMRC means that it is not equipped to operate a separate Scottish tax system, implying substantive costs would be incurred in developing and operating HMRC's capacity or the creation of a separate Scottish tax collection authority. It is not possible to estimate the costs of either of these actions because the tax policies that would be introduced are not known. By way of comparison, HMRC's annual administrative budget for all of the UK is around £4 billion—distinct from the capital costs of the creation of the required infrastructure and systems. The administrative costs of operating a tax system will reflect the inherent number and complexity of systems rather than being simply proportionate to the number of tax payers.

Both of these constitutional alternatives would require separate sets of rules for each and every tax levied by the Scottish Parliament and the UK Government. So companies such as retail multiples purchasing, processing and selling goods across both jurisdictions would then need to record what they were doing in each in order to determine their liabilities for VAT and Excise duties in each. They would need to comply with two different sets of rules for each tax collected and remitted to each administration. Similarly, such companies would need to establish the proportions of profits liable for Corporation Tax in each jurisdiction, whilst again complying with potentially different rules for each. Similar requirements would apply to companies withholding and remitting income taxes on behalf of employees on either side of the border in that they would have to meet not just potentially two different rates (as with either the SVR or the Calman proposals), but potentially different administrative rules and definitions. Potentially, the compliance burden for cross border businesses would be duplicated for each tax, although this could be marginally reduced by the Scottish Parliament not collecting income tax under PAYE type arrangements, but rather applying a universal self assessment type regime, although that is associated with higher administrative costs and higher levels of non compliance.

This same analysis applies to each and every tax, and as the vast majority of UK taxes are remitted by businesses, the greatest burden would fall on businesses rather than individuals, and especially, businesses operating across the border. It is not possible to quantify the number of businesses this would therefore impact upon, but it is estimated⁴ that 65% of Scotland's exports are to the rest of the UK. Even those only operating in Scotland would face an unchanged compliance cost only if the Scottish Parliament chose to apply exactly the same administrative requirements and operating systems for the taxes it chose to levy.

The KPMG "*Administrative Burdens: HMRC Measurement Project*" helps to explore this point further. It lists the specific elements of tax compliance that create the greatest burden on business. Of these, the top five are:

- Issuing VAT invoices;
- Submission of quarterly VAT return;
- Income Tax return for self employed;
- Submission of customs declarations;
- Self Assessment of profits for the corporation tax return.

Three of these top five cover taxes that a fiscally autonomous Scotland would have to apply to comply with EU law, so these specific administrative burdens could be doubled under fiscal autonomy for any business operating across the border with the rest of the UK. Number four on this list, the submission of customs declarations, might be invoked if

⁴ See Scottish Executive/Government experimental series in Scottish Economic Statistics 2007

Scotland separated from the rest of the UK, thus creating an entirely new compliance cost burden for any business trading with the rest of the UK.

Quantifying the precise increased compliance cost burden under fiscal autonomy or indeed in a separate Scotland is not possible as no details are available of the taxes that might be levied, other than some (such as VAT and fuel taxes) would need to be imposed at particular rates to comply with EU Law. But the need for businesses operating across the border with the rest of the UK to separate affairs between each tax jurisdiction would clearly create a significant and novel burden. Some firms will be unaffected in the long run, they will merely have to meet the compliance and regulatory needs of a new Scottish tax system. For others, the burden would require a separation of their affairs, which in itself would add a burden, as well as doubling tax compliance costs.

It is also the case that change creates uncertainty. KPMG noted that *“There is a strong theme that much of tax administration works reasonably well once it is certain and has been around for long enough for business to set up a smooth machine to deal with the requirements. What causes actual or perceived increased costs is change that interferes with the smooth machine”*.

Economic Efficiency and Competitiveness

Any divergence away from a unified UK tax system and the creation of a separate Scottish tax system could potentially have a major impact on the way firms operate, this is in part why the Commission on Scottish Devolution’s proposals require the detailed analysis ongoing at the time of writing. As well as adding significant compliance costs to any cross border business, significant departures from the UK unified tax system also create opportunities for individuals and businesses to arbitrage between the two jurisdictions to reduce their tax burden. In other words, it would create scope for economic inefficiencies as behaviours became influenced by taxes.

The Independent Expert Group supporting the Commission on Scottish Devolution considered the scope for a fiscally autonomous Scotland to engage in tax competition. In particular, they estimated that cutting the rate of a devolved Corporation Tax in Scotland from the current UK rate to the Irish rate of 12.5% would reduce revenues by £744 million annually. If this, and the long term evidence from GERS that Scotland spends more than it raises, is correct, then the affordability of significant cuts in corporation tax seems questionable, especially given the increased administrative costs associated with full fiscal autonomy or separation.

CONCLUSIONS

- The unified UK tax system offers significant administrative and economic efficiencies, in particular, to individuals and businesses operating across the border between Scotland and the rest of the UK. The taxation recommendations of the Commission on Scottish Devolution were predicated on preserving Scotland within this unified system.
- Separation and Devolution Max (an alternative term for full Fiscal Autonomy) involve the creation of an entirely separate tax administration for Scotland. The Scottish Parliament would have to determine which taxes it would apply at what rates, what the associated rules would be and how the taxes would be collected.
- HMRC is not structured to operate the UK tax system separately for Scotland and at present its role is legally confined to operating the UK tax system. Separation from the United Kingdom would require the establishment of a new Scottish tax collection authority. The establishment costs of doing so are not known, but it is not clear if the ongoing operational costs would be radically less than the £4 billion/ year for HMRC which covers all of the UK.
- The creation of separate Scottish tax regimes required by full fiscal autonomy or the separation from the rest of the United Kingdom would especially impact upon individuals and businesses operating across the border with the rest of the UK. Income, profits, sales and purchases of goods liable to VAT and excise duties, share transactions, insurance premia, and national insurance contributions and every other tax would all need to be attributed and recorded separately between operations in Scotland and the rest of the UK.
- At the same time, individuals and businesses operating in Scotland and the rest of the UK would need to comply with two, rather than one, tax legislatures and the associated regulations. Any departure from the status quo itself creates cost and uncertainty.
- Business has a pivotal role in the operation of the UK tax system - an estimated 92% of all HMRC taxes are remitted by business. The Scotland Office estimates that the total tax compliance costs borne by business in Scotland are to the order of £505 million annually. The nature of tax compliance means these costs are highest for SME's.
- The increased tax compliance costs of full fiscal autonomy or separation would impact on businesses foremost. Businesses trading solely within Scotland would be relatively unaffected, beyond having to adapt to change. Others could have tax compliance costs more than doubled as they would have to comply with two tax administrations (UK and Scotland) and segregate Scottish transactions from those with the rest of the UK. This could double the overall tax compliance burden to Scottish business to over £1 billion.
- No estimates exist of the rates of taxes that might be needed in Scotland under full fiscal autonomy or separation from the rest of the United Kingdom. The response to any divergence in tax rates in Scotland compared to the rest of the UK is not known. Scotland's long term fiscal position, allied to the creation of new administrative costs, suggest that lower taxes are unlikely to be affordable.

GLOSSARY OF TAXATION TERMS

ADMINISTRATIVE COST

The cost incurred by tax authorities in establishing and operating systems to manage all aspects of taxation

COMPLIANCE COST

The cost to tax payers of complying with their tax related obligations, including actions by third parties involved in, for example, remitting payments on behalf of others.

PAYE

UK system of employers withholding income tax and remitting to HMRC associated with small compliance and administrative costs and covering around 80% of income tax revenue.

REMIT

To transmit funds to the tax authority. This is distinct from being liable for taxation. For example, employees are liable for Income tax, but under the UK's PAYE system, their income tax payments are withheld by employers who remit them to HMRC

SVR or SCOTTISH VARIABLE RATE

The existing tax varying power of the Scottish Parliament, defined in the 1998 Scotland Act as up to +/- 3p variation in the basic rate of income tax in Scotland.

TAX AVOIDANCE

The act of legally minimising tax liability.

TAX BASE

The activities on which taxes are levied, so for direct taxes, this relates to incomes, for indirect taxes, this relates to transactions. To operate a tax system, the tax base needs to be tightly and legally defined. For example, to tax income, a definition of which incomes are subject to taxation is needed. To tax company profits, a definition is needed of profit.

TAX EVASION

The act of illegally avoiding paying tax

TAX RATE

The level of taxes applied to particular tax bases. So for corporation tax, the tax base is the definition of profit, the rate is the % in the £ of that taxable profit.

WITHHOLDING TAX

Tax that is collected at source and remitted directly by a 3rd party, before the taxpayer has seen the income or capital to which the tax applies. In other words, that part of the income or capital due in tax is withheld from the taxpayer, who therefore cannot easily avoid paying the tax. Examples in the UK are income tax withheld and remitted by employers on behalf of employees and income tax on bank interest withheld and remitted by financial institutions.

KEY REFERENCES

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