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AUDITOR GENERAL

16 January 2026

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Convener
Public Audit Committee
Scottish Parliament
Edinburgh
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Dear Convener

In 2014, the predecessor Public Audit Committee of the Scottish Parliament recommended that the Auditor General for Scotland should provide additional assurance on the National Audit Office's (NAO's) audit work on Scottish income tax. This letter to the Public Audit Committee addresses that recommendation.

The Scotland Act 2016 extended the Scottish Parliament's power to vary all income tax rates and thresholds to the non-savings, non-dividend (NSND) income of Scottish taxpayers. The power to determine any reliefs or exemptions, including the personal allowance, remains with the UK Government. From 2017/18 onwards, the total amount of NSND income tax, now referred to as Scottish income tax, collected by HM Revenue and Customs (HMRC) in Scotland is paid to the Scottish Government.

The Comptroller and Auditor General (C&AG) issued his qualified opinion on the 2024/25 HMRC annual report and accounts in July 2025. The qualifications relate to the levels of error and fraud within reserved areas and do not impact on the administration of Scottish income tax.

In November 2025, I published a report on Financial sustainability and taxes. It explored the opportunities, risks and challenges of using tax as a lever to achieve fiscal sustainability and assessed how well the Scottish Government is managing these. It also includes more detail on how taxes operate in accordance with the Fiscal Framework, including the role of budget reconciliations.

Background

HMRC collects and administers Scottish income tax on behalf of the Scottish Government as part of the UK's overall income tax system. This includes separately identifying the amounts that relate to Scottish taxpayers. The Scottish Government is responsible for:

- reimbursing HMRC for the cost of implementing Scottish income tax

- ensuring that the cost of implementing Scottish income tax represents value for money
- seeking assurances that the system collects the correct amount of tax
- discussing and agreeing with HMRC aspects of the approach to the administration of Scottish income tax as set out in a Service Level Agreement.

The amount of Scottish income tax collected each year is identified separately in HMRC's annual report and accounts. The NAO report relates to 2024/25 and includes the final outturn calculation of Scottish income tax for the 2023/24 tax year. This outturn is used in the reconciliation that is applied to the Scottish budget for 2026/27.

The NAO's report also covers HMRC's provisional estimate of Scottish income tax receipts for 2024/25. This provisional estimate does not affect the Scottish budget, with the final outturn for 2024/25 expected to be reported in summer 2026.

Overall conclusion

The C&AG made his eleventh annual report to the Scottish Parliament on 16 January 2026. I requested Audit Scotland to consider:

- the NAO's approach to identifying the key risks to the successful administration of Scottish income tax
- the NAO's audit working files, with focus on the audit evidence underpinning the key findings and conclusions in its report
- the NAO's arrangements for ensuring the quality of the audit work and reporting.

The review was limited to consideration of the NAO's audit work; it did not directly assess the evidence obtained from HMRC and did not discuss any matters directly with HMRC.

The judgements and conclusions set out in the C&AG's report are his alone, based on the audit work undertaken by the NAO on his behalf. Based on Audit Scotland's review, I am satisfied that the NAO's approach was reasonable and that its audit work covered the key audit risks. I am also satisfied that the findings and conclusions in the C&AG's report are reasonably based.

Correctness of the sums brought to account

2023/24 final outturn

The C&AG concludes that Scottish income tax revenue outturn for 2023/24 is fairly stated.

The 2023/24 outturn calculation of £17,093 million is largely based on established tax liabilities, after the tax owed has been finalised and the taxpayer records have been reconciled. HMRC makes adjustments or estimates where it has not yet finalised the tax due, or where it must estimate the Scottish share of uncollectable amounts or tax reliefs. The reduction in Scottish income tax outturn arising from these adjustments was £115 million. The methodology used to arrive at these adjustments was agreed between the Scottish Government and HMRC. The C&AG notes that this methodology has remained broadly the same since the prior year.

The C&AG notes that in Scotland, the outturn for 2023/24 represents an increase of 12.7 per cent compared with 2022/23 (£17,093 million compared to £15,169 million). The outturn for non-savings, non-dividend income tax for the rest of the UK increased by 10.1 per cent. HMRC attributes the higher growth in revenue from Scottish income tax in 2023/24 to the increase in higher and top rates in Scotland, while rates in the rest of the UK stayed the same.

In his report last year, the C&AG stated that between 2016/17 and 2021/22, HMRC had double counted PAYE liabilities where PAYE taxpayers had also submitted unsolicited self-assessment returns. This led to HMRC overstating the Scottish income tax outturn by an average of £78 million per year. As such, the Scottish budget should have had undergone a further negative reconciliation of £29 million to account for this. I note that this year the Scottish Government and HM Treasury remain in discussion as to any adjustments that may be required.

2024/25 provisional estimate

The C&AG concludes that HMRC’s approach to establishing the provisional estimate is reasonable. HMRC’s provisional estimate is for reporting purposes and does not affect the Scottish budget. Instead, the Scottish budget uses forecasts provided by the Scottish Fiscal Commission (SFC).

I note that the Scottish Fiscal Commission’s most recent forecast for 2024/25 Scottish income tax receipts is £18,844 million which is broadly in line with HMRC’s provisional estimate of £18,967 million (a difference of 0.65 per cent).

Adequacy of HMRC’s rules and procedures and compliance with these

The C&AG concludes that 'HMRC has adequate rules and procedures in place to assess and collect Scottish income tax and that these are being complied with’.

The administration of Scottish income tax is governed by a Service Level Agreement (SLA) between HMRC and the Scottish Government. This is updated every year to reflect HMRC’s planned work. The SLA sets out the requirements and performance measures for the operation of Scottish income tax. HMRC shares the results of assurance exercises and compliance activities with the Scottish Government throughout the year and publishes an annual summary of its performance against the requirements.

Scottish Tax Base

Accurate identification of Scottish taxpayers remains fundamental to the effective operation of the Fiscal Framework, to the size of the Scottish budget and in ensuring that the right amount of tax is collected from individuals.

The C&AG reports that HMRC carries out several assurance activities to maintain the completeness and accuracy of the Scottish taxpayer population. This includes a series of checks on HMRC's records of Scottish taxpayers. Third-party data checks (where taxpayer address records held by HMRC are compared with third-party data sources) is the main source of assurance over HMRC's address information.

Last year I noted that the completion of additional third-party checks on an annual basis was a positive development, albeit that the results were not published in time for inclusion in the report. This year I note that the data has been published in time for inclusion in the NAO report, which is welcome.

The C&AG has reported that HMRC was able to successfully match 72.2 per cent of address records through the 2025 third-party data check exercise. This was a slight increase from the 2024 result of 71.7 per cent. HMRC reviewed the records that could not be verified with third-party data and checked them against its internal sources. This enabled HMRC to match 95.12 per cent of the records to a Scottish address (94.96 per cent in 2024). I note that HMRC is working with the third-party data provider to explore ways to access third-party addresses and potentially correct more mismatched records. I would encourage the Scottish Government to continue discussions with HMRC on this matter, to give further assurance over the remaining records that have not currently been matched.

Third-party data checks are currently run annually. HMRC and the Scottish Government agreed in 2024 that they would return to undertaking the third-party data assurance exercise every two years if there are fewer than 15,000 address records where the residency data held by HMRC does not match the residency suggested by third-party data. The C&AG notes that in each of the last three years the records identified have been less than the agreed threshold. The C&AG notes that although the 2025 number mismatched is below the agreed threshold, the schedule for the next data assurance exercise is not yet confirmed. HMRC and the Scottish Government will decide in February 2026 whether to commission an additional annual exercise in 2026 or revert to the biennial timing with the next exercise in 2027.

Compliance activity

HMRC continues to assess compliance risk for Scottish taxpayers in the same manner as it does for the entire UK taxpayer population; through its Strategic Picture of Risk (SPR). Scotland's share of the estimated revenue lost through non-compliance and revenue gained through enforcement and compliance activities continues to be calculated based on a proportion of the UK figure, rather than using Scotland-specific data. HMRC did not identify any compliance risks in its SPR specifically relating to Scotland.

As noted in last year's report, unlike the income tax system which can flag Scottish taxpayers, HMRC's compliance system cannot readily identify people living in Scotland. The C&AG notes that HMRC has discussed internally the possibility of adding Scottish identifiers to the compliance system, but it had not progressed this as it did not identify a clear benefit. The Scottish Government may wish to consider discussing this with HMRC, including determining the costs involved, as well as the potential benefits of having improved compliance data. This could have future value, given the increased tax divergence since 2023/24, as an additional tool to support better understanding of compliance risk.

Last year I highlighted that the Scottish Government and HMRC had set up a compliance working group, which had been directed by the Scottish Income Tax Board to evaluate HMRC's approach to compliance in Scotland. The group has not identified any significant additional compliance risk to date, with the C&AG highlighting analysis of online discussion on tax avoidance, and engagement with wealthy individuals as examples.

The C&AG notes that the evaluation work of the Scottish Income Tax board is ongoing, and that the Scottish Government and HMRC have shifted focus towards the possibility of producing a Scottish income tax gap. This would estimate the difference between the amount of tax that should be paid by Scottish taxpayers and what is actually paid, allowing a better quantification of compliance risks. This would cost at least £5 million annually to produce.

The C&AG reports that in April 2025, HMRC produced a Scotland-specific estimate of tax debt of £2.4 billion, around six per cent of UK tax debt. This is lower than Scotland's seven per cent share of the total UK income tax revenue estimated for 2024/25.

The C&AG concludes that HMRC has adequate rules and procedures in place to assess and collect Scottish income tax, and that devolved tax issues are being complied with.

I have previously raised both in last year's additional assurance report and in my November publication on financial sustainability and taxes that there is a time lag between tax years and when outturn information is available. HMRC's assessment of compliance draws on insights gathered through compliance investigations which typically apply to tax liabilities from two years previous. This means that any increased risk from diverging tax policy such as the introduction of the new advanced rate band in 2024/25 may not be apparent until 2026/27 at the earliest.

The C&AG highlights the importance of HMRC reviewing its compliance strategy to ensure a coherent, well-planned approach is in place to address potentially changing compliance risks. Specifically, he recommends that with the introduction of the advanced tax rate band, HMRC should complete its planned evaluation of the Scottish compliance approach as soon as possible, so it can identify areas for improvement and prioritisation. This should include a clear plan of actions and deadlines for delivery for the evaluation. I agree that this is important, given the increased tax policy divergence since 2023/24, and that the Scottish Government should work closely with HMRC to consider where further Scottish-specific data or other initiatives would give further assurance and to help inform future decisions.

The accuracy and fairness of the administrative expenses

The C&AG notes that ‘based on our audit work, we have concluded that the amount paid by the Scottish Government (for the year ended 31 March 2025) was accurate and fair in the context of the agreement between HMRC and the Scottish Government’. HMRC invoiced the Scottish Government for £1.2 million of costs relating to the administration of Scottish income tax in 2024/25 (£1.0 million in 2023/24). Of this amount, £0.5 million (2023/24 £0.6 million) related to running costs and the remaining £0.7 million was for the implementation of the advanced rate of Scottish income tax.

I trust the above information is useful, and I am happy to engage further on any specific points raised if that would be helpful to the Committee.

Yours sincerely

Stephen Boyle

Auditor General for Scotland