From: [Redacted]
Sent: 16 May 2018 15:09
To: [Redacted]; Grisewood A (Aidan); **[Redacted]**; Fuller S (Simon); **[Redacted]**
Cc: [Redacted] Ireland J (John); **[Redacted]**
Subject: OFFICIAL SENSITIVE – Final Forecasts and Fact-check – Income Tax – May 2018

All,

In accordance with the Protocol, the Commission is now formally sharing our final forecasts with the Scottish Government and sharing our report for fact-checking purposes. Please find below the final forecast for Income Tax – this has remained unchanged since R3. In the absence of a significant QA issue this forecast will not change.

Non-Savings Non-Dividends income tax outturn and forecast

£ million	2015-16 Outturn*	2016-17	2017-18	2018-19	2019-20	2020-21	2021-22	2022-23	2023-24
	10,948	11,267	11,467	11,969	12,345	12,805	13,335	13,936	14,547

The Scottish Government is invited to confirm the factual accuracy of the report, accompanying spreadsheets and the presentation of Scottish Government policy. As per the protocol we require any comments to be received by the end of Monday 21st May. For ease we are sending the report in sections directly to the relevant teams, please ensure that all relevant people in the Scottish Government are included on this copy list and have sight of the report.

This report and forecasts are being shared strictly for the purposes of commenting on the factual accuracy of the report and for the development of the Scottish Government's Medium Term Financial Outlook. The report and forecasts contains Scottish Fiscal Commission assumptions and determinants that are classified as OFFICIAL-SENSITIVE until the time of publication, they must be protected at all times and must not be shared beyond those requiring access for the purposes of fact-checking.

Please note that the report is still being finalised and the Commission retains the right to change any element of the report. In particular, the 'Uncertainty' section within the draft chapter still has to be drafted. As per the protocol the report will be shared with the Cabinet Secretary for Finance and the Constitution on Thursday 24th May. A final pre-release version will be shared with the Cabinet Secretary on Wednesday 30th May and the final version of the report will be published on Thursday 31st May.

<< File: DRAFT - Scotland's Economic and Fiscal Forecasts - May 2018 - Chapter 3 - Income Tax - 180516.docx >> << File: DRAFT - Scotland's Economic and Fiscal Forecasts - May 2018 - Chapter 3 - Income Tax - Charts and Tables - 180516.xlsx >> << File: DRAFT - Scotland's Economic and Fiscal

Forecasts - May 2018 - Annex B - Charts and Tables - 180516.xlsx >> << File: DRAFT - Scotland's Economic and Fiscal Forecasts - May 2018 - Annex B - Income Tax - 180516.docx >> << File: DRAFT - Scotland's Economic and Fiscal Forecasts - May 2018 - Chapter 3 - Income Tax - Supplementary Tables.xlsx >>
We will also cover Income Tax in the summary section of the report, this is still in development as we work on the overall narrative of the report. We will provide this separately for fact-checking on the 22nd May, and invite comments on factual accuracy back from the Scottish Government by the morning of the 24th May. The final version of the report will be provided to the Cabinet Secretary for Finance and Constitution in the afternoon of the 24th May.

[Redacted]

From: [Redacted]
Sent: 21 May 2018 18:08
To: [Redacted] Grisewood A (Aidan); **[Redacted]**; Fuller S (Simon); **[Redacted]**
Cc: [Redacted] Ireland J (John); **[Redacted]**
Subject: RE: OFFICIAL SENSITIVE – Final Forecasts and Fact-check – Income Tax – May 2018

[Redacted]
Many thanks for sharing your draft of the income tax chapter for fact checking purposes.

With many thanks to colleagues for their contributions, please find attached our factual comments.

<< File: MTFS - forecasts - Final and Fact-check - Income Tax - 16 May 2018.docx >> << File: Income Tax - MTFS - Correspondence - SPI vs outturn note - SG comments.docx >> << File: DRAFT - Scotland's Economic and Fiscal Forecasts - May 2018 - Annex B - Income Tax - SG comments.docx >>
In our previous discussions, we also highlighted the need to explain the revisions to the income tax forecasts, and what is driving them, and Figure 3.1 is very useful in this context.

In order to further improve the transparency of the report, you could also consider breaking down the impact of the "economic determinants" into i) employees and ii) average earnings. This follows the approach taken by the OBR in their report (see table 4.9 in the latest EFO) and would make it easier for readers to link back to the economy chapter.

[Redacted]

From: [Redacted]
Sent: 22 May 2018 18:40
To: [Redacted] Grisewood A (Aidan); **[Redacted]**; Fuller S (Simon); **[Redacted]**
Cc: [Redacted] Ireland J (John); **[Redacted]**
Subject: RE: OFFICIAL SENSITIVE – Final Forecasts and Fact-check – Income Tax – May 2018

[Redacted]

Many thanks for the comments – we will be reviewing. For fact-checking purposes I also attach two additional sections drafted for the income tax section: Sensitivity Analysis and Comparison to Block Grant Adjustment. I'd be grateful for any comments by 17:00 tomorrow.
<< File: Scotland's Economic and Fiscal Forecasts - May 2018 - Chapter 3 - Income Tax (Sensitivity + BGA).docx >>
[Redacted]

From: [Redacted]
Sent: 23 May 2018 16:55
To: [Redacted] Grisewood A (Aidan); **[Redacted]** Fuller S (Simon); **[Redacted]**
Cc: [Redacted] Ireland J (John); **[Redacted]**
Subject: RE: OFFICIAL SENSITIVE – Final Forecasts and Fact-check – Income Tax – May 2018

[Redacted]

Many thanks for providing the two additional sections. Please find attached some comments from Steven, Andrew and myself.

Any questions, please let me know.

[Redacted]

Chapter 3
Tax

3.1 This chapter presents the Scottish Fiscal Commission's tax forecasts. A summary of the forecasts is shown in Table 3.1 below.

Table 3.1 Summary of Tax Forecasts 2017-18 to 2023-24

£ million	2017-18 Outturn*	2018-19	2019-20	2020-21	2021-22	2022-23	2023-24
Income Tax	11,467	11,969	12,345	12,805	13,335	13,936	14,547
Non-Domestic Rates							
Land & Buildings Transaction Tax							
of which, Residential							
ADS							
Non-Residential							
Air Passenger Duty							
Scottish Landfill Tax							
Total Tax							

Source: Scottish Fiscal Commission, * Figure for Income Tax is not outturn data, as none is yet available for liabilities in 2016-17. See the income tax section for further detail. Figures may not sum to totals because of rounding

3.2 In the following sections, each tax will be examined in turn. The sections will explain the methods used to produce the forecasts, the differences from earlier forecasts, the impacts of any new policy measures, and comparisons to OBR forecasts.

Box 3.1 OBR forecasts of devolved taxes

Box 1.2 explains the operation of the Fiscal Framework, and the respective roles of the Scottish Fiscal Commission and the OBR.

The OBR also produce forecasts of receipts from devolved taxes, not because this is a requirement of the Fiscal Framework but rather because their role as the UK-level fiscal forecaster requires them to produce forecasts of all revenue streams raised in the UK, whether they are set and administered by the UK Government, Devolved Administrations, or Local Government.

All forecasts of devolved taxes are set out in detail in their Devolved Taxes publication, which is produced alongside each UK fiscal event. The OBR published a forecast of Carer's Allowance expenditure in Scotland in their March 2018 publication.As further social security benefits are devolved to the Scottish Parliament the OBR may expand their work into other social security expenditures.

In each tax section, differences to the OBR forecasts are discussed and explained, which may be because of modelling approaches, timing, data used or differences in judgements made.

As set out in Box 1.2, the OBR revenue forecasts of devolved taxes are not used as part of the block grant adjustment calculations which are based on the OBR forecasts of UK Government receipts of corresponding UK taxes.[1] The Land and Buildings Transaction tax and Scottish Landfill tax sections now include a comparison between Scottish Fiscal Commission and Spring Statement 2018 block grant adjustment forecasts.

[1] Please see Box 3.2 of our December 2017 forecast publication for an explanation of how the BGA works with Income Tax (link)

1. Income Tax

1.1 Forecast

Table 3.2: Non-Savings Non-Dividends income tax outturn and forecast

£ million	2015-16 Outturn*	2016-17	2017-18	2018-19	2019-20	2020-21	2021-22	2022-23	2023-24
	10,948	11,267	11,467	11,969	12,345	12,805	13,335	13,936	14,547

Source: Scottish Fiscal Commission *Outturn in this context for income tax refers to our analysis of the 2015-16 Survey of Personal Incomes (SPI) data.

1.2 Background

3.3 The Scotland Act 2016 transferred new tax powers to the Scottish Parliament. From 2017-18, the Scottish Parliament took full responsibility for non-savings and non-dividend (NSND) income tax rates and thresholds, with the exception of the personal allowance.[2] Since April 2017, the Scottish Government receives all the revenue from income tax on the NSND income of Scottish taxpayers.

3.4 The responsibility for defining the income tax base, including setting or changing income tax reliefs and the personal allowance continues to rest with the UK Government. HMRC remains responsible for the collection and management of Scottish income tax. It is HMRC's responsibility to decide who is and who is not a Scottish taxpayer as provided for in legislation. The Scotland Act 2012 defines a Scottish taxpayer as someone who is a UK taxpayer and has their main place of residence in Scotland.[3]

3.5 The Scottish Government have implemented policy changes to income tax for both the 2017-18 and 2018-19 tax years. For 2017-18, most rates and bands were set at the same level as the UK. The only difference was the higher rate threshold, which was unchanged in cash terms from 2016-17 at £43,000. In 2018-19, a new five band income tax policy was introduced. We implemented the final agreed policy as part of our February 18 updated income tax forecast.[4] This policy is set out in Table 3.3 below:

Table 3.3: Final income tax policy measure description (2018-19)

Gross income (£)	Tax band	Tax rate (%)

[2] This is primarily income from employment, pensions and property

[3] Scotland Act 2012, Section 25, 80D (link)

[4] Scottish Fiscal Commission (2018) Scotland's Economic and Fiscal Forecasts Supplementary Publication Updated Income Tax Forecasts (link)

Comment [SM1]: 3.1The wording here is a bit confusing as to what the Scottish Parliament can / can't do. We'd suggest that the following is clearer for people to understand:
3.2
3.3The Scotland Act 2016 transferred new tax powers to the Scottish Parliament. From the tax year 2017-18, the Scottish Parliament took responsibility for setting the rates and bands for tax on non-savings and non-dividend (NSND) income. Other aspects of income tax policy, including the power to set the tax free personal allowance, remain reserved to the UK Government. Since April 2017, the Scottish Government receives all the revenue from income tax on the NSND income of Scottish taxpayers.
3.4
3.5The responsibility for defining the income tax base, including defining who is a Scottish taxpayer, what kinds of income are subject to tax, setting or changing income tax reliefs and setting the personal allowance continues to rest with the UK Government. HMRC remains responsible for the collection, management and enforcement of Scottish income tax. It is HMRC's responsibility to decide who is and who is not a Scottish taxpayer as provided for in UK legislation. A Scottish taxpayer is defined as someone who is a UK taxpayer and meets one of three other criteria, most commonly that they have "a close connection" with Scotland, generally meaning that their main place of residence is located in Scotland.

11,850 - 13,850	Starter rate	19
13,851 - 24,000	Basic rate	20
24,001 - 43,430	Intermediate rate	21
43,431 - 150,000	Higher rate	41
Above 150,000	Top rate	46

Source: Scottish Government

3.6 The Scottish Government have not announced any income tax policy changes for this fiscal event. We have updated costings for the two policy measures to take account of model developments and new data published since February. Further information on the policy recostings can be found in paragraph 3.19, Table 3.4 and Annex B.

1.3 Modelling approach – key judgements and changes since February

3.7 Our approach to creating the income tax forecast was set out in our 'Current Approach to Forecasting' publication.[5] The modelling is based on detailed taxpayer data published by HMRC called the Survey of Personal Incomes (SPI). The latest available SPI is for 2015-16. We use outturn data on income and earnings from other sources to estimate changes in the number of taxpayers, their incomes and tax liabilities up to 2017-18. From 2018-19 onwards, we then use forecasts of earnings and employment from our economy forecasts to estimate incomes and tax liabilities in future years.

Comment [AN2]: This is factually incorrect as earnings growth in 2017-18 is based on a forecast rather than outturn data.

Outturn data on employment and earnings therefore only determine the forecast up to 2016-17.

3.8 While our overall approach is unchanged, there have been some small developments and new data received since our previous forecasts in February. The rest of this section discusses the key judgements in the income tax forecast and some of the changes introduced since our February publication.

1.3.1 2015-16 SPI data

3.9 In February 2018 our forecast was based on the 2014-15 SPI data, the latest available at the time. We have now incorporated the 2015-16 data. This data suggests slightly higher tax liabilities of £15m for 2015-16 - rising to £96m by the end of forecast horizon. This is predominantly driven by higher than the anticipated number of basic rate taxpayers in 2015-16 (around 30,000).

1.3.2 Latest employment and earnings outturn data

3.10 As we are using base SPI data from 2015-16, our modelling uses outturn employment and earnings data covering 2016-17. The most significant change to this has been the inclusion of the latest Annual Population Survey (APS) employment data for 2016-17. This resulted in a small upward revision

[5] Scottish Fiscal Commission (2017) Current Approach to Forecasting (link)

to the number of taxpayers which is persistent across the forecast horizon - increasing the forecast of tax liabilities by £30m in 2015-16 and by £92m in 2022-23.

1.3.3 Economy forecast

3.11 The income tax forecasts published in February 2018 were based on our economy forecasts published in December 2017. The income tax forecasts have been updated to include the latest economy forecasts detailed in Chapter 2 of this report.

1.3.4 Tax Motivated Incorporations (TMI)

3.12 Throughout the UK there has been a steady rise in the proportion of people working for themselves, rather than as an employee. Individuals who choose to work for themselves may be self-employed or have the option to incorporate and manage their business as directors of a limited company. For individuals who choose to 'incorporate', this changes their tax liabilities from NSND to corporation tax and dividends.

3.13 Consistent with our approach in December 2017, we received updated TMI modelling outputs from HMRC to estimate the reduction in tax liabilities across the forecast horizon. This adjustment is calculated and applied to our baseline forecast - excluding the impact of recent policy changes. We have a separate approach for estimating additional TMI as a result of a change in policy.[6]

3.14 Further information on TMI can be found in the OBR's 2017 Fiscal Risk report, and in our December 2017 forecast publication. [7] [8]

1.3.5 UK tax policies

3.15 We undertake additional modelling for certain policy measures introduced by the UK Government which will affect Scottish NSND income tax liabilities. Using the OBR's policy measure database, our approach calculates the relevant adjustments needed to the Scottish NSND forecast to account for previous UK Government policy measures that have affected income tax revenues since 2015-16, the latest year of our base SPI data.

1.3.6 Public Sector Pay

3.16 The Scottish Government announced basic pay awards for 2018-19 that were above previous years and higher than our previous baseline expectations for growth in public sector pay. This included a three per cent basic pay award for those in scope earning less than £36,500 per year, a limit of up to 2 per cent

[6] See: Scottish Fiscal Commission (2018) How we forecast behavioural responses to income tax policy (link)

[7] OBR (July 2017) Fiscal Risks Report paragraph 5.5 (link)

[8] Scottish Fiscal Commission (2017) Scotland's Economic and Fiscal Forecasts (link)

on the increase in baseline paybill for those earning above £36,500 and below £80,000 and a limit on the maximum pay increase for those earning £80,000 or more to £1,600. The Commission set out its approach to capturing the impact of these higher basic pay awards in its December and February publications.

3.17 The Scottish Government confirmed to the Commission on 8 May 2018 that it did not anticipate making any further changes to public sector pay policy at this time. We have therefore left our assumptions about future public sector pay awards unchanged since February. The Scottish draft budget will set out the Public Sector Pay Policy for 2019-20.

Comment [SM3]: I've e-mailed Finance Pay Policy to QA these two paragraphs

1.3.7 Recosting previous policies

3.18 We have previously published estimates of the additional revenue raised from the two recent changes in income tax policy in Scotland - the 2017-18 higher rate threshold freeze, and the new 2018-19 five band income tax. Our policy costings include both the 'static costing' (the amount of revenue raised assuming no taxpayer behavioural change) and the 'post-behavioural costing' (the final revenue raised including the effects of taxpayer behaviour).

3.19 We provide updated costings with this report. There have been small changes in our policy costings as a result of other changes, such as inclusion of the latest economic forecast and moving to the latest 2015-16 SPI data.

3.20 In March 2018, we published an occasional paper 'How we forecast behavioural responses to income tax policy' which provides more detail on our income tax behavioural approach. [9] We have made no changes to our assumptions or underlying judgements on taxpayer behaviour.

1.3.8 HMRC RTI data

3.21 HMRC have been developing more timely estimates of Scottish income tax earnings than currently available from the SPI. In January 2018, HMRC published its first experimental quarterly Real Time Information (RTI) statistics.[10] This includes estimates of numbers receiving pay and their pay from HMRC's RTI administrative data, covering April 2014 to September 2017 inclusive.

3.22 RTI data offer a potentially valuable source of real time information on income growth from employed taxpayers in Scotland. However, RTI is a new source of data and also has some drawbacks. For example, RTI only covers the PAYE population (excluding the self-employed). We have some reservations

[9] Scottish Fiscal Commission (2018) How we forecast behavioural responses to income tax policy (link)

[10] HM Revenue and Customs (2018) UK Real Time Information, Experimental Statistics (link)

about using these data to adjust our forecast at this time, and so we make no direct adjustments to our forecast using the RTI data.

3.23 We will continue to monitor RTI data and may choose to introduce changes to our approach to forecasting income tax as a result.

Comment [AN4]: Should this section make reference to the RTI **liabilities** data?

Here, data is already available for the entire financial year 2017-18.

1.4 Forecast

3.24 Since February 2018 the Commission has revised its forecasts of NSND income tax liabilities. Table 3.4 presents in detail the differences our February 2018 forecast and the latest forecast.

Table 3.4: Comparison with previous February 2018 forecast

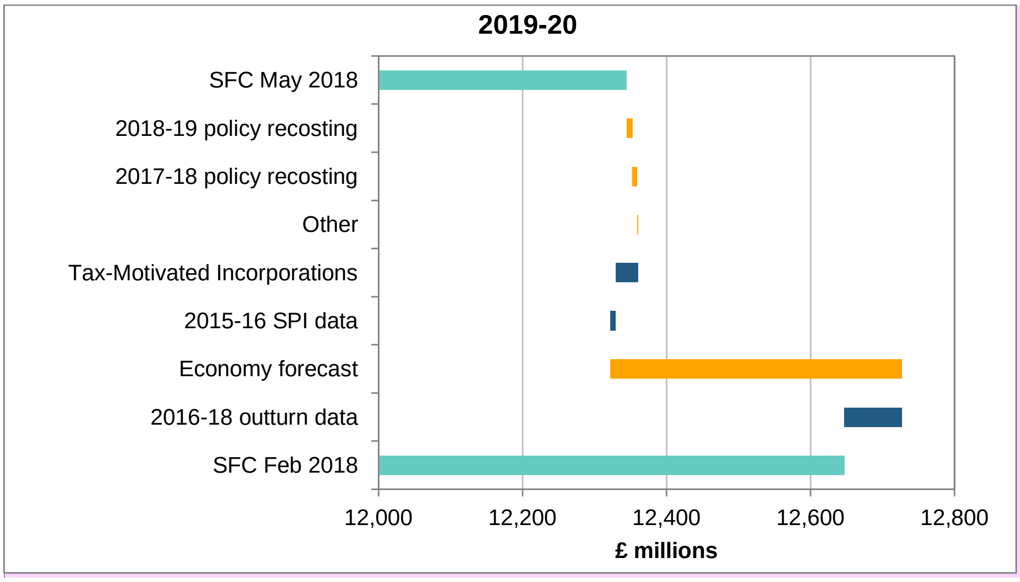
2. £ million	3. 2015-16	4. 2016-17	5. 2017-18	6. 2018-19	7. 2019-20	8. 2020-21	9. 2021-22	10. 2022-23
11. February 2018 post-measures	12. 10,932	13. 11,214	14. 11,584	15. 12,177	16. 12,647	17. 13,152	18. 13,733	19. 14,372
20. 2016-17 outturn data	**21.** 0	**22.** 30	**23.** 53	**24.** 78	**25.** 80	**26.** 84	**27.** 87	**28.** 92
29. Economy forecast	**30.** 0	**31.** 6	**32.** -198	**33.** -317	**34.** -405	**35.** -474	**36.** -545	**37.** -614
38. 2015-16 SPI data	**39.** 15	**40.** -5	**41.** -21	**42.** 5	**43.** 7	**44.** 25	**45.** 66	**46.** 96
47. Tax-Motivated Incorporations	**48.** 0	**49.** 21	**50.** 43	**51.** 26	**52.** 31	**53.** 35	**54.** 10	**55.** 13
56. Other[11]	**57.** 1	**58.** 0	**59.** 7	**60.** 8	**61.** -1	**62.** 0	**63.** 1	**64.** -3
65. 2017-18 policy recosting	**66.** 0	**67.** 0	**68.** -2	**69.** -2	**70.** -7	**71.** -7	**72.** -7	**73.** -8
74. 2018-19 policy recosting	**75.** 0	**76.** 0	**77.** 0	**78.** -6	**79.** -8	**80.** -9	**81.** -11	**82.** -12
83. May 2018 pre-measures	84. 10,948	85. 11,267	86. 11,467	87. 11,969	88. 12,345	89. 12,805	90. 13,335	91. 13,936
92. May 2018 policy changes	**93.** -	**94.** -	**95.** -	**96.** -	**97.** -	**98.** -	**99.** -	**100.** -
101. May 2018 post-measures	102. 10,948	103. 11,267	104. 11,467	105. 11,969	106. 12,345	107. 12,805	108. 13,335	109. 13,936
110. *Change from February 2018*	***111.*** *16*	***112.*** *53*	***113.*** *-118*	***114.*** *-209*	***115.*** *-302*	***116.*** *-347*	***117.*** *-398*	***118.*** *-437*

Source: Scottish Fiscal Commission (February 2018) forecast (link), Scottish Fiscal Commission. Figures may not sum to totals because of rounding

3.25 The table shows a range of factors and developments, since our forecast in February, that have led to a small upward revision in 2015-16 and 2016-17 tax years, with downwards revision for subsequent years. While the latest economy forecasts have reduced future tax liabilities, other factors such as strong employment outturn data in 2016-17 have had a positive impact on the forecast. Figure 3.1 presents the relative scale of these factors for 2019-20.

[11] Includes revisions to OBR triple lock and CPI forecasts, HMRC Gift Aid estimates, inclusion of 2017 mid-year population estimates and model developments.

Figure 3.1: February 2018 compared to May 2018 forecast by factor, 2019-20



Source: Scottish Fiscal Commission (February 2018) forecast (link), Scottish Fiscal Commission

3.26 Changes since February have led to a downwards revision for 2019-20 of around £300 million. The chart clearly shows that changes to the economy forecast are the most significant of these factors.

Comment [AN5]: Typo – 2016-17 outturn data.

118.1 Uncertainty (to be updated)

3.27 In this section, we assess the sensitivity of our income tax forecast to the alternative economy scenarios considered in the economy chapter, Table X. The results of this analysis are shown in Table X.

Table 3.5: Average percentage variance of income tax forecast liabilities to economic scenarios across forecast horizon

	Low variant	High variant
Migration	-0.27	0.28
Unemployment	0.32	-0.54
Average hours	-1.44	1.89
Productivity	-1.92	6.71

Source: Scottish Fiscal Commission

3.28 Changes in income tax receipts are most sensitive to changes in our assumption about productivity growth. In the high productivity scenario, income tax revenues are on average estimated to be 6.71 per cent higher over the forecast horizon. Productivity is one of the most significant risks to our NSND forecast.

118.2 Comparison to OBR forecast

3.29 As part of their role as UK-level fiscal forecaster, the OBR also produce a forecast of income tax receipts. Table 3.6 below compares the latest OBR forecast as presented in their March 2018 devolved taxes publication and our latest forecast.

Table 3.6: Scottish NSND forecast OBR & SFC

£ million	2015-16	2016-17	2017-18	2018-19	2019-20	2020-21	2021-22	2022-23
OBR March 18	10,957	11,415	11,873	12,403	12,712	13,139	13,575	14,116
SFC May 18	10,948	11,267	11,467	11,969	12,345	12,805	13,335	13,936
Difference	-9	-148	-407	-434	-367	-334	-240	-181

Source: OBR (March 2018) Devolved Taxes Publication (link), Scottish Fiscal Commission

3.30 Our forecast is consistently lower than OBR's forecast. There are a few reasons why our forecasts are different.

- **Modelling differences:** In our forecasts we use a 'bottom-up' micro simulation forecast based on our SPI model. This allowed the Commission to develop an income tax model which is suitable for Scottish demographics and the distribution of taxpayers. The OBR (or HMRC on their behalf) utilises a 'top-down' approach by first producing a forecast of the NSND income tax for the whole UK and then estimating a Scottish share which is applied to this forecast.
- **Data:** Our forecasts are based on the 2015-16 SPI, and are projected forward using Scottish specific economic determinants which we produce as part of our economy forecasts. The OBR forecast of future earnings growth is based on UK economic determinants. In addition, they partly adjust their UK income tax forecast based on the available 2016-17 and 2017-18 outturn receipts data for the UK. This will correspondingly be reflected in their Scottish NSND forecast.
- **Policy costing:** Included in both forecasts is the policy costing for Scottish Government's 2018-19 five band income tax system. Table 3.7 below **compares the OBR's costing with our latest estimate. The two costings are broadly similar - there are small differences in our static costings (assuming no taxpayer behaviour) because of differences in our base forecast. On the behaviour element, OBR have disaggregated the policy effect of TMI and migration, where as our behavioural approach includes this as part of our Taxable Income Elasticities (TIE). The OBR's costing has an increasingly higher behavioural reduction percentage because of the accumulation of additional TMI behaviour. Further information on our approach can be found in our March 2018 Occasional paper *'How we forecast behavioural responses to income tax policy'.*** [12]

[12] Scottish Fiscal Commission (2018) How we forecast behavioural responses to income tax policy (link)

Table 3.7: Comparison between OBR and SFC of 2018-19 Scottish Government policy costing

£ million	2018-19	2019-20	2020-21	2021-22	2022-23
OBR Costing					
Static Costing	274	281	290	302	317
Behavioural response	-49	-58	-64	-70	-77
Post-behavioural Costing	225	223	226	232	240
Reduction due to behaviour (%)	*-18*	*-21*	*-22*	*-23*	*-24*
SFC Costing					
Static Costing	266	274	288	303	321
Behavioural response	-53	-55	-58	-61	-66
Post-behavioural Costing	213	219	230	242	255
Reduction due to behaviour (%)	*-20*	*-20*	*-20*	*-20*	*-20*

OBR (March 2018) Devolved Taxes Publication (link), Scottish Fiscal Commission

The Commission bases its forecasts on the best information available at the time of publication. However, over time, new and sometimes better data sources become available. The Commission forecasts Scottish income tax liabilities using the Survey of Personal Incomes (SPI). This is a sample of HMRC's personal tax records. Currently, this is the best available source of information on income tax liabilities for Scotland, though it does have some limitations. The latest available SPI is for 2015-16, and this is the starting point from which we create our income tax forecasts.

In Summer 2018, HMRC will publish its first full estimates of outturn income tax liabilities in Scotland, covering the year 2016-17. For the first time, this will be based on full administrative data using Scottish taxpayer flags. Once available, this will be the primary measure of income tax liabilities in Scotland.

There will be a number of underlying differences between the Commission's 2015-16 SPI based estimate of income tax liabilities in 2016-17 published in this report and those published by HMRC using outturn data in the Summer. The Commission expects there will be a degree of error between its current best estimate of 2016-17 income tax liabilities and the figure that will be published by HMRC. At present, there is insufficient information to know the likely magnitude or direction of this error.

Once published, the Commission will review the new data and look to make appropriate adjustments to its forecasting approach for future forecasts and publications. We expect to be able to provide analysis of this issue in our September 2018 Forecast Evaluation Report.

There are likely to be a number of underlying differences between the Commission's 2016-17 NSND income tax liabilities estimate and the outturn data published by HMRC in summer 2018. These include:

- The SPI is only available up to 2015-16. At least some of the difference between the Commission's estimate of income tax liabilities in 2016-17 and the outturn data published in the summer will be due to forecast error.
- The SPI is only a one to two per cent sample of all income tax records. The outturn data will be based on full administrative data.
- The Commission uses an anonymised version of the SPI called the Public Use Tape (PUT), which aggregates some high value records.
- There are likely to be differences in the way Scottish taxpayers are identified between the SPI and the outturn data.

Comment [IP6]: The SPI is used as the estimate of outturn income tax. I don't think it is correct to say that income tax is forecast using the SPI.

Comment [AN7]: Neither this, nor the current draft report, makes any reference to the RTI liabilities data which provides estimates of PAYE liabilities for the entire financial year 2016-17 and 2017-18.

You only mention the RTI earnings data which is only available for the first two quarters of the financial year 2017-18

Comment [AN8]: This could be clearer.

The HMRC annual report out in most likely July will in addition to the SRIT 2016/17 outturn will also provide a SIT 2016/17 outturn, and also a SIT forecast of 2017/18.

Comment [AN9]: Both the SPI and the administrative approach to taxpayer identification are done on a postcode basis. The difference will more be that the process has been more thoroughly applied from 2016/17, with a significant cleaning on the HMRC database

Annex B
Policy Recostings

119.

120. Introduction

B.1 A policy recosting is a revised estimate of a policy that has previously been costed. There are two main reasons why we may recost previously announced or implemented measures:

- The administrative outturn data which includes the new policy is not yet be available. For example, we will not receive full data on the 2017-18 Higher Rate threshold policy until Summer 2020.

- We revise key judgements or assumptions relating to our previous policy costing - particularly in response to new evidence coming to light.

B.2 This Annex sets out the latest policy recosting estimates and how they have changed from the previous costing. All of the policy recostings contained in this Annex falls under the first category (administrative outturn data not yet available). We intend to publish this Annex twice a year as part of our Scotland's Economic Fiscal Forecast (SEFF) series.

Comment [AN10]: Outturn data for 2017-18 will become available in summer 2019.

Table B.1: Latest policy recostings

£ million	2017-18	2018-19	2019-20	2020-21	2021-22	2022-23	2023-2
Income Tax[13]							
2017-18 Higher rate threshold freeze	54	59	61	70	75	85	9
2018-19 five band policy, of which	0	213	219	230	242	255	27
Introduction of starter rate	0	-48	-50	-51	-53	-55	-5
Introduction of intermediate rate	0	136	140	146	153	161	16
Higher rate threshold adjustment	0	54	55	58	61	65	6
Increase in higher rate	0	70	71	74	78	82	8
Introduction of top rate	0	3	3	3	3	3	

Source: Scottish Fiscal Commission. Figures may not sum to total due to rounding.

Comment [AN11]: In general, it would be helpful to set out what the baseline, or counterfactual, here is.

For example, we are comparing the 2017-18 HRT freeze against a statutory indexation baseline.

This is different from comparing it against rUK policy, for example. I think there may be a risk that this can be misinterpreted as the additional revenue generated from diverging from the UK Government's income tax policy which it isn't.

Comment [AN12]: Spreadsheet has £87 million here

[13] The full Static Costing, Behavioural adjustment and Post-Behavioural Costing breakdown can be found in our Supplementary table S3.2 and S3.3 (link)

Table B.2: Change from previous costing

£ million	2017-18	2018-19	2019-20	2020-21	2021-22	2022-23	2023-24
Income Tax							
2017-18 Higher rate threshold freeze	-2	-2	-7	-7	-7	-8	-
2018-19 five band policy, of which	0	-6	-8	-9	-11	-12	-
Introduction of starter rate	0	-1	-1	-1	-1	-1	-
Introduction of intermediate rate	0	1	0	0	0	0	-
Higher rate threshold adjustment	0	-2	-2	-3	-3	-4	-
Increase in higher rate	0	-4	-5	-5	-6	-7	-
Introduction of top rate	0	0	0	0	0	0	-

Source: Scottish Fiscal Commission (December 2017) forecast (link), Scottish Fiscal Commission (February 2018) forecast (link), Scottish Fiscal Commission. Figures may not sum to total due to rounding.

Uncertainty

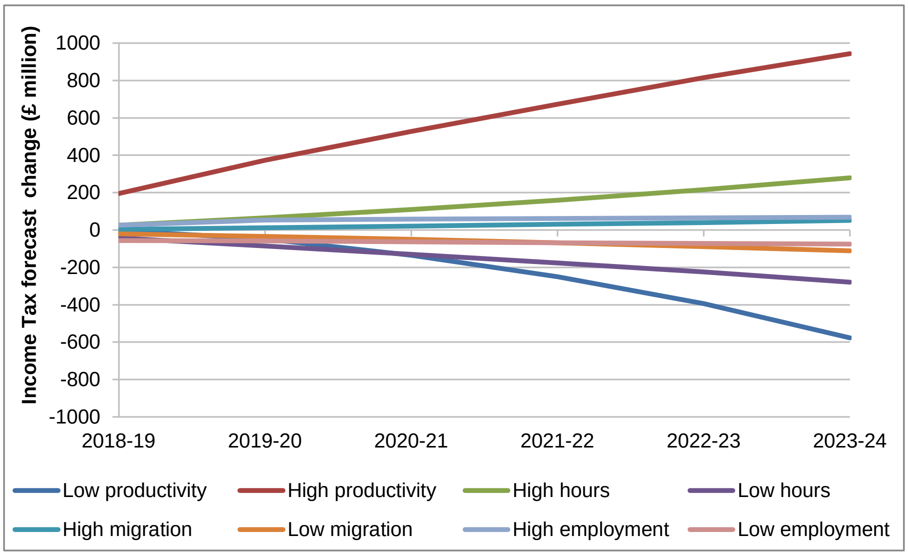
3.31 In this section, we assess the sensitivity of our income tax forecast to the alternative economy scenarios considered in the economy chapter, Table X. The analysis are shown in Figure 3.2 below.

Comment [AN13]: Think it might be helpful to re-state the table from the economy chapter here in a slightly different version, showing the **difference** in employment and earnings growth (the key determinants), relative to the central scenario.

Also, would it be worth explaining the underlying assumptions further?

For example, if I interpret the table in the economy section correctly, the high/lower migration scenarios do not account for any (second round) effects of changes in the labour supply on wages? So it is simply an employment shock?

Figure 3.2: Income Tax sensitivity analysis



3.32 Changes in income tax receipts are most sensitive to changes in our assumption about productivity growth. In the high productivity scenario, income tax revenues are on average estimated to be around £200 million higher in 2018-19, rising to around £940 million by 2023-24. Across the forecast horizon this amounts to a cumulative increase of £3.5 billion. In the low productivity scenario we estimate a cumulative decrease of around £1.4 billion. Productivity is one of the most significant risks to our NSND forecast.

Comparison to Block Grant Adjustment

3.33 The OBR published updated economy and fiscal forecasts at the Spring Statement on 13 March 2018. These forecasts have been used by the Scottish Government to produce indicative updates of the Scottish Government's block grant adjustments. The income tax BGAs will have no immediate bearing on the budget as they are updated and applied to the Scottish Government's block grant at the Autumn Budget. A comparison between SFC Income Tax forecasts and the most up to date block grant adjustment estimates is shown in the table below. As the 2016-17 outturn data are not currently available the BGA figures use our December forecast for 2016-17 as the baseline. This forecast has been updated in this publication. However, the

Comment [AN14]: "These forecasts have been used by the Scottish Government to produce indicative updates of the Scottish Government's block grant adjustments, **in line with the methodology agreed with HM Treasury**"

Comment [U15]: Agree with Angela's suggestion – we produced all IT BGAs in MTFS as we're using a different baseline from the one provided by HMT at Spring Statement.

Comment [U16]: This is not correct – the baseline we're using is the SFC's MTFS 16-17 forecast.

income tax baseline will all be updated once the outturn data for 2016-17 are published in Summer 2018.

Table 3.8: Comparison between SFC forecast and Spring Statement 2018 Block Grant Adjustment forecast estimates

£ million	2017-18	2018-19	2019-20	2020-21	2021-22
SFC May 2018	11,467	11,969	12,345	12,805	13,335
Block Grant Adjustment Estimates*	11,626	11,930	12,215	12,612	13,015
Difference	-159	39	130	193	320

Source: Scottish Fiscal Commission, Scottish Government 2018 Block Grant Adjustment Estimates written letter (link)
* Estimates are based on Indexed Per Capita methodology
Figures may not sum to totals because of rounding

Comment [U17]: This should be removed, as I read it that the 17-18 and 18-19 figures will change once we have an outturn baseline. That is not the case.

Comment [SM18]: May be helpful for the reader if you mention here that the 2017-18 and 2018-19 figures are “locked in” for Budgetary purposes, so the “difference” line does not indicate a Budgetary impact on these years. Rather, this table is showing where the numbers might end up given current data and thinking, so indicates the direction of travel of any future reconciliation.

Comment [AN19]: It may be worth adding a footnote here to say that the 2017-18 and 2018-19 figures are different from what was published at each Budget Act as Steven notes.

I’m just highlighting this as this is causing a lot of confusion on our side.