Land and Buildings Transaction Tax (LBTT)
Scottish Parliament: Call for Evidence

The Law Society of Scotland’s response
August 2016
Introduction
The Law Society of Scotland is the professional body for over 11,000 Scottish solicitors. With our overarching objective of leading legal excellence, we strive to excel and to be a world class professional body, understanding and serving needs of our members and the public. We set and uphold standards to ensure the provision of excellent legal services and ensure the public can have confidence in Scotland’s legal profession.

We have a statutory duty to work in the public interest, a duty which we are strongly committed to achieving through our work to promote a strong, varied and effective legal profession working in the interests of the public and protecting and promoting the rule of law. We seek to influence the creation of a fair and just society through our active engagement with the Scottish and United Kingdom governments, parliaments, wider stakeholders and our membership.

This evidence has been prepared on behalf of the Law Society by members of our Land and Buildings Transaction Tax working party, a sub-group of our Tax Committee. The working group welcomes the opportunity to respond to the Scottish Parliament’s call for evidence on the operation of the Land and Buildings Transaction Tax in its first full year.

General Comments
Land and Buildings Transaction Tax (LBTT) is Scotland’s replacement for Stamp Duty Land Tax (SDLT). It was introduced from 1 April 2015. LBTT is a tax applied to residential and commercial land and buildings transactions (including commercial purchases and commercial leases) where a chargeable interest is acquired. Revenue Scotland administers LBTT with support from Registers of Scotland.¹

In November 2015, the UK Government proposed the introduction of a supplementary SDLT charge of 3% on the purchase of additional residential properties, to take effect from 1 April 2016. In order to ameliorate any distortions between Scotland and the rest of the UK, the Scottish Government introduced a supplementary LBTT charge of 3% on the

¹ LBTT was introduced by the Land and Buildings Transaction Tax (Scotland) Act 2013 and came into effect from 1 April 2015 - http://www.parliament.scot/parliamentarybusiness/Bills/56718.aspx
purchase of additional dwellings in Scotland. This additional charge is known as the Additional Dwelling Supplement ("the ADS").

The impact on both the residential and commercial property market of the various rates and bands

LBTT is a progressive tax (like income tax) and slices of the price are charged at different rates on both residential and non-residential purchases.

Following changes in the December 2014 Autumn Statement, UK SDLT now also has progressive rates for residential purchases, and from 17 March 2016 for commercial property transactions as well.

Rates for non-residential purchases:
For LBTT the rates are:
- 3% for the part of the price between £150,001 and £350,000 and
- 4.5% for any excess over £350,000

For SDLT the rates are:
- 2% for the part of the price between £150,001 and £250,000 and
- 5% for any excess over £500,000

Rates for residential purchases:
For LBTT the rates are:
- 2% for the part of the price between £145,001 and £250,000
- 5% for the part of the price between £250,001 and £325,000
- 10% for any part of the price between £325,001 and £750,000 and
- 12% for any excess over £750,000

For SDLT the rates are:
- 2% for the part of the price between £125,001 and £250,000

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2 The ADS was introduced by the Land and Buildings Transaction Tax (Amendment) (Scotland) Bill and came into effect from 1 April 2016 - [http://www.parliament.scot/parliamentarybusiness/Bills/96000.aspx](http://www.parliament.scot/parliamentarybusiness/Bills/96000.aspx)
5% for any part of the price between £250,001 and £925,000
10% for any part of the price between £925,001 and £1.5m and
12% for any excess over £1.5m

Essentially, some buyers are better off than they would be under the UK SDLT system. For some, there is little difference. For others, there is more tax to pay when purchasing a property in Scotland. The tipping point at which there starts to be a tax increase is for properties being purchased for over £333,050. Anyone purchasing a property above that level is paying more LBTT than they would under the UK SDLT regime.

We have some concerns about these diverging tax rates north and south of the border. At the upper end of the residential market, where LBTT rates are higher than SDLT rates, many purchasers are relatively mobile and can choose where they will live and purchase property. The existing rates of LBTT combined with the ADS has led to significant levels of amounts of LBTT being applied at the higher end of the residential property market in Scotland, with overall rates of 13% on property worth in excess of £325,000 and 15% on property worth in excess of £750,000. We have received feedback from practitioners that these levels of LBTT rates at the upper end of the residential market might be deterring clients from purchasing high value property. Whilst LBTT has undoubtedly been beneficial for first time buyer (because of the lower overall charge at the lower end of the market), it is possible that the higher rates have created a slowdown in the market in the upper bracket.

While LBTT rates will never be a dominant factor, increased divergence from rUK rates are bound to have an effect in marginal decisions; and it is obviously necessary that decisions on changes to UK rates are informed by the rUK position (as clearly happened with the introduction of ADS). The mirror of this may be said to have happened at the outset with the introduction of progressive rates of SDLT – but the difficulties of interaction were then clearly illustrated with the first announcement of LBTT rates requiring to be swiftly changed before their introduction, following the SDLT changes announced for rUK. This kind of “back and forth” process may on occasions be unavoidable, but it is undesirable.

It is also the case that, in absolute terms, the highest rate of LBTT (without ADS) is historically an extremely high marginal rate (and indeed, compared to historic SDLT
average). Given that LBTT is a transaction tax incurred in a lump sum at the time of purchase, this levy represents a considerable additional initial burden for prospective purchasers already incurring significant transactional costs. Lenders may be less willing to extend loans to cover such additional costs given understandable tightening of the lending market since the last recession, and demands for increased equity funding by prospective purchasers.

Sub-sales

We remain concerned that there is no general sub-sale relief for LBTT. Following representations raised by the Society and others about the lack of sub-sale relief, the Scottish Government introduced a targeted relief. This Sub-sale Development Relief can be claimed in transactions where there is a sub-sale of land and significant development is in prospect.

The relief can be claimed up front by the purchaser who is buying the land and selling it on but the relief is withdrawn (in whole or in part) if development does not take place within 5 years. In sub-sale transactions where Sub-sale Development Relief is not available (which are common), LBTT is payable by both purchasers. This means there is a double LBTT charge compared with the position under SDLT.

We have concerns that a strict interpretation of the legislation does not allow for this Sub-sale Development Relief to be claimed at all. Section 14(1)(c) of the Land and Buildings Transaction Tax (Scotland) Act 2013 (LBTTSA) has created significant difficulties in this regard (see below). It is not possible to supply the necessary evidence at the point of contract to demonstrate qualification for the relief, as such evidence would not yet be available. This could prejudice the biggest developments in Scotland as they have the longest lead-in periods, which again will have a negative impact on economic development.

We are also concerned that a strict interpretation of the wording of Section 14(1)(c) of the LBTTSA suggests that in a sub-sale transaction where Sub-sale Development Relief is not available, LBTT is payable by the mid-purchaser at the time the onward sale contract is entered into, and not when the contracts are completed. This makes no sense at all, since
at that stage the mid-purchaser would have no funds to pay the LBTT and indeed the transactions may never actually complete. The rule applies even where the sub-sale is of a small part of the subject matter of the original transaction. Having to pay LBTT at the contract stage is not a requirement anywhere else in the LBTT legislation. We believe that the LBTT legislation should be amended to make it clear that on a sub-sale transaction where no Sub-sale Development Relief is available, the LBTT on both purchases is payable when the purchases complete.

Unlike SDLT sub-sale relief, Sub-sale Development Relief is not available where the sub-sale takes the form of an assignation.

We have anecdotal evidence of a number of transactions which have not proceeded because of the absence of sub-sale relief. In one case the position was as follows:

A client was purchasing six casinos (three in Scotland and three in England), and was putting together a deal to flip them on. Matters were far advanced commercially; however, the client withdrew from purchasing the three casinos in Scotland on learning that there was no sub-sale relief. The figures for the Scottish properties that did not proceed were:

Casino 1: purchase price £5m; on-sale price £6m
Casino 2: purchase price £2.1m; on-sale price £2.6m
Casino 3: purchase price £6m; on-sale price £7.5m.

Other Differences between LBTT and SDLT

Under the UK SDLT higher rates system (the equivalent of the ADS), purchasers have 36 months rather than 18 months to claim a refund of the 3% supplement if they buy a new main residence before disposing of their previous main residence. Purchasers also have 36 months rather than 18 months between selling a main residence and replacing it with another main residence without having to pay the supplement.
There are other marked differences which overall make the SDLT supplement less financially onerous for those purchasing homes in the rest of the UK.⁴

We are concerned that the combination of these differences and the higher rates might, in the longer term, have an impact on the level of property purchases in Scotland, particularly at the higher end of the residential property market. Particularly in rural Scotland where there is a considerable market in second homes, the ADS may well have a detrimental effect (without proving enough of an incentive to first-time buyers unaffected by ADS).

The extent to which the rates and bands are consistent with the principles of “fairness, equity and the ability to pay”

We recognise LBTT was introduced as a progressive tax and believe that, generally, it is consistent with the principle of ability to pay because of its progressive structure. This is because the amount of LBTT payable relates more closely to the value of the interest in the property acquired compared to the old ‘slab’ system.

There has been a partial reintroduction of the ‘slab’ structure through the ADS, as the ADS is charged at 3% on the whole of the consideration, provided the consideration exceeds £40,000. The ADS is chargeable even if no LBTT would be chargeable because the price is below the nil rate band. This creates problems for purchases of properties at the lower end of the market as the supplement effectively creates a cliff edge at the £40,000 threshold. We can see no reason why the ADS could not have been introduced on a more progressive basis, in keeping with LBTT structures generally. As it stands, the structure of ADS is directly in conflict with the principles of fairness, equity and ability to pay. It is not a tax which has higher rates in relation to higher levels of consideration. The lower threshold for ADS and the slab structure in contrast to that for basic LBTT provides an underlying level of complexity which is undesirable (although it is recognised that a single rate of ADS does mitigate the complications arising from the two different structures). A similar degree of structural difference is seen in the need for apportionment between residential and non-residential elements for ADS purposes, which does not exist in the basic LBTT structure.

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More broadly, we believe that ADS, as currently applied, is not consistent with the principles of fairness. In our response on the ADS Bill, we suggested it would be more appropriate (and in keeping with the overall policy objective) for any acquisition of a main residence to attract only standard rates of LBTT. As things stand, home owners moving from one main residence to another are generally unaffected whether or not they own additional homes, whilst the additional 3% is imposed on a person who is buying their first main residence if he or she has an interest in another dwelling. This latter scenario can arise through a number of situations e.g. inheritance of a part share on death of a grandparent/parent where the ability to sell that interest before acquiring the main residence can be limited (and the question of when the purchaser “owns” the inherited interest is opaque, to say the least). There are a range of scenarios which entail unplanned or temporary ownership of a property. The complications are such as to allow for the possibility of someone owning another interest (or because of the rules on connected persons, being deemed to own such an interest) without actually being aware that they are potentially liable for ADS. Such persons should not be in a worse position than those who already own a second home along with a main residence and are replacing the latter. We maintain that it would be fairer for any acquisition of a main residence to attract only standard rates of LBTT. It would be relatively straightforward to determine if a person is buying a main residence or not, given that it is a question of fact.

The ADS has an impact on the deposit savings of the buyer, either reducing the deposit percentage he or she can put down or prolonging the amount of time he or she is forced to save for. Additionally, at the higher end of the residential property market, there might be difficulties for the buyer in attracting lending for the large up-front sums required.

Furthermore, there is perhaps some confusion as to the policy aims of the supplement. The ADS was ostensibly introduced to prevent housing stock being purchased by buy-to-let investors and instead allow more first time buyers to enter the market. The ADS legislation, however, provides a full relief from ADS for those buying six or more properties. The

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4 They are able to reclaim ADS within the 18 month period.
legislation therefore seems to incentivise larger purchases of the housing stock by single entities.

**Penalties**

In our view, the penalties which are chargeable for late submission of, or failure to submit, a return are disproportionate in relation to the errors that have been made. The maximum aggregate penalty for a late return will be 100% of the LBTT that was due so paying double LBTT. That is just the maximum aggregate for the late return. If the LBTT itself is also paid late (which is likely if the return is late) then there will also be interest and the relevant applicable penalty for late payment. We are aware that the LBTT penalties are higher than the SDLT penalties and we believe they are excessive and should be reviewed.

Penalties are also chargeable even where no LBTT is payable, for example where a relief such as group relief is available. We are particularly concerned about the imposition of late return penalties in connection with leases. Tenants have to submit lease returns every three years, as well as when a lease is assigned or terminated, even if no LBTT is payable. We are concerned that late return penalties could be charged in relation to “no LBTT” lease returns where tenants are not aware of the requirement to submit a return every three years. We believe the imposition of any penalty where no LBTT is payable is disproportionate and should be reviewed.

**The level of receipts for residential and non-residential transactions in relation to the forecasts**

The total LBTT tax take in its first year was £416.1m. The tax raised by residential LBTT was £201.9m, which was £33.1m less than expected. The tax raised by non-residential LBTT was £214.2m, which was £68.2m more than expected.\(^5\)

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A small number of large transactions within year one has meant that the commercial LBTT tax revenues delivered a higher amount than anticipated. It is difficult to estimate future levels of receipts on the basis of a small number of high-value commercial sales. Individual commercial transactions can be of such a size as to skew even annual receipts and forecasts. We believe that forecasts based on anticipated numbers of domestic transactions are likely to be more reliable.

The impact of forestalling and whether it is likely to have a short-term impact only or lead to longer-term changes in the market

It is difficult to measure levels of forestalling, but feedback from our members suggests that there was increased activity in the housing market in the run up to the implementation of LBTT on 1 April 2015 and also in advance of the ADS being introduced on 1 April 2016. LBTT revenues were likely to have been affected as households brought transactions forwards in order to minimise their tax bill. However, it is clear that tax changes such as these will always result in some people taking forestalling action. There are other organisations that will be better placed to comment on whether the forestalling activity will have a short term impact or lead to longer-term changes in the market. However, the undoubted existence of forestalling behaviour does have an impact on the timing and method by which future changes to LBTT are introduced, particularly but not exclusively in relation to changes in rates.

Whether there should be any changes to the rates and bands in the draft budget for 2017-18

In our evidence on the ADS Bill,6 we commented on the partial return to the previous ‘slab’ system. We believe that the ‘cliff edge’ introduced by the ADS could be replaced with a more progressive system.

More generally, at the higher end of the residential property market, some of the same problems of the old ‘slab’ system have been recreated despite the ‘slice’ effect. At this end

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of the market, there is a clear incentive where possible to apportion the maximum reasonable amount of overall consideration to items other than land and buildings; this creates a tension (and possibly significant expense) because of an understandable wish to minimise tax compared to the need to report such apportionments accurately.

**The performance of Revenue Scotland in administering and collecting the tax**

Overall, we believe that Revenue Scotland has been successful in administering and collecting the tax.

Our members have found the SETS online system easier to use than the HMRC SDLT system. It requires much less information to be provided than the SDLT online system, and all the information is relevant to the tax which some of the SDLT information is not. It is possible to amend LBTT returns online and to submit returns in advance, which is not possible for SDLT returns.

The online systems have generally worked well and there is clearly a dedicated staff team that works hard to fulfil the goals of the organisation. For example, the publication on a monthly basis of Revenue Scotland's aggregated figures for LBTT and ADS is very helpful.

Revenue Scotland and indeed the Scottish Government have been willing to engage in meetings, correspondence and discussion to a significant degree in attempts to smooth the introduction of, and developments in, the tax. We very much appreciate the positive and open environment in which such contact has taken place and sincerely hope that this continues, even in the relatively few situations where we disagree with the position taken.

We believe that there could be yet more, and more immediate, concrete results from this engagement. We would always welcome some more time to consider the input we can give and perhaps some more recognition that timescales for response make the kind of detailed input we would wish to supply difficult to achieve. As taxation becomes of more significance to the work of the Scottish Parliament, a more regular timetable for tax changes (see below) may improve the cooperative efforts even further.
There are certain areas where we believe the performance of Revenue Scotland could be improved.

**Opinions Service**

Revenue Scotland offers an Opinion Service.\(^7\) It will, in certain circumstances, provide its opinion on the tax consequences of specific transactions. Revenue Scotland’s website states that this service is offered in “order to allow taxpayers to file with certainty”.

We have received mainly negative feedback from members about this service. Our members have reported that, following a request for an opinion, Revenue Scotland will often state that the person has not identified an uncertainty. This response can be issued a few weeks after a request is submitted. We appreciate that a request for an opinion should be specific but our members do not experience these difficulties obtaining a substantive opinion from the HMRC. This means solicitors are often able to obtain an opinion on a matter relating to UK SDLT from HMRC but cannot get an opinion on the equivalent Scottish position for LBTT (even where it relates to the same matter).

It is particularly important that the Opinions Service should work well in the early days of a new tax, as guidance is still being developed, and there are areas on which no guidance has been published. One of the areas of difficulty in relation to the Opinions Service has been in areas where HMRC have issued guidance but Revenue Scotland has not, but on being asked for an opinion Revenue Scotland have advised that they do not see an uncertainty.

We appreciate the existence of resource constraints, but speed of response is often essential especially in relation to commercial transactions; it is often unrealistic to expect transactions to complete without certainty as to the LBTT liability.

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\(^7\) [https://www.revenue.scot/contact-us/revenue-scotland-opinions](https://www.revenue.scot/contact-us/revenue-scotland-opinions)
We also believe that in a number of cases, opinions negative to a view put forward on behalf of a taxpayer have been issued without a reasoned response for the difference of view.

The opinions that have been issued by Revenue Scotland have not been published. We believe it would be helpful to publish the opinions where they cover common general areas. We cannot imagine that it would be difficult to anonymise the opinions. We query why Revenue Scotland does not, at least, provide a list of the areas where people have sought opinions and statistics on the numbers of opinions sought or issued. But in our view, a programme of publishing anonymised opinions may in fact conserve resources, as we are certain that fresh opinions on the same or even analogous matters would be less likely to be sought in the knowledge of the position taken by Revenue Scotland already.

**Gaps in Guidance**

Similarly, there is published guidance from HMRC for certain aspects of SDLT but there is no equivalent guidance from Revenue Scotland for the same areas. This creates ambiguity and has caused difficulties for clients.

In relation to SDLT, there are some areas where HMRC has been felt that there needs to be guidance. It would be helpful if Revenue Scotland could clarify if it would take the same approach as HMRC in these areas, particularly where there is no obvious reason why there would be any difference (as there is, for example, no difference in the underlying property law concepts and/or the wording of the legislation is identical or materially the same). We are aware of a number of areas, for example in relation to the meaning of substantial performance, where Revenue Scotland has indicated that it does not agree with HMRC’s approach but has not published its own view. Taxpayers are keen to have certainty in relation to their tax affairs, and it is really essential that guidance in these areas is issued.

There are quite a large number of areas where guidance is limited or unclear – examples include the meaning of substantial performance, details for apportionments where these are required, the “Prudential” principle in contracts for purchase and construction and a
significant number of questions on leases and in particular their variation (although guidance has been expanded on leases, especially on transitional issues).

**Enquiries**

Revenue Scotland has various statutory powers to help check that taxpayers meet their tax responsibilities and pay the right amount of tax at the right time. We are not aware that there have been many formal enquiries raised and would be interested in how many LBTT enquiries were opened by Revenue Scotland in the first year. This is an important aspect of Revenue Scotland’s obligations, to ensure that the taxes are operating as intended and to detect and to deter the minority who do not comply with their obligations. We are aware that Revenue Scotland will be setting up a protocol for enquiries which might mean that there will be a greater number of enquiries in the future. However, given the resource constraints already mentioned, we trust that such enquiry efforts will be carefully targeted and if necessary constrained, as responding to enquiries which do not have a serious and realistic basis in expected error (or worse) generate considerable and unproductive expense for both Revenue Scotland and compliant taxpayers.

We are aware that Revenue Scotland has raised queries with taxpayers or agents which have been resolved without the need for a formal enquiry. We welcome this approach, but would suggest that it is still desirable for enquiries to be carried out on a risk basis for the reasons set out above.

**Resource**

We are concerned that the issues outlined above might be the result of a lack of funding in Revenue Scotland and that the organisation might not have access to sufficient resource to perform all of its functions in the most efficient and effective way.

We suggest that the Scottish Government reviews the resources spent by HMRC in administering and collecting SDLT (and whether that there have been any changes in funding due to recent changes in SDLT). This could help to provide a comparator for determining whether Revenue Scotland has sufficient resource.
Short Term Improvements

In the short term, we would suggest that Revenue Scotland:

- Sets up a support helpline to avoid the need for formal requests for opinions
- Produces a form of mandate
- Produces a 3 year lease form
- Drafts additional sections to the guidance, particularly where there are gaps and where SDLT guidance exists on the same wording. This is necessary and indeed urgent where Revenue Scotland’s views differ from those of HMRC on the same or analogous wording
- Issues drafts of guidance for comment in areas of particular complexity
- Improves the Opinions Service so that it is easier for taxpayers to achieve certainty in relation to their tax affairs and also by publishing opinions requested and provided (on an anonymised basis).

Parliamentary Procedures

In relation to the implementation of ADS, Revenue Scotland carried out a range of activities to help with its introduction. The organisation had a very difficult task – the short timeframe between the announcement and date of implementation meant that advisers had little time to prepare themselves for the new regime.

The deadlines also affected timescales for parliamentary procedures and consultation on the ADS Bill. The Scottish Government sought to introduce the ADS at the same time as the SDLT supplement came into force in England and Wales (in order to mitigate the risk of any related impact on the Scottish property market). That meant that the usual consultation process could not be undertaken fully, in order to facilitate a truncated timetable for parliamentary consideration of the Bill.

At stage 1 of the Bill, the Finance Committee stated:
“The Committee recognises that as more financial powers are devolved to Holyrood there will be occasions such as with the current Bill when a tension arises between the need to take swift decisions on tax matters and the consultative principle which underpins budgetary and legislative scrutiny within the Scottish Parliament.

In particular, given the inevitable impact of tax policy changes at a UK level, as has already been clearly demonstrated in relation to residential LBTT, the Committee recognises the need to build an element of flexibility into the scrutiny process. In essence there is a need to balance the risk of not responding immediately to tax changes at a UK level with the risk of unintended consequences from making legislative changes without conducting a full consultation and full parliamentary scrutiny.”

We believe that further consideration should be given to the potential impacts on the devolved taxes of tax policy changes at a UK level. With the devolution of additional tax powers, both the Westminster and Holyrood Governments will need to work closely together to ensure that both Governments are aware of what the other is doing. This is particularly important in the context of mitigating the risk of tax changes in one jurisdiction impacting on the other.

We appreciate that in every tax jurisdiction situations might arise where changes may need to be made to the tax system swiftly without advance consultation. However, generally, and where there are significant changes involving complex legislation, we would welcome full discussion of principles and consultation before the necessary parliamentary scrutiny and the eventual passing of legislation. We would also be very grateful for any procedural reform that would lead to greater certainty on when announcements for proposed changes to the devolved taxes might be made.

The UK regime works with the annual Budget and Finance Bill cycle. Each year the Chancellor of the Exchequer presents the Budget, which contains all the tax measures for

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the year ahead. Traditionally the Budget has been in March, prior to the start of the tax year on 6 April. More recently, some tax measures are also announced in the Autumn Statement, late in the calendar year. The latter in particular often contains detailed announcements, with opportunities for consultation and draft legislation made available. It is fairly well known when these announcements are likely to be made. The statutory provisions to effect these tax measures are generally set out in a single Bill: the annual Finance Bill. The UK also has the provisional collection of taxes regime which enables the UK Government to introduce changes to tax rates and amend tax thresholds on Budget Day prior to the Finance Bill receiving Royal Assent, subject to the House of Commons approving these measures.

We suggest that Scottish Ministers consider the introduction of an annual Scottish Finance Bill, with changes to the tax regime included in the Scottish Budget or within another fixed announcement. Providing a timescale for when the Scottish Government is likely to declare tax changes would help to ensure a greater level of certainty for the business community generally. We would also encourage Scottish Ministers to consider introducing a Scottish equivalent of the provisional collection of taxes regime which might allow for a more effective mechanism for altering changes to tax rates in particular; this method of operation is also extremely effective in relation to some anti-avoidance rules and militates against the forestalling mentioned earlier.

Finally, we are aware that HMRC has a close relationship with the Treasury, and that HMRC plays a greater role in the development of tax policy than Revenue Scotland does. Indeed some tax changes are promoted by HMRC rather than by the Treasury. We suggest that consideration is given to the creation of a “policy partnership” between Revenue Scotland and the Scottish Government to ensure that there is effective interplay between strategic tax policy development and policy implementation.

We have no further comments.
For further information and alternative formats, please contact:

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