The Scottish Parliament
Pàrlamaid na h-Alba

Official Report

FINANCE COMMITTEE

Wednesday 22 May 2013

Session 4

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FINANCE COMMITTEE
15th Meeting 2013, Session 4

CONVENER

*Kenneth Gibson (Cunninghame North) (SNP)

DEPUTY CONVENER

*John Mason (Glasgow Shettleston) (SNP)

COMMITTEE MEMBERS

*Gavin Brown (Lothian) (Con)
*Malcolm Chisholm (Edinburgh Northern and Leith) (Lab)
*Jamie Hepburn (Cumbernauld and Kilsyth) (SNP)
Michael McMahon (Uddingston and Bellshill) (Lab)
*Jean Urquhart (Highlands and Islands) (Ind)

*attended

THE FOLLOWING ALSO PARTICIPATED:

Alan Barr (Institute of Chartered Accountants of Scotland)
Stephen Coleclough (Chartered Institute of Taxation)
Isobel d'Inverno (Law Society of Scotland)
Neil Ferguson (Scottish Government)
David Melhuish (Scottish Property Federation)
John St Clair (Scottish Government)
John Swinney (Cabinet Secretary for Finance, Employment and Sustainable Growth)

CLERK TO THE COMMITTEE

James Johnston

LOCATION

Committee Room 5

Scottish Parliament

Finance Committee

Wednesday 22 May 2013

[The Convener *opened the meeting at 10:00*]

Decision on Taking Business in Private

The Convener (Kenneth Gibson): Good morning, everyone. Welcome to the 15th meeting in 2013 of the Scottish Parliament's Finance Committee. First, I remind all who are present to turn off mobile phones, tablets and other electronic devices.

We have received apologies from Michael McMahon. Committee members and others will also have noted that the clerk for today's meeting is Eugene Windsor. Our usual clerk, Jim Johnston, is unavailable because his wife, Emma, gave birth to a daughter, Alice, last week. She came in at a whopping 9lbs 8oz and will be a very noisy sister to young Lucy. I wish Jim, his wife, Emma, and his whole family all the best.

The first item is to decide whether to take item 3 in private. Do members agree?

Members *indicated agreement.*

Land and Buildings Transaction Tax (Scotland) Bill: Stage 2

10:01

The Convener: The second item on our agenda is an evidence-taking session on the Land and Buildings Transaction Tax (Scotland) Bill with Alan Barr of the Institute of Chartered Accountants of Scotland, David Melhuish of the Scottish Property Federation, Isobel d'Inverno of the Law Society of Scotland, and Stephen Coleclough of the Chartered Institute of Taxation. I welcome the witnesses to this morning's meeting and invite one of them to make a short opening statement.

Isobel d'Inverno (Law Society of Scotland): Shall I start, convener?

The Convener: You can toss a coin if you like.

Isobel d'Inverno: I am convener of the Law Society of Scotland's tax committee and am delighted to give further evidence on the Land and Buildings Transaction Tax (Scotland) Bill in relation to leases and partnerships. We have been working with the bill team on the non-residential lease stakeholder group and are pleased that that work is coming to fruition in the form of an amendment that will come before the committee shortly. We found our interaction with the bill team through that stakeholder group and in other aspects to be very helpful, and a lot of our comments have been taken on board. We are pleased with how things have gone and we hope that as a result of all the work, certainly on leases, the LBTT provisions will be a lot simpler and easier to operate than the stamp duty land tax provisions, and that they will be more in keeping with Scots law.

Alan Barr (Institute of Chartered Accountants of Scotland): Although I am representing ICAS this morning—I serve on one of its capital tax committees—I am a lawyer by trade. ICAS has contributed a lot to the tax process more generally and has made written submissions on this bill in particular.

All that I would like to do is draw the committee's attention to some general comments that have remained valid through the process and which are, in fact, probably becoming more valid. The new Scottish tax legislation, of which this bill is the first example, provides an opportunity to avoid complexity and to simplify and modernise the tax system.

I agree entirely with what Isobel d'Inverno said, having worked on some of the same committees as her with the bill team, but it has also been demonstrated that this is very hard stuff to do properly. It is debatable whether enough time has

been devoted to getting the legislation right in order to meet the need to bring it into line with Scottish law and practices. There is still considerable danger of provisions going through because they have to, rather than enough time being taken to get them through correctly and properly, given that the tax is not to be introduced until April 2015.

I hope that Parliament takes the opportunity of the time between now and then to change what needs to be changed and not just to go with what we have but instead, before the system comes in, to change it so that it will work better. We are up against timescales that make it extremely difficult to get everything right.

The subjects for today—leases, partnerships and deed trusts—are prime examples. The committee has not got the provisions on leases yet, because they are not in the bill. The same applies to partnerships; all that we have at the moment is a straight reproduction of very extensive and incredibly complex United Kingdom legislation, which in many ways does not, in the view of the people who work with it, work.

That is what we have at the moment. To get it all right in the timescale that the Parliament has set itself will be extremely difficult—perhaps impossible.

The Convener: On that cheery note, I invite Mr Melhuish to speak.

David Melhuish (Scottish Property Federation): I endorse my two colleagues' statements, which were fair. Alan Barr made a good point about taking the time to make the bill as good as it can be in the timeframe that is available. Given that the Scottish Property Federation's particular interest is in leases, as my written submission says, I want to add to what has been said on competitiveness, which is very important to our industry and those who lease properties from it.

Stephen Coleclough (Chartered Institute of Taxation): Since I last appeared before the committee, I have moved from being deputy president to president of the Chartered Institute of Taxation. However, I am not here today in that capacity; I am here because stamp duty land tax is one of my specialist areas.

Wearing another hat, I have been working with the bill team on the partnerships provisions. As they are currently drafted, they are very similar to the UK provisions and are extremely complex. Because of the absence of the specific anti-avoidance provision that is in stamp duty land tax, planning opportunities are available that really should not be available. We have had a lot of discussions with the bill team on that, and I urge that the recommendations from those discussions be taken on board.

I reiterate what I said in January, which is that with the bill you have a great opportunity to make a tax that is simpler and easier than what exists, that conforms with Scots law and that can be run at relatively low cost to the Government and taxpayers.

The Convener: Thank you very much. We will explore some of the comments that you made previously, but I make it clear that the committee is appreciative of all the work that you and your organisations have done on taking the bill to this stage. Clearly, that could not have been done without your expertise.

I will ask questions of the panel generally. You need not all answer each question, but feel free to answer any question. I might direct one or two questions to individuals. I will, of course, let colleagues in, but I might ask more questions later, depending on how things progress and the time that we have left.

On your references to Scots law, the bill team gave evidence at a previous meeting, but also gave some information to the committee in private. What are your views on the designation, as far as reflecting Scots law in practice is concerned? Isobel d'Inverno and Stephen Coleclough touched on that with regard to problems in leases in Scotland because the SDLT lease code is based on English law. How far do you feel we have gone in addressing that? In terms of the relation between Scots law practices and the bill, have we got it just about right without having to make a huge number of amendments that may have unintended consequences?

Isobel d'Inverno: The draft of the proposed lease schedule that we have been looking at with the bill team is probably most of the way there—of course, it is a draft, and we will have to wait to see the actual amendment. As Alan Barr said, this is tricky stuff, and the question is whether the words on the page will work as it is intended they will work. If we assume that all the points that have been discussed are reflected, I think that the draft is most of the way there.

With the best will in the world, there will be glitches, which ought to be fixed. I endorse what Alan Barr said about the need to take the time to do that in the two years until 2015. However, the draft that we have seen much better reflects the reality of how leases work in Scotland than the SDLT legislation does.

The Convener: Yes. In the private discussion it was indicated that work would go on to hone the bill in order to address some issues that have been raised.

The calculation of LBTT is one of the main issues. There are five options, as it says in our papers. For the benefit of the public record, will you take us through the options and explain why option 3 was chosen?

Isobel d'Inverno: I am afraid that I cannot remember the numbering of all the options. We rejected the option of just keeping the SDLT system, because the way SDLT works for leases is terrifically complicated and people waste a lot of time trying to figure out how to apply the legislation. The system works particularly badly for Scottish leases, because we can vary Scottish leases in ways that cannot happen with English leases. For example, the extension of leases is not dealt with at all in the SDLT legislation, and we had to agree working practice with HM Revenue and Customs. All those things meant that maintaining the status quo was not a good plan.

Another option, which was quite attractive to the Law Society of Scotland, was to base LBTT on a percentage of the rent that is paid. The idea was that that approach would be simple and it would not be difficult to find out what rent is paid. However, on further consideration a number of issues emerged. For example, there would be a need for people to do lots of returns, which would be administratively cumbersome. The tax authority might have difficulty getting the LBTT from the tenant, because that would happen over a long period of time rather than in a one-off payment at the beginning.

There was also the question of moving from the current system based on net present value to an annual payment system, which would create a cash-flow issue for the Scottish Government. For those reasons, it was accepted that LBTT as a percentage of the rent was probably not the best way forward.

Other NPV-based options were variations on a theme, such as the option to have an NPV-based calculation but to pay the tax in instalments.

We fixed on an approach whereby the NPV calculation is used, but is periodically recalculated because that will be a lot simpler than dealing with the various rules that we currently have with SDLT. For example, variation of a lease to increase the rent is treated as the grant of a new lease, which means that in SDLT-land there can be lots of new leases floating around, while in the real world there is just one lease.

If you recalculate an NPV calculation, you can do what happens in reality; after all, after a tenant takes a lease, the rent might be changed, its term might be extended and so on. A lease is a moving target, but the problem with SDLT is that it tries to take a snapshot at the beginning and then says, "But that picture might not be right, so here are lots of hoops you can jump through to try to amend your picture and take account of what happens later." Actually, what you need is a video rather than a snapshot, which is what the option of recalculating NPV tries to achieve. Under that approach, when you as the tenant get to the end of the lease and do your three-year returns, you should have paid LBTT on the actual rents. That is the aim.

10:15

Alan Barr: I endorse the suggestion that where we are getting to with LBTT is better than where we are at present. Speaking personally rather than on behalf of ICAS—I think that the principle of simplicity suits the institute—I was more fundamentalist and thought that it made sense to pay LBTT on the rent that was paid annually, if that was deemed necessary. Nevertheless, what we have is a revision and I absolutely endorse Isobel d'Inverno's comment that the problem is the snapshot approach. LBTT wants to capture a tax on a transaction that by its very nature goes on for 10, 25 or, theoretically, up to 175 years, and that is very hard to do.

Although the proposed amendments, which we saw only yesterday and to which we have made further input, are a good move towards where we want to go, one should not underestimate the complexity that remains. It will still be necessary—indeed, it will be more necessary than it is under SDLT—to go back and revise on a more formal and regular basis what has gone before. It is proposed that all that should be based on the rules and rates that are in force at the commencement of leases, but that means that the recalculation will involve a combination of the past—what has happened since either the lease began or the last three-year review—and what will happen in the lease. After all, rates might have changed and might yet change. As a result, a significant amount of estimating and the like will have to go on.

As for the practicalities, those who are much more expert in computer systems than I am tell me that it would be very possible to produce an online calculator that would do this sort of thing more readily—certainly more readily than one could do it with bits of paper and the scratching of heads—but that calculator will still be quite complicated and will not simply mirror the current SDLT calculator. The taxpayer or his or her agents will need that kind of online calculator, rather than their trying to do it without the aid of such tools. In short, the revision is an improvement but, as far as complexity is concerned, I do not think that we are there yet.

I want to take this opportunity to raise two more fundamental points that I do not think have been addressed and which, again, reflect differences

between Scotland and England. First, the date of commencement of a lease and therefore its duration—in other words, how long it lasts—are quite nebulous concepts; for example, there are a number of different days on which one might say that a lease commenced. The date of the last signature on a bit of paper is one such day and the date of entry is another; the link between the two is complicated. That has not been specifically dealt with. In a way, I do not really much care which date is set down, but something needs to be set down to clarify when a lease commences.

My second general point partly goes back to what I was saying about the process's length and difficulty. A lot of the terminology in leases with regard to SDLT at present and in the bill does not match basic Scots law. For instance, there are references to "lessees" when the Scottish term—technical and otherwise—is "tenant", which is used throughout Scots law. In my view, such an approach requires a wholly unnecessary series of changes to be made when time could be devoted to addressing more fundamental issues such as, for example, the date of a lease's commencement.

The Convener: That is a good point and I will certainly put it to the Cabinet Secretary for Finance, Employment and Sustainable Growth when he gives evidence.

Isobel d'Inverno: As well as ensuring that the words on the page reflect what we discussed, we need to be sure that—as Alan Barr said—the computer systems will deal with the mechanisms adequately. That is important, because it will make a huge difference if the online system is easy for tenants or their advisers—a lot of LBTT returns will be done by solicitors—to use. If the system is not easy to use, there will be problems. That is an issue for the future, but I hope that the committee will pay heed to it once the system has been developed.

The Convener: Yes—the bill team has told us that taxpayers will have access to an online calculator to assist them with the NPV calculation. We have before us a very interesting mathematical demonstration of what that will involve.

Under the formula given, NPV equals the sum from i equals 1 to n of r_i divided by (1 plus T) to the power of i, where r_i is the rent payable in respect of year i, i is the first, second, third and so on year of the term of the lease, n is the term of the lease and T is the temporal discount rate. However, we will not go into that at the moment.

I will switch to the issue of sub-sale relief. Mr Coleclough, in your submission you state:

"the LBTT Bill contains no sub-sale relief. As the Law Society of Scotland said, and the CIOT agrees, this is a mistake."

You go on to say:

"taxpayers should have a choice to use sub-sale relief, or another relief or provision which reduces the amount of duty payable, but not both. It is the combination of sub-sale relief with another relief which has led to avoidance."

How would that work in practice?

Stephen Coleclough: That follows up on our conversation in January. With sub-sale relief, there are always at least three parties: the original vendor, the purchaser in the middle and the final purchaser. It is possible to have a circumstance in which the original vendor does not know about the final purchaser, and vice versa.

The original vendor does not really matter; it does not affect them. The people who are affected are the intermediate purchaser, who is also a vendor, and the final purchaser. I would expect a final purchaser who is expecting to claim a relief, such as a charity or someone who for whatever reason—perhaps they are taking advantage of the partnership provisions in schedule 17—is claiming a reduced amount of tax to ask the person who is selling to them, "Please confirm that you are not taking advantage of sub-sale relief."

If the person cannot give that confirmation, there must be a conversation between the intermediate purchaser and the purchaser. They should say, "Hang on. If you are taking sub-sale relief, we need to have a discussion about whether I claim my relief"—which could be charities relief or whatever—"or you claim sub-sale relief." That discussion would be partly about price.

I would expect that, 99 times out of 100, claiming the relief would be of more value to the final purchaser than to the intermediate purchaser, although one can envisage cases in which it would be better for the intermediate purchaser to do so. There needs to be a grown-up conversation—which is partly a negotiation—to follow an initial statement such as, "I am the charity, so I will be claiming charities relief—please confirm that you are not claiming sub-sale relief."

At present, with SDLT, sub-sale relief can apply only if both the property transactions are completed on the same day. We do not currently have a situation in which the first leg can be completed and the second leg is completed years later—it all happens on the same day.

There will—or should—be that visibility in the returns process to enable people to see that the same property has gone from A to B to C on the same day. It should not be beyond the wit of man to pick that one up—even just through exception reports—on an automated system.

Before that, the final purchaser and the intermediate purchaser would need to have a negotiation about who is going to claim which relief. At the moment, one of the popular general features of sub-sale relief planning in the UK has

been that it is possible to do it without the vendor knowing. The vendor thinks that the purchaser is paying 100 plus 4 or 5 per cent duty but, in reality, they are not. The vendor would be taking into account the fact that the purchaser is having to pay an extra slug of tax on top of the price, and that will go into the price calculation. The vendor will think that the purchaser is paying 104—they get 100 and the taxman gets 4. Then, the purchaser does a sub-sale without the vendor knowing, that 4 disappears and the purchaser pockets the savings.

The Convener: So we need transparency in the process.

Stephen Coleclough: It is no more transparency than what we would get through the inquiries that someone makes about a building as to its status, survey, environmental condition or the tenants who are currently in it. Those sorts of inquiries and that sort of information would have to be asked about and examined anyway. The one extra thing that would be asked is whether there is an intention to claim sub-sale relief.

The Convener: Colleagues will probably explore that issue further.

Time is marching on, and I want to allow colleagues in, so I will just ask one other question, about partnerships, which are another issue that you have all touched on in your written submissions. Turning to Stephen Coleclough, I note that the CIOT submission states:

"there is a question over a transfer in a partnership which has an interest in a partnership which in turn owns land in Scotland. Is such a transfer liable to LBTT and/or entitled to the special provisions in schedule 17 of the Act?"

You then state:

"The answer ... should in our view be 'yes' ... We think the Scottish Government has implicitly accepted that a transfer of a partner does not give rise to tax."

Could you talk a wee bit more about the whole issue of partnerships and where we should go from here in that regard?

On a point of clarification, there is something in paragraph 2.4 of your paper that has mystified me, and possibly other colleagues. It states:

"there is no LBTT equivalent of ss75A-75C FA 2003".

Could you tell us a wee bit more about what that is? I personally am baffled by that.

Stephen Coleclough: Referring back to what I said in January, I advise all members to take two Nurofen before we start this conversation.

I will first pick up on the multitiered partnerships point in paragraph 2.2. At the moment, the SDLT rules say that someone should look through all partnerships to the partners. The wording is not clear on whether that means that someone should go just one level through the partnership that owns the land. If one of the partners is themselves a partnership, should the person go up to the partner at the top? If that partner is a company, everybody accepts that, if the company is sold, there is no tax at all. We cannot deal with that.

The question is this: if the top partner sells his interest in a partnership that has an interest in a partnership that owns land in Scotland, does HMRC want the tax? The current position under SDLT is that HMRC will say that it indeed wants the tax. If you ask HMRC, referring to the same provision, whether that means that you can pay a lower rate of tax under the partnership schedule, the answer is no. The words and the provision are the same, but HMRC's answer is yes, it wants the tax, but no if you want a reduced amount of tax.

I am saying, "Please nail your colours to one mast." The HMRC should say either yes or no. My advice would be to say yes. That would mean that the provisions of schedule 17 to the bill, parts 4, 5 and 6, would apply all the way up the tiers of partnerships, and so would the charge to tax. Are you with me so far?

The Convener: So far.

Stephen Coleclough: My advice would be to say yes—we look all the way through for all purposes. We should be clear about that.

I do not think that you need to change the wording of the bill in that regard, but you need to be clear in your published policy that that is your view and that is what you think the law says. The position in the UK at the moment, on the other hand, is that the answer to the question depends on the question that you are asking. That is not acceptable, because it creates uncertainty and gives power to the Executive rather than to Parliament.

Sections 75A to 75C of the Finance Act 2003, to which paragraph 2.4 refers, are a targeted anti-avoidance rule that is aimed at stopping avoidance in stamp duty land tax. In summary, that rule involves looking in a series of transactions at who had the land first and who has it at the end, imagining a notional transaction between the first party and the final party for all the money that has flowed between them, and multiplying that by the rate of duty. If that is more than the duty that has been paid, HMRC will have the remaining duty. It is a general provision of that sort.

10:30

That provision came in in 2006. When it came in originally, it said that, in computing the rules for sections 75A to 75C of the 2003 act, account could be taken of what is in parts 4, 5 and 6 of schedule 17 to the bill. That meant that certain

planning schemes could still be carried out, notwithstanding the targeted anti-avoidance rule, because that rule allowed for the provisions that are contained in parts 4, 5 and 6 of schedule 17 to the bill. That was countered in stamp duty land tax by saying that, for the purposes of the anti-avoidance rule, schedule 15 to the UK act—or schedule 17 to the bill—could not be relied on. That is how such planning was stopped. That anti-avoidance provision, as it was amended in 2010, prevents such planning. As the bill does not include such an anti-avoidance provision, what is being implemented in schedule 17 is the pre-2010 version of SDLT partnership rules. That means that, in certain circumstances, a number of planning opportunities will be available, to which the Scottish Government is basically inviting people to help themselves.

In paragraph 2.4 of our submission, we have repeated what we said to the UK Government in 2010 about the best way to deal with the issue. The schemes in question rely on creating what HMRC calls "contrived connections"—in other words, making the seller and the buyer connected for tax purposes through contrived means. In 2010, the way in which we suggested that HMRC could deal with that was to say that people could take advantage of the connection rules that are in schedule 17 to the bill only if they had been connected not only at the time of the transaction, but for the entire 12-month period before that. In reality, if I were someone who wanted to sell a property, I would not hang around for 12 months waiting for a planning scheme to mature so that the purchaser could save money. I would want to sell the building. If the purchaser asked whether we could wait 12 months to save 4 per cent, I would say that I had a better offer.

The Convener: We will come to Alan Barr once we have heard from David Melhuish, who said in his organisation's submission:

"It would appear to be a missed opportunity if we do not at least clarify the law relating to LBTT and partnerships."

Will you expand on that?

David Melhuish: I was comparing the situation on partnerships to the constructive engagement that has taken place on the leases side of things and how the Government has worked that through. We are now in a position in which there will be detailed provisions on that in the bill.

I just felt that, to date, partnerships have not had quite the same attention. For the reasons that we have just heard, I think that it would be a missed opportunity if we did not get some clear provisions on partnerships into the bill before the end of stage 3. Touching on some of the comments that Alan Barr made at the beginning, I think that it feels as if partnerships are another area in which, had there been just a few more months' time, the officials would have had a chance to work up their proposals further and to put them before the Parliament again after holding further deliberations with people who have the kind of expertise that the committee is benefiting from today.

One of the problems with the SDLT legislation is that it has been built on over and over in 2003, 2004, 2007, 2010 and again in 2013, which does not make for good legislation.

The Convener: Indeed. All the submissions talk about that.

Alan Barr: I am going to urge the committee to be much more radical than Stephen Coleclough has urged it to be. As he pointed out, the provisions on partnerships in the bill are, essentially, the partnership legislation on SDLT at a particular point of its evolution. That legislation is a disgrace. In many cases, there is a complete lack of comprehension of it on the part of people who have worked in the area for many years, including those in HMRC. It does not work and, in many cases, is ignored because people do not know that there is a potential liability when transactions happen.

I strongly urge you to start again; instead of trying to build on what is already there, you should in the time available start again completely with the partnership rules and move to a simpler—if I can stick to the same theme—and effective means of dealing with transactions through partnerships. You also have what might be called a Scottish speciality opportunity, given that Scottish partnerships are different from those in England and Wales; they constitute a separate legal person, although I note that that is often a distinction without a difference, particularly in tax terms. If you work with the existing schedules—schedule 15 to the UK legislation and schedule 17 to the bill—you will be using an entirely broken toy. Instead, you should attempt to introduce a completely new system for partnerships.

It is unfortunate that, given the parliamentary process, the provision is essentially a cut and paste from SDLT and there is simply no time available to change it before the bill goes through this year. The other—and entirely reasonable—alternative would be to take it out entirely with the acknowledgement that, before a certain date, it is replaced via the tax management bill or secondary legislation. Otherwise, I regard this to be a huge missed opportunity to deal with some of the most complex and incomprehensible legislation that we have—and I can tell the committee that there are plenty of competitors for that title in the UK tax legislative system. This legislation is one of the absolute top dogs and here is a chance to do something about it. You can either reproduce a version of it or do something different and better,

and I strongly urge the committee to do something different and better.

The Convener: I will certainly raise that issue with the cabinet secretary in the next evidence session.

I note that the Law Society's submission has suggested that

"a working party should be established to consider LBTT and partnerships in more detail over the coming months."

Isobel d'Inverno: Absolutely. Alan Barr was quite right to call the SDLT partnership legislation a disgrace and a dog. It offends against all of Adam Smith's principles, as mentioned by the cabinet secretary. Stephen Coleclough's earlier response is an excellent illustration of how complicated the system is and how people cannot understand it. Admittedly, it has to deal with a wide range of different partnerships from big funds set up through partnership vehicles to family partnerships, farming partnerships and so on but, as Alan Barr pointed out, it is often ignored because people do not understand it. It really needs to be looked at again.

Although we should bear in mind that partnerships have been used a lot for tax avoidance, the fact is that SDLT partnership rules are based on income-sharing ratios. People find that difficult to understand because in real partnerships in the real world there are profit-sharing ratios and capital-sharing ratios, which are different. Automatically, therefore, you are off on the wrong foot and trying to work out how the partnership rules apply is like being Alice in Wonderland. It is simply not a good state of affairs.

That said, sorting all this out will not be the simplest thing in the world and certainly would not have been possible in the timescale that we had. As a result, I recommend that, as Alan Barr has suggested, the provision be deleted and a working party be set up to put together a better and more appropriate partnership code.

Alan Barr: Although this is all horrendously complicated, the principal starting point—and the Scottish Parliament is rightly a great believer in principles in legislation—is that transfers of economic value of land and buildings through partnership should be treated no better and no worse than the same transfers done directly. That, if you like, is the principle. Although attempts to apply it through the complicated legislation that we have have pretty well failed utterly, if you start with that principle instead of building on what you already have, we have every chance of having a system that embraces it.

The Convener: I open out the session to questions from colleagues. The first will be from the deputy convener, John Mason.

John Mason (Glasgow Shettleston) (SNP): I want to press Mr Barr on the issue of timescales. The submission from ICAS—I should say that I am a member of ICAS—suggests that we want decisions made more quickly, particularly in relation to the bands and rates. The cabinet secretary has said that he will announce them nearer the time, but ICAS and others have said that they want them sooner. However, Mr Barr now seems to be saying that he wants us to put the whole process on hold while we go away and write some completely new legislation, which would therefore not be ready until very close to the date. Will you explain that?

Alan Barr: I appreciate that there is a dichotomy. ICAS's request for an indication of rates is as much for commercial certainty as anything else. Individually, I fully understand that we do not know what the rates will be in April 2015 and that we might not know that before December 2014.

The difference, however, is in the form of the legislation. The issue is not about the fundamentals, but there is a need to concentrate on the details by such means as working parties and, if necessary, schedules to bring in measures by secondary legislation. That is by no means ideal, but I appreciate that we do not live in an ideal world. The suggestion is not at all to put the process on hold; it is to devote the time that we have available between now and the necessary introduction to getting the provisions more and more correct and usable, which would have to be done gradually. That does not at all preclude putting through the fundamentals that can be got through at the earliest possible stage. It is a question of choosing between doing it quickly, doing it cheaply and doing it properly. Maybe we can have only two out of the three. I would rather have it slowly and properly done than quickly and ill done.

John Mason: That is perhaps where there is a slight difference between accountants and lawyers. In my opinion, lawyers prefer things to be done properly in the long term, whereas we accountants have to do audits by three weeks after the year end and so on.

A balance has to be struck. I wonder whether the Government has not got the balance right. Frankly, if all that the Parliament had to do was to consider a piece of proposed tax legislation, we could spend the next three years on it but, unfortunately, we also have to consider the landfill tax and the forthcoming tax management bill. We would like five or 10 years or whatever, but is the approach a reasonable compromise? I am also interested in what the other witnesses have to say on that. We have taken some of the SDLT provisions, but that is just inevitable because of

the timescales, and there is not a huge amount that we can do about it.

Alan Barr: There is a compromise, but I do not think that it is reasonable yet. We have no detailed provisions on partnerships, which is a good example of our not knowing what we are going to get. We have got what has already been produced. Yesterday, we had first sight of the leases stuff, although the Parliament has not yet had sight of that. On current timescales, the bill is supposed to be enacted by the end of June. That is a swift timescale in any sense, if we are to have time to give even a kind of detailed technical comment—rather than just a comment on the principles—to members of the Scottish Parliament, or time for the bill to be considered by people who are genuinely anxious to assist with getting it right.

There is a compromise, but it would be a better compromise if it was recognised and accepted that some bits require a good deal more work and if that work was done in the time available. That would not need to hold up anything, including the setting up of the practical systems that will be needed so that the first bit of LBTT is collected on 1 April 2015. None of that work needs to stop; indeed, it needs to leap ahead.

John Mason: Is it the opinion of the other witnesses that we have not reached a proper compromise between timescales and getting it right?

10:45

Isobel d'Inverno: I do not think that we can make that comment about the bill as a whole. You mentioned the difference between lawyers and accountants; the partnership SDLT rules are perhaps often not well known to accountants but they are encountered by lawyers and they do not work well in practice for everyday, regular partnerships. They focus too much on potential tax avoidance and big partnerships.

Those rules are far too complicated and they need to be fixed so, in relation to partnerships, it would be worth trying to do something with the bill rather than leaving it as drafted. The provisions are a cut and paste from SDLT and, as Stephen Coleclough pointed out, need some fixes to prevent some tax avoidance schemes from being able to be pushed through the cracks. Therefore, it would be worth spending some time between now and 2015 on trying to get a better partnership code.

However, our view on the bill as a whole is that it is nowhere near ready. The provisions on partnerships are a particular issue.

John Mason: Is it inevitable that we have to go through the partnerships stuff line by line and go through all the nitty-gritty? Is it not possible to have an overarching purpose provision that would sweep some of it together?

Isobel d'Inverno: It might well be. Alan Barr's expression of it is probably valid. However, I do not think that it would be possible to draft and test such an amendment by stage 3. That might be quite a big ask. We should not continue with the cut-and-paste approach that we have at the moment. That is not a good thing for the long term.

As you mentioned, the Parliament has many other things to consider. From dealing with Westminster, we have the experience that, although there may be a focus on legislation when it is being brought through the Parliament, it can be mighty difficult to get the Parliament to go back and look at it afterwards.

John Mason: That has very much been the case.

I will move on to another subject. The net present value proposal fills everyone with horror. It is a horrible calculation. I quite liked the idea of using actual rent, but I accept that things have moved on and that everybody accepts that that is not possible. The supplementary information from the Government talks about using the same discount rate to calculate net present value as is used for SDLT. Are any of you able to explain why that is the case and why it is 3.5 per cent?

David Melhuish: It is a Treasury set rate and is to do with the Treasury's green book, if I am correct. I think that it is described as the temporal discount rate. It was set at 3.5 per cent from the outset when the changes to leases—which did not happen immediately with SDLT but came in later—were set. As I understand it, the Scottish ministers will take powers in the bill to enable them to change that rate as the tax is devolved. Therefore, the Scottish Parliament will have the flexibility to change it.

John Mason: To my mind, the rate might be related in some way to inflation or interest rates.

David Melhuish: It could be.

John Mason: It seems quite strange just to choose a figure.

Stephen Coleclough: The figure was the UK Government borrowing rate in 2003, which was before the credit crunch. I think that the expectation was that long-term interest rates were moving out and that, therefore, the discount value would increase from 3.5 per cent to whatever the higher rate was. Then, of course, 2007 and 2008 happened and we now have a base rate of 0.5 per cent, so the rate has been stuck at 3.5 per cent and not been amended. That is where it came from. It was the UK Government borrowing rate from 2003.

John Mason: There is a risk that, if that became very different, there could be a gain or loss to the public revenue because the figure is way out of line with property prices and inflation.

Stephen Coleclough: That could happen, but it will be entirely within your control; you will be able to set what number you want. You could make it 0 per cent, in which case it would be actual rents.

John Mason: Okay. That is fine. Thank you.

Gavin Brown (Lothian) (Con): We have heard a lot about the partnership provisions, so I will not dwell on them for too long. The witnesses have used all sorts of adjectives and nouns to describe what they think of them. Should the provisions be deleted entirely from the bill and put into the proposed tax management bill or another piece of primary legislation? Do the witnesses have a view on what should happen?

Alan Barr: Yes. My view is that they should be deleted in their entirety from the bill. It should be recognised, however, that they will be brought back as an amendment to what will be the LBTT act before it comes into force. Whether that is by means of the proposed tax management bill or by secondary legislation is beyond my parliamentary and constitutional competence to say. However, it could be done by either of those methods.

Gavin Brown: Is that view shared by the Law Society?

Alan Barr: I am on the same Law Society committee, so with that hat on I share that view. However, Isobel d'Inverno is wearing that hat today.

Isobel d'Inverno: Our view is that that would be a better approach.

Alan Barr: It would also focus the mind. If there is legislation in place, there will be a temptation to say that we will muddle through with a version of that, perhaps as amended in some of the ways suggested by Stephen Coleclough. However, if there is a gap, and a recognition that that has to be dealt with before 1 April 2015, well, it will have to be dealt with. The worst-case scenario—horror of horrors—would be to say that we have got what is here to fall back on. We could say, "We have not managed to solve the problem. This is how it is done for SDLT now; there was provision for that in our original LBTT bill and we will bring that back." That would be a counsel of despair, but there it is.

Gavin Brown: At the start, the convener asked Isobel d'Inverno how well we have done on getting Scots legal terms into the bill. You answered that you feel that the leases proposal is quite positive, although you have not yet seen the actual amendment. Are there other elements of the bill where you think that we still need to do work to get rid of England-only legal terms, such as "lessee", and ensure that the bill is Scots-law specific?

Isobel d'Inverno: I think that there are. I ask Alan Barr to answer that question, if possible, given that he has concentrated on the issue more than I have.

Alan Barr: It is slightly odd that Isobel d'Inverno, who is an accountant, is representing the Law Society and that I, a lawyer, am representing ICAS. We are a small but friendly pond.

I have been looking at a lot of the terminology, with contributions from Professor Kenneth Reid, who was heavily involved in the land law reforms from the Scottish Law Commission that led to the abolition of the feudal system. Some amendments have been lodged as a result of the extremely useful meeting that I had with him and some of the bill team, though I suspect that more need to come.

That gives me an opportunity to mention other things that relate to the balance, which Mr Mason asked about. The committee's other subjects today include that balance. Trusts, which we have not mentioned at all, are provided for with a particularly egregious and purely English bit of law, extracted from the SDLT legislation, which I believe needs to be changed. I confess that I have not seen whether the amendments to do that have been lodged.

The sub-sale stuff provides another example of where we need to work on the detail. Quite a lot of the detail has been accepted, although the terminology was not in the original bill, and amendments now need to be lodged to bring it into play. I have mentioned the use of the word "lessee" rather than "tenant", which is just a terminology issue. There are issues that are slightly more than terminological and actually reflect practice. I have mentioned the start date and duration of a lease, which need to be looked at. It is fair to say that we are getting there, rather than that we are there at the moment.

Gavin Brown: You mentioned trusts, which prompts me to ask something else. The supplementary information provided to the committee by the Scottish Government says:

"The LBTT Bill as introduced broadly replicates SDLT legislation governing trusts."

Is that a missed opportunity in the same way as the approach to partnerships is? Is it a less contentious matter with which, broadly speaking, you are happy, subject to seeing the amendments?

Alan Barr: Yes—subject to seeing the amendments. I think that that is possibly less of a problem. It is the same sort of issue—the principle

that should be struck at is that the economic value of land is being sold, in this case through a trust, rather than a partnership. That still needs to be looked at. The provision in the bill refers to the trust law of England and Wales; that is the bit that needs to be changed. I have not seen the amendment on that yet, so I do not know whether that is to be changed.

Stephen Coleclough: I have spent a lot of time on the trust provisions independently and with the bill team. In January, we went through one point to which Mrs Urquhart found the solution, which was quite straightforward. The SDLT provisions do not work in Scotland now, and all that has been done is to copy them. They do not address Scots law at all; that is a glaring example of how the provisions need to be made to work with Scots law.

Another point that I should make is the one that I made in paragraph 8 of our submission to the committee. In a lot of places, the bill cross-refers to UK statutes, and we would much prefer it to copy out what the UK statute now says. That would make the bill easier to read and it would mean that, if the UK Government amends a provision, the bill will still have what was wanted rather than LBTT plus bits that the UK Government has tweaked without this Parliament's consent, power or control.

Alan Barr: We endorse that. That approach has been used on a few occasions, notably in relation to companies acts, and what Stephen Coleclough suggests would be useful. It might use more bits of paper, but I do not think that it is harder to extract and copy into our bill the version that we want to use now.

Gavin Brown: On a separate issue, Stephen Coleclough talks in his paper about exchanges and raises a particular concern about local authority regeneration when landowners transfer their land "to a central entity". Will you expand on that?

Stephen Coleclough: The starting point in SDLT is that, if land is exchanged for any kind of property rather than cash, SDLT is payable on the market value of that property. Practitioners quickly realised that the market value does not include VAT, and SDLT is normally payable on the price plus VAT, so HMRC thought that it was losing out.

Eventually, HMRC amended the exchange provisions in a way that it believed would allow it to collect VAT and counter tax avoidance. The amendments and the SDLT law as it stands are utterly incomprehensible; I do not know anyone who understands them. The revenue policy starts off from the proposition that HMRC wants 4 per cent SDLT on the market value of the land plus VAT.

That is fine for someone who is swapping an office block for a shopping centre. However, the situation is often that there is a run-down area in a community, such as a town centre, a high street or a redundant industrial complex, and the local authority starts a planning consultation and says that it wants to regenerate the area. The local authority could try to do that on its own with commercial partners and use compulsory purchase provisions to compulsorily acquire the whole lot, and there would be relief in SDLT and in the LBTT bill if it used the compulsory purchase order process.

The local authority would be taking and then giving out later, as there would be no tax on the acquisitions because they were under a CPO. However, the CPO process takes a long time. It is adversarial because people are not agreeing to give away their land—it is being taken from them. CPOs can be subject to judicial review. The process can go on for years while the area of land lies redundant and does not generate value for anyone. The CPO route is rarely used in practice. In practice, local authorities try to work with landowners and developers to regenerate an area.

People will own different bits of the land and those bits will be shaped for whatever the land was used for in the past. If the use is to be changed completely, the land needs to be divided into different bits with different shapes. The mechanism is therefore usually that everyone puts their property into a development vehicle and jointly develops the land, and interests are given out at the end of the process.

11:00

The processes whereby a person gives someone land and someone else gives them something back are all exchanges in terms of the SDLT legislation and the LBTT proposals. I do not have a problem with that; the problem is in the application of the provisions.

We are in the bizarre position of having to write to HMRC to argue that the value of what we are doing is nothing, even though we all know that it is many millions of pounds, because otherwise we end up with 4 per cent tax when people put everything together in one pot so that they can knock it all down and build what they want, and 4 per cent tax on the way out. That is 8 per cent tax leakage on what is basically a public-private project to regenerate an industrial area or town centre. At a time when public finances—and private finances, to some extent—are limited, that never seems to make sense. It certainly does not accord with UK Government policy.

Members need to be aware that how the exchanges provisions are drafted and how the

system applies in the UK create that problem. I urge you not to repeat the problem, because people will end up in the unsatisfactory position of having to argue that values are minimal, to avoid a tax that HMRC does not want to collect, because no one thinks that that is a sensible way of taxing anyone.

You must try to find another solution, whether that is by amending the exchange provisions, which are the root cause of the problem, or extending the CPO reliefs to include quasi-CPOs, if I can call them that—situations in which a local authority could have compulsorily purchased but is proceeding by agreement rather than by CPO. There is a precedent for that in the capital gains tax legislation, which provides for rollover relief when the threat of a CPO is sufficient.

Gavin Brown: Have you had the opportunity to raise the issue with the bill team or others in the Scottish Government before now?

Stephen Coleclough: Yes, I did so when I came up for the Chartered Institute of Taxation's joint presidents luncheon at the Signet library—I think that it was on 15 March.

Gavin Brown: You and other witnesses have said that it would be a mistake to lose sub-sale relief entirely. You suggested:

> "taxpayers should have a choice to use sub-sale relief, or another relief or provision which reduces the amount of duty payable, but not both."

Others have suggested that there should be a requirement to apply formally for sub-sale relief, as opposed to simply doing it. Do you want to say anything more about sub-sale relief, to try to persuade the Government to change its view? Have you had further discussions that suggest that the Government might be open to compromise?

Stephen Coleclough: I have not had further discussions. Sub-sale relief should be claimed. Claims are not very formal: under SDLT, reliefs are claimed by ticking a box or putting in a number—that is the full extent of the formality. The system is then policed through the inquiry mechanism or, more often than not, by the tax inspector who is dealing for the purchaser in relation to all the other taxes, such as corporation tax, who will compare what has happened on stamp duty land tax with what is before them in the accounts and tax computations.

In paragraph 7 of my submission, I alluded to the necessity of having that relationship with HMRC, which will look at forms, so that LBTT can be policed. Sub-sale relief should be claimed by ticking a box, to flag up to the tax authority in Scotland—revenue Scotland—that it has been claimed, and there should be a cross-check to see whether anything else has happened on another return on the same property on the same day. If there are flags on the return to show what has happened, there is a mechanism for policing the system.

Isobel d'Inverno: I am not convinced that just making sure that people could claim only sub-sale relief or another relief would counter all the schemes that are going about, which other advisers have offered clients of ours in the past couple of months. I am not quite so sanguine that that would be an answer to the problems of avoidance that has relied on sub-sale relief.

That is why the Law Society has suggested that the way forward is a targeted relief in relation to forward funding, for example. Perhaps such a relief could be subject to a more formal clearance approach, so that it is not just a question of ticking the box or putting the claim code in; it would be more of a formal process with the tax authority, so that it could look at the paperwork and satisfy itself.

Obviously, there is a balance to be struck between the cost of having to do that and the aim of stopping tax avoidance schemes being implemented. We have a concern because some of the schemes would make people's hair stand on end. We really do not want to have them in Scotland.

Jean Urquhart (Highlands and Islands) (Ind): Would you accept what is being proposed, with exceptions—if you know what I mean—so that there is a default position?

Isobel d'Inverno: What is in the bill is no sub-sale relief at all.

Alan Barr: We have seen no proposals yet for what is to come—if anything.

Jean Urquhart: My understanding is that we will not have sub-sale relief. In relation to Gavin Brown's questions, if we maintain that position—with the exception of the discussion in advance—will there be so few occasions when it might be considered that it could be the exception? That would be instead of leaving it open to the kind of abuse that I understand has happened through stamp duty land tax.

Isobel d'Inverno: We feel that having targeted reliefs would be a better way forward, so we focused on the forward funding transactions, which the committee has heard evidence about, the possibility of having a targeted relief for those and, perhaps in order to police that more closely, having an advance clearance system. I do not think that we have been urging the Government to bring in sub-sale relief across the board.

Alan Barr: You are asking whether, if there was to be no targeted relief or nothing along the lines that Mr Coleclough suggests, the complete absence of sub-sale relief would be better than

what we have now. The answer is possibly yes, as long as the question of what I describe as nomineeship is dealt with properly—that concerns title to the property being taken in another name from that of the person with whom the original contract was made, without any economic movement involved. That might be seen as a sub-sale in some sense, but in fact it is just taking title in another name.

If I contract to buy something and instead I wish it to be held by a company that I own 100 per cent of, so I make provision to buy it in the name of myself or my nominee, my company should be able to take title under the original contract. It is not absolutely crystal clear, but I have been told that that is permitted under the bill—it would not involve a sub-sale that would be a second chargeable event, as it were. If that is the case, what we will have is possibly better than what we have under SDLT.

David Melhuish: There have been a lot of discussions. The principal concern that we have had from an industry point of view is about the financing possibilities that could be lost if sub-sale relief just goes away and there is no targeted relief.

We agree that some form of targeted relief to support financing is very important right now. It is a necessary alternative mechanism, because debt finance is simply not available, particularly in the commercial property world, to the extent that it is needed. We therefore see it as essential that there is some form of relief that will cover what sub-sale relief previously achieved.

I slightly disagree with what Alan Barr has just said, because I know from talking to our members in the development and institutional world that they are not agreed that the nominee route would address the problem of the cabinet secretary not wanting to replicate sub-sale relief, for the tax avoidance reasons that were made plain at stage 1. There is concern about the unintended consequences of that decision for the finance and funding of development going forward. We certainly urge the committee to push for targeted relief.

Alan Barr: Just to be clear, I do not think that nomineeship solves the kind of problem that David Melhuish referred to. I agree that targeted relief would be much better for that. The problem is different and real; the difference is that there are financial consequences of forward funding, which there are not in pure nomineeship.

Isobel d'Inverno: The nominee clause is terribly common; it just says that, in exchange for the price, the seller will convey the property to the purchaser or the purchaser's nominee. That happens in commercial contracts all the time. For SDLT, we are relying on sub-sale relief in order not to have two SDLT charges. We do not have LBTT relief, so we need something that fixes that. The bill team has said that that will be fixed, although we have not seen yet quite how. It might be done by guidance, published statements or whatever.

The Convener: The committee seems to have concluded its questions. We have touched on leases, partnerships, exchanges, sub-sale relief and unit trusts. Would each of you like to make any additional points?

David Melhuish: On leases, the reason for the approach quickly boiled down to a choice between what we have and the proposal to have an annual retrospective charge. The important point to stress is that it is not just about the mechanics and technicalities of how the tax is paid; there was also concern about what might happen to the number of taxpayers who might be caught. If we had an annual charge, the threshold at which the tax is paid could have reduced considerably, which would have meant a much wider net of taxpayers, with obvious implications for administration and compliance. More important is the perception of businesses and taxpayers facing a charge that, under the current system, they probably would not have to pay.

I mentioned competitiveness at the beginning, but we should not forget that, for those who pay the tax at the moment, there is just a single 1 per cent rate on the leases side of things—purchases are different. We should also bear it in mind that many of the taxpayers of SDLT on leases are probably quite large businesses that are often multilet across the country. We must bear it in mind that there will always be some form of competitive comparison in how we structure the charge.

Isobel d'Inverno: To reiterate some earlier points, we have a tight timescale but, as has been said, nothing can really be done about that, because the start date is 2015. To an extent, the date of enactment of the Scotland Act 2012 has eaten up some of the timetable. However, we must not lose the opportunity to make the first Scottish tax as good as it can be. We really do not want to have sections of it that are entirely incomprehensible.

The Convener: As there are no further comments, I thank you very much for your evidence, which as always is much appreciated. I will certainly take up directly with the cabinet secretary some of the points that you have raised.

Alan Barr: Thank you and good luck.

The Convener: We will have a five-minute recess to change witnesses and give members a natural break.

11:14

Meeting suspended.

11:22

On resuming—

The Convener: Continuing the committee's oral evidence taking on the Land and Buildings Transaction Tax (Scotland) Bill, I welcome to the meeting John Swinney, the Cabinet Secretary for Finance, Employment and Sustainable Growth, who is accompanied by Neil Ferguson and John St Clair from the Scottish Government bill team. I invite the cabinet secretary to make a short introductory statement.

The Cabinet Secretary for Finance, Employment and Sustainable Growth (John Swinney): Thank you, convener. I welcome the steps that are being taken to proceed with stage 2 of the bill. We have made substantial progress on considering issues in the bill that were raised at stage 1 and in the parliamentary debate on 25 April and, as the committee will be considering those issues as we move through stage 2, I would like to address some of them.

First of all, I pay tribute to the work of the non-residential leases working group, which has been meeting in parallel with stage 1 consideration of the bill. As the committee will be aware, the group examined a range of options for the taxation of non-residential leases against a number of criteria and, after considering the group's evidence on each of the options, I met it to discuss and identify the best way forward. Since then, the working group has provided invaluable assistance to officials in preparing provisions on the taxation of non-residential leases that will better align LBTT with Scots property law and practice and it has considered and agreed a comprehensive approach to a whole range of issues affecting the taxation of leases that will be reflected in the amendments that I propose to lodge for stage 2.

I was delighted to note that in its formal stage 2 evidence to the committee the Law Society of Scotland supports the chosen approach on the grounds that it

"should remove the many complexities which bedevil the SDLT lease code."

First, on partnerships and trusts, the provisions in the bill that cover the taxation of transactions involving partnerships broadly mirror those for stamp duty land tax. Although the provisions are complex, they have been working in practice for some years now. We had hoped to undertake a thorough review of the provisions with a view to simplifying the bill but, after carefully examining the issues, we found that even apparently minor changes might give rise to a significant risk of unintended consequences and unpredicted outcomes that would not be in the interests of either the taxpayer or the tax authority.

It has not proved possible to review the partnership provisions and discuss detailed proposals with stakeholders prior to stage 2. Although we will propose minor amendments to the provisions, any major review will have to wait until later. I note the issues that have been raised in this respect, particularly by the Law Society, and I will look carefully at the proposal to establish a working group to consider taxation of partnerships.

Secondly, on the energy efficiency proposals, a number of members noted during the stage 1 debate the existing homes alliance's proposal to link the amount of LBTT paid in residential transactions to the average energy efficiency rating for housing in Scotland. Given the issue's importance and our strong support for improving energy efficiency, I have given very careful consideration to the proposals that have been discussed. In doing so, I have sought to balance the need for a simple, certain and efficient tax system with the likely improvements to energy efficiency that would flow from the change proposed to calculating the tax liability on the sale of residential property.

I believe that the proposal would add considerably to the complexity of the tax, because additional information would be required to calculate the liability. That information might change over time and, with every house sale transaction, would have to be checked carefully for reliability and accuracy. Moreover, although I support the proposal's objectives, I could not see how it would have a direct positive impact on the energy efficiency of Scotland's housing stock. Against that background, I welcome the interest and enthusiasm that have surrounded the introduction of the proposal but I confirm to the committee that I do not intend to take it forward in the bill process.

Thirdly, on the setting of tax rates and bands for residential transactions, I understand the Edinburgh Solicitors Property Centre's view that the time between the announcement of the tax rates and bands and the introduction of the tax itself should be short to avoid any freezing of the market. Other factors that should be considered include arrangements for introducing the new tax, testing systems and communicating with taxpayers and their agents. I have also carefully considered the views of witnesses who were looking for earlier certainty on tax rates and bands for non-residential property transactions. The property development industry is key to Scotland's continued economic prosperity and I am keen to do what I can to support the issues that it has raised. My discussions with stakeholders on the

optimum time for setting out the tax rates and bands are on-going and I will clarify my thinking to the committee as the bill progresses.

On sub-sale relief, in my closing remarks in the stage 1 debate I committed to further exploring options to ensure that the property development industry in Scotland was treated fairly following my decision, supported by the committee, not to replicate stamp duty land tax sub-sale rules, which have been the subject of aggressive avoidance activity. Since then, I have met industry representatives, who have provided a range of suggestions on how we might proceed. Discussions are continuing and I will keep the committee updated on what is happening. Essentially, I am trying to balance, on the one hand, providing the development industry with the ability to structure transactions in a fashion that meets their requirements and, on the other hand, preventing the creation of opportunities for tax avoidance. Preventing tax avoidance has been one of the bill's hallmarks and I do not wish to undermine the bill's strength and reputation in that respect. I am weighing up and balancing those two considerations at this stage.

Finally, I want to thank the wide range of stakeholders who have significantly assisted the Government in this very complex policy area and look forward to continuing that consultation and dialogue with them and with the committee into the bargain.

The Convener: Thank you for that comprehensive opening statement. I will of course ask a number of initial questions and then open the discussion up to colleagues around the table. I note that Jean Urquhart has put in a bid before I have even asked my first question.

Cabinet secretary, you addressed in your opening statement many of the points that I was going to put to you. Some of the points that I, and other colleagues, will raise with you will be based not on the committee's recommendations but on the evidence that we received in the evidence session preceding this one.

My first question is a fairly straightforward one about leases. Alan Barr of ICAS asked whether there will be clarification of when a lease begins for LBTT purposes. Would it be considered to begin from when it was signed or from when someone accesses a property? We received a battery of amendments just this morning, but obviously committee members have not had time to look at each and every one of them. Will clarification be provided on that issue?

11:30

John Swinney: When a lease will commence will be consistent with the rules associated with SDLT. There will be an amendment to section 30 of the bill to provide for that. I will ask my officials to clarify.

Neil Ferguson (Scottish Government): The amendments on leases will be lodged in good time for the second day of the committee's consideration of amendments—sorry, in fact, this particular issue is dealt with in the amendments to section 30, which were lodged on Monday. The notification section—section 30—deals with that issue. The substantive schedule on leases will be part of the second day of stage 2 consideration of the bill. The committee already has the amendments to section 30, which were lodged on Monday.

The Convener: I want to move on to partnerships, which were discussed at great length earlier this morning. Most of the comments were made by Alan Barr, but other representatives around the table from the Law Society of Scotland, the Scottish Property Federation and the Chartered Institute of Taxation all said much the same—although they perhaps did not say it quite as assertively as Mr Barr. Mr Barr said that there was no detailed legislation on partnerships and that the legislation as it currently stands is "a disgrace" and completely lacking in comprehension. Other witnesses agreed with that and said that it did not work. Mr Barr also said that we should start again from first principles, that what we have is a broken toy and that all that appears to be happening with LBTT is a cut-and-paste job. Witnesses commented that the bill was a missed opportunity. Of greatest significance is the fact that they suggested that at this stage partnerships should be taken out of the bill because there is not enough time to discuss the issues.

Isobel d'Inverno of the Law Society of Scotland said in her submission, at paragraph 26:

"a working party should be established to consider LBTT and partnerships in more detail over the coming months."

Colleagues around the table suggested that there should perhaps be an amendment to the bill later on or secondary legislation on the matter.

I was taken aback by the vehemence of the evidence on this issue, which we have not really dealt with prior to now. What is your view of those comments?

John Swinney: It sounds as if the committee has had a very fruity morning, given some of the language that has been used.

In your summary of the remarks, I am not sure whether you said that the provisions on LBTT had been described as a cut-and-paste job. I would want to reject that comment very clearly.

The Convener: I was talking specifically about partnerships.

John Swinney: That is slightly different and it is helpful to have that clarified. I assure the committee that I do not view the LBTT legislation as a cut-and-paste job.

On partnerships, what we have decided to do is to replicate the provisions on SDLT, and there will be minor amendments coming forward at stage 2.

There was a very good reason why we did that. I accept that these are complex pieces of legislation; I would not deny that. We commissioned external advice to assist us in the effort to simplify the legislative provisions in relation to partnership rules. The work generated by that external commission demonstrated the complexity in the legislation that I have highlighted, which itself is a product of the commercial complexities in partnership and trust arrangements. Therefore, we were faced with the choice of entering into a debate at this particular stage in the legislative process that would see us doing one of two things.

One option would be to try to amend existing provisions to make them less complicated. I could not be confident that in doing so we would not create unintended consequences as we got to such complex territory in the legislative opportunity that we have now. It would be a dangerous step for Parliament to take.

The alternative would be to remove the provisions altogether and leave a vacuum; and I have no intention of leaving a vacuum. Therefore the rules are there and they are currently operational. I am prepared to consider the issues raised by the Law Society as part of the suggestions that it has made and to consider how best we might proceed on any further review of the question.

The Convener: May I follow up on that? Although the witnesses were broadly supportive of the Scottish Government's work on LBTT to date, the particular issue of partnerships causes concern. The witnesses said that they understand that you will be going forward with much of what exists in the current SDLT provisions. As they said, though, the problem is that those provisions, as they stand, do not work, so in transferring the provisions to this bill, that is a missed opportunity. That is why the witnesses suggested that it would be better to work on the partnership issue from first principles, so that we can add it to the LBTT bill later on, rather than include it at this stage.

John Swinney: The Government is lodging an amendment to the bill at stage 2 that will provide us with the power to amend this area of the bill by secondary legislation. Obviously, that will be subject to scrutiny and consideration by Parliament in the usual fashion. That power will enable us, for example, to enact alternative provisions if the need for those arises from the consultation and dialogue that we take forward with stakeholders. As I have said already, I am very keen to explore the suggestions that the Law Society is making.

The provisions are currently part of the SDLT legislation. Although I accept that they are complex, they are part of the existing provision and they are workable. We will seek from Parliament through the legislative process the power to amend those provisions by secondary legislation. I hope that that provides the committee with the reassurance that there is an opportunity for us to explore these questions further.

The Convener: Thank you. In your opening statement you mentioned the issue of reliefs in some detail. In your response to the committee, you said that you want to ensure that forward-funding arrangements are not subject to double taxation under LBTT and that you will work with stakeholders to achieve that objective. You said that progress is on-going. Will targeted relief be considered specifically, given the lack of debt financing? That issue was raised again this morning.

John Swinney: That is a material part of the consideration that I am undertaking. From the evidence that I have been able to discern, that is one of the factors that is a genuine issue in the marketplace. Therefore we need to ensure that opportunities to attract finance are in place to enable developers to take forward transactions of that character. It is important that that is reflected in how we structure any provisions in the bill.

As I said in my opening remarks, essentially I am trying to take forward measures that will assist the development industry and recognise the contribution that it makes to the Scottish economy. However, I do not want to do that in a fashion that opens up the opportunity for avoidance, because we have taken a very clear line on that and I do not want to dissipate that.

I do not think that we could do proper justice to any alternative provisions within the legislative process that we have in front of us, so I do not foresee bringing to the committee or to Parliament stage 2 or stage 3 amendments on this provision. However, I am exploring what opportunities we have to design mechanisms that would enable us to take forward an approach of this type. Of course, that would be provided for through the order-making powers in the bill and would be subject to consideration by Parliament under the affirmative procedure.

The Convener: Before I open up the session to colleagues, I have one final question, which came

from the Law Society this morning. On the deliverability of LBTT, where are we on the computer technology and systems that are needed?

John Swinney: Progress on the development of the necessary procedures is assessed on a regular basis to determine whether the plans are on target. The last report that I saw indicates that the work programme is being maintained, so I am confident that the preparations are in order to ensure that the necessary operational arrangements are in place to support the introduction of LBTT in April 2015.

Jean Urquhart: Good morning. I have never been the second person to ask a question, which is why it is so extraordinary that I have put my bid in early.

Although I accept that you are making allowances in the bill for changes to be made later on, would you have liked to have had more time to address the bill, in an ideal world? Are you confident that the issues that need to be addressed are going to be addressed in reasonable order?

John Swinney: Yes, I am happy with the time that was available. We have undertaken extensive consultation on the formulation of the bill. Some of that throws up issues of genuine disagreement, so on the question of sub-sale relief, for example, I have taken a particular policy position. I did not need any more time to come to that policy position; I had all the time in the world. Arguments are being marshalled now that were marshalled during the consideration of the bill about particular issues in relation to the development industry, which I considered at the time and by which neither I nor the committee were persuaded. In the light of further representations, I am considering those again and I will come to a conclusion about whether there is a satisfactory balance between providing for those issues and not jeopardising our position on tax avoidance.

We have also been able to undertake, for example, quite extensive consultation with stakeholders on issues around leases that were not concluded by the end of stage 1. I understand from this morning's panel that there is general agreement that that work has been well undertaken and well consulted on. Further issues about partnerships have been raised this morning, but they relate to a specific and narrow set of provisions and I am happy to consider what other measures can be taken in that respect. There are provisions in the bill that deal satisfactorily with partnerships.

11:45

Jean Urquhart: On the cut-and-paste suggestion, Stephen Coleclough spoke about how the bill cross-refers to the United Kingdom statute. He suggested that we would be vulnerable if the sections of the UK legislation to which the bill cross-refers were changed because we do not have any control over that legislation, and that those provisions should be written out in full. What do you think about that?

John St Clair (Scottish Government): There are only one or two references in the bill to UK acts, and they are firmly rooted in company law. There did not seem to be any reason for writing out at great length the provisions in the Companies Act 2006, for example, which are very unlikely to change. If we had time later and there was such a change, we would certainly introduce our own legislation. Our approach also gives users of the legislation some link to the old legislation, so it is easier for them to know where particular provisions came from.

Jean Urquhart: Can you give us an example?

John St Clair: The definition of "connected persons" in section 1122 of the Corporation Tax Act 2010 is a very long provision, and we reference it in our bill rather than replicate the language. That is the main reference that Stephen Coleclough is talking about. It would have added quite considerably to the length of the bill if, every time we referenced it, we had to write it out in full. It is very unlikely that that definition will change in the near future so there is no immediate risk. What we have done gives users a link to the old legislation, and we think that that is a user-friendly approach. There is not a particularly Scottish thing about "connected persons".

Gavin Brown: On that point, if there are not many such references in the bill, would it not be easier just to cut and paste? Would it not be more user friendly to have the entire text contained within one act instead of people having to go and look at one or two UK statutes?

John St Clair: Apart from in one or two cases, we have taken that approach in other areas of the bill, where we have written out at length other, more obscure, references in our own language. We called the balance in this case. It was not thought to be a big issue but we will certainly reflect in future on whether there should be a blanket policy of never referring to UK statutes. That has not been the policy in the drafting of the bill.

Gavin Brown: The convener's first question was about the definition of when a lease commences, which has been raised in evidence. I understand that amendments to section 30 have been lodged to address that point. I have just

looked at those amendments, which, if I am right, are amendments 19 to 23. Where is that definition?

John St Clair: The amendments, which the committee will consider on day 2 of stage 2, will introduce the leases schedule, which goes into fine detail on the stage at which a lease becomes an effective land transaction for the purpose of the tax statute. You probably know that lease paperwork is not simple. Missives for let can be a lease, and there can be missives that are acted on and substantially performed, and then that becomes the date of the effect of transaction. All those scenarios will be spelled out in the leases schedule when it is introduced.

Neil Ferguson: I am grateful to Mr Brown for asking that question. The information that I gave earlier was not quite right. In relation to section 30, I was referring to when a lease becomes notifiable—in other words, when a tax return is due. As regards the beginning of the lease, that will be in the schedule that will be considered on the second day of stage 2 consideration. I am grateful to have the opportunity to clarify that.

Gavin Brown: I return to the partnership issue, which the convener raised and which was heavily emphasised in our first evidence session today. The contention of the witnesses was that the proposed provisions are not workable. You spoke about the existing provisions, which you said are workable. The other witnesses used terms such as "broken toy", "dog" and "disgrace". Their central contention was that the provisions as drafted are not workable. Is it possible simply to delete them and have the public position that you will not leave a vacuum and will deal with the matter in the fullness of time? By doing that, there would be no way in which we could revert to the current provisions. I am slightly concerned about having a section that says that we can consider the provisions using an order-making power, because that retains the option of keeping them. The evidence from today, at least—I appreciate that it was from only four people—is that the provisions are not workable. Can you not simply delete them? That would force the Government to replace them with something that is deemed to be workable.

John Swinney: People use their own terminology—it is up to them what words they use. I do not find those terms particularly insightful. Things might be complex, complicated, tiresome and exhausting, but they are still workable. That is my contention. The provisions are not easy, simple, straightforward or particularly user friendly; neither are partnerships or trusts particularly user friendly, convenient or simple. The whole area is very complex.

It is better to be considerate with regard to how we approach these questions and to reflect on the fact that, although there are complexities, challenges and difficulties, they are of the essence or nature of the activity involved. In my view, the provisions are workable, although they could do with being simplified. I commissioned external advisers to provide me with a route through that, but it was not possible to provide me with one that I could conclude during this legislative process.

Throughout this process, the Government has aimed to act in good faith in all the approaches that we are pursuing. I gave the committee an assurance that I was going to consider the leases question in detail in order to reach a satisfactory outcome. We set up the non-residential leases working group, which has been a highly participative process. I have met the group and, from what I could see, it has had a pretty good go at resolving the issues. The Government will make the necessary amendments to the bill to enact the conclusions that we have reached.

I intend to take exactly the same approach to partnerships. I do not think that anybody would think it particularly appropriate for me to leave a vacuum. I do not think that that would be a responsible thing to do. I give the committee a commitment that we will very actively consider all the areas with stakeholders, as we have done for every other provision in the bill. If there are solutions that we can pursue, we will pursue them through the amendments that we will advance to the committee.

Gavin Brown: If I heard you right, your intention is to set up a working group along the lines of what you did in relation to non-residential leases—or am I putting words in your mouth?

John Swinney: A working group is an option. As I said, I am considering what the Law Society has suggested in its submission to the committee. We will seek order-making powers to enact any changes that are required. I am happy to give the committee an assurance that we will take forward our approach to these matters in the same spirit and ethos in which we have taken forward our approach to non-residential leases.

Gavin Brown: At this stage, you take a different view from that of the witnesses from whom we heard earlier. You feel that the partnership provisions are workable.

John Swinney: I think that they are workable, because they are working at the moment. I am not being facetious—they are working, so they must be workable. That does not mean to say that they are not complicated, difficult or onerous. I am not suggesting that what the witnesses said in that respect is not the case, but the current arrangements are workable. I think that we should

keep them in place and consider the issues that have been raised about them. The amendments for which the Government will seek parliamentary consent will ensure that we have the necessary instruments in place to take forward any alternative provisions.

Gavin Brown: I will leave it there. Suffice it to say that there is a debate about that. The view that our earlier witnesses took was that the partnership provisions are not working or workable, but I appreciate that you take a different view.

John Swinney: I have said that they are working, so I consider them to be workable.

John Mason: We have just been talking about non-residential leases. As I understand it, you and the working group considered five options. When I first read those options, I found the idea of basing the tax on rent that is actually paid quite appealing, because that is a real number rather than a complicated formula. Will you explain to us why that option has not been chosen and we are going down the net present value route?

John Swinney: Essentially, the rent that is actually paid will be a material consideration that underpins the net present value consideration that is undertaken. That is an important strengthening element in the approach that has been taken.

The issue of administrative complexity has a bearing on some of the judgments about making the calculations based on actual rentals paid, as that would increase the amount of bureaucracy that all parties had to become involved in through registering and supplying information. The approach on which we have agreed is designed to minimise that administrative complexity and to strengthen the relevance of the substance of the judgments that are arrived at on the net present value.

John Mason: Was I right to get the impression that the delay in the tax coming in, whereby it would come in only after, rather than ahead of, the end of the year, was a reason for not accepting that option?

John Swinney: In addition to the issue of administrative complexity, there is a likelihood that there would be delays in tax payments, some of which might be difficult for us to overcome in the context of our commitment to the bill being revenue neutral. I think that that would be a genuine risk.

John Mason: So even if the bill were revenue neutral over, say, five or 10 years, would I be right in saying that you do not have the flexibility to cover such delays in payments with your borrowing powers?

John Swinney: I would prefer not to exhaust that. I think that the approach that we have agreed on minimises the administrative bureaucracy and reduces the extent to which we might have to seek to utilise the mechanisms that are available to balance tax revenues.

John Mason: The net present value calculation includes the question of the discount rate, which I asked the previous witnesses about. As I understand it, the 3.5 per cent discount rate is based on UK Treasury borrowing levels some years ago. I think that I am right in saying that you will have the power to vary that rate.

John Swinney: We will have.

John Mason: Will you look at doing that? I would have thought that, because inflation and interest rates are likely to vary over the long term, that could seriously affect the tax that we get in.

John Swinney: That gets to the nub of the calculations that will have to be made around rates and the variety of other financing factors that we have to take into account. Yes, it is a material consideration and it will be part of the financial modelling that I will take forward. Once the block grant adjustment is made, we have to give active consideration to what revenue will be raised as a consequence of the type of measures that we put in place, bearing in mind that there will be an effect on the overall resources that are available to the Scottish Government to support our priorities.

12:00

John Mason: That is reassuring. I was just a bit uneasy at the 3.5 per cent appearing almost out of nowhere, but obviously the figure could vary over time.

The final area that I want to touch on is charities, which we have spent quite a lot of time on. Amendment 13 states:

"the body is registered in a register corresponding to the Scottish Charity Register".

It goes on to detail the alternatives, such as that the body is approved in England and Wales or other European Union countries. Will you expand on that a little bit? The words "corresponding to" seemed a little vague to me and I wondered whether we are happy that the wording will ensure that we really will get charities that fit in with what we mean by charities.

John Swinney: We have endeavoured to recognise the issues that were raised at stage 1 around charities relief and to recognise the status that charities that are not registered with the Office of the Scottish Charity Regulator and are not habitually operating within Scotland have as registered charities in another jurisdiction. The wording that we have put in place is satisfactory in that respect. I think that it provides clarity about our intention. It means that a body would be able

to operate in Scotland in the fashion envisaged without there being the need for separate registration. We are certainly confident that the wording will enable that to happen.

John Mason: I think the point was made that if we were too rigid, we would be open to challenge from the European Union that we were excluding European charities. Is the feeling now that this will stand up—

John Swinney: Those are the considerations that we have been trying to overcome with the wording that we have put in place. The terms of amendment 13 give us sufficient clarity on that point.

The Convener: There are no further questions from committee members, but I want to touch on a couple of points. One is a point that Neil Ferguson explained in our private briefing prior to the first evidence session this morning, but I want to ask about it on the public record. It is about bringing the legislation into line with Scots law and practices.

The supplementary information from the Scottish Government states:

"Scots property law is different to English property law and the LBTT non-residential lease provisions have been designed, as far as practical, to reflect Scots law and practices."

Will you tell us a wee bit more about that?

John Swinney: In essence, we have tried to formulate the legislation in a fashion that is reflective of the character and terminology of Scots law. That was one of the weaknesses of the SDLT provision that has been in place. The exercise that we have gone through has been designed to formulate a set of provisions that are able to be judged consistently and in accordance with the body of Scots law. There will of course be reference points to matters—the point that John St Clair made is relevant here—where terminology that is used in other legislation but which is not significantly material to require to be changed into the terminology of Scots law has been maintained. Our effort has been to provide as comprehensive an exercise as we possibly can in that process.

The Convener: Finally, I will touch on the issue of residential property holding companies, which has not been raised today so far.

The supplementary information provided by the Government to the committee states:

"The LBTT Bill contains a power to allow Scottish Ministers to make regulations to ensure that qualifying transfers of interests in 'residential property holding companies' are subject to LBTT."

The submission continues:

"The Scottish Government intends to bring forward some minor amendments to the regulation making power."

The document gives further detail about that, but can you give us a wee bit more information for the record?

John Swinney: The amendments will clarify that regulations can be made to cover residential properties that are part of larger property holdings. We are anxious to ensure that all the vehicles that it would be possible to construct in that area are properly taken account of in relation to the provisions in the legislation. We also want to have the flexibility to set different tax rates and bands to apply to charges for the transfer of interest in a residential property holding company. We aim to put in place a particular device to ensure that all transactions that inherently and philosophically give rise to a charge are caught by the charge that is brought forward.

The Convener: Essentially, you are looking to ensure that there is no avoidance.

John Swinney: Our aim is to ensure that the provisions are as comprehensive as they need to be; clearly, that is to ensure that the tax is fully complied with and that as far as possible we minimise avoidance.

The Convener: I thank the cabinet secretary and his officials for their contributions, and thank our colleagues for their questions.

12:07

Meeting continued in private until 12:12.

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