The Scottish Parliament
Pàrlamaid na h-Alba

Official Report

FINANCE COMMITTEE

Wednesday 12 March 2014

Session 4

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FINANCE COMMITTEE
8th Meeting 2014, 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 (Law Society of Scotland)
Isobel d'Inverno (Law Society of Scotland)
Philip Simpson (Faculty of Advocates)
John Swinney (Cabinet Secretary for Finance, Employment and Sustainable Growth)
James Wolffe QC (Faculty of Advocates)

CLERK TO THE COMMITTEE

James Johnston

LOCATION

Committee Room 5

Scottish Parliament

Finance Committee

Wednesday 12 March 2014

[The Convener *opened the meeting at 09:30*]

Decision on Taking Business in Private

The Convener (Kenneth Gibson): Good morning and welcome to the eighth meeting in 2014 of the Scottish Parliament's Finance Committee. I remind everyone present to turn off mobile phones and other electronic devices, please.

Our first item of business is to decide whether to take in private items 5, 6, 7 and 8. Do members agree to do so?

Members *indicated agreement.*

Subordinate Legislation

Budget (Scotland) Act 2013 Amendment Order 2014 [Draft]

09:30

The Convener: The second item on today's agenda is to consider the Scottish statutory instrument that provides for the 2013-14 spring budget revision. Before we come to the motion seeking our approval of the order, which is agenda item 3, we will have an evidence-taking session on it.

I welcome to the committee John Swinney, Cabinet Secretary for Finance, Employment and Sustainable Growth. The cabinet secretary is accompanied by two Scottish Government officials: Mr Gordon Wales, deputy director, finance programme management division; and Mr Terry Holmes, principal accountancy adviser, corporate reporting division.

I invite the cabinet secretary to make a brief opening statement.

The Cabinet Secretary for Finance, Employment and Sustainable Growth (John Swinney): Thank you, convener.

The spring budget revision provides the final opportunity to formally amend the Scottish budget for 2013-14. It deals with four different types of amendment to the budget. The first is funding changes that impact on the spending power of portfolios and programmes. Secondly, it makes a number of technical adjustments that have no impact on spending power. Thirdly, it makes a small number of Whitehall transfers. Finally, it makes some budget-neutral transfers of resources between portfolio budgets. The net impact of all those changes is a £5.5 million increase in the approved budget, from £33,698.9 million to £34,704.4 million.

Table 1.2 on page 7 of the supporting document shows the approved budget following the autumn budget revision and the changes sought in the spring budget revision. In relation to funding changes, the spring budget revision reflects a net reduction in funding of £28.1 million. The supporting document to the spring budget revision and the brief guide that has been prepared by my officials provide the detailed background on the net funding reduction.

The following is a summary of the main adjustments. First, there is a funding reduction of £27.4 million for the receipt of police authorities' historical reserves, which accumulated prior to the creation of the Scottish Police Authority. The sum involved reflects the arrangement agreed by the

joint Convention of Scottish Local Authorities and Scottish Government settlement and distribution group. As I confirmed to Parliament in May 2013, the sum accruing to the Scottish Government has been used to address the £54.8 million reduction in our fiscal resource departmental expenditure limit budget arising from the March 2013 United Kingdom budget. The second factor is a £3.3 million reduction to the budget for the Scottish Parliamentary Corporate Body. That reflects the outcome of a rebate for rates paid for the four years from 2010-11 to 2013-14. The third is the deployment of £3.1 million of available capital DEL to the health and wellbeing portfolio to support capital investment.

The second set of changes comprises a number of technical adjustments to the budget. These non-cash and budget-neutral technical adjustments have a net positive impact of £24.7 million. It is necessary to reflect those adjustments to ensure that the budget is consistent with Her Majesty's Treasury budgeting and accounting guidance and with the final outturn reported in our annual accounts. With regard to Whitehall transfers and allocations from HM Treasury, there is a net positive impact on the budget of £8.9 million.

The final part of the budget revision concerns the transfer of funds within and between portfolios to better align budgets with profiled spend. There are a number of internal transfers as part of the revision process and they have no impact on overall spending power. The main transfers between portfolios have been set out in the guide. As in previous years, there are also a number of internal portfolio transfers that have no effect on portfolio totals but which ensure that internal budgets are monitored effectively.

The committee will wish to note that, as part of our robust budget management process and in line with good practice, we have taken the opportunity at the spring budget revision to deploy emerging underspends to ensure that we maximise public expenditure in 2013-14, in particular to support capital investment where possible. The spring budget revision records the deployment of £48.3 million of redirected budget, representing less than 0.2 per cent of the fiscal DEL budget. Details are given at annex C of the brief guide that has been prepared by officials.

The spring budget revision also reflects the proposed transfer of budget from resource to capital in respect of the Scottish budget. Members will note that the Scottish budget records capital that scores in the Scottish Government's consolidated accounts or the accounts of directly funded bodies.

In the context of our HM Treasury budget, the planned resource-to-capital transfer is £220 million. The switching is managed within the total DEL available to the Scottish Government. That is a slight reduction compared with the estimated £243 million transfer set out in the 2013-14 draft budget, and it takes account of the latest profile of the Government's overall capital programme.

Once we have provisional outturn figures in June, I intend to write to the Finance Committee with a table that sets out, in a similar format to the table provided in my letter of July last year, actual resource-to-capital transfers by portfolio and programme in respect of the financial year 2012-13.

As we approach the financial year end we will continue, in line with our normal practice, to monitor forecast outturn against budget, and we will seek wherever possible to utilise emerging underspends to ensure that we maximise use of the resources available to us in 2013-14 and that we proactively manage the flexibility provided under the budget exchange mechanism agreed between HM Treasury and the devolved Administrations.

In line with previous years, I confirm that it is my intention to make a statement to Parliament, prior to the summer recess, on provisional outturn in respect of both our Scottish Parliament budget and our HM Treasury budget.

The brief guide to the spring budget revision that has been prepared by my officials sets out the background to and details of the main changes proposed. I look forward to answering members' questions.

The Convener: Thank you, cabinet secretary. As usual, I will start with a couple of questions before opening the session out to colleagues around the table.

You touched on capital, and the spring budget revision states:

"Table 1.7 on page 11 ... provides a complete picture of capital spending."

However, table 1.7 does not allow us to establish a picture of resource-to-capital transfer by portfolio—in other words, we cannot establish which resource budgets have fallen to accommodate the capital increases or the changes that have taken place since the plans were set out in the draft budget for 2014-15. Can you provide us with some information on that?

John Swinney: I can best give definitive information to the committee on the resource-to-capital transfers when we are in a position to assess totals by portfolio, and that will be when we are dealing with the outturn situation after the end of the financial year. We gave an estimate; the latest figures were provided in response to an oral question, S4O-01396, in October 2012, and that information was publicly available.

If we were to restate those figures during the financial year, we would run the risk of putting additional numbers into the discussion at the portfolio level when we are still working on the operational decisions on capital expenditure and on the likely outturn of particular programmes. I felt that it was helpful to the committee to give my current assessment, which is that I estimate that the resource-to-capital transfer will be of the order of £220 million at a global level within the budget, but, as I indicated in my statement, I will make a more comprehensive explanation of that transfer by portfolio when it comes to the outturn statement after the end of the financial year.

The Convener: That is helpful. However, I do not think that the SBR should say that it

"provides a complete picture of capital spending."

There should be a wee bit of rephrasing in future.

Regarding health and wellbeing, I understand that there is a net revenue-to-capital transfer for national health service and special health boards of about £95 million, as detailed on page 20 of the SBR. That compares with £105 million in the draft budget. Why has that change been made?

John Swinney: The estimate that we have from the health and wellbeing portfolio is that most of the resource-to-capital transfer activity that was to be undertaken by that portfolio relates to addressing the backlog of maintenance in the NHS estate.

The committee will be familiar with the fact, which I have rehearsed with it before, that although we all think of maintenance expenditure as capital expenditure, it sometimes has to be defined as operating or resource expenditure. Perhaps the best illustration of that relates to maintenance of the road infrastructure, where the definition of what counts as capital or resource depends on how far a road has to be dug into.

The judgments can be affected by the nature of the maintenance activity. The current estimate is that £95 million will require to transfer to capital in the health and wellbeing portfolio, although the £105 million of maintenance expenditure that was envisaged when the budget was settled last year will be undertaken.

Jamie Hepburn (Cumbernauld and Kilsyth) (SNP): You mentioned a change in the local government portfolio that relates to police authorities' historical reserves and you referred to a process that involved COSLA. So that the record is clear, will you confirm that that process was agreed with COSLA?

John Swinney: Yes.

Jamie Hepburn: I presume—you can confirm this—that that is a technical matter that is bound up with the change to the police structure that Parliament agreed. As that is the case, I presume that it will have no effect on local government spending power.

John Swinney: Historically, the Government and local government funded police authorities in proportions of 51 per cent and 49 per cent, and local police boards had the ability to retain reserves. As it became clear that Parliament would agree to establish a single police service, we opened discussions with local government about the accumulation of reserves, to which local government and the Scottish Government had each contributed roughly 50 per cent.

We reached a settlement with local government on the return of the accumulated reserves once a variety of factors and costs to local government and the Scottish Government had been dealt with. Local authorities are to receive a sum that is roughly equivalent to what the Government is to receive. It is for local government to deal with that as it sees fit.

Jamie Hepburn: That is a bit of a windfall for local government.

John Swinney: I suppose that the sum could be described as that.

Jamie Hepburn: You will be aware that I am a member of the Welfare Reform Committee, so I have an interest in welfare reform. I presume that the £37.9 million that is to be transferred from the infrastructure, investment and cities portfolio to the local government portfolio is the money that you have previously talked about. With that contribution, what is a rough figure for the Scottish Government's overall investment in welfare reform mitigation up to now?

John Swinney: The transfer is to be made from the infrastructure, investment and cities portfolio, where the money sat in the budget line for the welfare reform mitigation programme. It will fund local government to implement measures such as the Scottish welfare fund. At a global level, the total annual expenditure—including expenditure on discretionary housing payments, the council tax reduction scheme and other measures—is in excess of £100 million. The Government has made a commitment to sustain that expenditure over time.

09:45

Gavin Brown (Lothian) (Con): Good morning, cabinet secretary. I refer you to page 16 of the spring budget revision document. In the bottom of the two tables on that page, there is a line for energy. The total figure is £52.9 million.

John Swinney: Can we pause a second to find that page?

Gavin Brown: I am referring to schedule 3.4 on page 16 of the spring budget revision document.

John Swinney: Okay. I am with you.

Gavin Brown: In the bottom table, there is £52.9 million in the energy line. The original budget figure was £115.9 million, and the autumn budget revision figure was £68.8 million. Can you explain why the figure is now £52.9 million?

John Swinney: Essentially, that will be because of the difficulties and challenges that we have experienced in releasing expenditure to the renewable energy investment fund. I have made clear to Parliament on a number of occasions the issues that we are wrestling with in respect of projects that are coming forward for investment. Those issues are largely caused by the uncertainty about electricity market reform, which has been a persistent factor that we have wrestled with for the best part of the past 24 months and which has resulted in an insufficient pipeline of projects reaching the stage that we can fund. We are exploring different opportunities in the market to provide support, but we have not had that sufficient pipeline, and that is largely attributed to electricity market reform issues.

Gavin Brown: If we go to the level 4 data when you initially published your budget, we see that there appear to be eight headings under energy. Can you tell us how the issue affects each of those headings? You might want to provide the information in writing.

John Swinney: I will certainly provide that information. I do not have the level 4 data in front of me, but I would be happy to provide that.

Gavin Brown: I would be grateful for that.

You said that there is not a sufficient pipeline of projects at the moment. It is clear that a substantial amount of money has been removed from energy. Will that be reinstated to energy in future budgets, or is it effectively gone?

John Swinney: I have an obligation under the Energy Act 2004 to ensure that any moneys that are made available under the renewable energy investment fund are used for the purposes of that fund. We put the sums of money into the budget at what we consider to be the most appropriate opportunities, when expenditure may be required. By its nature, that involves an estimate that is based on when we think projects will crystallise to a point of meriting and attracting funding.

Unfortunately, not all our predictions will be correct, and we use opportunities to redeploy those resources so that they can be used to support other priorities. However, there is a commitment that the resources that have been allocated to the renewable energy investment fund, which totals £103 million, must be spent on the purposes of that fund over time. I think that I indicated to Parliament in my previous statement on budget-related issues and in-year expenditure changes that I would reprofile and extend the period within which I expected the renewable energy investment fund to be deployed.

Gavin Brown: What about moneys that were originally under the energy heading and which were not part of the REIF? Will they be reinstated in future?

John Swinney: It depends on what those budget headings were intended to support. If there is a demand-led budget, for example, and the level of demand has not been equal to the level for which we planned so that we cannot spend the money for that purpose, I will redeploy that money into some other area of expenditure within Government. Whether we made further provision in those areas of activity would be a matter for us to consider in any future budget rounds or spending reviews. In relation to the budget, we would make those decisions annually; in relation to a spending review, we would make them periodically.

Gavin Brown: Okay. We will move on to page 20 of the spring budget revision. In schedule 3.1, on health, fairly low down on that page there is a heading “Miscellaneous Other Services” and the figure that is attached to that is £130 million. The figure in the autumn budget revision appears to be £157 million. While “Miscellaneous” no doubt means miscellaneous, I just wondered whether you were able to shed any light on that reduction of £27 million, either now or in writing.

John Swinney: I will probably have to write to the committee about that. It is not immediately obvious to me what the relationship is between the numbers. I will be very happy to write to the committee on that point.

Gavin Brown: Okay, I will move on.

Schedule 3.9 on the Scottish Prison Service is on page 39 of the spring budget revision. Near the bottom of that page, there is the line “Scottish Prison Service Current Expenditure” and the figure that is attached to that is £266 million. Again, at the time of the autumn budget revision, that figure was £296 million. The Scottish Prison Service’s current expenditure appears to have gone from £296 million to £266 million. Can you shed any light on that?

John Swinney: It was envisaged that the Scottish Prison Service would make transfers from resource to capital. I have, however, been able to deal with that capital requirement by transfers from other portfolios and I have redeployed the resource expenditure that we have been able to free up within the prison service budget to meet a change in the profile of the cost of police and fire

pensions. During the financial year, we have seen more retiring police officers, as a result of the low interest rate climate in which we are operating, opting for a greater proportion of their pension entitlement in lump sums as opposed to recurring payments. We have to meet that short-term resource pressure that has emerged because of the choices that have been made by officers retiring from the police and fire services. The adjustments that I have made to the balance between resource and capital expenditure have enabled me to meet that particular pressure.

Gavin Brown: We are paying more now in pension lump sums but the profile over time then reduces.

John Swinney: Correct.

Gavin Brown: I note that, on page 73, the second of the tables in schedule 3.1, which relates to administration, says that the figure for Scottish Government staff costs is £164.8 million. In the autumn budget revision, the figure was £149.9 million. Are you able to explain the increase in that figure?

John Swinney: The increase is the result of our factoring in various elements of expenditure from different programmes of activity that, although taking place in other parts of Government, are subsumed within that particular figure and the administration budget at this time of year.

Gavin Brown: I did not quite follow that. Can you explain it a bit further?

John Swinney: Certain items of expenditure are undertaken by different parts of Government under what are called programme budgets, which are essentially portfolio activities. We will subsume some of that expenditure within this particular line. Indeed, if my memory serves me right, the committee and I have gone through this issue before at the time of the spring budget revision, because the number is always different from that in the autumn budget revision. We are simply taking items of expenditure that would normally be allocated under a programme budget heading and deploying them under the administration heading.

Gavin Brown: Will that require a reduction in the money for other parts of Government?

John Swinney: It is in essence the same amount of money; it is just being spent through a different channel instead of through the programme budgets in question.

Gavin Brown: Given that we are talking about an increase of the best part of 10 per cent in the staff costs budget, can you give us, if not now then in writing, a breakdown of the programme budgets that money has come from?

John Swinney: I am happy to do that.

Gavin Brown: I have just one more question, convener.

I note that, in the second table in schedule 3.14 on page 69, the figure for "Referendum on Scottish Independence" is £0.6 million. In a Scottish Government press release that was issued yesterday on the costs of the white paper and various other items of expenditure, the figure that was mentioned was higher than £0.6 million. I assume, therefore, that all the money for those items of expenditure is not coming from that budget. Is some of the figure that was mentioned yesterday being met from that budget or is it all being met by a different budget line? I have not been able to tell.

John Swinney: Of the figure announced yesterday, £405,000 comes from the £8.4 million transfer from other SG portfolios for social advertising and public information in 2013-14. Some of the costs are subsumed within that figure, which becomes £11.9 million as a consequence of the wider transfer of the £8.4 million for a whole variety of public information campaigns, including those on road safety, detect cancer early, credit union support, healthier choices and infection control.

10:00

Gavin Brown: Just for clarification, then, is the money that was announced yesterday to be found in the strategic communication line, which refers to £11.9 million?

John Swinney: It is part of that £11.9 million, which is driven by the transfers from other SG portfolios for social advertising and public information in 2013-14 mentioned in the top part of page 69.

Gavin Brown: So all the money mentioned in yesterday's press release is contained in that one line and is not split across different budget lines.

John Swinney: From the information available to me, it appears that there might be some in the strategic communications line and some in the referendum on Scottish independence line. To be on the safe side, I had better say that the money is contained in either of those two lines. It will certainly not be included in any other lines.

Gavin Brown: I am grateful for that.

John Swinney: I should also put on record that a full and clear explanation of the costs involved was given in a parliamentary answer yesterday.

John Mason (Glasgow Shettleston) (SNP): Cabinet secretary, I wonder whether you can clarify some of the technical adjustments in the spring budget revision, which, according to annex

B to the document, total £24.7 million and do not involve any cash. First, can you tell us about the

"Justice allocation non-cash DEL"

figure of £12.8 million, which is also mentioned in schedule 3.6 on page 36 of the spring budget revision document?

John Swinney: Can you give me that figure again, Mr Mason?

John Mason: Yes. It is the £12.8 million mentioned in the "Technical changes" section of annex B.

John Swinney: That is for the management of the year-end risk with regard to impairments in the physical assets of the justice portfolio. That portfolio has a significant estate footprint, large parts of which have been renewed or developed. In particular, new buildings have been developed at Her Majesty's prison Grampian and the Scottish crime campus.

John Mason: Does it mean that a building that has been gradually depreciating is now worth less than it had been?

John Swinney: It is all about trying to get our accounting treatment of the valuation of properties into alignment.

John Mason: Another line in that section is

"Technical adjustments to align budgets with accounting requirements",

which totals £113.9 million. Paragraph 15 in the briefing that your officials have provided gives some detail, saying:

"The substantive adjustments of this nature include the alignment of IFRS based budgets for PPP/PFI schemes (-£54.4 million)".

Can you tell us what that £54.4 million is for?

John Swinney: Under international financial reporting standards, we are obliged to budget and account to the Scottish Parliament for public-private partnership and private finance initiative arrangements in accordance with the "Government Financial Reporting Manual" and in line with Audit Scotland's expectations with regard to transparency between budgets and accounts. We have to follow a combination of that factor and the consolidated budgeting guidance published by Her Majesty's Treasury, and ensure that our accounts are consistent with IFRS requirements, which, of course, have been applied to the budget provision in a budget-neutral fashion.

In essence, this is about consistency in the preparation and presentation of the material. In other words, these accounting adjustments relate to our presentation of particular costs in line with the budgeting guidance that we are required to follow by either Audit Scotland or Her Majesty's Treasury, depending on which presentation of the accounts we are making.

John Mason: Does it stem from previous thinking that PFI schemes could be kept off balance sheet altogether? Are we, to some extent, suffering from that by having to ensure that they are on the balance sheet, because they always were and always will be real liabilities?

John Swinney: The short answer is yes. In all honesty, the fact is that, although these projects might have appeared as distant or remote from Government, Government was ultimately paying the costs. The relationship was an awful lot more direct than I think it was made out to be.

John Mason: Thank you.

The Convener: That concludes the committee's questions.

We now move to our consideration of the motion on the order. I invite the cabinet secretary to move motion S4M-09255, that the Budget (Scotland) Act 2013 Amendment Order 2014 be approved.

If members have no comments, I will put the question. The question is that—[*Interruption*.] You did move the motion, didn't you, cabinet secretary?

John Swinney: I did not quite get round to doing that, convener. If it helps, I move,

That the Finance Committee recommends that the Budget (Scotland) Act 2013 Amendment Order 2014 [draft] be approved.

Motion agreed to.

The Convener: I thought that you had moved it while I was chuntering, but never mind. I apologise. The committee will publish a short report for the Parliament setting out our decision on the order.

Thank you very much, cabinet secretary. I suspend the meeting for a couple of minutes to allow a changeover of witnesses.

10:06

Meeting suspended.

10:08

On resuming—

Revenue Scotland and Tax Powers Bill: Stage 1

The Convener: Our fourth item of business is the continuation of our stage 1 consideration of the Revenue Scotland and Tax Powers Bill. We will take evidence from the Faculty of Advocates and the Law Society of Scotland. I welcome to the meeting Philip Simpson and James Wolffe QC from the Faculty of Advocates, and Alan Barr and Isobel d'Inverno from the Law Society of Scotland.

There being no opening statements, we will go straight to questions, which will be asked by me and then other committee members. Most of the witnesses have been here before, so they will know the drill.

I was impressed by the submissions, which are concise but cover a lot of ground. I am sure that we will delve into them in great detail. Paragraph 9 of the submission from the Faculty of Advocates, on appeals to the Court of Session, states:

"The Faculty recognises the policy issues behind restricting appeals to the Court of Session to cases raising important issues of principle or practice, or in which there is some other compelling reason for allowing the appeal to proceed. However, the Faculty is concerned that this may unduly restrict the right of individual litigants to have access to the supreme court in Scotland."

Why would that be the case? How long would someone have to wait before a case came to the Court of Session?

James Wolffe QC (Faculty of Advocates): I preface my direct answer to those questions by observing that the bill proposes to establish a system of tribunals, the first of which will be the first-tier tribunal, which will sit with up to three members. Appeals will be made to the upper tribunal, which, as I read the bill, will be required to sit with a single member, who may or may not be qualified in Scots law and may or may not have greater tax experience or expertise than the members who sat in the first-tier tribunal have. A separate point that the committee might wish to consider is whether it would be appropriate to allow the upper tribunal to sit with more than one member. Otherwise, one will have the odd situation in which a decision by three people will be subject, on appeal, to a decision by a single individual.

One must look at onward appeals to the inner house in that context. The test that is articulated in the bill for access to the inner house, which is restricted, has been described as the second-tier appeals test. A necessary consequence of that test is that, although the upper tribunal might have got a case wrong, the right of appeal will be cut off if no point of general importance arises. If that provision is enacted, that will be a deliberate decision to live with mistakes, even if they are relatively obvious, simply to avoid the possibility of a litigant having yet another bite at the cherry.

It is important for the committee to understand that the test that will be applied will deliberately exclude a well-founded appeal—even a well-founded appeal in which it is reasonably clear that there is a seriously good point to be argued. If all that the litigant can say is, "This is really important to me; the tribunal has got it wrong," they will not get leave to appeal, because the case does not raise a point of general importance.

The question is whether it is right to say to a taxpayer—revenue Scotland might be on the other side—"We are content that the system might have got it wrong but, nevertheless, we're not going to let you appeal to Scotland's supreme court," particularly when the upper tribunal decision might have been made by a single individual, who may or may not be qualified in Scots law and may or may not be as well qualified as members of the first-tier tribunal are. I suggest that the committee should be concerned about that restriction.

The Convener: I noted your comments on that in your submission.

How long would someone have to wait before their case was heard at the Court of Session?

James Wolffe: I do not have the current statistics on waiting times, but we can provide the information after the meeting. An appeal to the inner house from a statutory tribunal must be taken within a statutory period. It is then a question of how long it takes from lodging the appeal to the point at which it is heard and determined by the court.

The inner house has significantly improved its internal procedures in the relatively recent past. The perception of practitioners is that the former problem of a delay in getting appeals heard no longer exists. In effect, the way in which the process works now is that the inner house insists on cases being much more front-loaded than they used to be. My perception is that the time to get a case to a hearing is much shorter than it used to be.

10:15

The Convener: It is months rather than years.

James Wolffe: My perception is that it certainly is not years; a case might run from one year into the next—that would depend on when in the year the appeal was marked. I do not know whether Philip Simpson has a different experience.

Philip Simpson (Faculty of Advocates): I agree with your comment. In the context of currently devolved taxes, another point is that a very small amount of litigation would end up in the Court of Session. As I mention in our submission, across the gamut of UK taxes, only about 50 or 60 cases have proceeded before the UK First-tier Tribunal each year since it came into existence four or five years ago. Off the top of my head, I am not sure whether any cases involving stamp duty land tax or landfill tax have been raised in that tribunal. Broadening the possibility to appeal to the Court of Session would not open any floodgates in a way that would have a material impact on the inner house's workload.

The Convener: Maybe I missed it, but I did not see privilege mentioned in your submissions. Interestingly enough, we have a solicitor and an accountant on the committee. The witnesses will know that the Chartered Institute of Taxation and the Institute of Chartered Accountants of Scotland are strong on extending privilege beyond the legal profession when it comes to taxation. What is the view of the Faculty of Advocates and the Law Society of Scotland?

James Wolffe: The clue is perhaps in the name—it is legal professional privilege. The privilege attaches when people seek and take legal advice; it allows the candid provision of information to the legal adviser and the candid giving of appropriate advice. It is a special privilege, which is there for a good reason, but it is important to confine it. If one expands it beyond the regulated professions whose job it is to give legal advice, where does one draw the boundary? One has to remember that tax advice in the broad sense can be given by entirely unregulated and unqualified people. I invite the committee to take the clue from the name and recognise the importance of seeing it as a privilege that attaches to legal advice that is given by qualified legal advisers.

The Convener: Our accountant friend wants to come in.

John Mason: Thank you for the opportunity to ask a supplementary question, convener. Is James Wolffe saying that non-legal advice given by a legal adviser should not be privileged? Would he accept that?

James Wolffe: I will not give the committee legal advice off the cuff in public, if I can put it in that way. I am not being difficult, but I would want to remind myself of the privilege's ambit before commenting.

Alan Barr (Law Society of Scotland): Perhaps unsurprisingly, the Law Society of Scotland supports the restriction as it exists and as was recently confirmed in the UK Supreme Court. I should say that our representation today is from a lawyer and a chartered accountant, so our evidence is not purely from the legal point of view.

If one is looking for the origins of and demands for privilege, the phrase "officer of the court" is important. Privilege is not restricted to things that do or could end up in court; it is the notion that advisers should be able to give candid advice and receive candid information when a citizen finds himself or herself liable to prosecution or other proceedings, which demands freedom from that advice being produced against them, as it were.

James Wolffe: I would not necessarily characterise the situation even as a restriction on the privilege; it is the logic of the privilege that it attaches to legal advice. It is concerned with advice that is sought and taken from the professions that are regulated for the giving of legal advice and, as Alan Barr observed, for pursuing or defending proceedings, should proceedings ultimately arise.

The Convener: I will not press the matter, although colleagues around the table might wish to.

The general anti-avoidance rule features in both your submissions. You both speak along similar lines. The first line of paragraph 22 of the Law Society's submission says:

"We are concerned at the lack of certainty inherent in the GAAR provisions."

In paragraph 13 of its submission, the Faculty of Advocates points out that it would like the general anti-avoidance rule to be

"more certain for both taxpayers and Revenue Scotland."

One issue is that, given the way in which the law is sometimes interpreted, it can be too certain. The difficulty is that, unless the wording of legislation is absolutely perfect, it can allow loopholes and potential avoidance, because there is no flexibility in how it is applied. In other words, even when the intention is clear—I have previously quoted a case on this issue—it can still be circumvented if the certainty is too tight. How tightly do we draw the legislation?

As a layperson—as a taxpayer, one could say—I think that what annoys the public more than anything else is seeing a lot of people using avoidance measures and loopholes to avoid paying their fair share, which, all else being equal, burdens the rest of the population who pay their fair share. I am concerned about tightening things up to make things more certain, regardless of what Adam Smith might have said in a previous century. Will the Law Society and the Faculty of Advocates expand a wee bit on what their submissions said?

Alan Barr: We recognise that the line is difficult to draw. The Law Society fully accepts—we accepted it in relation to the equivalent UK statute—the absolute and understandable need to stamp out unacceptable avoidance. That is best characterised by circular transactions, which create a non-economic loss that nonetheless leads to a tax deduction. Through the long history of the courts, it has proved extremely difficult to stamp that out without a general anti-avoidance rule—or anti-abuse rule, as in the UK legislation. Such avoidance needs to be stamped out, and we understand why both legislatures wish to do that.

We appreciate that absolute certainty is impossible in tax legislation, particularly in a world whose economics is more complicated than that of Adam Smith's days. The question is much more about where the certainty has to come from. That relates to the production of enough evidence of what will or will not be regarded as falling within the general rules, without the need to further complicate those general rules by saying that various things are disqualified or qualify.

That is what is required in guidance, so that people can be told that revenue Scotland regards a certain kind of transaction as falling within certain provisions and that it will pursue the matter on that basis. Perhaps more important, it would white-label things that definitely do not fall within the provisions, so that people can proceed with their transactions in the knowledge that they will not be challenged later.

It is perhaps understandable that revenue Scotland would wish to make the sole decision, but we support a more independent view of what is reasonable in the circumstances. That is why we recommend having an expert panel of some description to give advice on what is available. That would not necessarily lead to any change in the bill. The guidance around it is particularly important.

We note the policy decision to restore the term "anti-avoidance" as opposed to "anti-abuse", which is used in the provisions that the UK eventually legislated for. That is deliberate and we understand that policy decision. It certainly leads to a perception—it is no doubt deliberate—that the measures are intended to be wider than the equivalent UK provisions in order to catch more things, to put it simply. That is fine—it is a matter for policy—but, if there is to be a difference from the UK provision, that probably adds even more to the need for the certainty that guidance will provide, rather than a tightening of the bill.

The Convener: That is interesting.

Isobel d'Inverno (Law Society of Scotland): The big advantage of having an external panel is that the people who were involved in it would have commercial experience of a wide range of transactions and actings and so on, so they might be better able to determine whether something was an unusual way of behaving or just the way in which the property industry now does a particular transaction, because of the changing economic circumstances in which we find ourselves or because of pressures from other legislation affecting how transactions are done. That is a particular aspect that is difficult to grasp without good guidance or an external body to which it is possible to apply to obtain a view.

Most business transactions have a tax element and most business decisions pay attention to tax. We must allow taxpayers to make a tax-flavoured decision, as John Whiting has referred to it, without worrying that, because they have taken tax into account, they are falling foul of the GAAR. The question is one of giving taxpayers more certainty as to how the GAAR will apply, rather than tightening the legislation, which would just lead to loopholes being created, as has been said.

James Wolffe: Sorry—[*Interruption*.]

The Convener: You do not need to press the button, Mr Wolffe—the microphone comes on automatically. You are clearly not a veteran of the committee, as Isobel d'Inverno is.

James Wolffe: I will make a couple of observations about certainty. I do so against the background of recognising the policy—or policies—significance, as Alan Barr has observed, of dealing with transactions that are, on a proper view of it, abusive or illicit avoidance.

We tend to think of certainty as having a constitutional significance. The notion of the rule of law is that individuals, in their dealings with the state, should be able to plan their affairs with a reasonable confidence that they can predict how the rules will be applied to them, once they have taken appropriate advice. There is therefore a constitutional dimension to trying to find mechanisms that give a sufficient measure of certainty to taxpayers.

10:30

That value, which we tend to think of as part of the rule of law, also has an economic significance. There is now a literature about the way in which the rule of law and its institutions promote economic success. Unless economic actors have a reasonable measure of certainty in carrying out their affairs and making decisions or, at least, are able to achieve a reasonable measure of certainty by taking advice and to ascertain how rules will be applied to them, perfectly legitimate innovation may be deterred.

Therefore, in any system, there is real significance to seeking to identify and create mechanisms that provide a reasonable level of certainty, recognising that absolute certainty is never possible. Against that background, the faculty would support the use of an advisory panel both to introduce a measure of certainty and to give an external and independent input into decisions that may be made.

That is my take on it. I do not know whether Philip Simpson wants to add anything.

Philip Simpson: The proposed Scottish GAAR is intended to be rather wider than the UK GAAR. The UK GAAR is quite narrow, and I suspect that the band of uncertainty within which the line will be drawn as time goes by and cases come through will be fairly narrow.

There is uncertainty about precisely where the line will be drawn, but the degree of uncertainty is reasonably limited, at least compared with the uncertainty about where the line might be drawn with the proposed Scottish GAAR. That is because the band of transactions that might be regarded as falling on one side of the line or the other is much wider and, therefore, there seems to be a higher degree of uncertainty as to how the proposed Scottish GAAR would operate in practice.

For that reason, something like an advisory panel in which, in effect, three expert witnesses give an advance view would assist, particularly if—as with the UK GAAR—the panel is required to publish anonymously annual guidance about the decisions that have been made. That would enable us to build up a corpus of decisions that indicate where the line will be drawn in any particular case.

Guidance from revenue Scotland would be helpful—and I think that the idea is that revenue Scotland will publish guidance. That would at least give certainty as to where it thinks that the line ought to be drawn.

That leads into one particular question. As the bill is drafted, the court is required to take into account any guidance by revenue Scotland in setting out how the GAAR should be operated. That is slightly unusual because we have the idea of the separation of powers at a constitutional level, whereby the Executive is not supposed to be the body that interprets legislation; that is a matter for the judiciary. On the face of it, the provision in the bill seems to be an inroad into the principle of the separation of powers, giving particular necessary weight to the Executive's view as to how a broadly drafted and, on its own, quite flexible and elastic provision should be interpreted.

Therefore, while the faculty supports an advisory panel, plus revenue Scotland guidance, I am not so sure that we support the proposition that the courts should be required to take that into account in interpreting and applying the GAAR.

The Convener: Okay—thank you. I think that Mr Wolffe touched on the issue when he referred to a reasonable measure of certainty. The question is how that is defined that. We do not want to see every i dotted and every t crossed, because that can cause difficulties.

I realise that other committee members are keen to come in, so I will not abuse my position in the chair; I just want to cover one other area. I refer to paragraphs 29 and 40 of the Law Society's submission, which deal with parts 6 and 8 of the bill.

In paragraph 29, you state:

"We do question the introduction of a general unjustified enrichment defence for Revenue Scotland across all devolved taxes when, to date, the same has been restricted to specific taxes in the UK context."

I am not really sure why anyone would be against that, because the word used is "unjustified". In paragraph 40, you state:

"There are copious provisions in the Bill to prevent 'unjustified enrichment' of the taxpayer; we see absolutely no reason why they should not be balanced by provisions against unjustified enrichment to the tax authority."

I would like you to talk to this unjustified enrichment issue, which you mention twice.

Alan Barr: I suspect that the point is little affected by the initially devolved taxes; the provision is more commonly found in some of the UK taxes.

The issue is best seen in relation to the pay as you earn system, in which a responsibility is put on the employer—which is a separate responsibility from the tax charge—to deduct and pay over to the revenue authorities the employee's tax. If the employer fails to do that, they are subject to the tax being collected and penalties and interest being applied in the normal tax enforcement procedure. It is in practice—although not in theory—taken into account whether the employee has in fact already paid the tax, to avoid the need for interest to be paid.

Because of those separate obligations, there are situations in which the state can end up collecting twice, as it were. One taxpayer has made a mistake, but his fault has been made up for by another taxpayer. It is not impossible to envisage that happening in the land and buildings transaction tax system—for example, somebody else could have paid what was primarily one taxpayer's responsibility.

I think that our point is that the provisions should be balanced. In other words, it should indeed be a factor, certainly as regards penalties but probably as regards tax as well, whether the amount of tax

in question has actually been collected from another taxpayer, perhaps incorrectly. In other words, the unjustified enrichment provisions should balance each other out. That was the thrust of our suggestions.

Isobel d'Inverno: In UK taxes, the issue also comes up in relation to VAT; it is a feature of that tax. There can be problems in practice with establishing whether there has been unjustified enrichment—in relation to the taxpayer trying to claim relief, for example—by looking back at transactions and trying to figure out what has happened.

We therefore thought that there would be dangers in applying the unjustified enrichment provision in the bill across the board. It would be another way of introducing uncertainty—the taxpayer might be able to go down a particular road only if they could demonstrate that there had not been unjustified enrichment.

Philip Simpson: The provisions are quite clearly based on UK tax provisions, which are applied tax by tax depending on whether it is thought appropriate for them to apply. One tax to which they apply is value added tax.

Another tax to which the provisions apply is landfill tax. That is because of the way in which landfill tax operates in practice; it is paid by the operator of a landfill site, who makes a charge for his or her services to the people who actually deposit waste to be put into the site. The landfill operator may make a separate entry specifically for the landfill tax in their invoice to the person depositing the waste, because landfill tax is simply charged by the tonne on the amount that is put into the site, depending on the nature of the waste involved.

In that context, one can quite clearly see the potential for unjustified enrichment of the person who has actually paid the tax, because the landfill site operator simply takes the money that he has received from the person whose waste it is and passes it on to Her Majesty's Revenue and Customs. If all that HMRC does in the event that money has been wrongly collected is to pass it back to the operator of the site, and if the operator of the site then retains it, that is unjustified, because it is not an amount that the operator has actually borne.

In those circumstances, one can enter into reimbursement arrangements between the operator and the person who has deposited the waste, in effect requiring the operator, if they receive any money from HMRC, to pass it back to the person who deposited the waste. In that way, unjustified enrichment is avoided, and there is still an opportunity to recover from HMRC unlawfully levied tax, or tax that was not due but was paid.

In UK tax, therefore, there is quite a specific instrument to deal with the way in which taxes operate. VAT is the other obvious example, because that is also an indirect tax. The tax is actually borne by the consumer of goods and not by the taxable person who pays the VAT to HMRC. Again, if VAT that was not due has been paid and if it is simply returned to the taxable person, that person receives a windfall because they have money from the consumer and from HMRC, so they have two lots of VAT instead of one. In such a case, one could enter into reimbursement arrangements—and that is a necessary condition of seeking to recover from HMRC VAT that has been paid but was not due.

The provision on unjustified enrichment is directed at scenarios of that sort that are to do with the structure of the tax. As the Law Society suggests, a different context such as PAYE is a more complex area of tax that does not necessarily sit comfortably with the broad unjustified enrichment rules that are set out in the bill. One would clearly be against the idea that a taxpayer, by receiving a repayment from revenue Scotland, should somehow make a windfall gain, but it is perhaps more appropriate to think about how that might be dealt with on a tax-by-tax basis, rather than by general rules that fit with specific taxes but not necessarily with all taxes.

The Convener: Thank you. I will now open out the discussion for questions from the rest of the committee, starting with Jamie Hepburn.

Jamie Hepburn: I return to the issue of privilege. The Chartered Institute of Taxation and Institute of Chartered Accountants of Scotland expressed their concern that privilege gives a competitive advantage to the legal profession, as opposed to people in their position. What is your perspective on that?

James Wolffe: If the intrinsic nature of the privilege is that it is legal professional privilege, the logic is that it is a privilege that attaches to advice sought and taken from regulated legal professionals. I suppose that the consequential question is where we ultimately draw the line, given that advice on all sorts of things—including on legal matters, provided that it does not trench into certain specific areas—can be given by members of all sorts of professions and, indeed, members of no profession at all.

10:45

Jamie Hepburn: Does the Law Society have a comment?

Isobel d'Inverno: It would be misleading to suggest that most of the work of lawyers is involved in advising taxpayers on tax avoidance schemes. That is very far from the case. Most tax

advice is geared towards advising people on the tax implications of transactions that they propose to carry out, so that they can avoid elephant traps, look into things and make reasoned decisions.

We are not aware of people flooding to lawyers' offices rather than accountants' offices to take tax advice because legal privilege exists. Accountants get more than their fair share of tax advisory work. Most clients who are not obviously trying to do schemes that are beyond the pale will not decide whether to take advice from a lawyer or an accountant on the basis of privilege; instead, they will take advice from whoever they think will best be able to advise them.

Jamie Hepburn: You used the interesting term, "schemes that are beyond the pale". Are you aware of any instances in which privilege has been used as a guise to devise avoidance schemes?

Isobel d'Inverno: We are all aware of situations in which that has happened. The case that has been in the news recently was about that very thing. Because advice was taken from accountants rather than lawyers, questions were asked about whether there should have been privilege and so on. However, that really is a small part of the work that accountants and lawyers, in relation to tax, are involved in. Most of the time, the issue of whether there is privilege is not at the forefront of people's minds when they are choosing a tax adviser.

Philip Simpson: I do not have any empirical evidence, but my impression is that most tax advice in the UK is given by the accountancy profession. Therefore, if the existence of privilege gives the legal profession a competitive advantage, it is not a very effective one.

We must remember that the case in the Supreme Court a couple of years ago in which the court decided not to extend the scope of legal professional privilege to accountants was taken by Prudential plc. Obviously, Prudential is a sophisticated user of legal and accountancy services, but it nonetheless chose to get tax advice from an accountancy firm rather than a legal firm, because, I suppose, that is where it is thought it would get the best advice. Clearly, Prudential must have been aware that, as the law stood, advice from an accountancy firm would not attract privilege, but it nonetheless chose to get advice from accountants. Therefore, I suggest that the point about competitive advantage is not terribly practical.

Jamie Hepburn: I appreciate that evidence and, to be fair, I made that point to the accountancy profession last week. I asked whether legal privilege had actively harmed the profession, and the answer that I received was that it had not particularly done so. Elspeth Orcharton said:

"Someone might say that they have never seen a starving accountant".—[*Official Report*, *Finance Committee*, 5 March 2014; c 3735.]

John Mason: Oh!

Jamie Hepburn: That was not meant as a jibe, Mr Mason. I suppose that it makes the point that the issue is not as big as it might first appear, although it is still important that we explore it.

I turn to the issue of whether some measures should be left to secondary legislation. The Law Society states that, because some elements are to be dealt with in secondary legislation, the bill

"cannot be said to have passed"

the

"tests of certainty and convenience".

I thought that that was quite a bold thing to say. Surely it is more about the system that has been put in place and whether it causes inconvenience to the taxpayers rather than everything having to go into primary legislation. Do you accept that?

Alan Barr: I think that we would accept that absolutely. It was not a very big point, but we noticed that, if anything, the bill was slightly unbalanced. Some things are gone into in great detail in great slices of legislation, whereas others, which will undoubtedly end up in the same kind of quantity of legislation, will be secondary.

It is not a huge point. Matters of principle in particular should always be in primary legislation, and the bill meets our criterion there. Details or procedure are much better suited to secondary legislation.

We would be more concerned if there was a huge use of the provision, and the Scottish Parliament as a tax-legislating Parliament is too early in that procedure for us to know whether that is going to happen. We would be more concerned if a lot of things were put into secondary legislation as a matter of course.

Jamie Hepburn: That is helpful. The convener raised the issue of tribunals. The Law Society says that there will be four forums for appeal—first-tier tribunal, upper tribunal, the Court of Session and the Supreme Court, and that until now Scotland has had one fewer layer than England and has not suffered because of it. Our adviser says that that puzzles him because the current layers in England are the first-tier tribunal, upper tribunal, the Court of Appeal and the Supreme Court. What is your comment on that?

Alan Barr: I absolutely accept that. Our comment is somewhat out of date. Until the relatively recent introduction of the first-tier tribunal

system, the Scottish system had three layers and not four. We accept that both systems have four layers at the moment. It is the preservation of four layers, particularly in a small jurisdiction, that we are questioning slightly. Again, it is not a huge point.

Jamie Hepburn: The Faculty of Advocates states the opposite view. It:

"welcomes the establishment of specialist first instance and appellate tribunals for tax matters."

However, it suggests that there could be confusion because of the names of the UK and Scottish systems. It would be interesting if you could put a bit more about that on the record.

Philip Simpson: The whole system reflects the current tribunal system for UK taxes. Since 1 April 2010, the system in Scotland has been aligned with the system in England and Wales, so that there is a first-tier tribunal, an upper tribunal, the inner house of the Court of Session, and then the Supreme Court. Before April, we went directly from the special commissioners of the VAT tribunal to the inner house with no intermediate layer. In England, they had the intermediate layer that has now been created in Scotland.

There does not seem to be any problem with that system, but I reiterate the dean of faculty's comments to the effect that there is not a terribly positive reason for restricting appeals from the upper tribunal to the inner house in the way in which the legislation as currently drafted does.

As far as the names are concerned, it is almost inevitable that, at some point, some litigant will confuse which tribunal they should be appealing to. In fact, it is likely to be a litigant who does not have a lot of tax at stake and who is unadvised: a lower-income type of litigant. It will simply create a procedural mess if an appeal is started in the wrong jurisdiction and the forms sent to the wrong address. It will have to be sorted out in one way or another. To avoid that confusion, I wondered whether different names might be chosen, but if the approach is, as I understand it, part of the broader reform of the Scottish tribunals system, that might not be possible.

Jamie Hepburn: We can certainly reflect on that point and report back.

Similarly, you state that the Land and Buildings Transaction Tax (Scotland) Act 2013 and the Landfill Tax (Scotland) Act 2014—which were passed in different years—should be described differently in the bill. What would be the practical effect of that change?

Philip Simpson: That is just a minor drafting issue. We anticipate that, if further taxes come within the competence of the Scottish Parliament, there is likely to be more than one act per year that concerns a tax. The shorthand that is currently used in tax law generally takes the initials of the tax statute plus the year, so everyone knows, for example, that ITTOIA 05 is the Income Tax (Trading and Other Income) Act 2005—

Jamie Hepburn: When you say "everyone", I am not sure that that is the case, but I take the point.

Philip Simpson: Yes, but all the statutes are referred to in that way—for example, ITEPA 03 for the Income Tax (Earnings and Pensions) Act 2003; ITA 07 for the Income Tax Act 2007; and CTA 09 for the Corporation Tax Act 2009. That is the form that everyone is used to, and it works quite well when there is a proliferation of statutes— rather than simply a reference to the 2012 act, for example. I have some difficulty remembering which act was passed in which year, so it makes life a bit easier if I am given additional help from the initials.

Jamie Hepburn: It would make it easier for you.

Philip Simpson: Yes.

Jamie Hepburn: I take your point, and we will take that issue on board.

Malcolm Chisholm (Edinburgh Northern and Leith) (Lab): You both expressed concern about the delegation of certain aspects of tax management to revenue Scotland and to the Scottish Environment Protection Agency. The Law Society goes so far as to question

"whether it is appropriate that Revenue Scotland is empowered to delegate any of its functions to the two Agencies",

while the Faculty of Advocates is a bit more selective. What is the basis of those concerns?

Alan Barr: Again, that is not a major point. The power is there for revenue Scotland to delegate "any of its functions"—by "any" we mean "every"—to the two agencies and we simply wonder whether that is appropriate if such a course is decided on in the future.

If we are to have a tax authority, it should act as a tax authority. There were very good reasons for large quantities of administrative functions being delegated to other aspects concerned with the administration of transactions under the land and buildings transaction tax or the landfill tax. It makes sense that the agencies that are involved in those transactions would also be responsible for administration of the tax.

I am sure that that is what is currently proposed, but a power to allow revenue Scotland to delegate everything to either of those—or indeed other—agencies in due course strikes us, as a matter of principle, as being a bit wide.

James Wolffe: Our point is the same, in a sense, but we are perhaps putting it the other way round. Certain powers are inherently the powers of a taxing authority, such as the power to levy a penalty, to make an assessment and the like, and we may have to be careful about permitting a taxing authority carte blanche, as it were, to delegate whatever it likes to somebody else.

I have just looked at the provision on the GAAR, which provides that an "authorised officer" can be a member of staff of revenue Scotland, or another person who presumably might not be a member of staff. That is perhaps part of the same question with regard to whether functions in relation to the operation of the tax system should, as they are inherently part of what a taxing authority is there to do, be retained and exercised by the taxing authority, even if there is a power to delegate certain functions.

Philip Simpson: I reiterate that; basically, certain core functions of a tax authority ought to be exercised by that authority. One thinks of the imposition of penalties, for example, and of debt collection, particularly when we start to consider lower-income taxpayers, who would not necessarily be affected by the currently devolved taxes.

If we think about taxes that might be devolved in the future, HMRC takes an attitude to debt collection that is very different from that of commercial debt collectors. It can take a more sophisticated approach with people on low incomes who are in serious difficulty, for example on the repayment of tax credits. It would be much better for that sort of activity to be kept as part of the tax authority's core functions.

11:00

James Wolffe: One has to remember that some of the powers of taxing authorities are intrusive in the sense that, in the public interest—rightly and properly—they have investigative powers. When powers such as the power to impose a penalty are exercised by an organ of the state, it is important that they are exercised by an organ of the state that has the appropriate structures of accountability to enable it to be trusted with such intrusive and coercive authority.

In that context, one must think carefully about which powers are ones that, constitutionally, should be exercised by the body that the Parliament sets up, which will have the structures of accountability and responsibility that the Parliament considers are right for a taxing authority, and which powers the Parliament is content to allow that body to, in effect, hand over to someone else to exercise on its behalf.

Malcolm Chisholm: That is interesting. It sounds as if you would like the bill to be amended to make some of that more explicit. That leads to the more general question about what should be in the bill that is not in it, which you touched on in your answers to Jamie Hepburn.

In that context, I was going to ask about the GAAR, but Mr Simpson made a comment that interested me. I think that you said that you did not think that guidance should be taken into account by the courts. I think that you were probably worried about the discretion that revenue Scotland might have. Were you implying that more of that kind of thing should be in the bill or that there should be statutory guidance, or did I pick you up wrongly?

Philip Simpson: The concern is a constitutional one. There is a separation of powers between the Executive and the judiciary. Broadly, that means that it is not the Executive that gets to interpret the laws that it has had passed. I was looking for something about that in Adam Smith's lecture on jurisprudence this morning, but I could not download it properly on to my Kindle. He was writing about the same time as Montesquieu, who came up with the idea.

If the courts are required to take into account guidance that revenue Scotland provides on where the line should be drawn, that will, conceivably, give revenue Scotland, as a branch of the Executive, more power than, properly, it should have to determine how the rules are interpreted and applied in practice. That would go beyond what one would normally anticipate, whereby that function is left to the judiciary.

In reality, as matters stand, the tribunals and the courts can look to HMRC manuals to see what HMRC says about how a rule works, but that is not something to which they give a great deal of weight—it can simply be regarded as HMRC's line, which might happen to be the same as the line that is being presented in a particular case. However, the proposition that revenue Scotland's guidance must be taken into account seems to elevate its view beyond its proper limits in the constitutional framework in the UK, in which we have the separation of powers.

Malcolm Chisholm: But statutory guidance has a well-recognised role in legislation. Is the guidance that you are talking about different, because it will come from the Government?

Philip Simpson: It is the obligation on the courts and the tribunal to take revenue Scotland's guidance into account that perhaps elevates it. The suggestion might be that the tribunal and the courts may take the guidance into account or may have regard to it, rather than must have regard to it.

Malcolm Chisholm: Okay. That was really interesting.

To touch on one of the first questions that the convener asked, I am not quite clear about something in your submission. You say that

"in any recent 12 month period there have been... 50 or 60 decisions made by the First-tier Tribunal (Tax Chamber)".

You suggest by implication that there would not be a large number of such cases in Scotland even if we had a larger number of devolved taxes. However, are we comparing like with like in that instance?

Philip Simpson: Yes. To be clear, the 50 or 60 cases in the first-tier tribunal that are mentioned are in the first-tier tribunal sitting in Scotland across the whole gamut of UK taxes. Those taxes include VAT, which is by far the most litigated tax in the UK. That is perhaps the volume that could be anticipated were all taxes devolved to the Scottish Parliament. So far as LBTT and the Scottish landfill tax are concerned, I have not checked but I am not aware of any first-tier tribunal cases on SDLT or landfill tax in the past four or five years. There has been one landfill tax case in the Court of Session. That was not anything technical—it was a judicial review matter. Certainly, I would not anticipate anything more than perhaps two or three cases a year in the first-tier tribunal on devolved taxes.

Isobel d'Inverno: In relation to SDLT generally, across the UK, there have not been a huge number of cases. There have been quite a few penalty cases and there have been the big avoidance cases, but there has not been a huge stream of cases. In relation to Scotland, I am sure that we could expect only a small number.

Malcolm Chisholm: In a way, that connects with the other, more general issue, which is to what extent the bill is about what might be called true taxes or whether it is a bill about several other taxes that will come through one constitutional route or another.

Sticking with tribunals, the Law Society seems to be concerned that the upper tribunal could have a single member judging the appeal at its second hearing. How does that compare with the existing arrangements and what is your concern about that?

Alan Barr: It is the same concern that was expressed by James Wolffe in relation to the nature of an appeal that could go from up to three experts and specialists to a single member of the upper tax tribunal. We do not know for certain who that single member might be, but they need not be a particularly experienced tax judge. There is something that just smells a little wrong about perhaps going from two or three experts to one person—someone who is no doubt highly qualified but not necessarily an expert in the area—as a mechanism for appeal. It would not be particularly different from where we are now.

Malcolm Chisholm: I do not really know much about tax tribunals—perhaps that is fairly obvious—but the Faculty of Advocates suggests that

"parties should not be required to pay fees to the Tribunal in relation to appeals. It is suggested that this be made clear in the Bill."

Again, how does that compare with the current system?

Philip Simpson: That is the current system. There are no fees payable—to the tribunals, at least—for raising appeals there.

Malcolm Chisholm: They do pay fees?

Philip Simpson: There are no fees.

Malcolm Chisholm: There are no fees at the moment, so that would be a change.

Philip Simpson: Yes, if fees were charged, that would be a change from the existing system.

Alan Barr: That knocks on to our comments about the expenses system, in which we are suggesting that unless one party is wholly unreasonable, there should be a system of no expenses awarded against a party at the first-tier tribunal. Rather than fees, it is often the fear of expenses—perhaps, particularly, the other side's expenses when the other side is the state—that deters people from making appeals.

Malcolm Chisholm: The Faculty of Advocates is concerned that

"The period for Revenue Scotland to correct obvious errors in returns is three years",

which again seems to be a lot longer than at present. I do not know why there is such a big discrepancy, but what is your concern about that?

Philip Simpson: Broadly, as matters stand, after one year has expired, taxpayers have certainty that, except in particular circumstances, the return that they have submitted and the payment that they have made on the basis of it have finalised their liability for the transactions of the year in question. To go from a period of one year to a period of three years seems quite a large extension. The concern is that there would be a longer period of uncertainty for taxpayers.

From the point of view of revenue Scotland—particularly if annual taxes start to be devolved—a one-year period in which random inquiries can be made would fit much more comfortably with a system of annual returns. There is nothing wrong with revenue Scotland taking inquiries at random; that is just part of the system and it helps the

system work. It is a much better means of organising inquiries than having to take large numbers of them. After one year has expired from the filing date for a year's tax returns, there will be another year's worth of tax returns coming in, so there will be an overlap in the period of open inquiries. Revenue Scotland might require additional resources so that it can deal with three years' worth of returns at the same time.

Alan Barr: We can give a specific example of such a proliferation of returns, relating directly to devolved taxes. Under the proposed, and now enacted, system for leases for land and buildings transaction tax, more returns will be made. If they were all to be left open for a period of up to three years after they had been made, there could conceivably be a three-year cycle for making returns relating to long-term leases. One could well see cases backing up in which people are uncertain about their previous return, because it has not been inquired into but still might be, by the time that they are ready to do their next one. That seems to be too long in the circumstances, and that is a direct example from one of the devolved taxes.

Malcolm Chisholm: The Law Society is not the first to be worried about the chief executive not sitting on the board. Could you comment on that? The Faculty of Advocates may wish to do so too.

Isobel d'Inverno: Our view is that it is important that revenue Scotland works well when it sets off as the new Scottish tax authority. It makes better sense for the chief executive to be involved in the board, in the same way as the chief executive of a commercial company is involved in the board; it would be unusual for that not to be the case. There are so many technical issues that revenue Scotland would have to be involved in—in relation to the administration and collection of taxes, policy and so on—that it makes a lot more sense for the chief executive, who has the greatest knowledge of those things, to be on the board.

Malcolm Chisholm: Does the Faculty of Advocates agree?

James Wolffe: We do not have a comment one way or the other on that issue.

John Mason: We have covered quite a lot of ground. One of the aims and opportunities is for Scotland, as a smaller country, to have a simpler system; witnesses have already referred to that. I wonder whether, if we were starting from scratch, we would have four levels of tribunals or appeals. We are adapting what we have got at the moment, and that is a factor, but it seems excessive.

Introducing an advisory panel on top of the current structure would bring in yet another body, and every time that another body is brought in it complicates matters because somebody else is involved in the mix. We are trying to get simplicity, but we also want safeguards. Presumably, bringing in new bodies also increases the uncertainty, and you have all been arguing for more certainty. Is there not a tension there?

11:15

Alan Barr: There are two separate things. I entirely accept your point about the number of appeal tribunals in a small jurisdiction. That fits in with our point about an appeal going from a panel of perhaps two or three experts to one person who is less expert. It seems to me that we did not do too badly in tax appeals before 2010 when the system involved going from a tribunal to the inner house of the Court of Session to, if necessary, the Supreme Court. That seems to be a more sensible appeals structure than simply replicating the current—but only recently introduced in Scotland—UK system.

The argument about another body being introduced for the general anti-avoidance rule is rather different, because that body would not exercise a judicial function. In terms of increasing certainty, that would depend on such a body publishing its results, the decisions it has reached and its advice. As that body of knowledge builds up, one would expect more certainty as time goes on. The fundamental difference is that that body would be separate from revenue Scotland. Revenue Scotland's job will include enforcing the tax law as it is enacted. Initially, I believe that there was talk about producing as much tax as possible, but that should not be its function; its function should be to produce the correct amount of tax. However, the correct amount and the largest amount possible might, in the eyes of the state, be the same thing.

John Mason: Would you accept that the public want the maximum tax?

Alan Barr: I certainly would not accept that as far as individual taxpayers are concerned. The public want the correct amount of tax and, as the convener said, the fair amount of tax, which is not the same thing as the largest amount of tax.

John Mason: But the public who want hospitals, schools and such things surely want the maximum amount of tax.

Alan Barr: Again, I do not accept that that is the case. The public want the correct amount of tax to fund things that the public want. I think that it would be reasonable to say that there is sometimes a gap when it comes to the perception of the amount of tax that is needed to fund the things that you are talking about. That does not equate to the largest amount of tax; it should equate to the correct amount of tax.

John Mason: Okay. Does the Faculty of Advocates have a comment?

James Wolffe: We have to remember that members of the public are also taxpayers.

John Mason: Yes.

James Wolffe: So it must be absolutely right that the aim of any tax system is to ensure that tax that should be collected is collected but that the taxing authority is not collecting more than should be collected. It may be that, ultimately, we are not at disagreement on that, but we should be clear that ordinary members of the public pay taxes, too, and the ultimate aim must be to collect the right amount of tax.

As Alan Barr said, you have raised two separate issues. The first is the structure of the tribunals. Our comment on that comes against the background of our already having within the UK structure, and now also separately within the more general devolved tribunals structure, a system of first-tier tribunals and appeal within the tribunal system and then an appeal to the inner house, which of course has the ultimate responsibility to ensure that the law in Scotland is being applied correctly across the board.

If one were starting from scratch, I would certainly have sympathy with what Alan Barr said and with the thrust of the question. In a small jurisdiction, where the volume of cases will be relatively small compared with the number of cases in the UK system, one might ask whether one really needs an intermediate tier or whether it is not enough to have a first-tier specialist tribunal that does the specialist work, subject to supervision by the inner house, which will ensure that the law is applied.

There is then the separate question of how one achieves a suitable measure of certainty about the operation of the GAAR. I support what Alan Barr said on that, which is that one is trying to build into a system in which, by the nature of the GAAR, there will be uncertainty about how it will be applied, ways in which the taxpayer can obtain clarity, if possible in advance, about how the taxing authority will apply it and a measure of independent input, as it were, into the decisions of the taxing authority.

In defining the GAAR, the bill states that a tax avoidance arrangement is artificial if one of two conditions is met. The second of those is that the arrangement "lacks commercial substance", which implies that, under the first condition, there might be an arrangement that has "commercial substance" but which nevertheless is going to be treated as artificial. Ultimately, the only test that will be applied is whether the arrangement is

"a reasonable course of action in relation to the tax provisions in question".

The bill then gives a very short list of circumstances that have to be taken into account. However, they may or may not be taken into account. The only test is whether an arrangement is

"a reasonable course of action in relation to the tax provisions in question"

and, by implication, it could be one that has "commercial substance". In the context of such a provision, there might be a question of ensuring, first, that taxpayers have mechanisms for achieving a reasonable measure of clarity about how it will be applied and, secondly, that there is some independent input into revenue Scotland's thinking about how it is to be applied, bearing in mind that ultimately, as Alan Barr said, the aim is to get the right amount of tax and not an excessive amount of tax.

John Mason: Or too little, for that matter.

James Wolffe: Indeed.

John Mason: Do you accept that certainty and clarity are good for a good taxpayer but bad for a bad taxpayer? For the bad taxpayers—the people who do not want to pay tax fairly—we want uncertainty because we want them to be scared.

Alan Barr: I do not think that we want uncertainty. We want certainty on what the tax is meant to collect. You are never going to get that perfect in primary legislation. This is where the line is a fuzzy one. One man or woman's sensible tax planning is another person's abusive avoidance, to combine the two systems. That is always going to be the case.

The certainty needs to come with the state's attitude about what falls on the wrong side of the line. That can be done only by examples and the like. You are never going to get absolute clarity out of the legislation itself, because some people will try to interpret it to minimise the amount that they are going to pay while, as they see it, still falling on the right side of the fairness line. It is all very well to talk of fairness, but some citizens might want the maximum amount of tax to be collected, while others want the minimum amount of tax to be collected on the basis that they are better placed than the state to decide what to do with their money.

John Mason: Yes—the individuals who are not paying the tax. However, do you accept that society feels that the balance is wrong at the moment? People feel that the balance is far too much in favour of large taxpayers in particular, who are not paying the tax that everybody thinks they should. The public would say that they want a

swing back towards having a bit more clout for the principles of the legislation as against the letter.

Alan Barr: I would absolutely accept that, particularly the point about the principles as against the letter. However, as I said, it is the moving of a fuzzy line rather than the establishment of an absolutely clear line. Even with the best will in the world, it will always be a fuzzy line.

Isobel d'Inverno: When some of the mass-marketed SDLT avoidance schemes were being undertaken, the Government was perhaps not firm enough in saying, "We are absolutely certain that this doesn't work." Often, taxpayers are advised by scheme promoters to do something, and they do not know whether it is the wrong side of the line. An ordinary taxpayer might not know that, but if there is clear guidance from the state that it is not acceptable and should not be done, taxpayers are less likely to undertake such a scheme. If there is clear guidance about where the line is and what is on the wrong side of it, that can give certainty without stopping the state from pursuing people who are trying to avoid tax.

John Mason: The Law Society's evidence refers, in paragraph 3, under "General Comments", to striking a balance between existing devolved taxes and taxes that might come in due course. It states:

"In striking this balance, we would urge strongly that priority is given to creating an effective system for the taxes already devolved".

Do you feel that the bill has achieved that?

Alan Barr: Yes, I do, but it still attempts to be comprehensive. In a sense, we are past that stage. The bill attempts to be comprehensive, so you should be able to slot in any number of devolved taxes, or indeed invented taxes, into the structure without too much trouble. The immediate way forward, given the pressures on legislative and administrative time, is always to consider how that structure will work with land and buildings transaction tax and with Scottish landfill tax from 1 April 2015, rather than wondering how it might work in five or 10 years' time, or three or four years' time, with the full panoply of income tax. That should be the thinking behind it. The question should be how is it going to work with these taxes.

John Mason: You are not suggesting that the present bill should be changed to fit?

Alan Barr: No.

Gavin Brown: Most of my issues have been raised already, but one that has not been covered is penalties, which are dealt with in sections 148 to 181. Both organisations have commented on penalties in their written submissions. Would both groups of witnesses like to put on record their views on how penalties have been structured so far in the bill? Does there need to be more in primary legislation, or is the balance about right?

Philip Simpson: I suggest that there should be more in primary legislation, to provide certainty to taxpayers. That is how it is normally done in current UK legislation, which sets out amounts and rates of penalties. For example, schedule 36 of the Finance Act 2008 is where one finds most direct tax penalties; for corporation tax matters, it is schedule 18 of the Finance Act 1998. That allows changes to be subject to full parliamentary scrutiny, as opposed to being made by ministers in delegated legislation, so it provides some degree of stability.

Gavin Brown: Does the Law Society have a view?

Alan Barr: We would echo that. Amounts may need to be firmed up. We have one particular bugbear, which is the automatic collection of small penalties in cases where it turns out at the end of the day that no tax is actually due—in other words, it is an administrative penalty.

We fully acknowledge the need for returns or other administrative compliance in situations where no tax is payable. No system can operate without the tax authority seeing things where there is no tax payable, but it is extremely galling, to say the least, that in situations where, for example, a return is made late but there is no tax payable, a penalty is then levied on a non-existent tax for an administrative error. We have suggested a compromise—that such penalties, where there is no tax involved, should arise only on a second or subsequent offence of failing to comply administratively. That used to be the case under the UK system and has only recently ceased to be the case.

One reason for the suggestion is that people often pay the £100 penalty, which is the current UK level for many administrative penalties, rather than go through the appeal system—we talked about it being relatively cumbersome—to make what might be entirely reasonable attempts to get the penalty removed as a matter of principle because, for example, there is a reasonable excuse. The cost of opposing a penalty would exceed the penalty. We think that the suggestion that we have made should be taken into account.

11:30

Isobel d'Inverno: The issue is particularly important because there might well be lots of nil returns in relation to leases, which Alan Barr mentioned.

Gavin Brown: Both organisations seem to agree that more is needed in primary legislation,

but the Law Society proposes that no administrative penalty should be imposed for a first offence, if I can call it that, when no tax is due.

Alan Barr: Yes—for a first offence, if you like.

Gavin Brown: You are not saying that somebody who consistently breached requirements should be exempt.

Alan Barr: Exactly. The system for VAT penalties is not dissimilar. Interest on the tax kicks in immediately, but penalties kick in only for persistent administrative failures. People get a yellow card before they get a red card.

Gavin Brown: For absolute clarity, are you saying explicitly that penalties should apply from the second offence?

Alan Barr: We have just made a suggestion. What might be thought to constitute a second offence will vary for different taxes. That is easier to judge with annual taxes; if somebody does not make a return in one year and does not do one in the next year, it is obvious. Land and buildings transaction tax will be a transactional tax, so a second offence might not turn up. However, Isobel d'Inverno's example of leases is right. A number of returns will relate to leases and it would be good to apply the suggested approach to them.

Jean Urquhart (Highlands and Islands) (Ind): I have a small point that arises from the discussion about the fact that we would all like everybody to pay their tax properly all the time, although they do not. I go back to legal advice being privileged. Is that part of the suspicion that arises? Although people are not happy to pay tax, they acknowledge that they must do so and they are content if they believe that everybody else is paying the tax that is due. We heard evidence previously that the privilege for your profession suggests a lack of clarity or a privilege to which most people do not have access. I am not sure whether I am clear about your defence of your position.

James Wolffe: It is important to keep it in mind that legal professional privilege is for all types of cases. The committee is interested in tax and tax collection, but legal professional privilege applies to every case. It is constitutionally important in a variety of contexts and perhaps most sharply in ordinary criminal cases.

That ties in with the discussion about the fact that a great deal of tax advice is not given by lawyers. I have no particular insight into that aspect. It might be a mistake to see legal professional privilege as a particular problem that relates to tax advice, because it is there for bigger constitutional reasons that concern citizens being able to speak candidly to and take advice from their lawyer and to organise their affairs or make decisions accordingly. Legal professional privilege exists for reasons that are not to do with tax, which is the issue that concerns the committee; it is there to address much broader concerns.

Jean Urquhart: I understand that, but I think that we were talking about tax advice only. We are not talking generally.

James Wolffe: I understand that, but the point is that the privilege exists for good reason, which relates to the relationship that individuals have with their lawyers and lawyers' professional responsibility in dealing with their clients. It is not particularly about tax advice. As we know, a lot of tax advice is given by non-lawyers.

Jean Urquhart: Does the Law Society want to add to that?

Isobel d'Inverno: I reiterate that most tax advice is not involved with tax avoidance and developing schemes; most of it is simply to help people to comply with their obligations to make tax returns, pay tax and all the rest of it. In most cases, whether or not there is privilege does not make any difference, but legal privilege is important if there is going to be litigation on a tax issue, for example. However, I do not think that the existence of legal professional privilege is the main reason why there is tax avoidance in the UK. That is simply not what causes it at all.

Jean Urquhart: No, I am not suggesting that. I accept that you have already said that the number of cases is small and that giving tax advice is not the mainstay of your profession but, given the circumstances, why does the accountancy profession, for example, clearly think that the privilege should be lifted as we write the legislation?

Alan Barr: I think that the accountancy profession's point is not that it should be lifted but that it should be extended to that profession—that the right not to reveal to the revenue or the courts the advice that has been given should be extended to it.

In my view, the answer is in the name—James Wolffe referred to this earlier. It is a legal privilege, which also involves consideration of where the boundaries of the law are drawn. Lawyers are subject to the rules. If somebody comes to me and says, "I want to murder my husband. What is the best way of doing it?" my legal professional privilege does not extend to my doing nothing about that particular question if she proceeds to murder her husband. Where the boundaries of privilege are drawn is a legal question. In our view, that is why it should be restricted to lawyers.

Jean Urquhart: Okay. Thank you.

The Convener: I thank the members of the committee for their questions. Do the Faculty of

Advocates and the Law Society of Scotland wish to make any further points to the committee before we end the session?

James Wolffe: No. I am just very grateful for the opportunity to give evidence to the committee.

The Convener: Not at all. We appreciate your being here.

Alan Barr: I do not think that we have anything to add. I have been involved in the tax legislative process for quite a bit, and such sessions are always directed at criticism of proposals. It would be fair to say that there are not huge areas where the Law Society found itself saying, "Oh my goodness. We wouldn't do that at all." There are details that we tried to deal with in the report, but in general we thought that the bill was a pretty good effort for a pretty significant piece of legislation in a new area for Scotland as a whole. The bill is in pretty reasonable shape, although there are some areas of disagreement or refinement, as you would expect.

The Convener: I am sure that that will cheer up the bill team, whose representatives are scribbling down your very positive comments.

I thank the witnesses very much for giving evidence.

At the start of the meeting, we agreed to take the next four items in private, so I close the public part of the meeting.

11:40

Meeting continued in private until 12:26.

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