SUBMISSION TO THE FINANCE COMMITTEE OF THE SCOTTISH PARLIAMENT

THE GENERAL PRINCIPLES
OF THE REVENUE SCOTLAND AND TAX POWERS BILL

19 February 2014
About ICAS

The Institute of Chartered Accountants of Scotland (“ICAS”) is the oldest professional body of accountants, and is a public interest body. ICAS represents around 20,000 members who advise and lead businesses. Around half our members are based in Scotland, the other half work in the rest of the UK and in almost 100 countries around the world. Nearly two thirds of our members work in business, whilst a third work in accountancy practices, many with expertise in a range of tax areas.

Introductory comments

ICAS welcomes the opportunity to give evidence to the Finance Committee at Stage 1 of the consideration of the Revenue Scotland and Tax Powers Bill.

ICAS commends the pragmatic approach to the Bill, with its use of existing UK tax powers that have been tailored to meet the requirements of Land and Buildings Transaction Tax (LBTT) and Landfill Tax, which will be devolved to the Scottish Parliament from April 2015.

ICAS also notes the significant time and effort that has been made by Revenue Scotland and the Bill team to consult and meet with interested parties throughout the period of drafting. Earlier discussions with stakeholders are reflected in the drafting of the Bill, which provides a clear and helpful framework for the management of taxes in Scotland. The comments below are put forward to enhance the effectiveness of the Bill.

In terms of priority, the most important area of the Bill to consider further is the General Anti-Avoidance Rule (GAAR). This is discussed in detail below.

There are a number of provisions, for example the penalty regime, where powers are delegated. However the delegation of powers beyond the administrative essentials reduces the legislative clarity, reduces the certainty that taxpayers might otherwise experience, and diminishes the role of Parliament in scrutiny. It would be helpful to include the key penalty principles and provisions in this Bill to address such concerns.

Achievement of policy objectives

The Bill establishes a legal framework for a tax system in Scotland, yet the taxes to which it is to apply in 2015 are not yet legislatively complete, the procedural model for the delegation of powers in particular is not yet finalised, and legal recourse is to a Tribunal system that is still being shaped. Whilst additional detail around intentions is included in the Policy Memorandum, it has no statutory force. The Bill therefore is a core framework only.

It is an understandable result of the parliamentary process and practicalities of timescale that the Bill consultation process is being launched now, but the consequence is that any Bill passed before those matters are finalised may need amendment or enhancement before implementation.

Whilst it is appropriate that minor administrative matters within Revenue Scotland should be dealt with by the general "collection and management" power it is given under section 3, we do not consider the extent of delegated powers or regulations, nor their piecemeal consideration, are necessarily appropriate for the most fundamental decisions to be made in establishing the foundations of a tax system for the first time in this Parliament.

A solution for both of these concerns may be to consider a timetabled, formal, review of the accumulated devolved tax legislation, regulations, guidance, operational plan and IT systems in their entirety, around September 2014. ICAS has suggested in the past that effective legislation is derived from properly testing draft provisions. It would be a positive step to include such testing in plans for a future review as it is generally the consideration of practical situations which highlights any gaps and weaknesses. This would allow time for considered remediation before 1 April 2015. That might best deliver the Parliament’s aims and the Scottish Government’s objectives for the Revenue Scotland and Tax Powers Bill.
The establishment and membership of Revenue Scotland and its functions

If Revenue Scotland is expected to deliver according to the Adam Smith maxims, but is to be independent of Ministerial interference, we question whether the draft Bill provisions around its purpose and directions are sufficiently specific. The Bill contains no direction, only providing for “functions of collection and management” without specification as to principles of conduct or taxpayer expectations; in particular a requirement around publication of Revenue Scotland’s equivalent of HMRC Manuals, or other guidance, would provide essential additional clarity. Section 10 describes a Tax Charter in principle, but it is to be an aspirational matter established by Revenue Scotland alone, with no accountability obligations or scrutiny; only that the Charter must be laid before Parliament. The duty on taxpayers broadly to pay the right tax at the right time is included at section 68 so it is perhaps anomalous that mirrored obligations for the tax authority are omitted.

Possible drafting amendments for discussion

It would be beneficial to have the duties and principles for Revenue Scotland specified and these could include:

- a duty to collect the right tax at the right time
- delivering on commitments to taxpayers and treating them fairly
- ensuring the security of customer data
- taking account of any hardship and/or other circumstances of taxpayers
- ensuring penalties are proportionate to the tax loss

Section 10, or a supporting schedule, could specify the Tax Charter essentials, to complement the rights and duties of taxpayers. Section 16A Commissioners for Revenue and Customs Act 2005 offers a template that could be used. The principles are for Parliament to decide but could include the following expectations of Revenue Scotland, its staff and those to whom it delegates its functions:

- Treating taxpayers with respect, courtesy and consideration
- Helping and supporting taxpayers to get things right by providing appropriate information
- Treating the taxpayer as honest (unless there is a good reason not to)
- Treating all taxpayers even-handedly
- Being professional and acting with integrity
- Tackling people who deliberately break the rules and challenge those who bend the rules
- Protecting taxpayers information and respecting their privacy
- Accepting that an agent can represent the taxpayer
- Keeping the cost of dealing with the authorities as low as possible.

The Bill is silent on the requirements and processes under which Revenue Scotland will, or may be, accountable to the Scottish Parliament and it might be expected that appropriate provisions would be included in the Bill. This is particularly the case when there is to be extensive and immediate use of delegated authority to SEPA and the Keeper.

The Bill is also silent on the approach to consultation on future legislative proposals that would be expected, and it would be appropriate to set out statutory obligations in this regard; this would also scope the role of Revenue Scotland staff in tax policy development.

The Policy Memorandum states that the majority of respondents to the consultation preferred the Board of Revenue Scotland to comprise both executive and non-executive roles, but this is not reflected in the Bill and should be re-considered. The risk of a Board not being sufficiently aware of the detailed issues would be avoided; the benefits of a mixed Board also include a greater alignment of the executive team to the Board’s objectives and enhanced accountability of staff. The Bill is also silent on the core skills or qualifications that the Board of Revenue Scotland should include, which will be particularly important in the early years of operation.
The proposed approach to the Scottish Tax Tribunals

The draft legislation in the Bill replicates much of the Tribunals (Scotland) Bill which has completed Stage 1 and, very recently, Stage 2. It is not clear whether Part 4 of the Bill should be considered as a standalone draft or whether there has been a policy decision simply to replicate provisions from the Tribunals (Scotland) Bill. Amendments to the Tribunals (Scotland) Bill have been made at Stage 2 and it may be that the same amendments should be made in due course to the Revenue Scotland and Tax Powers Bill. The tribunals will also operate substantially on the basis of the Scottish Tax Tribunal Rules which also need to be drafted.

The UK tax tribunals system offers the administrative efficiency of categorising appeals to the First-tier Tribunal into the four categories Default paper, Basic, Standard, and Complex according to the issue, with the tribunal complexity increasing accordingly. A number of “presiding members” are authorised to decide Default Paper and Basic cases alone. It is not clear whether this is intended for the Scottish tax tribunals.

The administrative arrangements for a new, separate, Scottish Tax Tribunal to be established should be clarified, particularly around the judicial staff, i.e. judges and members with appropriate experience of judicial skills, taxation (ideally SDLT/LBTT) and anti-avoidance provisions.

Of particular importance to the interpretation of the new legislation, this Bill might also be expected to provide clarity around the role and precedent of UK tax case law on the same wording and principles, as applied with regard to the devolved taxes.

The General Anti-Avoidance Rule (“GAAR”)

The rule has been introduced to provide a counteraction measure to “artificial tax avoidance arrangements”. It is wider than the UK regime; it is worth considering firstly the drafting approach, before commenting on the possible consequences and effectiveness of the rule.

Firstly, the definitions and drafting are substantially copied from the UK General Anti-Abuse Rule in the UK Finance Act 2013. Both rules have a test requiring the respective tax authority to conclude the tax planning arrangements were not a “reasonable course of action”, however in Scotland an additional test catches any transaction which “lacks commercial substance”.

The UK has a second “reasonableness” test, in that a “reasonable view” needs to be taken in regard to the wider prevailing business practice, which the Scottish provisions have incorporated as an example rather than a separate test, for “reasonable business conduct”. “Reasonableness” at a UK test has been criticised as being too subjective, but certainty was offered instead by the appointment of an independent General Anti-Abuse Rule Advisory Panel. It will provide advance interpretative guidance and a “reasonableness” opinion to taxpayers and HMRC alike in disputes which must be taken account of in the courts. The current Bill does not have a second “reasonableness” override provision, nor does it establish an Advisory Panel for Scotland, but leaves instead the view on what might have been “reasonable business conduct” and “lacks commercial substance” essentially to Revenue Scotland to determine and challenge alone. This generalised drafting in the Bill lacks balanced safeguards.

There is a further requirement in the Bill that the Scottish courts “must” take into account non-statutory, not yet written, guidance in interpreting “reasonableness” “and “lacks commercial substance” as well as the wider provisions of this GAAR. Overall then, Revenue Scotland will make the detailed law, decide when it is to be applied and this Bill binds the courts to take Revenue Scotland’s view into account. The lack of parliamentary or other scrutiny on the scope and application of the law and the lack of independence of the courts in this matter is less than would be expected in this opportunity to establish a fresh, high quality approach to tax legislation. It also results in there being no certainty at the moment on the real impact of the GAAR, thus failing that maxim.

The uncertainty resulting from the Bill’s drafting causes concern to taxpayers undertaking commercially motivated transactions and could be a disincentive to do business. There will be greater tax uncertainty for transactions undertaken in Scotland when compared to the rest
of the UK and uncertainty gives a less competitive business environment. It will be important to consider the proposed impact of these provisions on the attractiveness of the Scottish property market, another matter that could be considered in a pre-implementation review as discussed above.

The Policy Memorandum recognises the Bill’s statutory uncertainties, and suggests that taxpayers could ask for a non-statutory, non-binding opinion, falling short of a clearance system and at the discretion of Revenue Scotland. There is however no such route in the Bill so this does nothing to adequately resolve the uncertainty concerns.

**Possible drafting amendments for discussion**

The need for certainty suggests that there should be an amendment to the “must” provision, or a statutory clearance system, and/or an Advisory Panel, particularly in the early years of operation of the new GAAR.

Clause 59(3) of the draft Bill identifies as able to be counteracted, any arrangement that “lacks commercial substance”. The identification of these is down to Revenue Scotland alone. It is difficult to see that Revenue Scotland staff will necessarily have the commercial property market and legal experience to operate the judgement necessary, so either this test B should be removed, or if it is to stay, the preferred route might be that an Advisory Panel be appointed to assess the commercial substance and reasonableness of the arrangements under challenge.

Clarity on the precedent value of UK case law on the relevant taxes and on the UK Advisory Panel’s opinions on similar transactions should be provided.

The effectiveness of any anti-avoidance provision depends on the tax authority concerned having the right level of resource to deal with the complexity and scale of the legislative obligations placed on it. As regards the GAAR, this requires the right level of commercial knowledge to assess the applicability of the provisions and understand the property market (for LBTT) and tax planning environment. We understand from Scottish Government officials that, contrary to the explanatory notes, no Disclosure of Tax Avoidance Scheme (DOTAS) regime will support the operation of the GAAR.

The Bill contains no provisions requiring the GAAR to be monitored, and the effectiveness of the provision reviewed and reported on at set intervals to assess its effectiveness; balancing the prevention of tax avoidance and creating sufficient business certainty.

**The proposed approach to tax returns, enquiries and assessments**

A provision missing from this Bill is one to give taxpayers a specific statutory right to appoint a tax agent to act on their behalf and for Revenue Scotland to respect that. For the Bill to be clear and comprehensive, the tax agent’s duties and responsibilities should be outlined in legislative powers, rather than subsumed under general “collection and management” powers in section 3. There is recognition in various provisions that someone may act on a taxpayers behalf, indeed it is core to the practical operation of LBTT that the return is likely to be completed by an agent (the solicitor undertaking the legal work on the land transaction). It is also core to the efficient and convenient operation of UK and international tax systems that a taxpayer’s agent can be involved.

**Proposed drafting amendment for discussion**

It should be specifically recognised in the Bill that a taxpayer can appoint an agent. Finance Act 2012 Schedule 38 paragraph 2 offers example wording for who is a ‘tax agent’ that could be replicated in this Bill.

It is noted that sections 100 – 104 have a range of defences to claims for overpayment of tax but it is questionable how some of these defences could relate to the two devolved taxes. It is not clear on what basis the state is entitled to keep money not owed to it. If taxpayers must pay the right amount of tax, the state must not keep the wrong amount.
The provisions relating to information notices in part 7 contain an interesting divergence from UK legislation, around professional privilege and documents. The UK legislation at present supports a level playing field across the service sector in relation to tax advisory advice, in that advice between a tax adviser (whatever professional background) and client is regarded as subject to privacy protection and a statutory exclusion from certain tax information notices. This is consistent and works well with a tax system where obligations are clear, views on interpretation may diverge and a clear appeal and tribunal framework is in place.

The Policy Memorandum explains that such privacy protection will only apply to a professional legal adviser (not defined in the Bill but apparently only solicitors in Scotland, who will undertake practically all LBTT transactions. Nevertheless, one of the difficulties with the Legal Services (Scotland) Act 2010 is that 'legal services' is sufficiently widely defined that it arguably could include accountancy practitioners. Clarity and consistency across Scottish legislation would be beneficial to all concerned. The Memorandum says that to do otherwise - that is to extend such this protection to tax advisers - would “unduly hinder efforts to tackle tax avoidance in Scotland”, which is unsubstantiated, misplaced and anti-competitive. This is because the greatest challenges a tax system can put to hinder tax avoidance in Scotland is to have a comprehensive package of measures which ensure the law on tax avoidance is certain, there are disclosure obligations on taxpayers and scheme promoters and there is a properly resourced compliance and enforcement regime. The weakness in the legislation is discussed above; the second point has been ruled out by the government and the third is as yet not visible; progress is needed on all of these areas rather than attempts to divert in this information notice point.

A vibrant professional services community needs a level playing field; it is widely recognised that tax advisers do much to support tax compliance and ICAS members in particular are governed by a professional standards code which gives specific prohibition to acting or advising clients to act in ways that seek to avoid or evade tax by non-disclosure to the tax authorities. It is also the case that some lawyers currently put forward their position regarding privilege as a competitive edge when offering for advisory work on tax matters, particularly where international businesses with different regimes give a different expectation.

To keep a level playing field and tax services competition open in particular to those already adhering to professional standards, supports the argument for a replication of the UK provisions in this Bill.

Proposed drafting amendment for discussion

Finance Act 2008, Schedule 36 paragraph 25 should be replicated in the Revenue Scotland and Tax Powers Bill so that there is a clear statutory authority regarding the position of tax advisors in terms of privilege.

There is also a need to define an auditor, being an office that meets the requirements of the Companies Act 2006.

The proposed approach to penalties

The Bill reflects an imbalance in the approach to penalties; those for errors are described in outline but those for late returns and late payments of tax are delegated to Ministers. Tax enforcement powers are so significant to the tone and impact of a tax powers Bill that it is a considerable weakness that these cannot be considered in the Bill as a whole.

Whilst it may be the case that for future devolved taxes it may be desirable to adopt a different approach, that is not a credible reason for failure to specify the levels, structure and shape of the penalties regime now for the known devolved taxes. The penalties sections included in the Bill are copied from UK provisions so it appears that only a policy decision has prevented a more comprehensive copying, or direct replacement for differences of approach. This fails to deliver a clear package for Parliamentary consideration and consultation.

The main concern arises from the possibility that penalties would be based on the UK provisions of VAT default surcharge, which can have an extremely harsh and disproportionate effect, where increasing penalty levels are imposed where repeated late payment arises,
even for example from a business having cash flow difficulties and even where only a day is involved. The penalty level under those provisions is at up to 15%, more recent provisions such as for PAYE are at up to 4%.

The proposed approach to interest on payments

Although a direct copy of the UK stamp duty land tax provisions, it is not clear why a delay of 30 days will be provided for before interest on late payment of tax is charged as a general principle, particularly when a penalty can be charged on the same amount (depending on secondary legislation yet to be published). If delay in payment has no cost consequences, taxpayers may be tempted to delay payment accordingly, reducing the efficiency of the collection system.

It is appropriate that the rate of interest may vary according to market conditions, but it seems inconsistent to provide that fees payable with online/credit card transactions are capped by what is reasonable in relation to the costs incurred, yet no reasonable reference point is established for interest rates.

The proposed approach to reviews and appeals

It is disappointing that the principle of payment before review or appeal is established without condition or circumstances being statutorily required to be taken into account. ICAS provided detailed evidence to the Scottish Government on a workable alternative proposal, yet the whole issue has again, inappropriately, been left wholly to the secondary regulations. Amendment is necessary to require Revenue Scotland and Ministers to take account of hardship and specific financial consequences.

Proposed drafting amendment for discussion

Value Added Tax Act 1994, section 84(3B) offers precedent wording to insert after the Bill section 210(1), where HMRC or the Tribunal (failing HMRC) are "satisfied that the requirement to pay or deposit the amount determined would cause the appellant to suffer hardship."

ICAS is interested to have confirmed that the Scottish Public Services Ombudsman will operate in relation to Revenue Scotland and the devolved taxes.

Other matters: gaps and inconsistencies, drafting details

The content of the Bill replicates a number of provisions in existing UK legislation but there are a few places where there are gaps or inconsistencies. These are:

- The use of varying terms for Revenue Scotland and its staff, for example, section 15 refers to ‘Revenue Scotland official’, section 57 to an ‘authorised officer’, section 78 and 89 to a ‘designated officer’, and section 111 to a designated investigation officer
- The use of the term ‘tax’ where it should be defined as ‘devolved taxes as in section 3(3)’ and this is required in sections 68, 77(1)(b) and 92.
- The use of the term ‘reasonable’, which has been widely used in the Bill. Concerns arise over this because it is a subjective term and, as yet, there is no Scottish legal precedent as to its interpretation, nor is there UK precedent. It is generally left to the courts to determine, based on the circumstances of the particular case.