Proposed LBTT supplement on additional residential homes – Call for evidence
Response by the Chartered Institute of Taxation

1 Introduction

1.1 This is a response by the Chartered Institute of Taxation (CIOT) to the Finance Committee of the Scottish Parliament’s call for evidence: Proposed LBTT supplement on additional residential homes. We welcome the opportunity to offer our comments on the proposal for a Land and Buildings Transaction Tax (LBTT) supplement to take effect from 1 April 2016; we would be pleased to amplify our points orally or in writing.

1.2 The CIOT is an educational charity concerned with promoting the education and study of the administration and practice of taxation. For more details see the statement about us at section 10 below.

1.3 The CIOT would like to assist in ensuring that the tax system in Scotland is effective and efficient for taxpayers, agents and the tax authorities.

1.4 Our response was prepared prior to the publication of the draft legislation on 28 January 2016.

2 Executive summary

2.1 While we welcome the opportunity to respond to the Finance Committee’s call for evidence, we note our disappointment that the proposed supplement will be introduced without full consultation and within such a short timeframe. When legislation is brought in in such a way, it is more likely that there will be unresolved issues.

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1 The measure was announced on 16 December 2015; the call for evidence was published on 6 January 2016 with a deadline of 29 January 2016. Legislation was published 28 January 2016, with the intention of it being passed by the Scottish Parliament prior to its dissolution on 24 March 2016 for the Scottish Parliament election. It is proposed that the measure will take effect on 1 April 2016.
complexities and unintended consequences. It will also prove challenging for Revenue Scotland to implement the changes required.

2.2 We think that due regard should be given to Adam Smith’s four principles in respect of this policy. We are concerned that the proposal will lead to uncertainty and not necessarily be convenient to pay.

2.3 One means of mitigating the uncertainty for many ordinary house buyers, simply moving house, (by selling their only home and buying a new sole residence) would be a targeted relief. Otherwise, most purchasers will have at the very least to address the risk of having to pay the supplement, for example if their buyer pulls out.

2.4 It is likely to prove difficult for Revenue Scotland to police compliance in respect of properties owned outside Scotland, and more particularly outside the UK; this is especially the case where the purchasers are non-resident and non-domiciled.

2.5 There are a number of areas of potential complexity, unfairness or confusion, such as the different definition of a main residence for LBTT from capital gains tax, the treatment of married couples and civil partners, and the rules for joint purchases and part sales.

3 1. The Scottish Government’s overall policy objectives in introducing the supplement and, in particular, whether it –

- is likely to ‘complement the Government’s commitment to supporting home ownership in a balanced and sustainable way.’
- ‘helps to ensure that the tax charge is proportionate to the taxpayer’s ability to pay.’

3.1 We acknowledge that the measure has been proposed in response to the announcement by the UK Government of a similar measure for Stamp Duty Land Tax (SDLT). It would be helpful for the Scottish Government to confirm the policy objectives of the proposed supplement, and consider its impact, given the Scottish Government suggests that the main aim of the measure is to prevent distortions as a result of the UK Government’s measure, rather than indicating that they would have introduced such a proposal independently.

3.2 The Scottish Government has committed itself to a tax system that has regard to Adam Smith’s four principles: certainty; the burden proportionate to the ability to pay; convenience; efficiency of collection. The CIOT agrees that these are important principles for a sound tax system. In view of this, we think it is key that due regard is given to all of these principles, not only ability to pay, in developing this LBTT policy.

3.3 Unfortunately, we can see difficulties in this policy reflecting Adam Smith’s principles. As regards certainty, all purchasers of residential property will have to factor the supplement into their considerations, unless they are buying a property from the

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3 For example, we understand that c. 70% of private rental sector properties are owned by small-scale landlords, who let out 5 or fewer properties – thus the Scottish Government will need to consider the likely impact on such investors and whether or not that meets the policy objectives.

position of non-ownership. For many people simply moving house, there will be uncertainty as to whether or not the supplement applies to their purchase at the time of the transaction.

3.4 It is unlikely that the tax charge will be convenient, since in respect of many transactions, the falling through of a sale or the delay of a sale will mean the supplement applies to the purchase, yet there will be no sale proceeds to assist with the financing of the payment of the supplement.

3.5 In respect of whether or not the supplement is proportionate to the taxpayer’s ability to pay, we recognise that in principle, this is the case. The inclusion of a relief or exemption for certain acquisitions, such as for multiple purchases of residential properties, may mean that the supplement does not always correspond to the taxpayer’s ability to pay.

3.6 The LBTT is a transaction tax. At present, the tax requires a purchaser to consider whether an acquisition concerns residential or non-residential property. The proposed supplement will mean a need to make judgements concerning the quality of occupation and even the intention to occupy a property as a main residence at the date of the transaction. This creates considerable complexity and uncertainty around the application of the supplement.

4 2. The proposed 3% rate for the supplement and the £40,000 purchase price at which it is proposed to take effect.

4.1 The CIOT does not generally comment on the setting of rates of tax, as these are decisions for politicians. In our view, the setting (and changing) of rates and bands should flow from policy decisions as to the aims of the Scottish Government and the Scottish Parliament.

4.2 As a general comment, however, we note that one of the progressive steps taken when creating LBTT was the move away from the ‘slab’ structure of SDLT. While acknowledging that the £40,000 threshold has been chosen for administrative purposes, the structure for the proposed supplement effectively creates a cliff edge for properties at the lower end of the market.

5 3. The Scottish Government’s estimate that the measure will raise between £17 million and £29 million in 2016-17.

5.1 This is not our area of expertise and we make no comment.

6 4. Any reliefs or exemptions that you consider should form part of the legislation.

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5 We refer to people who only own one property, sell it and buy another property.
6 Land transactions where the chargeable consideration is less than £40,000 are not notifiable – an administrative saving for Revenue Scotland, agents and taxpayers – section 30, Land and Buildings Transaction Tax (Scotland) Act 2013: http://www.legislation.gov.uk/asp/2013/11/section/30
6.1 To a large extent, the inclusion of reliefs and exemptions should follow the policy objectives. In addition, consideration should be given to the Adam Smith principles – in particular, ideally it will be clear to a taxpayer whether or not a relief or exemption applies in their case. Reliefs and exemptions should also be straightforward to operate such that they do not introduce unnecessary complexity. One possible model for reliefs could be Schedule 4A Finance Act 2003, which sets out some reliefs from the higher rate of UK SDLT.7

6.2 One relief that has been proposed is for the simultaneous purchase of multiple properties (whether new build or not). In the UK consultation, the threshold that has been suggested is 15 properties. Given that there is another LBTT relief in respect of multiple property transactions, and that that relief uses a threshold of six properties, it would appear more sensible to align any relief from the supplement for multiple purchases with the current LBTT relief.8 Different thresholds could result in purchasers paying commercial rates of LBTT and also being liable for the residential LBTT supplement, offering a source of confusion. Given the wording of section 59, it would also be helpful to have confirmation that the supplement can in fact apply to such transactions in the first place.9

6.3 The Scottish Government will need to consider and clarify whether the multiple purchase test applies to the purchase of properties that form part of the same sale and purchase agreement or linked transactions, or both. Given developments may become available for purchase in phases, consideration should also be given to taking account of phased purchases for the purposes of determining eligibility for a scale purchase relief. In addition, it has been suggested that relief might only apply where a purchaser already owns a specified number of properties, although this would seem to unfairly disadvantage those investing in their first tranche of properties compared to existing investors.

6.4 There would also need to be consideration as to how such a relief would operate in respect of purpose-built student accommodation, for example, where a development may consist of properties intended for multiple occupation.10 Should the relief take into account not only the number of properties, but also the number of occupants within each property?

6.5 Consideration should be given to an exemption for purchases by providers of social housing in Scotland,11 such as local councils and housing associations (registered social landlords), or clarification that such purchases will not fall within the ambit of the supplement if this is already the intention. It would not be possible for such purchasers to rely on a multiple purchase relief, since not all transactions would consist of multiple properties.

6.6 Consideration should be given to a targeted relief for house buyers who are intending to simply move house by selling their only home and buying a new sole residence – therefore there is no intention to own two properties simultaneously (see paragraph 9.1). Otherwise the risk of having to pay the supplement for such

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7 http://www.legislation.gov.uk/ukpga/2012/14/schedule/35/paragraph/4
8 Section 59 (8) Land and Buildings Transaction Tax (Scotland) Act 2013.
9 Section 59 (8) Land and Buildings Transaction Tax (Scotland) Act 2013: ‘Where six or more separate dwellings are the subject of a single transaction involving the transfer of a major interest in, or the grant of a lease over, them, then, for the purposes of this Act as it applies in relation to that transaction, those dwellings are treated as not being residential property.’ http://www.legislation.gov.uk/asp/2013/11/section/59
10 Typically such properties would consist of a number of private (lockable) bedrooms, a shared living / dining area, a shared kitchen and shared bathroom facilities.
11 For example, to increase social housing stock for letting or as part of an economic regeneration project.
purchasers may deter them from moving house completely. Although there may be relatively few purchasers who actually end up having to pay the supplement, far more purchasers will have to address the risk, just in case their sale falls through or is delayed. It would be possible to include anti-avoidance measures, for example disclosure of the property to be sold, and a requirement for the original property to be sold within a specified time period, such as three months; otherwise the LBTT supplement would become due.  

6.7 Our understanding is that the intention is to charge the 3% supplement on all purchases of residential properties by a partnership, where one partner owns a property already. Consideration should be given to a relief for partnerships where they purchase a residential property to be occupied by an employee of the partnership as a condition of their employment.

7 5. The potential for tax avoidance under the supplement and how this should be addressed.

7.1 The inclusion of exemptions and reliefs will potentially provide more opportunity for tax avoidance.

7.2 It should be noted that it might be possible for the order in which properties are bought to affect whether or not the purchaser pays the supplement. Thus a purchaser with sufficient funds to plan their affairs might be able to avoid the supplement, while a purchaser who has less resource may have to pay the supplement if for example their sale falls through (see paragraph 9.1).

7.3 A cause for concern must simply be that of compliance in respect of properties owned outside Scotland, and more particularly outside the UK; in addition, there is a similar concern in respect of non-resident and non-domiciled purchasers. It is unclear how Revenue Scotland will be able to police compliance in terms of the declaration of ownership of properties overseas.

7.4 The fact that all residential purchases by companies and similar entities will be subject to the supplement is a key anti-avoidance provision. We note that there are also likely to be extensive deeming provisions in relation to trusts. Both of these approaches will help to address some possible routes for avoidance, as will the GAAR.

12 We note that the UK Government might consider a grace period, such that the additional charge would only apply if the old main residence was not sold by the time the SDLT return was filed. It would not be possible to have a grace period along exactly the same lines in Scotland, due to the way in which sales are registered and returns made. However, a targeted relief as suggested would allow delayed sales to go through, reduce the number of purchasers faced with paying the supplement, and also reduce the administration of reclaiming the supplement for both the purchaser and Revenue Scotland.

13 This might typically affect farming partnerships.

14 For example, a purchaser could sell their main residence (1), then purchase a buy-to-let property (2), and finally purchase a new main residence (3) within 18 months of the sale at stage (1) – they would not be liable to pay the supplement. A further example, is that a purchaser who owns a buy-to-let property (but no main residence) will be liable to the supplement if they purchase a main residence; whereas someone who already owns a main residence and a buy-to-let property will not be liable to the supplement, if they sell their main residence within 18 months of buying a new main residence.

8 6. The likely impact of forestalling.

8.1 We are not experts on the property market. Nevertheless, where investors have the opportunity and means to purchase buy-to-let property and second homes prior to April 2016, it appears likely that this will be the case, meaning a potential increase in buyer activity in the first quarter of 2016.

9 7. Any other comments you may have on the proposed supplement.

9.1 Although the general perception may be that this proposed supplement will not affect the majority of transactions, (and indeed, many purchasers will not have to pay the supplement), in fact most purchasers will have at the very least to address the risk of having to pay the supplement, for example if their buyer pulls out or their sale is delayed. Thus a purchaser has to bear in mind that they may have to arrange bridging finance to complete their own purchase, and in addition pay the 3% supplement, on top of their expected LBTT charge.

9.2 We understand that there is an intention for an 18 month window for the replacement of a main residence that has been sold. Thought will need to be given as to when the 18 months window commences for purchasers who have already sold their main residence (prior to the announcement on 16 December 2015) and those who sell prior to 1 April 2016. Will their 18 month window commence on 1 April 2016 (when the supplement is introduced) or does it commence on the date of sale of their old main residence? In the case of those who sold prior to the announcement of the supplement, it would appear to be inequitable for the replacement window to commence at the date of sale of the old main residence.

9.3 Further, in relation to transitional provisions, it is proposed that transactions where missives were concluded prior to 16 December 2015 will not be subject to the supplement. Given Scottish property law, it might be more appropriate to consider transactions for transitional relief where an offer to buy has been made and accepted prior to 16 December 2015.

9.4 The proposal is for the definition of a main residence to be based on the facts. This means that unlike capital gains tax, it will not be possible to elect one’s main residence for LBTT purposes. This is a possible source of confusion. In addition, for taxpayers resident in Scotland, there are further complications with the need to consider their residence position for the purposes of the statutory residence test and Scottish taxpayer status. It will be essential for the guidance to address this clearly.

9.5 We note that the buy-to-let sector will also face potentially higher tax bills as a result of changes being introduced from April 2017 by the UK Government in respect of tax relief for finance costs. In effect, this means that relief for interest on loans taken out to purchase assets that generate taxable income will be restricted. By way of example, buy-to-let landlords could have a taxable profit in respect of buy-to-let properties, even where they have actually generated a loss. Thus, when considering the likely impact of the proposed LBTT supplement on the Scottish housing market, the Scottish Parliament and Scottish Government need to take into account the likely impact of the change to relief for interest on loans too.

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9.6 It is our understanding that married couples and civil partners will only be entitled to one main residence between them. Where they separate, they will continue to be treated as a couple until there is a court order or formal deed of separation. At the same time, the intention is for a main residence to be determined as a question of fact (see paragraph 9.4). We can envisage two difficulties here. Firstly, the rules differ from those for capital gains tax, which treat couples as separate individuals in the tax year following separation. As a result, where a member of the separated couple purchases a new residence prior to the court order or formal deed of separation, they will be exposed to the LBTT supplement. Secondly, there is potentially a tension between determining a main residence on the facts and the rule for married couples and civil partners, since the facts may not point to the same main residence for each member of the couple or partnership, particularly in the case of separation.

9.7 Where there is a joint purchase, we understand that the likely position will be that if one of the joint purchasers already owns a residential property, the LBTT supplement will apply to the whole purchase, even if one or more of the joint purchasers is buying their main (and only) residential property. This could be viewed as inequitable for the purchaser(s) that do not hold any other property. Options that could be explored, while acknowledging that there would probably need to be targeted anti-avoidance rules, include only charging the supplement on those joint purchasers who already own a property and having a de minimis equity holding exemption by reference to the property value at the transaction date, for example where parents purchase a home for a child. Alternatively, one could consider the nature of the purchase, such that if one of the purchasers is replacing a main residence (or buying a new sole residence), then the supplement does not apply at all or does not apply to their interest in the property.

9.8 Consideration needs to be given as to whether and how the supplement will apply in cases where a purchaser buys an interest in a property, becoming a joint-owner with the existing owner(s). Will the position of all owners have to be considered, even though only a part-interest in the property is being purchased? Would it be equitable for the supplement to be payable by a purchaser who owned no other properties (only the share it is buying), just because the existing owner(s) holds other residential property?

9.9 From a practical point of view, it will be essential to set out clearly the respective roles and responsibilities of purchasers and professional agents. Equally, it is important that administrative arrangements are thought about as the policy is developed and that in due course, Revenue Scotland consults widely on the operational guidance. In particular, the refund mechanism must operate smoothly to ensure that purchasers do not pay additional finance charges due to delays in processing their reclaims. One option might be to include notification of the intention to claim a refund in the original LBTT return, such that Revenue Scotland is put on notice.

9.10 As a final point, the proposed supplement appears to be following the policy design of the higher rates of SDLT proposed by the UK Government. Scottish property law differs considerably from the law in the rest of the UK. It is important that the drafting of the legislation to implement the proposed policy takes account of the Scottish legal

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17 Section 1011 Income Tax Act 2007 as applied to capital gains tax by section 288(3) Taxation of Chargeable Gains Act 1992. One option would be to add the alternative circumstance that applies to capital gains tax, so that couples are not treated as living together when they are in fact separated in circumstances in which the separation is likely to be permanent. Alternatively, a refund could be allowed if separation is formalised (under a court order or formal deed of separation) within a certain time period, for example 18 months.
system, for example, ownership does not transfer until the point of registration with
the Land Register.\textsuperscript{18} However, there is a further complication in that worldwide
properties will be taken into account when determining whether or not the purchaser
owns more than one residential property at the end of the day of the transaction. The
Scottish Government therefore needs to consider the rules that will apply to overseas
properties – will ownership be determined according to Scottish law principles or
according to the law in the other country?

\section{The Chartered Institute of Taxation}

The Chartered Institute of Taxation (CIOT) is the leading professional body in the
United Kingdom concerned solely with taxation. The CIOT is an educational charity,
promoting education and study of the administration and practice of taxation. One of
our key aims is to work for a better, more efficient, tax system for all affected by it –
taxpayers, their advisers and the authorities. The CIOT’s work covers all aspects of
taxation, including direct and indirect taxes and duties. Through our Low Incomes
Tax Reform Group (LITRG), the CIOT has a particular focus on improving the tax
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The CIOT draws on our members’ experience in private practice, commerce and
industry, government and academia to improve tax administration and propose and
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the designatory letters ‘CTA’, to represent the leading tax qualification.

\textbf{The Chartered Institute of Taxation}  
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\textsuperscript{18} This would need to be taken into account in an equivalent manner for looking at the property being purchased
and the property being sold.