

CORRESPONDENCE FROM THE CABINET SECRETARY FOR FINANCE, EMPLOYMENT AND SUSTAINABLE GROWTH TO THE CONVENER, DATED 31 JULY 2014

REVENUE SCOTLAND AND TAX POWERS BILL: STAGE 3

During the Committee's consideration of the Bill at Stage 2 on 11 June I promised to reflect further on points which were raised by Malcolm Chisholm and Gavin Brown relating to sections 59 and 151 of the Bill respectively. Having done so I would like to explain the amendments I intend to lodge at Stage 3 to address both of these issues; and also to outline the reasons for other Government amendments which I will be bringing forward, all of which I believe are essentially minor and technical.

Section 59: Meaning of "artificial"

As you are aware, section 59 of the Bill provides that a tax avoidance arrangement is artificial if either Condition A or Condition B is met. As originally introduced the Bill provided that Condition B is met if the arrangement lacks commercial substance. However the Committee recommended at paragraph 38 of its Stage 1 Report:

"that the references to commercial substance in subsection (3) & (4) of section 59 need to be broadened to cover non-commercial transactions that have real economic consequences for the taxpayer and the reference to reasonable business conduct in subsection (4) extended to include personal conduct."

I brought forward two amendments at Stage 2 which were designed to meet the Committee's recommendation, by providing first that Condition B is met if the arrangement lacks either economic **or** commercial substance; and second that an additional example of something which might indicate that an arrangement lacks economic or commercial substance is where the arrangement results in a tax advantage which is not reflected in the business risks undertaken by the taxpayer.

The Committee agreed both of these amendments but Malcolm Chisholm asked why I had not specifically extended the reference to "reasonable business conduct" to cover "reasonable personal conduct", and pointed out that the example cited by the Committee was the matter of a personal gift that has no commercial substance and would not normally be employed in reasonable business conduct.

I propose to address this point by lodging a further amendment to make it expressly clear that the example in section 59(4)(a) of something which might indicate that an arrangement lacks economic or commercial substance is "whether the arrangement is carried out **by a person** in a manner which would not normally be employed in reasonable business conduct."

This amendment, together with those already made at Stage 2, would put it beyond doubt that Condition B and the associated example in section 59(4)(a) covers transactions between individuals as well as companies or businesses. It is intended to address in full what I understand to be the thinking behind the Committee's recommendation at paragraph 38 of its Stage 1 Report, together with Malcolm Chisholm's specific point about personal gifts which have no commercial substance (but which would have economic substance).

I have taken advice on whether we should also amend section 59(4)(a) to refer to arrangements carried out by a person in a manner which would not normally be employed in

reasonable **personal or** business conduct, and have reflected carefully on that advice. I have reached the view, for the following reasons, that it would not be appropriate to make that particular amendment:

- The concept of ‘reasonable personal conduct’ would be highly subjective and there is therefore a real risk of introducing uncertainty about the scope of Condition B, potentially giving taxpayers an opportunity to blunt the effectiveness of this aspect of the GAAR by claiming that their conduct is reasonable personal conduct;
- The examples in section 59(4)(a) – (e) of something which might indicate that an arrangement lacks economic or commercial substance are all closely based on recent EU Council Directives which means that Revenue Scotland and the Scottish Tax Tribunals would be able to rely on EU jurisprudence, which would not be possible if we depart from the terms of the corresponding EU Directives; and
- Genuine gifts would not need to be considered against Conditions A or B because they would not be tax avoidance arrangements under section 59(1) of the Bill, as obtaining a tax advantage would not be one of the main purposes of the arrangement. If however there were concealed consideration, and this came to light, the transaction would be taxable on the basis of the concealed consideration. The taxpayer would also be liable to be charged at common law with fraudulently evading an obligation to pay tax.

Section 151: Penalty for failure to pay tax

As recommended by the Committee in its Stage 1 Report, I lodged a series of amendments at Stage 2 which were designed to set out the penalties regime in full on the face of the Bill rather than leaving this to secondary legislation. While the Committee welcomed that approach, Gavin Brown suggested that making the penalty if tax is outstanding payable the day after the due date could be a little harsh on the taxpayer on some occasions, for example if there has been a genuine oversight or error by the taxpayer or if there has been a bureaucratic error by Revenue Scotland.

Once again, I undertook to reflect further on this point, and having done so I propose to lodge an amendment to the table in section 151 in respect of Land and Buildings Transaction Tax to provide that the date after which a penalty is incurred is 30 days after the date by which the amount of tax due must be paid. I hope this provides the element of flexibility that Gavin Brown called for at Stage 2.

I do not however believe that a similar amendment is necessary in relation to Scottish landfill tax, since by definition that tax applies to landfill site operators who will be required to make regularly quarterly returns to Revenue Scotland and will therefore be well aware of their obligations in that respect. If however a landfill operator is able to satisfy Revenue Scotland under section 157 of the Bill that there is a reasonable excuse for a failure to make a return then the penalty in section 151 does not arise in relation to that failure. That would cover circumstances in which, for example, there were genuine reasons beyond a landfill operator’s control which meant that the operator was unable to pay the tax on time.

Other Government Stage 3 amendments

In addition to the two issues which members of the Committee raised at Stage 2, I will be lodging further Government amendments at Stage 3 to improve the clarity and consistency of the Bill and also the interface between the Revenue Scotland and Tax Powers Bill and the two tax-specific Acts which Parliament has already passed, the Land and Buildings

Transaction Tax (Scotland) Act 2013 and the Landfill Tax (Scotland) Act 2014. None of these amendments will represent any change in our thinking on policy aspects of the Bill; and although there will be a significant number of amendments, I hope that you and other colleagues will agree that they are all entirely minor and technical in character.

In conclusion, I would like to express my thanks once again to the Committee for the substantial work which it has done in considering, taking evidence and reporting on all three tax Bills which the Government has brought forward in the current Session, and the non-partisan approach which it has adopted throughout. I have no doubt that the legislation we have passed is much the better as a result.

JOHN SWINNEY