Scottish taxes in the spotlight

Management of taxes

06 May 2021

Ahead of the Scottish parliament election on 6 May, Charlotte Barbour, Joanne Walker and Chris Young set out the tax priorities for CIOT and ICAS in the 2021-26 parliamentary term

Key Points

What is the issue?

CIOT and ICAS have published a new paper setting out their priorities for the devolved taxes in the Scottish parliament following the elections on 6 May.

What does it mean for me?

The tax profession has a role to play in understanding and communicating the impact of devolved tax changes and their implications for the wider UK tax system.

What can I take away?

The next Scottish parliament needs to take a number of steps to improve the way it scrutinises tax decisions and to improve awareness and understanding of tax devolution among the wider public. This has implications for both Scottish taxes and their relationship with the wider UK tax system.

CIOT and ICAS have been active stakeholders in the development of the Scottish parliament's devolved tax powers, through the work of our Scottish Taxes committees, appearances before parliamentary committees and as commentators on tax matters in the media.

We engage with the Scottish parliament in order to advance public education in taxation, increase general understanding of tax matters by non-specialists, and by making ourselves available for consultation and engagement with policy makers.

In April 2021, we published a new paper, 'Building a Better Tax System', (see bit.ly/3ehnUmL) which sets out three broad areas of policy development for the coming parliamentary term.

A path of divergence

The more things change, the more they stay the same. Scotland's devolved tax regime has continued on a path of divergence from the rest of the UK since the last Scottish parliament elections in 2016.

The most notable change came in 2018 with the introduction of a five band structure of Scottish income tax, chargeable on non-savings, non-dividend (NSND) income. This comprised the introduction of a 'starter' rate of 19% and an 'intermediate' rate of 21%, and an additional penny on the Scottish 'higher' (41%) and 'top' (46%) rates of income tax.

Other aspects of the income tax regime in Scotland remain set at a UK-wide level. They include (but are not limited to) deciding who is a 'Scottish taxpayer', defining the tax base and setting the personal allowance and rates and bands of savings and dividend tax. The differences between Scotland and the rest of the UK in 2021/22 are shown in the table opposite.

Since the last Scottish election, the Scottish parliament has also flirted with reform of some of the taxes under its jurisdiction but has seen plans for the devolution of some tax powers from Westminster founder under political and legislative challenges. There have also been proposals for new taxes, but these too have faced difficulties.

Towards a better tax system

Devolution has increased the complexity of the tax system, which in turn has reinforced the need for strengthened oversight, increased accountability, and a need for greater awareness of the Scottish parliament's tax responsibilities. These are the three themes that have guided the preparation of our paper.

Theme 1: Strengthening decision making

The structures of the Scottish government have adapted considerably with the increased devolution of tax powers, but this has been less so in the Scottish parliament.
Within government, notable developments have included the establishment of a tax directorate and the creation of a ministerial portfolio (albeit part time) with responsibility for tax policy. On the whole, these developments have helped to create a consultative and collaborative approach to tax policy making and enabled the tax profession to provide input on a regular basis. The 2017 Scottish government consultation that heralded the changes to the Scottish income tax regime is often held up as a gold standard of engagement.

In the Scottish parliament, we consider that more could be done to improve the way that tax decisions are scrutinised. Expanding the remit of the Finance Committee to also include constitutional matters has, in hindsight, taken some of the focus away from tax matters. It is a source of regret that a 2016 inquiry into Scotland's approach to tax stopped taking evidence in 2017 and did not conclude its work, although there is hope that this will be resurrected early in the new term.

The structures in parliament for introducing and amending tax legislation have highlighted the need for processes that support increased scrutiny and more efficient use of scarce parliamentary time.

Most changes to tax legislation in the Scottish parliament take place using delegated powers or secondary legislation, which limit opportunities for scrutiny. Significant or retrospective changes require bespoke bills, which must battle for a space in the legislative calendar. This has meant, for example, that a commitment to introduce a Bill giving retrospective effect to a change in land and buildings transaction tax legislation (relating to group relief and the use of share pledges) made in 2018 has still to be fulfilled.

CIOT and ICAS have called on ministers and officials to look at a Scottish equivalent of the UK Finance Bill.

A Devolved Taxes Legislation Working Group (see bit.ly/325cSLE) (including CIOT and ICAS representation) was set up to look at ways of improving the process but was put on hold due to the pandemic.

The decisions in 2019 and 2020 to postpone the UK budget added an extra layer of uncertainty to the Scottish budget process, shortening the time available to MSPs to agree tax plans without the full picture of UK tax and spending proposals. Such delays do not just cut across the devolution settlement; they may also make for bad tax policy making. The need to reset relations between the governments and organisations responsible for Scottish tax policy is therefore a consideration in our paper.

Theme 2: Making the case for new taxes

Our experience of the devolved tax system suggests that there is a very strong case for the development of a longer-term, strategic approach to tax policy making in the devolved context.

There have been challenges to the devolution of air departure tax and VAT assignment. Concerns have also been raised about the lack of process and consultation with the last-minute nature of the 2019 budget agreement to introduce new taxes on car parking and tourism. There is a need for a more formalised approach.

This is particularly true when we consider that, in addition to resolving the problems encountered with the introduction of the taxes detailed above, further reform is likely in the coming years as politicians grapple with the economic impact of the pandemic.

The most immediate of these is likely to arise in the form of local government finance reform – council tax and land reform are expected to be prominent topics – but we may also see calls from some political parties for the devolution of further tax powers.

Our paper does not prejudge the outcome of such discussions, but it acknowledges that tax reform is never simple. Having the right processes in place can help to promote healthy debate and encourage the development of tax legislation that supports wider government and societal objectives.

To that effect, we have proposed a more formalised process for introducing or reforming taxes, developed around a process that: evaluates the purpose and locus of the tax; provides opportunity for early consultation; considers how the proposal would interact with existing taxes; offers opportunities for robust parliamentary scrutiny; and ensures that the resulting tax is easy to collect and comply with.

Theme 3: Improving public understanding

Public awareness and understanding of devolved taxation in Scotland is low, as the findings of opinion polls commissioned by CIOT since 2018 continue to show. Our latest survey of 1,098 adults was conducted by the Diffley Partnership in March 2021. It found that:

- 33% said they were unaware that the Scottish parliament had made changes to tax since 2015, such as to income tax and council tax.
- 27% correctly identified that income tax powers are shared between the Scottish and UK parliaments.
- 83% say they need better information about how taxes are decided in Scotland (similar to 86% in 2019 and 84% in 2018).
- 39% know a little or a lot about the ‘Scottish Taxpayer status’.

A lack of public understanding of how the tax system works is a common theme in our work. If people fail to understand how it works, they are more likely to fail to comply with the rules and regulations. Because taxes are now different, and in some cases more complex, in Scotland, there is a greater need for effort to ensure that taxpayers understand what these differences mean.

The issue of tax awareness is not unique to Scotland, but devolution offers an opportunity for the country to take the lead and promote greater awareness of the tax powers it has, how these are used, and the benefits that they help to deliver.

The Scottish government had plans for developing a tax communications strategy prior to the pandemic. It is important that this work resumes and the tax profession stands ready to support these efforts. This is a strategy that will require the support of all the organisations of government concerned with the tax and benefits system. We would also like to see a more prominent role for tax within the school curriculum, with the Office for Tax Simplification's 2019 'Life Events' review (see bit.ly/3a2dKVX) a useful starting point for discussion.

Image

ADVANTAGES OF THE NEW OSS NON-UNION SCHEME

- **Registration:** A UK business only needs to register for VAT electronically in a single member state for all of the eligible services it provides to B2C customers in the EU.
- **Returns:** VAT is declared on a single quarterly OSS return submitted electronically to the tax authority of registration, with individual entries recorded for the VAT collected in each country.
- **Payments:** A single payment is made to the same member state where the return was submitted.
- **Liaison:** The UK business will only liaise with a single tax authority for VAT purposes. There is no requirement to appoint a local tax representative in that country.

CLOTHES SELLER: EU SHIPMENTS OF €150 OR LESS

Betty is based in the UK and sells t-shirts to private individuals in many different EU countries. Some sales are generated from her website and other sales are made via an online marketplace. The shipments are all valued at €150 or less, so will be subject to 'sales VAT' in the EU from 1 July 2021 if she registers for IOSS.

Betty will zero-rate her invoices to the online marketplace for goods sold through its platform – i.e. as a B2B sale (she is referred to as the 'underlying supplier'). For her direct sales, she will register for the IOSS with a single tax authority of her choice, charging 'sales VAT' to her customers.

Note that Betty or her chosen customs agent must still make a customs declaration when the goods arrive in the EU.

Image

SUMMARY OF DOMESTIC INITIATIVES BY ESTONIA, DENMARK AND FRANCE

	Estonia	Denmark	France
Motivation for creating reporting system	• Facilitating platform work • Simplifying tax and social contribution compliance • Business friendly environment • Open government	• Facilitating platform work • Simplifying tax compliance • Not disadvantaging Danish platforms • Developing a technologically sophisticated system that can be used by all member states and types of platforms	• Reducing tax evasion • Facilitating entrepreneurship • Ensuring collection of social contributions
Reporting system launched	2017	2020	?
Automated vs semi-automated	Semi-automated	Automated	?
Mandatory vs voluntary	Voluntary	Mandatory	Voluntary for social contributions and mandatory for tax purposes
Scope	All platforms	Letting platforms	All platforms
Legislative limits on data	Require legislative amendment for mandatory collection	Mandatory collection permitted by law. No need for user consent	New legislation introduced for mandatory collection
Data points collected	• Universal personal identification code • Income amount	• Income year • Taxpayer identity • Letting location • Income amount	?
Stakeholders	• Platform owners • Platform users	• Platform owners • Platform users	?
Initial investment	Low: semi-automated, integrating easily with existing systems	40 million Danish kroner, comparable to other tax authority development projects	?
Running cost	Low, but could increase if take-up among platforms increases, since it requires some manual labour	Expected to be low, but depends on quality of data submitted by platforms	?

? denotes insufficient data to make an accurate statement

Read the manifesto and opinion poll highlights here:
bit.ly/3ehnUmL
bit.ly/3v8bzrJ