



Finance Committee

Devolved taxes

Introduction

Scotland Act 2012 devolved Stamp Duty Land Tax and Landfill Tax to the Scottish Parliament. Stamp Duty was substantially changed to the Land and Buildings Transaction Tax (LBTT) and the Landfill tax regime remained largely unchanged with a Scottish Landfill Tax (SLfT). The new devolved taxes have been collected in Scotland since April 2015.

This briefing considers first the forecasts for devolved taxes and then the first six months of outturn data for devolved tax receipts. The focus is largely on the outturn information for LBTT.

Scottish Government Forecasts

The Scottish Government set out its forecasts for the newly devolved taxes during Parliamentary scrutiny of the 2015-16 Budget. Initial rates and revenue forecasts were presented in the Draft Budget 2015-16, published in October 2014. The LBTT residential tax rates and revenue forecasts were subsequently adjusted during passage of the Budget Bill in January 2015.

The final forecasts for the various elements of LBTT and SLfT are presented in table 1. These are the numbers upon which the Scottish Government has based its budget planning. As such, if these forecasts are less than outturn, the Scottish Government will have a budgetary surplus, and if these forecasts are more than outturn, the Scottish Government will have a budgetary shortfall.

Table 1: Final LBTT and SLfT revenue forecasts for 2015-16

	Forecast revenue (£m)
Land and Buildings Transaction Tax	381
<i>of which</i>	
Residential Transaction	235
Non-residential transactions	146
Scottish Landfill Tax	117
Total	498

OBR forecasts

The Office for Budget Responsibility (OBR) produce revenue forecasts for devolved Scottish taxes at each UK fiscal event (typically in March for the UK Budget, and in November/December for the UK Autumn Statement). The most recent OBR forecast was published in July at the time of the post-election Summer Budget¹. New forecasts will be published at the Spending Review on 25 November 2015, but were not available at the time of writing. The latest OBR forecasts for the two devolved taxes are presented in table 2.

Table 2: OBR forecasts for devolved Scottish taxes (£m)

£m	2015-16	2016-17	2017-18	2018-19	2019-20	2020-21
LBTT	540	616	689	780	874	974
<i>Of which residential</i>	264	324	385	462	541	623
<i>Of which commercial</i>	275	291	304	318	333	351
Landfill tax	94	88	87	90	96	103
Total	634	704	776	870	970	1,077

Source: OBR 2015

The OBR's latest forecasts for 2015-16, will have no practical impact on the Scottish Government's budget, because the Block Grant Adjustment (BGA) for 2015-16 has already been agreed and set.

However, no agreement has yet been reached for the BGA beyond 2015-16. As such, the OBR forecasts beyond 2015-16 could have a material impact on the BGA in subsequent years. We currently do not have Scottish Government forecasts beyond 2015-16, and these will not be available until the Scottish Draft Budget 2016-17 is published. As can be seen in table 2, the OBR's latest LBTT forecasts for 2015-16 are significantly higher (+£159m) than the Scottish Government, but the OBR's SLfT forecasts are lower (-£23m) than the Scottish Government.

If, as seems likely, the OBR's combined forecasts for devolved taxes are higher than the Scottish Government forecasts in 2016-17, then there is potential for a BGA that is higher than the Scottish Government's forecast tax receipts (depending on how agreement over a suitable BGA is reached).

Block Grant Adjustment

The combined devolved taxes BGA finally agreed with the UK Government in advance of the Scottish budget being set for 2015-16 was £494m – the mid-point of the Scottish Government and OBR forecasts. This was a one-year

¹ Summer budgets have taken place after the last two UK elections, in 2010 and 2015.

BGA agreement. This meant that assuming receipts come in as forecast by the Scottish Government, there would be a small £4m surplus in tax receipts over the final BGA. In his letter to the Finance Committee of 22 January 2015, the Cabinet Secretary stated:

“I have assessed revenue neutrality for 2015-16 in terms of the headline one-year BGA agreed with the UK Government of £494 million, which as you know represents the mid-point of the Scottish Government and OBR forecasts of the aggregate tax revenues foregone by the UK Government. My 2015-16 tax revenue forecasts for non-residential LBTT and Scottish Landfill Tax remain unchanged from the Draft Budget - at £146 million and £117 million respectively. This leaves a remaining balance of £231 million to be raised from residential LBTT in 2015-16, before forestalling effects are taken into account. I considered it prudent to build some modest headroom into the pre-forestalling revenue to be generated by residential LBTT in order help manage the risk that the forestalling adjustment which the UK Government is prepared to agree to the BGA falls short of my assessment of the likely revenue losses to the Scottish Budget, as scrutinised by the Scottish Fiscal Commission. Should there be any remaining flexibility once forestalling effects have been agreed and calculated, I would intend to use this to make the first payment into the cash reserve at the end of 2015-16.”

John Swinney [letter to the finance Committee, 22 January 2015](#).

Forestalling

The no detriment principle agreed in the Smith Commission states that neither the Scottish or UK budgets should be worse off at the point of devolution. In light of that principle, the Scottish and UK governments agreed that there will be some requirement for a compensatory amount to be subsequently added to the Scottish budget as a consequence of forestalling of transactions arising from the UK Autumn Statement 2014 changes to the UK Stamp Duty regime. The changes made in that UK fiscal event provided an incentive for certain transactions in Scotland to be brought forward into financial year 2014-15 to reduce tax burdens, thus impacting positively on 2014-15 SDLT receipts and negatively on 2015-16 LBTT receipts.

The Deputy First Minister wrote to the Committee on 22 January confirming the new bands and rates and the revised forecast for residential LBTT receipts. He also stated that as “this is the first year of LBTT and there are significant differences in the tax charge between LBTT and the UK tax which it replaces, I also intend to make an adjustment to this forecast to reflect potential revenue losses to Scotland as a result of forestalling effects.”² He

²http://www.scottish.parliament.uk/S4_FinanceCommittee/General%20Documents/Cabinet_Secretary_for_Finance_Constitution_and_Economy_to_the_Convener_dated_22_January_2015.pdf

advised the Committee that the SFC “has begun its work to scrutinise the approach which we are taking to estimate the value of these forestalling effects, and I will provide a further update to the Committee when that work has concluded.”³

The SFC wrote to the Scottish Government on 21 January with its assessment of the revised forecasts. They stated that they were content that the revised forecasts were based on a consistent application of the forecasting methodology which they had previously viewed as reasonable. They added that:

“The calculation of the forestalling effect is both desirable and relatively straightforward in itself. However, it depends upon identifying the elasticity of the transactions with respect to anticipated changes in the tax schedules, which is less straightforward.

We have engaged with your officials, reviewed early and later versions of their analysis, and asked them to provide further and sufficient evidence on the value of this elasticity in order to enable the SFC to form a view of the reasonableness of that calculation.

Our understanding is that they continue to refine this work. We appreciate that it is complex and requires judgement. We will review any further evidence they can provide in support of the assumptions underpinning their forestalling calculation as and when it becomes available.”⁴

In its response to the Committee’s report on Draft Budget 2015-16 the SFC stated that it had “responded in brief to the forecasters’ initial work on forestalling” and “requested that further evidence be provided in relation to the assumptions underpinning the calculation.” They advised that when “the next iteration is ready, we will review it and make a further judgement.”⁵ None of this work has been made public and the SFC has not reported on its work on forestalling.

The Committee wrote to the SFC on 27 August 2015 inviting the SFC to provide a commentary on the first 6 months of outturn figures for the devolved taxes relative to the Scottish Government forecasts including the impact of forestalling. The Committee also expressed concern about the lack of transparency in relation to the work which the SFC has been carrying out with the Scottish Government on forestalling. The Deputy First Minister told the Committee on 2 September that work on forestalling is still under way and we “will obviously have much clearer data from the end of the previous financial

³http://www.scottish.parliament.uk/S4_FinanceCommittee/General%20Documents/Cabinet_Secretary_for_Finance_Constitution_and_Economy_to_the_Convener_dated_22_January_2015.pdf

⁴http://www.fiscal.scot/media/media_388463_en.pdf

⁵http://www.scottish.parliament.uk/S4_FinanceCommittee/General%20Documents/Scottish_Fiscal_Commission_response.pdf

year and the start of this financial year.”⁶ Discussions are also taking place around forestalling as part of the fiscal framework negotiations.

The SFC wrote to the Committee on 19 November 2015 with its commentary on the outturn figures for the devolved taxes. This was described as a “concise summary of the work we have done” – it is not clear whether this work is to be published. Given the points summarised below, it might be helpful for the Committee to receive more information on the workings behind some of the numbers in the letter. Generally speaking, it is not possible to replicate the figures shown in the SFC letter.

For example:

- The SFC refers to a forecast in January 2015 for forestalling of £12m to £37m. The SFC has not provided any commentary on how these figures were arrived at. It is unclear where these figures come from or how they were produced and they do not appear to have been previously published.
- Likewise it is ambiguous how the £215.5m (min forestalling) and £247.4m (max forestalling) figures are arrived at. Following the methodology in the commentary, the six-month outturn, £96.2m plus the minimum forestalling of £12m gives a “corrected” outturn of £108.2m. This is then taken to be 53% of the annual projected revenue giving a forecast for the year of £204.2m rather than the £215.5m from the SFC. Similarly for maximum forestalling the forecast outturn is £251.3m rather than £247.4m. The SFC calculation appears to involve some factor not mentioned in the letter.
- The paper also refers to preliminary analysis of an actual shortfall in revenues of £30m over the period of April to September 2015. Again, it is not clear how this figure has been arrived at and the SFC has provided no commentary.

The Committee will be aware that one of the key OECD principles for independent fiscal institutions is transparency:

“Given that promoting transparency in public finances is a key goal of IFIs, they have a special duty to act as transparently as possible. Full transparency in their work and operations provides the greatest protection of IFI independence and allows them to build credibility with the public.”⁷

The Committee may wish to consider whether the provision of “a concise summary of our work” is consistent with this principle.

OBR forestalling estimate

⁶ Finance Committee, 2 September 2015, OR Col. 30

⁷<http://acts.oecd.org/Instruments/ShowInstrumentView.aspx?InstrumentID=301&InstrumentPID=316&Lang=en&Book=False>

The OBR's July Devolved Taxes forecasts estimates the impact of forestalling at £20m. It states:

“Our forecast takes into account the bringing forward of some higher-priced transactions in order to avoid the higher rates in 2015-16 and some delayed transactions at the lower end. These behavioural responses reduce the LBTT forecast by £20 million in 2015-16 with the effect concentrated in the earlier months of the year.

Outturn data

Revenue Scotland publish monthly aggregated figures for LBTT in the third week of the month. SLfT figures are also published on the Revenue Scotland website on an aggregated basis quarterly in arrears, in the second month of the following quarter. The latest available LBTT outturn figures are presented in tables 3 and 4.

As can be seen by tables 3 and 4, compliance with LBTT in both the residential and commercial sector is high. For example, in the residential sector in the first 6-months of operation £96.2m has been collected from £96.4m due (99.8%).

Forecasts are based on an accruals basis (how much money would be expected to be raised from a given number of transactions), while receipts are recorded on a cash basis (actual receipts in a given time period). As taxpayers are allowed 30 days to complete a return, expected receipts might differ from actual receipts at a given point in time. The difference will only arise where payments for transactions in a given month end up taking place in a later month. Eleanor Emberson, in evidence to Finance Committee on 18 November, referred to this issue, but did not indicate the size of any difference. However, it is likely that this will not be a significant issue as most residential LBTT tax returns are completed on the day of purchase as part of the transaction.

Table 3: LBTT Residential outturn figures

	Residential Returns Received ¹	Total Residential Tax Liabilities ²	Total Residential Tax Received By Month To Date ³	Average Revenue per transaction
Apr-2015	6,880	£7,000,000	£7,000,000	£1,017
May-2015	7,810	£11,400,000	£11,400,000	£1,460
Jun-2015	10,030	£18,500,000	£18,500,000	£1,844
Jul-2015	9,940	£19,400,000	£19,400,000	£1,952
Aug-2015	9,540	£21,400,000	£21,400,000	£2,243
Sep-2015	9,040	£18,700,000	£18,500,000	£2,046
Total	53,240	£96,400,000	£96,200,000	£1,807

All figures are provisional

- 1: All valid residential returns received during the stated month.
- 2: Total self-reported tax due on residential returns received during the stated month.
- 3: Total payments received by date of data extraction relating to returns received during the stated month.

Key points to note from the LBTT residential outturn figures are as follows:

- In the 6-months to September 2015, 41% of the forecast residential revenues for the year have been collected.
- The 6-months for which outturn data has been collected are the spring and summer months, typically the strongest months for house sales
- Revenue Scotland states on its website that “Residential property transactions follow a fairly regular seasonal pattern, whereby there is higher number of sales in the spring and summer and relatively few in the winter, particularly January and February. Consequently we expect notifications and revenue from LBTT to follow a similar pattern.”
- Adding the OBR’s £20m estimated impact of forestalling to the collected revenue figure, would take the 6-month collected receipt figure up to 49% of forecast revenues
- Deducting the OBR’s £20m estimated impact of forestalling from the Scottish Government’s forecast revenues, would take the 6-month collected receipt figure to 45% of forecast revenues.
- With tax on transactions above £330,000 increasing in April 2015 compared to the previous UK Stamp Duty system, there appears to have been significant forestalling effects in the opening two months of the financial year.
- Rettie and Co (2015) state that the number of higher value properties coming to the market early in the year increased dramatically, then retreated after 1 April. In April, the average revenue per transaction was £1,017. The average revenue per transaction increased in May 2015 to £1,460 and continued rising in each month until August.
- After a slow first two months (April and May), transaction numbers and revenues have increased, averaging £19,450,000 per month in the June to September period. Were that average monthly figure to be replicated across a 12 month period, forecasts would be close to predicted at £233m.
- However, as mentioned above, property sales tend to be highest in spring, summer and autumn (with October typically being a strong month) before the market cools in the run up to Christmas.
- Average revenues per transaction peaked in August at £2,243.

Table 4: LBTT non-residential outturn figures

	Non-Residential Returns Received ¹	Total Non-Residential Tax Liabilities ²	Total Non-Residential Tax Received By Month To Date ³	Average revenue per transaction
Apr-2015	610	£10,900,000	£10,900,000	£17,869
May-2015	810	£12,600,000	£12,600,000	£15,556
Jun-2015	950	£13,800,000	£13,800,000	£14,526
Jul-2015	970	£18,100,000	£18,100,000	£18,660
Aug-2015	900	£15,500,000	£15,500,000	£17,222
Sep-2015	970	£15,800,000	£15,700,000	£16,186
Total	5210	£86,700,000	£86,600,000	£16,622

All figures are provisional.

1: All valid non-residential returns received during the stated month.

2: Total self-reported tax due on non-residential returns received during the stated month.

3: Total payments received by date of data extraction relating to returns received during the stated month.

Key points to note from the LBTT non-residential data is as follows:

- In the 6-months to September 2015, 59% of forecast revenues for the year have been collected.
- The Scottish Property Federation (2015) state that behavioural responses have been much less of an issue in the commercial sector compared with the residential sector “due to a closer alignment to the previous tax regime as well as a rising market”.
- As such prospects for meeting the LBTT non-residential forecast revenues in 2015-16 look much higher.
- Average revenue per transaction has been fairly consistent, averaging £16,622, peaking at £18,660 per transaction in July.

Scottish Landfill tax outturn data

At the time of writing [only the first quarter of SLfT receipts had been published](#), covering the period April to June 2015. A total of £37.4m had been received to date from 34 returns. This amounts to 32% of forecast annual revenues (£117m) after one quarter of the financial year, suggesting that the Scottish Government’s revenue forecasts are likely to be reached.

Sources

Office for Budget Responsibility (2015) *Economic and Fiscal Outlook: Devolved Tax Forecasts*. Available at: <http://cdn.budgetresponsibility.independent.gov.uk/Devolved-taxes-forecast-July-2015.pdf>

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Ross Burnside
Financial Scrutiny Unit (SPICe)
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The Scottish Parliament, Edinburgh, EH99 1SP www.scottish.parliament.uk