



The Scottish Parliament
Pàrlamaid na h-Alba

Official Report

FINANCE COMMITTEE

Wednesday 25 February 2015

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FINANCE COMMITTEE

7th Meeting 2015, Session 4

CONVENER

*Kenneth Gibson (Cunninghame North) (SNP)

DEPUTY CONVENER

*John Mason (Glasgow Shettleston) (SNP)

COMMITTEE MEMBERS

*Richard Baker (North East Scotland) (Lab)

*Gavin Brown (Lothian) (Con)

*Malcolm Chisholm (Edinburgh Northern and Leith) (Lab)

*Mark McDonald (Aberdeen Donside) (SNP)

*Jean Urquhart (Highlands and Islands) (Ind)

*attended

THE FOLLOWING ALSO PARTICIPATED:

Isobel d'Inverno (Law Society of Scotland)

John Hamilton (Scottish Property Federation)

Philip Hogg (Homes for Scotland)

David Stewart (Scottish Federation of Housing Associations)

John Swinney (Deputy First Minister and Cabinet Secretary for Finance, Constitution and Economy)

CLERK TO THE COMMITTEE

James Johnston

LOCATION

The Adam Smith Room (CR5)

Scottish Parliament

Finance Committee

Wednesday 25 February 2015

[The Convener opened the meeting in private at 09:30]

09:54

Meeting continued in public.

Decision on Taking Business in Private

The Convener (Kenneth Gibson): Good morning and welcome to the seventh meeting in 2015 of the Finance Committee of the Scottish Parliament. I remind everyone present to turn off any mobile phones, tablets or other electronic devices.

We took item 1 before the public part of the meeting. Our second item of business is to decide whether to take items 13 and 14 in private. Do members agree?

Members *indicated agreement.*

Subordinate Legislation

Land and Buildings Transaction Tax (Sub-sale Development Relief and Multiple Dwellings Relief) (Scotland) Order 2015 [Draft]

09:55

The Convener: Our next item of business is to take evidence on a draft order from Isobel d'Inverno of the Law Society of Scotland and David Stewart of the Scottish Federation of Housing Associations. I welcome our witnesses to the meeting.

Members have copies of all the written evidence that the committee has received, so we will go straight to questions from the committee. You have both been at the committee before, so you will know that I usually start off with some questions before opening out the session to colleagues round the table.

My first question is for Isobel d'Inverno. We received a paper from you in which you talk about significant developments and say that you support the revised definition of that. The paper also describes how, if a significant development does not take place within five years, the relief will be withdrawn or partially withdrawn and the tax will become payable. It continues:

"In these cases we would suggest that it should be possible for an extension of the five year period to be made available."

I am wondering how long the extension would be. Would it go on for years and years? If there is going to be a sacrifice of tax income at the start of the period—the Chartered Institute of Taxation suggests that it would be good if we charged straight off—we could be talking about who knows how many years. Can you put a bit more meat on the bones of your suggestion?

Isobel d'Inverno (Law Society of Scotland): It would be unfortunate if, because of delays in planning or whatever, the development was not able to start until, say, year 6, and the sub-sale development relief was all lost. The period would just need to be reasonable. A reasonable period might need to be decided at the discretion of Revenue Scotland, having regard to the circumstances and what has actually been going on, rather than setting a particular period in stone. That might need to be discussed with others who are involved in the industry to get some idea about it.

I take the point that the extension could not go on for 15 or 20 years, although some

developments go on for that long because they have to wait for planning and other things.

The Convener: What if someone decides to put in for planning four and a half years into the five-year period, for example? That is hardly the fault of the local authority, but it still has to go through its processes.

Isobel d'Inverno: It would be unlikely that someone would delay deliberately. There could be some saving in the provision that would say that, if the end purchaser deliberately caused a delay, there would be no extension. Also, if the decision is at Revenue Scotland's discretion, it could take that into account.

The Convener: You suggest what would happen if there was a delay of up to five years, but that might have an impact on revenue coming in to the Scottish Government. Do you have any idea how much that might be if a development was to be late? One would assume that it would be several millions of pounds.

Isobel d'Inverno: It is very difficult to say. Many of these transactions are structured along the lines that the development will start as soon as possible. That is in everybody's best interests. The developer who is involved in the development is—obviously—keen to get on with it and the end purchaser does not want to be hanging around for ages, either. I do not think that anybody is out to delay things.

Quite how many projects fall into what sort of timescales, I really cannot say. Other organisations such as the Scottish Property Federation might be able to give some suggestions about how the figures might fall out.

The Convener: The CIOT has said:

"The amended relief mechanism poses a higher risk to the public revenue".

Do you accept that the overall amount that will come in to the Scottish Government will not increase but might decline for all sorts of reasons, such as companies going bust, if the money is not received at the beginning of the five-year period?

Isobel d'Inverno: It is not my experience from advising on projects that a huge number of developers or end purchasers go bust. That does not happen in most of the transactions that we are involved in, so I do not think that there is a huge risk of the relief being allowed up front and then the development not happening. Revenue Scotland has other mechanisms if people were to try to abuse the relief, such as the general anti-avoidance rule. If people set up fictitious arrangements in order to claim the relief, the GAAR would be one way of attacking that. I do not think that the relief presents a huge risk of loss of revenue.

10:00

The Convener: Okay. You also state in your written submission:

"Where development has started but not been completed the tax chargeable is an 'appropriate proportion' of the tax which would have been payable without the relief."

However, if any of us round the table bought a house that cost more than £145,000, we would have to stump up land and buildings transaction tax straight away. Why should only a proportion of the tax be paid? Once work has started on a development and the developer has the money in place to complete it, why should the tax not just be paid?

Isobel d'Inverno: It comes down to what would be fair and reasonable in the circumstances. I think that the original wording of the regulation said that, if a development had not been completely finished by year 5, there would be no relief. That does not seem proportionate. If a development was all but complete, people would think that they ought to be able to get a proportion of the relief. It is a question of proportionality. It is obviously different from the situation of buying a completed house and having to pay LBTT.

Having said that, it is not impossible for the construction of houses to be done in a different way whereby people would not end up paying LBTT on the whole of the construction costs. That is not uncommon. However, the idea of the relief is to give developers who are setting up projects the same kind of cash-flow advantage that they would get in the rest of the United Kingdom so as to ensure that Scotland is not at a competitive disadvantage with the rest of the UK in forward funding projects.

The Convener: I just wonder how big an issue that really is.

The Chartered Institute of Taxation's written submission states that

"Provision could be made to initiate a claw back"

or

"provide security to cover"

that. When a developer plans to build on a site, they often provide a bond to the local authority to pay for street lighting, roads and so on, so that if the company goes bust or whatever, that is covered. What about a clawback, or a kind of indemnity to provide security? Is that something that you think should be considered?

Isobel d'Inverno: No. I do not think that that will be necessary. Situations where a development does not happen because the end purchaser has gone bust are not frequent and the commercial arrangements are often such that everything is tied up for the development to go ahead.

It is worth noting that the Chartered Institute of Taxation is the only body that responded to the consultation that thought that the original version of the relief was appropriate. Everybody else who looked at it took the view that, if developers had to pay the tax up front and could reclaim it only when the development was complete, they would say, "This is too uncertain. We'll have to assume that we're not going to get this money back, therefore we'll ignore it in pricing deals." It would have been a fairly useless relief.

I think that the general consensus now is that, if the developer can claim the relief up front, they can be reasonably certain that it will be available, which means that they will be able to price it into deals.

The Convener: Surely the public purse has to be protected. I live on a housing development site for which the local authority did not ask for a bond. The developer did go bust and the council had to find £300,000 to put in roads, street lighting and so on. Surely, if we are going to protect the public purse, some kind of bond or whatever should be in place. Otherwise, the taxpayer will ultimately lose out.

Isobel d'Inverno: Arranging that sort of bond would introduce unnecessary complications into deals. There is always the possibility of keeping the provision under review and, if it turns out that the public purse has been threatened by projects going belly up, it will be open to the Scottish Government and the Scottish Parliament to remove the relief or amend it in some way. It is not set in stone for ever. It might be appropriate for the Finance Committee to keep it under review and to ask for detailed information on how many times the relief has been granted, what is going on in the projects and so on.

The Convener: Thank you, Isobel.

David, you have a big focus on mid-tenure homes and you talk about

"Ensuring no tax is paid on properties costing £135,000 or less",

although I think that that should be £145,000. What do you mean in cost terms by "mid-tenure homes"? I have been looking at your submission and I cannot see any detail on what you mean by that, in financial terms.

David Stewart (Scottish Federation of Housing Associations): I am sorry. I can certainly provide details of the rents that our members charge, but I do not have any figures on that with me at the moment.

Mid-tenure homes are where a housing association or a council provides homes and the rent is set in the middle band between what a socially rented home would cost and what the

private rental market would charge. They are aimed at people who are working but are on relatively low incomes, who would struggle to access a home of their own through the private rented market or a mortgage but who are also unlikely to be housed in social housing because of the high levels of waiting lists. Mid-tenure homes look to meet a gap in the market.

Since the financial crash, it has become more difficult for first-time buyers to obtain mortgages. We would argue that mid-tenure homes are increasingly important to help to meet housing needs and to allow young people to leave their parents' homes or move to a different area in order to take up employment.

The Convener: Are you talking about homes that cost more than £145,000 for each unit?

David Stewart: In some cases, homes might cost that to build, but I am probably talking mainly about developments—for example, buying land to build 30 or 40 homes for mid-market rent. Another situation is where, as happened on a number of occasions in Edinburgh following the financial crisis, a housing association subsidiary buys homes from a builder that has decided that it cannot sell them on the market.

In our written submission, I talk about the fact that housing associations can then get caught up in paying reasonable sums of tax. Given that they are providing a service that the market does not provide and they tend to need grants from the Scottish Government or to acquire land at nil value from the local authority to make the scheme stack up, we argue that it does not make sense for the Government then to draw a tax on that.

The Convener: Are you saying that, if 50 houses were to be built on a site in Edinburgh and it was going to cost something like £8 million, they should not be subject to LBTT at all, even after five years, because of the type of people for whom you are providing housing?

David Stewart: Yes—that is the argument that we are making. Although it is not a tiny part of the market, it is quite small. The case that I would make for it being excluded from the tax is, first, that it would not have a significant impact on the overall tax take—I note that the Scottish Government is keen to ensure that it draws in the same amount of tax from LBTT that it would have drawn in under stamp duty—and secondly that we are talking about housing people whose needs are not met by the market. In effect, it is something that needs to be subsidised, albeit to a lesser extent than social rent.

The Convener: To go back to the example that I gave earlier, if there are 50 houses on an £8 million site, the average cost per unit would be £160,000. We could argue that that is above the

threshold that many people would pay. A lot of people buy houses for a lot less than that. My mum's house is on sale for £58,000, and it is beautiful. There is a lot of low-cost private housing. My assistant bought an absolutely lovely flat for £43,000. You are talking about a significant scale of development. Where would this apply? Would it impact across Scotland or is it an issue only in specific areas such as Edinburgh and Aberdeen?

David Stewart: I think that it would impact across Scotland. Previously, the view was always that housing for mid-market rent really only worked in pressured areas where housing for sale was expensive and there was a lack of social rented housing. Traditionally, most mid-market rent was in Edinburgh, with pockets in places such as Aberdeen and Glasgow. However, I spoke to a couple of housing associations recently that have developed units for mid-market rent—Loretto Housing Association, which has provided units in Springburn, and Shettleston Housing Association—and both said that, because it has become difficult for many people to access housing for sale, there is now a market for mid-market rent in such areas. The people who are being housed are mainly, I suppose, adults who were staying at home with their families and who were looking to move into a house.

The issue is probably not so much the tax on the overall cost of the property but the fact that the association would have to pay a tax on the cumulative cost of land for, say, 20 or 30 units and on the cumulative cost of development. That is probably not what the tax aims to do. We are talking about people who might, 10 years ago, have bought a relatively low-value property in the Scottish market but who now struggle to access a mortgage.

The Convener: Do you have any idea how much the tax will cost housing associations each year if there is no change to the current position?

David Stewart: I do not have that global figure—I would need to research it—but I do not think that it would be an enormous amount. However, it could be significant for individual developments. Given that, in the Scottish Government's refresh of its housing policy, it sees mid-market rent as a potentially significant element and it is building that into its joint delivery plan, anything that can be done to make it easier for association subsidiaries to provide mid-market rent to help to meet the need in the housing market and deliver the Scottish Government's aims would be helpful.

The Convener: You are saying that there is no real contradiction, as it is not a significant amount for the Scottish Government but it could be for individual associations.

David Stewart: Yes, and it could make it more difficult for schemes to stack up. As I said, for the schemes to work, they need either grants or land to be transferred to the subsidiary at below-market or nil value. In a way, a tax would just be moving public money about.

The Convener: Yes. You are saying that, in effect, a larger grant would be required if the tax has to be paid.

David Stewart: Yes.

The Convener: I now open out the session to colleagues.

John Mason (Glasgow Shettleston) (SNP): Ms d'Inverno, in answering the convener's questions, used the term "competitive disadvantage", which I assume is in relation to building in Scotland compared to building down south. How much of an issue is that? If somebody wants to live in a place, a thousand pounds or two here or there will not make a difference. People still want to be in London, despite the fact that there is a huge competitive disadvantage. Does that amount of money really make a difference?

10:15

Isobel d'Inverno: In respect of the sorts of transactions that we are talking about, many developers operate throughout the UK. They might have a choice between doing a project in Newcastle and doing one in Edinburgh or Glasgow. If there is an extra tax cost for the developer in putting the project together, given the time that the projects take and the fact that the margins are not incredibly high, if the developer does not get the relief, it might decide to do the project in Newcastle, which would mean that it would not happen in Scotland. That is one of the reasons why most people were keen to have the development sub-sale relief available in Scotland.

John Mason: Clearly, developers want to pay no tax and want everything to be as cheap as possible. However, by your logic, no one would be developing in London, but I thought that there were developments going ahead in London.

Isobel d'Inverno: Throughout the UK at the moment, there is sub-sale relief for such transactions, because stamp duty land tax has sub-sale relief across the board for all types of sub-sales. Obviously, in LBTT that does not exist, so we are looking at a targeted relief for transactions involving development. Once we get past 1 April, if the relief is not introduced, a developer will see that it will cost more to do a project in Scotland and that the margin would be lower than it would be if it were done in Newcastle. That could well lead to the developer deciding to do the project in Newcastle.

John Mason: However, in the scheme of things, is that not quite a small factor? I presume that the first issue is demand—developers want to build where there is demand, which is why people keep building in London despite the fact that the costs are absolutely huge. Would it be the case that demand is the most important thing and that the issue of tax is pretty minimal?

Isobel d’Inverno: That is not necessarily the case—not in the way that the costings for such projects work. The imposition of a tax charge in Scotland that does not exist in England could mean that a project in Scotland would not be viable whereas a project in England would be. It is a simple sum: the developer adds in a tax charge that is not there in the other location, looks at the numbers and says, “Well, I’ll go for the one in Newcastle rather than the one in Scotland.” That would be a shame, which is why we are extremely encouraged by the fact that the Scottish Government proposes to introduce the sub-sale development relief to address that possibility.

John Mason: I still feel that you have not answered my question about the relative importance of the tax, but I cannot force you to do that if you do not want to.

The other subject concerns the term “significant development”. As a layperson, that seems vague to me, but your response suggests that you are quite comfortable with that.

Isobel d’Inverno: The problem with the previous iteration of the proposal was that it was too rigid. It said that planning permission was required, whereas, in fact, a lot of development activities do not need planning permission. It needs to be one of those tests that are a bit like the elephant test—you can recognise one when you see it, but it is quite hard to describe it. That is a bit unsatisfactory because it is a bit subjective, but most of the time it will be possible to see whether there is significant development.

John Mason: Will we end up with a lot of wrangles in which developers say that something is significant but Revenue Scotland says that it is not?

Isobel d’Inverno: I would not have thought so; I hope that there will be detailed guidance. Time will tell, once we have some experience of what view Revenue Scotland will take of these things. In many projects, it will be obvious that there is going to be significant development; there will be an enormous development agreement that has been negotiated and a plan to build an office building, a hotel or whatever.

John Mason: Following on from what the convener was saying, at a previous meeting it was suggested to the committee that mid-market rent is often about 80 per cent of private rent—I do not

know whether that is a figure that you are comfortable with. It strikes me that, although it is called mid-market rent, it is really just a slightly cheaper version of private rent. It can be compared with social rent, which is heavily subsidised. Do you see it in that way?

David Stewart: I am not sure that I entirely agree with that; the rent differences can be significant. I think that 80 per cent would be the maximum that might be charged as a proportion of private rent, but it really can make a big difference.

To go back to the examples in Glasgow that I talked about, we are talking about providing quality housing that people have security around. That housing is well managed, and people would not be able to access it otherwise. Therefore, it would be unfair to characterise mid-market rent as being virtually the same as private rent. It has a distinctly different market. As I said in my answers to the convener, it cannot be achieved without either land at nil value or the provision of subsidy.

John Mason: I presume that, in a sense, it does not really matter whether you get away with paying a lot less tax or get a bit of a grant or a subsidy. I take it that you will look at the net figures.

David Stewart: I suppose that that is true, but I also argue that there will always be pressures on the level of grants that are available to subsidise new-build council housing, new-build affordable rent by associations and mid-market rents, so anything that can be done to keep the costs down and make the grants go further would be the best approach. However, I take your point that, if the scheme goes ahead and gets the grant—

John Mason: There is a fear for the committee, which we have faced with the question whether we should have relief for eco-friendly houses, or whatever they were called in the past. As soon as we bring in a relief, somebody out there will start to try to use it as a loophole; they will pretend that they are a housing association or something else. However, we can target a grant or a subsidy—we can say that only SFHA members or whoever will get it. I would see that approach as being more effective, but maybe it does matter too much from your point of view.

David Stewart: I take your point, but I cannot really comment on it. I am not an expert on taxation or the dangers of creating loopholes, but I hope that it would be possible to frame a relief in such a way that it clearly specified what rent could be charged in order to be eligible for it and who could provide the housing. Therefore, I would have thought that that situation could be avoided. However, I take your point. The committee and the Government must absolutely be wary of introducing any reliefs that could be used as loopholes.

John Mason: Thank you.

Paragraph 5 of your paper talks about back-to-back land sales. I think that that is where we are with sub-sale relief. You say:

“It is our understanding”—

it is mine, too—

“that while the SSI has introduced a new schedule which provides that a developer purchasing land ... will get relief from LBTT, the purchasing association or subsidiary would still have to pay LBTT”.

I think that, instead of two people paying tax, only one will.

David Stewart: Yes.

John Mason: However, you are arguing that nobody should pay it.

David Stewart: I agree that the change is an improvement on the previous situation, but my argument is consistent with my other argument. Mid-market rent is a provision that needs subsidy that would not be provided for the market, so I am arguing that it should have relief from tax. However, I fully take your point that the change is an improvement on the previous position. That is the case from our members' point of view.

John Mason: In the annex on the last page of your submission, you give an example that relates to multiple dwellings relief. If I am reading the figures correctly, we are talking about a purchase of £4 million, and the extra tax is £2,562. By my calculation, that is 0.064 per cent. That is not significant, is it?

David Stewart: No. It is similar to the previous question. The situation now is a big improvement, from the point of view of mid-market rent, on the situation that existed when I came to speak to the committee before Christmas. To go back to my previous answer, I suppose that what I am arguing is that, given that it is a form of housing development that needs subsidy, mid-market rent housing should be exempt from tax. However, I take your point that the increase is not significant.

Richard Baker (North East Scotland) (Lab): My questions are for Mr Stewart, on relief on multiple property acquisitions. The convener mentioned buyers of properties costing under £160,000. In Aberdeen, in my region of North East Scotland, that would be significantly below mid-market, so for us it is a significant issue. Can you clarify, beyond any argument over an exemption, whether the current proposals would be financially detrimental compared with stamp duty in terms of developing such properties?

David Stewart: Yes, they are detrimental. They are not so significantly detrimental as the proposals were prior to the introduction of the Scottish statutory instrument that we are

discussing, but they would still be marginally detrimental. For areas such as Aberdeen or Edinburgh, anything that can be done to reduce costs and allow mid-market provision would be a good thing.

Richard Baker: In places like Aberdeen, a saving of 20 or 30 per cent is 20 or 30 per cent of a very high rent and can make a huge difference. Is it fair to say that you do not think that an exemption would place a significant financial burden on the Scottish Government, but that it could be of real benefit in pursuing more of those mid-market schemes?

David Stewart: Yes—very much so. On the scale of mid-market rent, the most significant provider in Scotland is, as far as I am aware, Dunedin Canmore Housing Association, which has provided several hundred such properties over about 10 years. By comparison with the numbers of homes that have been developed for sale, or even for social rent, annually by associations and councils, we are not talking about a huge number. However, to answer the second part of your question, it could make a difference by making a scheme affordable and workable in a place such as Aberdeen or Edinburgh.

Richard Baker: John Mason mentioned potential misuse of an exemption. I presume that it is, given the regulation of housing associations, quite hard to pretend to be a housing association.

David Stewart: Something could be written in to say that the body must, for example, be a subsidiary of a charitable association. The sector is quite strictly regulated by the Scottish Housing Regulator and by the Office of the Scottish Charity Regulator, so I hope that it would be possible to draft legislation that would make it impossible for that to happen.

Richard Baker: You mentioned issues regarding the development of housing association homes by their non-charitable subsidiaries. How does that work in practice? How many housing associations have such subsidiaries?

David Stewart: Quite a few do, and the number is increasing. Development of homes by non-charitable subsidiaries happens because housing associations are largely charities and have strict rules and are strictly regulated, so it is generally not possible for them to provide homes for sale for shared ownership or homes for mid-market rent, because that would not meet their charitable objective of housing those who are in greatest housing need. As far as mid-market rent goes, the developer has to be the non-charitable subsidiary of an association that provides and manages such properties, and that is where they get caught up in the tax.

Richard Baker: In dialogue and negotiation with the Scottish Government, why has it not been more receptive to the proposal for an exemption, or at least to ensuring that the proposal is not financially detrimental?

10:30

David Stewart: I cannot be certain, but associations and subsidiaries being quite negatively impacted by the initial proposals would be an unintended consequence of the fact that the tax aims to move the burden of taxation from higher-value properties to lower-value properties. Because associations and subsidiaries might be developing groups of properties or buying significant pieces of land, there might be a detrimental impact. The Scottish Government has responded by introducing the sub-sale relief, which means that the detriment would not be so great, but it is a service that meets a need that is not met by the market, so it should be exempt.

The Convener: You said that the Scottish Government is trying to shift the burden from higher to lower-priced properties; did you mean to say it the other way around?

David Stewart: I am sorry. Yes—that was a slip of the tongue. I meant quite the opposite to what I said.

Richard Baker: Thank you.

Malcolm Chisholm (Edinburgh Northern and Leith) (Lab): I will continue on the same theme. Edinburgh has similar housing problems to Aberdeen, perhaps; there is not a lot of social rented housing and people cannot afford private rents or to buy. Mid-market rent is therefore very important in Edinburgh, so I was initially attracted to your proposal, although we will obviously have to interrogate it a bit. Many people have done that so there might not be much for us to do, to be honest.

The comparison with stamp duty land tax did not come to a large differential but I presume that a total exemption would mean a much bigger benefit.

David Stewart: Yes—absolutely.

Malcolm Chisholm: If we do not get that, would the supply of mid-market houses for rent be affected or could it mean that the mid-market rents would be slightly higher than they would otherwise be? What do you think the effect would be? In other words what would the effect of an exemption be? Will it affect supply or rents or both?

David Stewart: It will probably affect supply. Mid-market rent can really work only within a parameter and it cannot really be raised above

that otherwise it will not meet the distinct need. It will almost become a slightly cheaper private rent.

There would be a benefit in that it might enable certain schemes to go ahead that might not otherwise have happened and that would increase supply. Alternatively—I do not think that this would be a huge impact—it would mean that the amount of grant that is available to fund mid-market rent or socially rented housing would go slightly further.

Malcolm Chisholm: We will certainly raise those points with the cabinet secretary in a little while. Stated policy is, particularly in places such as Edinburgh and Aberdeen, to increase the number of homes for mid-market rent, so we will put it to him that the supply might be affected as an unintended consequence. He might have some response to that that we cannot anticipate, but I do not think that there would be a great deal of scope for loopholes. We will wait to see what the cabinet secretary says. Thank you for drawing it to our attention.

David Stewart: Thank you.

The Convener: In case the witnesses were wondering, Gavin Brown has left because has been taken unwell.

Mark McDonald (Aberdeen Donside) (SNP): As Malcolm Chisholm has said, we have given the issue quite a good go but there is something that I would like you to clarify about your proposals. Have you calculated how much revenue would not be realised as a consequence of this decision? LBTT was introduced as a revenue-neutral scheme, and any exemptions or otherwise that might impact on income would affect that neutrality. Have you done any calculations or educated guesswork on what the results of an exemption would be?

David Stewart: Not as yet. As I have said in response to previous questions, mid-market rent is a relatively niche provision at the moment. That is not to say that it is not important; it just does not constitute a high proportion of new-build housing developments in Scotland. If time allows, I am happy to look into the issue with member housing associations and, indeed, the Scottish Government, which I am sure will be able to provide statistical returns and will know how many mid-market rent schemes or properties were developed in the past financial year. I do not think that it would be difficult to go beyond that and work out broadly what tax would have been paid or lost. All that I can say is that I do not think that it would be a significant proportion of the tax, but I am happy, if time allows, to interrogate the matter further.

Mark McDonald: Richard Baker spoke about the situation in Aberdeen, which I represent, and Malcolm Chisholm mentioned the situation in

Edinburgh. Have you had any direct representations from your members about specific developments that they have in the pipeline that they might put on hold or might not be able to proceed with, or on which they think there might be an impact?

David Stewart: Not as such. The representations that I have had have been mainly from Dunedin Canmore, which sees mid-market rent as an important part of its business and an important part of the service that it provides to the community. It has looked at what the difference would be between developments built under stamp duty land tax and developments under the new tax.

Mark McDonald: I would like to pose the same question to Isobel d'Inverno, who spoke about development choices and used an example involving Newcastle and Edinburgh. I am not sure that that is always the calculation that is made by a developer, because most developers look at the need and demand in individual areas. Have you had any representations from developers or members of the Law Society of Scotland to the effect that this is a real situation as opposed to a hypothetical one?

Isobel d'Inverno: In relation to sub-sale development relief, lots and lots of developers have raised concerns about the fact that there is no general sub-sale relief under LBTT.

Mark McDonald: I appreciate that they have raised that concern, but you have raised the prospect of a developer choosing to develop south of the border as opposed to north of the border. Is that a real concern? Have developers said that they would make such a decision, or is it just a hypothetical scenario that you have come up with on the basis of differentials?

Isobel d'Inverno: It is a real concern that has been raised by developers. The Newcastle example is obviously hypothetical, but developers have asked how the system works in Scotland and how it works in the rest of the UK, and they have mentioned the possibility of doing projects outside Scotland because of the additional cost of doing them in Scotland. That is not a hypothetical scenario. Many organisations, including the SPF, have raised the same concerns.

Mark McDonald: Okay.

Isobel d'Inverno: I should also say that although the relief for mid-market rent that is being discussed is not something that the Law Society has considered in any great detail, we can see that it certainly deserves to be looked at further. One would imagine that it would be possible to design a relief that could not be claimed by those who did not really deserve it. There are plenty of reliefs that are focused on bodies such as housing

associations, so it should not be too difficult to make it foolproof.

Jean Urquhart (Highlands and Islands) (Ind):

I want to continue with the comparison between Newcastle and Edinburgh, albeit a slight variation on the theme. It seems to me that when developers decide where to develop they look at a large range of issues. For example, the price of land must be a consideration. It is inevitable that that will vary across the country, whether someone is developing in Shetland or Dumfries, or Newcastle or Edinburgh. On top of that, there is the cost of building materials, transport and so on. Many factors must be taken into consideration. Anyone listening to the discussion might think that the tax relief that is available is the only important issue but surely it cannot be such a big consideration in the greater scheme of things if all the other ducks are in a row.

Isobel d'Inverno: I believe that the issue comes down to the margins. Although the land might be cheaper in one location than in another, that is factored into the model and the price at which the finished development is sold takes that into account. However, if a tax charge is introduced in one jurisdiction that does not exist in another, that eats up the margin and means that the playing field is not level. That is why there was such concern among developers about the removal across the board of sub-sale relief from LBTT, even though people appreciated the reasons for such a move.

Jean Urquhart: Do you accept that there was also a lot of concern on the part of HM Revenue and Customs, which wanted to redesign SDLT because this issue was one of the biggest loopholes in tax avoidance?

Isobel d'Inverno: Yes.

Jean Urquhart: Tightening up those loopholes was seen as being of key importance.

Given that Westminster seems to have followed the changes that the Scottish Government has made in certain areas, this situation, too, could change elsewhere. In other words, sub-sale relief might not be available in Newcastle in due course.

Isobel d'Inverno: The thing is that the UK Government considered sub-sale relief in relation to SDLT and even after taking into account everything that it knew about avoidance, it decided to continue it under SDLT. Under SDLT, sub-sale relief is available for any sub-sale transaction. The rules have been tightened up, in that it is now necessary to claim the relief, but it is available for all transactions. There is quite a difference between LBTT and SDLT in that respect. After April, people will pay LBTT on these transactions in Scotland, but they will not pay SDLT on the same transactions in the rest of the UK. As a

result, it is important that we put in place a sub-sale development relief that is targeted at transactions for which such relief is terribly important—but without creating a vehicle for avoidance, which I am sure we will not have done, assuming that the order is passed.

Jean Urquhart: Thank you.

The Convener: That concludes the committee's deliberations. I thank the witnesses very much for their evidence.

We will have a one-minute suspension to allow for a change of witnesses.

10:42

Meeting suspended.

10:44

On resuming—

Land and Buildings Transaction Tax (Tax Rates and Tax Bands) (Scotland) Order 2015 [Draft]

The Convener: We have another 11 items on our agenda, so let us fire away.

Item 4 is to take evidence on the tax rates and tax bands draft order. I welcome our witnesses, who are Philip Hogg of Homes for Scotland and John Hamilton of the Scottish Property Federation, to the Finance Committee once again.

Committee members have copies of the witnesses' written submissions. As with the previous session, we will go straight to questions. As the panel will be aware, I always start off, before opening out questions to colleagues round the table.

The Homes for Scotland submission is as good a place as any to start. I notice a comment on the second page:

"An English family moving for work reasons and I guess they are thinking why should they be penalised for moving to Scotland."

Would they be penalised? The average price of a detached house in Scotland is around £170,000, with the price much the same in England. However, the price in London is £510,000, so you would pay a colossal amount more tax if you lived there. Is it not the case that, under the Scottish Government proposals, anyone buying a house worth less than £392,000 would be paying less tax than they would have paid in December 2014?

Philip Hogg (Homes for Scotland): First, our members welcome the new progressive tax system. It is a massive improvement on where we

were. I come here today to be complimentary rather than critical. However, we have maintained consistently in our submissions and in oral evidence that we need a fully functioning market that allows movement up and down the scale.

Secondly, Scotland has a housing crisis that no one seems to have taken consideration of. Audit Scotland has said that we need to build 500,000 homes in the next 20 years—that is 25,000 homes each and every year. Last year, we built 15,000, the lowest rate since 1947.

We have a major problem. Although we are today talking about LBTT and addressing the stamp duty levels, we must promote a healthy housing market. Our members have provided me with evidence on that basis. Rather than submit a dry paper, I sought to provide you with unedited and completely authentic feedback that I received from members on the latest announcements. I do not seek to justify each and every sentence in the submission; rather, it is provided to you as is so that you get a sense of what is happening.

As we move up to the prices around the £325,000 to £350,000 level, there is a very steep increase in the amount of tax payable in Scotland compared with south of the border. That is a fact; the figures show that. Our members are saying that it increases too steeply too quickly, and that it would be better evened out were the 5 per cent tax band broadened out a little bit further from where it is. We are calling for that because it would promote a healthier market, it would allow much more movement and fluidity in the market and, all in all, it would provide a better tax system and a better tax break.

The contrary of that is that we have genuine concerns that the market between £350,000 and £500,000—and possibly above that—will start to stagnate. We must bear in mind that moving home in those price brackets is largely a discretionary choice that people make. Many people do not have to move; they could equally not make that decision. We partly had the housing crisis a few years' back because of that. Yes, mortgages became more difficult to get, but people were also very concerned about taking on bigger commitments, about moving and about their job security.

I mentioned that we must tackle the housing crisis. We need to talk about how we are going to solve that. I have a lot of sympathy with David Stewart from the previous panel, who provided evidence about the need to address mid-market rent as well as all tenures. We should be looking at what we can do to get the housing market back so that we are housing all our population across all tenures. That is the basis of our submission.

The Convener: I have to say that I do not think that anyone considers that stamp duty was a major factor in the housing market slowdown over the past few years; I do not think that anyone seriously considers that to be the case. There were a variety of reasons for that. We all know what those were, so there is no point going into them in any great detail.

An issue that caused difficulty was house price inflation because, year in, year out, it was much higher than the increase in wages and we ended up with a bubble. One would have thought that any significant tax imposition on the purchase of large houses would in itself have a counter-inflationary impact on house prices. Therefore, as well as bringing in revenue for the Scottish Government, would imposing a reasonable tax on those houses not make houses more affordable overall rather than less? If taxation were, for example, to be removed from those large houses, would that not just lead to greater house prices? No one in the general public would benefit, because they would have to pay more for houses that already, in some parts of Scotland—we will hear a bit more about Aberdeen and Edinburgh—are chronically overpriced already.

Philip Hogg: I think that you are absolutely right that housing prices need to be brought back closer to affordability levels. I have no issue with that.

However, the best way of addressing what is a classic supply and demand issue is to resolve the supply situation by adjusting taxation levels, as I have said, with a larger discretionary move. Some people will simply say, “If that means that the price of my property, which I am currently living in, has gone down, I may decide simply not to move.” That creates the stagnation that we are talking about. Unless they are moving for personal reasons or job relocation, many people will simply decide that it is easier for them to stay where they are. If the price of their property has, in theory, devalued, that does not promote the healthy market that we are looking for.

We need a healthy market. We have an ageing population and there may be older people who have equity in their homes or who are living in larger family homes than they need as they reach later stages of life and who could consider downsizing. If they see property prices declining, they might decide that that is just not palatable.

The Convener: Hold on a second. Are we not concerned with building homes? If the prices are lower rather than higher, that will make them more affordable.

Philip Hogg: Sorry, I do not understand.

The Convener: You are talking about people deciding not to move, but there are other people who want to enter the market and are aspirational.

If the house price that they would have to pay—for a new home, for example—is less because house price inflation is less, would that not boost the industry and indeed help your members?

Philip Hogg: The best way of boosting supply is to tackle the lack of land availability in the planning process. The best way to address affordability and pricing is to resolve the supply and demand equation, which, as you can see from the figures that I quoted earlier, is so far out of kilter that fiddling with taxes is not going to have a significant impact on either supply and demand or house prices.

The Convener: Mark McDonald has a brief supplementary.

Mark McDonald: To follow on from what the convener has said, I am struggling with the logic here. You say that you are in agreement that reality needs to be brought into the pricing of housing and that the market needs to be much more affordable. It strikes me that you are saying to the committee that we need to increase the threshold for the 5 per cent band on higher-value properties, while you seem conversely to be arguing for a much greater supply of more affordable properties, probably below the £250,000 band. Those arguments do not seem to match up, given what you seem to be aspiring to. If you are saying that we need to provide more houses below £250,000, where the bandings are set should be of no consequence to that, because those are properties that under LBTT will pay less in tax.

Philip Hogg: I did not argue for more properties below £250,000. I said that we need more homes across the board, including more mid-market and more socially rented, as David Stewart was arguing before. We need more homes at all stages and all parts of the market. We simply do not have enough at the moment.

Mark McDonald: At the moment, though, there is no part of Scotland where someone buying at the average house price will pay more under LBTT than they would have paid under stamp duty. It is not until the price is way above £300,000 that people will pay more than they would have paid previously. There is nowhere in Scotland that that is the average house price. Again, I am not entirely sure how that meets what you are saying about increasing supply.

Philip Hogg: There is one quite large example in our submission, which I think is quite significant and which might help illustrate the point. The majority of new-build housing in Scotland is provided by the large-volume UK-wide home builders, who will typically provide products at the lower entry level of the market at the sort of prices that you might recall.

The small to medium-sized home builders that tend to operate in more rural or secondary locations, outside the big conurbations, have almost halved in number as a result of the recession. We desperately need to encourage such home builders back into the marketplace. I know that some work has been started by the Scottish Government to address that. We welcome the recognition that we need to bring those people back. The smaller home builders will typically be providing higher-value properties, and they operate on a smaller scale. Their operational costs are a lot higher.

The larger example that I provided in our submission was from a smaller home builder, operating in Fife and providing aspirational family homes. I have similar evidence from other firms. Another one in the Borders has just lost a sale. The property was priced at £425,000, which represents 10 per cent of that firm's turnover.

We are told that those are the discretionary purchases that are now starting to drop away. One sale on that sort of level can make a massive difference to smaller home builders. If we do not get those people back providing capacity in the marketplace, we will increasingly have a smaller supply chain, and we will never get anywhere near the 25,000 homes a year that Audit Scotland tells us we need and we will never have any way of tackling the house price issue. All these things are interconnected.

The Convener: I point out that, under the Scottish Government proposal, in a given year, £53 million less tax will be recouped than was previously the case. There is a significant reduction in the amount of tax that is going to be paid by people buying houses relative to previous years.

Mr Hamilton, you say that the average price for a detached property in Edinburgh is £394,000, which is £2,000 more than a figure that I quoted under which everyone would be better off. What proportion of houses in Scotland sell for that amount of money or more?

John Hamilton (Scottish Property Federation): A key point for us is about the proportion of houses that contribute to the tax that is generated. We have not focused particularly on the average house price across the board, because it gives a slightly distorted picture of the amount of revenue that is generated in any particular sector or category.

We have pointed out that 8 per cent of residential transactions are expected to account for 75 per cent of the revenue. The principle involved is that quite a small proportion of the market contributes a very large proportion of the tax that is generated.

From the start of our consideration of the new proposals, we understood the need for some neutrality between the revenue that was generated previously and the revenue that will be generated under the new proposals. You have made the point that the estimate under the current proposal is for a slight reduction in revenue. As I understand it, however, that would be expected, and it would be hoped that the difference would be closed in future years, so that there is no long-term shortfall in the revenue that is attracted by the new tax system. If that is not the case, and if part of the market is not operating effectively, there could be a shortfall to the Scottish Government in the revenue that is attracted in the long term.

In a sense, there is an element of our wanting the same thing, which is a stable market that operates effectively at all levels and allows people to sell properties—whether new build or resale—if they are in a position to do so. If someone is in a position where they have to make a choice about selling their property, they may be dissuaded from putting that property on the market.

The Convener: Sorry, but why would they be? If someone is selling their house, they do not pay any tax. It is only the purchaser who pays it.

John Hamilton: But they may have bought at a certain level and have a high mortgage, and they may get advice that the cost of selling the house to a new purchaser means that the equation just will not work. Therefore, those properties might not come on to the market.

11:00

The Convener: Surely the whole market must have been stimulated by the fact that, six months ago, people had to pay £7,500 stamp duty on a £250,000 house, and they will now have to pay £2,200. That is a £5,300 difference.

John Hamilton: I am not talking about £250,000 houses.

The Convener: I am aware of that, but surely the whole market must have been boosted by the fact that, overall, there is to be a £53 million reduction in tax. You are focusing on a very small part of the market. Where is the evidence that there will be a significant reduction in transactions or houses being built at those costs? There is a lot of assertion rather than evidence that that will be the case. I mentioned London, where house prices are sky-high, and I do not see the housing market collapse there. Instead, a lot of people cannot afford to live anywhere, more or less, because of the sky-high prices. If what you suggest was brought in, all that we would have would be higher house price inflation, and fewer people would be able to buy those houses.

John Hamilton: No, that is not the case. We agree that it is not particularly healthy for the UK to have prices that are too high and a market that is too active in London, at the expense of other parts of the country. We would like an improvement in market conditions in Scotland, with more house building and more property transactions generally, so that there is demand for property business to take place in Scotland. London has been referred to quite a lot this morning. To us, too much is happening in that part of the country, and we argue that we need to make Scotland more competitive. In London, there is overdemand for property, but we do not have that in Scotland. We want to create a situation where there is demand in the major cities of Edinburgh, Aberdeen and Glasgow and in the more regional parts of Scotland. Putting a higher burden of tax on all those areas will not improve Scottish competitiveness.

The Convener: If your proposals were implemented as you have suggested, what would be the revenue implications? There seems to be a suggestion that they would not impact on revenue because there would be more transactions. Is that your view?

John Hamilton: We were satisfied with the principle of the 5 per cent rate being introduced. We have not suggested quite such a high figure as Homes for Scotland has, but the principle of moving the band up from £325,000 is important because we think that the current band will lead to a distortion in the market as house builders, and for that matter home owners, will be looking at a very narrow band of pricing, and houses will come to the market at the expense of larger properties, which will not. The principle of what we propose is very much the same, although the numbers are slightly different. Although we agree on the rates that have been set, we are slightly at odds on the band. A band of £75,000, between £250,000 and £325,000, in an important part of the market is too narrow.

The Convener: Mr Hogg, you suggest that the figure should be £500,000 rather than £400,000. Do you have any figures to suggest how that would impact on revenue?

Philip Hogg: We have not made any calculations on that. We are all trying to forecast the future, and I make no claims of being any better at doing that than the next person. What we bring to our case is our members' first-hand experience of dealing with home buyers at the sharp end. We are talking about buyer behaviour and we are all trying to second-guess what might happen in the event of the new rates coming into effect. All that I can bring to you is evidence from our members and from potential home buyers. That is the reason why I provided verbatim

comments about what is happening on the ground. We are not economists, but we are telling you what people are saying to us and what their likely actions might be, and our evidence is based on those forecasts.

The Convener: Before I open up the session, I have one further question for Mr Hamilton, on the non-residential rate. I asked Mr Swinney about the change from 4 per cent to 4.5 per cent, which would represent £10,000 for a £2 million development. His view was that a half per cent would not make any difference to a strategic decision on whether to bring a development to Scotland.

John Hamilton: We covered that in our previous session with the committee, and I gave an example in which the figure was far higher. All large-scale residential developments are now undertaken by the major UK house builders—there are very few small house builders here in Scotland, and it is probably the same in England. As Philip Hogg said, the number of SMEs has dwindled, and the market is now dominated by a relatively small number of UK house builders, virtually all of which, if they have a presence in Scotland, also have a presence in England.

I do not agree that the issue of competitiveness should be ignored. I gave an example in our previous evidence session. The house builders with which my company deals are selling land typically not at £2 million but in the £6 million, £8 million or £10 million price brackets. The people who are making the choices about whether to proceed with those transactions are based largely in England, and I know from personal experience of dealing with those companies that they will make that choice. There is an element of competition among those companies with regard to whether a development proceeds in Edinburgh or Newcastle, for example. There is one very large business located in Newcastle—which I do not have to name here—that makes those choices. The imposition of another half per cent of tax on that land will come into the equation for that company.

The Convener: Thank you for that. I will now open up the session. John Mason can go first, followed by Mark Griffin.

John Mason: Mr Hogg, you commented earlier on land not being available. That might apply in some areas, but I do not think that it applies in all areas. In my constituency in the east end of Glasgow, we have a lot of land and no problem with planning permission, but nobody wants to build on it despite the need for housing. At the end of my street, there is an area where the roads are laid out and the street lighting has been on for 25 years, and no one is building there. Do you think

that tax could bring about movement on that sort of land?

Philip Hogg: I am not a developer, and I will not assess the viability of any piece of land without knowing what it is. I was trying to make the general point that, although we need the tax system to work efficiently, it is only a very small part of a bigger market problem.

As you said, in some parts of Glasgow we do not have the right type of housing. In Aberdeen, we are finding that the market is racing away so affordability is an issue, and planning processes are a major problem. As has been mentioned, the Scottish Government is in the process of finalising a joint housing delivery action plan. I was at a meeting late last night working on some of the land issues that are related to that. The reality is that there simply is not enough land throughout the country to meet Scotland's housing needs. Even in places where there is enough land, the planning system is so painfully slow and difficult to get through that we cannot progress the development of land at the necessary rate. If we are seeking to tackle issues with house price affordability, that is where we should be directing most of our efforts.

John Mason: But you accept that, in some cases, there is land and planning permission and yet no one is building.

Philip Hogg: Absolutely, and there could be a raft of reasons for that. Perhaps there is no market for housing there, there are constraints on the site, or the financial viability does not stack up—

John Mason: But the tax is probably not the major factor in that situation.

Philip Hogg: Do you mean LBTT?

John Mason: Yes.

Philip Hogg: I simply have no idea, but I suspect that it is probably not. It would depend on house prices.

John Mason: Following on from that, you give some examples in your submission in the form of bullet points with quotes, which is helpful. Referring to the tax, I think, the second one states:

"It is just about to cost me £3,350."

The example that is given is a house that might have cost £430,000 and has been bargained down to £400,000. The bargaining, therefore, has affected £30,000, which is about 7.5 per cent of the total; I guess that that is not unusual. The tax—the £3,350—is 0.8 per cent of the total.

It suggests that, in that example, the tax is a very small part and is almost irrelevant, and that the big movement comes when someone bargains over a house price. Is that your understanding?

Philip Hogg: That example supports John Hamilton's case that, with such a high proportion of the total tax take under the new scheme being on a very small number of properties or transactions, there is a fragility to be considered. If we suppose that the prices for a good number of those properties are negotiated downwards and the corresponding tax comes from there, that would potentially leave a big hole in the forecast tax take.

John Mason: Mr Hamilton, Mr Hogg referred to your view that the band from £250,000 to £325,000 is too narrow. If there was going to be a bit of bargaining, would you be happier if the band was wider but the 5 per cent rate went up to 7 per cent?

John Hamilton: As I said before, in terms of the principle we are, to a large extent, looking for the same thing: a stable market that generates revenue. We cannot predict exactly how much business will be done next year or the year after, but we are seeking to maintain the budgetary conditions in which we can all operate our businesses.

To an extent, we overcomplicate the situation again by bringing in yet another proposed tax rate. We have said that we feel that the structure of 0, 2, 5, 10 and 12 per cent is probably now appropriate. However, I still make the point that we should look now at the bands rather than the rates, and ensure that there is enough market activity in each of those bands to generate the amount of revenue year after year in which the Government can see tax revenue being generated and the property and housing industry can see stable business.

John Mason: You are in a market in which bargaining is very much part of the equation. You are asking for a wider rate and a reduced tax level. Is there nothing that you are willing to give in return?

John Hamilton: We are asking for a wider band.

John Mason: A wider band, which means a reduced tax take. Is there nothing that you are willing to give to balance that out?

John Hamilton: I think that we are giving. From the start, the point has been conceded that there must be—or there should be—a similar amount of tax being collected. In a way, we are almost arguing from the Government's side: we think that there is a risk that the tax will not be collected. That is not good for the industry either, because it will show that part of the market is not functioning correctly and that there is not a choice in the market. Not all our members, and not all Homes for Scotland members, serve the same part of the market.

I will give you one extreme example. We have members in the Aberdeen area who have very difficult trading conditions in front of them, and the changes in legislation that are ahead are making that situation worse. It results from the combination of an unforeseen drop in oil revenues, which had not been factored in when the proposals were introduced, and the new tax rates themselves, which make it extremely difficult for those businesses to survive.

John Mason: On the other side there are constituents like mine, who think that if someone has spent more than £750,000 on a house, they are fabulously rich, and that 12 per cent is too low and we should go to 20 per cent. Are you not willing to concede on a wider band, a higher rate or anything like that?

11:15

John Hamilton: As I said, I think that the rates are probably set pretty much in the right place now. There might be some debate about whether the rate should be 5 or 6 per cent, or 5.5 per cent. There is often discussion about the housing ladder, and the important point is that the steps on the ladder have to be manageable. People must have the ability to make those steps; if they do not, they can be stuck for a long time and the market will not operate effectively.

We do not have a great issue with the rates, but we concede that there could be room for negotiation around the mid rate at 5 or 6 per cent.

John Mason: I am interested in particular in paragraph 2 of your paper, in which you refer at least twice to detached properties in Edinburgh and elsewhere. There are very few detached properties in my constituency. A detached property is, per se, a luxury. Do you accept that? Nobody needs a detached property.

John Hamilton: It is not a necessity. I have lived in all sorts of properties in my lifetime. The housing market tends to address wherever the demand for housing is. The demand has to exist across the market. As Philip Hogg said, that applies to all levels of the housing market, whether mixed tenure, social rent, mid-market rent or private rent.

The issue is still what part of the market is making the biggest tax contribution. I do not want to overegg that point, but if we put so much of the burden on one particular tenure and house type, we have to give some consideration to the ability to sell the property. If the property does not sell, there is an implication for the tax that is generated.

John Mason: The other side to that is that the people who need the tax are at the bottom end.

John Hamilton: Yes.

John Mason: Is your submission and your organisation basically arguing for the richer part of society?

John Hamilton: No, not at all. The welcome element of the proposals is that a larger part of the housing market has been removed from tax. I welcome the changes that have been made in that respect. However, that does not detract from the point that that is a larger market. We do not feel that it is a case of penalising one part of the market at the expense of other parts. We would like to see a fair tax system. Fairness always comes into the question of tax. We do not believe that the levels that we are talking about are fair. We do not believe that it is appropriate for such a burden to be carried by a small element of the tenure and house types that will be sold.

John Mason: Thank you.

Mark McDonald: The other day, a friend of mine shared on Facebook a four-bedroom, semi-detached family property in Bridge of Don in my constituency, which is located quite close to a local primary school. It is obviously a very desirable property at offers over £250,000. It is important to put that example on the record, because I think that we are straying into the realms of assuming that it is not possible to buy a family-sized property in my constituency, or in Aberdeen, at such a price.

I am struggling with some of the evidence that we are hearing. Mr Hamilton, you seem to be suggesting that the rates that we have been discussing, which nobody is paying yet, are creating great difficulties for businesses in the north-east of Scotland.

John Hamilton: No. I have not said that.

Mark McDonald: You mentioned it in combination with other factors.

John Hamilton: I mentioned the bands.

Mark McDonald: I presume then that you would advise your members to build properties at £250,000 or below. If you are telling us that house purchase prices will be driven by the rates that will be paid under the bandings, there will be a rush of people seeking to purchase properties that, as the convener highlighted, they will pay significantly less for than they would have paid under stamp duty.

John Hamilton: Yes. I agree with that.

Mark McDonald: Technically, however, nobody will pay more or pay less, because stamp duty or LBTT is paid only at the point of purchase—it is not an on-going tax. For example, I paid stamp duty when I bought my house but I have not paid it since. I am not paying that tax at present and I will pay it only if I decide that I want to buy another

property. It is not an on-going tax like income tax, so surely it is misleading to portray it in those terms and say that people will pay more or pay less; people will pay the tax only at the point of purchase.

John Hamilton: I am struggling to see the point.

Mark McDonald: In the grand scheme of what drives the behaviour of house purchasers, I am struggling to conceive that the tax is the primary motivation. That is the point. If people are looking to upscale to a larger property, that is driven by a range of factors. Most people who will buy properties that will attract LBTT will have the ability to pay the tax as part of the purchase, particularly if, as the Homes for Scotland submission highlights, they have negotiated a £30,000 reduction in the purchase price in some cases because the seller is making—

John Hamilton: I am struggling with the idea that people have no concern about paying tax.

Mark McDonald: I did not say that they have no concern about paying tax.

John Hamilton: No matter whether the tax is paid once or annually—no matter its frequency—it will have an influence on people's choice about what type of property to buy and on the type of property that is brought to the market.

Mark McDonald: Mr Hogg, are you detecting a change in market behaviour currently because of the future introduction of the bands?

Philip Hogg: When you say "market behaviour", who are you referring to?

Mark McDonald: Purchasers.

Philip Hogg: Yes.

Mark McDonald: To what extent?

Philip Hogg: To the extent that, from the anecdotal feedback that I have, the market has slowed down significantly for the higher-priced properties since the rates were announced.

Mark McDonald: That is interesting. The rates are not yet active, but surely if behaviour was driven by them we would expect to see sales taking place in advance of the rates being introduced and other sales being brought forward as a consequence.

Philip Hogg: As you know, the process of moving house is not the sort of thing that happens over a weekend. Realistically, anyone who makes a decision today to purchase a new home is probably in for a three to six-month process. Anyone who decides today that they want to purchase a new home has virtually no chance of

doing that before the new tax rates are introduced—

Mark McDonald: Forgive me for interrupting, but the previous rates, in terms of the initial consultation, were announced in November, which was about six months before they would have become live. Did you notice anything then?

Philip Hogg: At that point, we saw an acceleration of people wanting to conclude sales; they were people who would have been disadvantaged from April. A rush of people wanted to conclude sales early. However, on this side of the financial year, no one who set out on a purchase from January on would have been likely to complete it before April. Since January, the market has gone a lot quieter—we are told—on the higher-value properties.

Mark McDonald: My concern is around how the issue is being portrayed. For example, your submission states that a developer suggested that people are being penalised for moving to Scotland. I do not think that that kind of language is helpful. Presumably, by the same token, if I were a first-time buyer and went south of the border to purchase, I would be penalised for moving to England, because I would pay a higher rate under stamp duty than I would pay under LBTT. If you anticipate a lack of people moving to Scotland at the higher end because they would pay more in tax, do you anticipate a greater number of people moving to Scotland at the lower end because they will pay less?

Philip Hogg: As I mentioned, the comments in our submission are verbatim, so whether or not you like what people are saying, that is how they feel; that is people's experience. I make no apology for giving you verbatim comments rather than couching it in terms of what I think our members are saying.

A factor that you perhaps need to take into consideration is that people who are purchasing higher-value properties have more mobile careers; that is not always the case, but it is a general rule. Those at more senior levels have the opportunity to move around and relocate a bit more. We have heard examples in which senior people are not only looking to move, but looking to bring colleagues with them to set up new departments, divisions and businesses. The main person could decide that they will not move or, to use the example that has been mentioned, they may say that they will move to Newcastle rather than to Edinburgh. In that case not only does that person not move, with all the corresponding tax benefits, but their colleagues who they would have subsequently employed do not follow them. There is quite a long chain of events that happen.

Mark McDonald: Okay.

Gavin Brown (Lothian) (Con): As you said, you are not economists, but what is your best estimate of the likely impact on the Scottish housing market after 1 April if the regulation is passed and the rates and bands in it take effect?

Philip Hogg: We will see a prolonged period of below-average activity in that section of the market. That is not say to say that activity will stop—it will not, because some people will have to move. We will see suppressed levels of activity. As I said, it is generally discretionary movement at that level, so people will say, “If that’s what it means, I’ll choose to stay where I am.”

As I have tried to explain, we will also see a disproportionate effect on small and medium-sized home builders who are more likely to build at those higher prices because they cannot compete with the larger volume home builders as they do not have the economies of scale.

As you will see in the examples in the submission, one person said that he aims at that market. That small, Fife-based company probably builds 20 homes a year or something of that scale. He will be disproportionately hit because he cannot compete with the larger volume guys on the entry-level products, which is the market below £250,000. That impact will take more capacity out of the marketplace; it will take homes away. Therefore, those people who might have bought at the £400,000 level might decide to stay where they are, so a more entry-level property would not be released.

John Hamilton: I agree. It is important to see the differentiation between the new-build market and the existing sales market. Most sales, and therefore tax revenue, are generated from the sale of existing property. However, the new-build market’s importance to the economy cannot be ignored, because of the massive shortfall in the number of houses that are being built, the wider economic implications of that and the lack of business activity in that gap. We should be aiming to build 25,000 to 30,000 houses a year, but we are struggling to build somewhere between 11,000 and 12,000 houses.

Generally, the implication of making it less attractive for a house builder to look at the full range of new housing that he might bring to the market would be a detriment to that position. It would not generate more house-building activity, which is key to the wider economy.

Gavin Brown: Let us assume, Mr Hogg, that your best estimate comes to pass and, to use your words, there are “suppressed levels of activity” in that section of the market. I think that you were referring specifically to the £325,000 to £500,000 level, but presumably it could apply to properties above that value as well. Does that market section

exist in a vacuum, or would there be an impact on other parts of the market and those houses that are below the £325,000 value?

11:30

Philip Hogg: We often refer to the concept of the housing ladder. As a generalisation, people move in their different life stages. Perhaps they will move from their family home to their first one-bedroom flat and look for something a little bigger when their new family comes along. That is a well-proven path, albeit that it is not scientifically accurate for everyone. However, we talk about progression.

If we find that there is a lack of suitable products available at the higher levels, it is clear that that will mean that those who can and want to move upwards will have fewer opportunities to do so. Again, we come back to classic supply and demand. If only one four-bedroom property in a certain price range is available that suits a purchaser, the seller will have the opportunity to bargain on the price. Having a market that does not move fluidly will not help to tackle house price inflation.

Gavin Brown: Okay. Does Mr Hamilton share that view? What are his thoughts?

John Hamilton: Yes. We have certainly come back to that point more than once. The market operates most effectively where there is fair demand that is generated by the wider attractiveness of living and working in the area. Fundamentally, we do not think that it is helpful to have more severe differentiation or too severe differentiation. We accept the point that, in general, people who buy more expensive houses should be able to afford them, but people are often heavily mortgaged. In many cases on that side of the market, people are starting businesses and making contributions to the economy. That applies specifically to the tax that we are discussing, which has been generated in that part of the housing market, and to people who will make contributions to the business economy.

Gavin Brown: Okay. So in your respective views, the way to get a better functioning or optimal functioning housing market is to make the changes to the bands that you have submitted in your written evidence.

Philip Hogg: Yes, I believe so. I reiterate my opening comments. I welcome the new system and where we are compared with where we were at this time last year. We came here today to genuinely provide our advice. The committee invited us here to provide our advice based on our members’ experience and the market, and we are genuinely bringing that to the committee. We think that, if the 5 per cent band were extended up to

circa £500,000, that would go a long way to creating a better and more robust tax system.

Jean Urquhart: I want a wee bit of explanation, Mr Hogg. I think that I will be quoting correctly; I am sure that the clerks will tell me if I have not done so. You said that

“there simply is not enough land”

across all of Scotland to satisfy housing needs.

Philip Hogg: Yes.

Jean Urquhart: What do you mean by that?

Philip Hogg: Every local authority has to provide an effective five-year land supply. I will not bore you with the intricate details, but only a handful of local authorities have an effective five-year land supply. That was discussed at a meeting that I was at late last night. We have long argued that a shortage of land and raw materials will drive prices upwards; any basic economics will tell you that. We have to ensure that there is enough effective land where people want to live that can be developed. That will start to tackle the housing shortage and then impact on house prices.

Jean Urquhart: But you would say that it is not a shortage of land for house building that is holding up house building at the moment.

Philip Hogg: I would say that there is a shortage. Because there is not enough land, that affects its price and availability.

Jean Urquhart: Okay. Is that common across the UK?

Philip Hogg: Yes. I fully recognise that home building can be very contentious and difficult at the local level. It is interesting that the UK political parties are talking in the run-up to the general election about building 200,000 or 300,000 homes. It is great that it is recognised that more home building is needed, but there is the issue of translating the top target and saying, “Oh, and by the way, we’re now going to build 50 of those just around the corner.” All of a sudden, it is then a little bit difficult for everyone who has signed up to that need.

The issue will not go away. We have a growing and ageing population, and we are simply not building enough homes to house our population. That is a sad reflection. Successive Governments—I am making no political point—have failed to recognise and grasp that issue. We are spending two hours here talking about tweaks to a tax system; I would welcome much more spending two hours talking about how we will address the housing crisis in Scotland. We are not having that discussion, but we should really be spending two hours talking about that.

Jean Urquhart: So the problems are much bigger than the tax and the tax bands.

Philip Hogg: Absolutely.

Jean Urquhart: That pales into insignificance.

Philip Hogg: It pales into insignificance.

Jean Urquhart: Very good. Thank you.

The Convener: I thank John Hamilton and Philip Hogg for coming along again and thank them very much for their evidence, which is very much appreciated.

As we have been in session for more than two hours, we will have a break until 11.45. That will give members a natural break, as we still have another 10 items on our agenda.

11:36

Meeting suspended.

11:45

On resuming—

Land and Buildings Transaction Tax (Sub-sale Development Relief and Multiple Dwellings Relief) (Scotland) Order 2015 [Draft]

Land and Buildings Transaction Tax (Tax Rates and Tax Bands) (Scotland) Order 2015 [Draft]

The Convener: We agreed to start back at 11.45 so that is what we will do.

Our next item of business is evidence from the Deputy First Minister and Cabinet Secretary for Finance, Constitution and Economy on two statutory instruments that relate to the land and buildings transaction tax. He is joined for this item by Neil Ferguson, Alison Cumming and John St Clair of the Scottish Government.

I welcome the cabinet secretary to the meeting, ask him to make an opening statement explaining the instruments and remind him not to move the motions at this point.

The Deputy First Minister and Cabinet Secretary for Finance, Constitution and Economy (John Swinney): Do you wish me to make an opening statement on both orders?

The Convener: Yes, please.

John Swinney: The primary purpose of the Land and Buildings Transaction Tax (Sub-sale Development Relief and Multiple Dwellings Relief) (Scotland) Order 2015 is to provide for a relief from land and buildings transaction tax in relation to a land transaction involving sub-sale

arrangements, but only where development of the land in question is in prospect.

The work to develop the provisions in the order followed a number of meetings of a working group that involved industry professionals and tax specialists, which was convened to explore the issues associated with a sub-sale development relief. I place on record my thanks to those who participated in the exercise.

Given the experiences of sub-sale rules applicable to stamp duty land tax, my core considerations in the design of the relief have been to ensure that it supports economic activity in the form of property development while not supporting land speculation and minimising any risk of tax avoidance. Members may recall that I made those points during passage of the Land and Buildings Transaction Tax (Scotland) Bill and placed my position on the subject on record during the stage 3 debate on 25 June 2013.

To achieve those aims, a consultation paper was published in June 2014 seeking views on draft regulations that would introduce a sub-sale development relief under which the first buyer in a sub-sale arrangement would pay the full tax due and then, provided significant development of the site had taken place within five years, the relief would be claimed and the tax returned by Revenue Scotland on receipt of a tax return.

However, the consensus of the responses to the consultation was that, to help with cash flow in development transactions, the relief should be available at the outset. If development was not completed within the five-year period, the relief could be clawed back. Otherwise, the industry argued, developers in Scotland would be placed at a disadvantage in terms of cash flow in comparison with their competitors in other parts of the United Kingdom.

That issue has been addressed in the revised regulations that are now before Parliament and are the subject of the committee's discussions. The order provides for a relief which has a number of features.

First, the relief will be available only to the first buyer in a transaction that involves sub-sale arrangements where "significant development" is in prospect. The order defines "significant development".

As has always been envisaged, the relief will be available to the first buyer when the whole site is sold to a second buyer. Partial relief is available if the first buyer retains part of the site and the remainder is sold to a second buyer or further partitioned to other buyers. To be clear, no relief is available for the proportion of the site that the first buyer retains.

The relief is restricted to the first buyer only; it is not available to a second or subsequent buyer where a series of sub-sale arrangements is in place. That reduces the risk of tax avoidance and is an improvement on the corresponding arrangements relating to stamp duty land tax.

In recognition of the development industry's concerns, the relief is to be claimed and granted at the point when the first buyer submits the land transaction return. Revenue Scotland may request that the first buyer provide specific evidence that the claim is valid—for example, that there are firm plans to undertake significant development.

Lastly, if significant development does not take place within five years, the relief will be withdrawn or partially withdrawn. The tax that should have been paid will then become repayable.

I am confident that the relief will provide a robust mechanism that balances appropriate safeguards to the property development industry in Scotland with the need to protect revenue and maintain a firm position on tax avoidance.

In addition, the relief has been discussed in detail with Revenue Scotland. Administration of the relief will have implications in terms of checking that significant development has indeed taken place and recovering the relief where that is not the case, which will increase administrative costs for Revenue Scotland in due course. Taken in the round, though, my view is that the relief represents an appropriate balance between equity, collection of revenue and administrative effort.

Finally, the order also amends paragraphs 11 and 12 of schedule 5 to the Land and Buildings Transaction Tax (Scotland) Act 2013 for multiple developments relief, to ensure that the calculation using the minimum prescribed amount of 25 per cent applies only to the acquisition of multiple dwellings, not multiple dwellings and other property. Under the drafting as enacted, it was felt that there might be ambiguity on that important point, which was undesirable and which, subject to Parliament's agreement, will now be clarified.

The order also makes a consequential change to provide that the minimum proportion prescribed in the Land and Buildings Transaction Tax (Prescribed Proportions) (Scotland) Order 2014, which has already been considered by committee, stays in force on the amended basis.

I move now to the Land and Buildings Transaction Tax (Tax Rates and Tax Bands) (Scotland) Order 2015. The primary purpose of the order is to set tax bands and percentage tax rates for land transactions that will be subject to land and buildings transaction tax. The instrument sets the rates and bands for residential property transactions and for non-residential property

transactions and, with respect to leases, it sets the tax rates for each band applicable to chargeable consideration that consists of rent.

The Scottish Parliament legislated for a marginal progressive rate structure for LBTT back in 2013. That was intended to replace the much criticised slab structure of stamp duty land tax, which was shown to cause distortions in the housing market around the tax thresholds. The reform was recently replicated across the United Kingdom, although for residential transactions only, following the reforms to SDLT that the Chancellor of the Exchequer announced in the autumn statement.

I set out the Scottish Government's proposed rates and bands for LBTT in the budget last October, and I updated Parliament on planned residential rates and bands during the stage 1 debate on the Budget (Scotland) (No 4) Bill in January.

I made it clear to Parliament last October that I intended the devolved taxes to be revenue neutral in their first year of operation. The Government did not want to raise any more or less from the two devolved taxes than would have been raised had the UK taxes remained in place, and we wished to maintain devolved spending at planned levels.

Of course, at the time of the draft budget, we had still to reach agreement with the UK Government on the block grant adjustment for the devolved taxes, despite two years of effort in that respect. The LBTT rates and bands presented in the order, taken with the proposed rates of Scottish landfill tax, are designed to be revenue neutral against the block grant adjustment in aggregate, as I set out to the committee in my letter of 22 January and in the chamber on 4 February.

The Scottish Government forecasts that we will generate revenue of £381 million from LBTT in 2015-16, of which £235 million will come from residential property transactions and £146 million from non-residential property transactions, including the taxation of leases. Those forecasts have been endorsed as reasonable by the Scottish Fiscal Commission. As the committee is aware, work is continuing on the estimation of the revenue losses arising from forestalling, and the Scottish Government's estimates will be subject to review by the commission. The impact of forestalling on the block grant adjustment also remains to be agreed with the UK Government.

I will now turn to the policy objectives underlying the decisions that I have taken on the three sets of LBTT rates and bands presented in the order. In setting the rates and bands of tax payable on residential property transactions, I have sought to prioritise support for first-time buyers and those

progressing through the housing market by redistributing the tax burden from lower to higher-value transactions. Those rates are consistent with the principle that taxes should be proportionate to the taxpayer's ability to pay.

The nil rate threshold is set at £145,000, which will take around 50 per cent of house purchases out of tax altogether—10,000 more purchases than under the new rates of UK SDLT. The marginal rate of 5 per cent, which I announced in January and which is to apply to the value of a purchase between £250,000 and £325,000, also ensures that the tax due on more than 90 per cent of transactions will either be less than the UK charge or will be zero.

For non-residential property transactions, the rates and bands are designed to ensure that Scotland remains an attractive location for business investment. They will reduce the tax charge for the majority of transactions below £2 million, ensuring that the tax due on around 95 per cent of transactions will be the same or lower than the SDLT charge.

Finally, the rates and bands for non-residential leases are set to ensure parity with the UK rates, which are also set on a progressive basis.

I consider that the rates and bands demonstrate clearly that the Scottish Government has placed fairness, equity and the ability to pay at the very heart of the first decisions that we have taken on national tax rates.

The Convener: Thank you, cabinet secretary. One reason why this session started about 45 minutes later than scheduled is that we have taken evidence from a number of witnesses on these items.

I will ask you one or two questions before I open out the session to colleagues around the table. In evidence that was presented to us earlier this morning, Homes for Scotland and the Scottish Property Federation advised us that the band restriction of 5 per cent from £250,000 to £325,000 is likely to lead to market distortions for more expensive properties, particularly those in the £325,000 to £400,000 range. Homes for Scotland would like to see the band widen to £250,000 to £500,000. Some evidence suggests that there has been an adverse impact on transactions in the £325,000 to £400,000 range as a result of the announcements that have been made. What is your view on that?

John Swinney: The only published data that we have is Registers of Scotland's data for the fourth quarter of 2014 on property transactions and property prices, and the volatility in the market and around the issues with which we are wrestling only crystallised for a limited time during that period.

I set out the rates in October, but the UK Government's changes were announced in early December, so we do not have a particularly reliable period of analysis. Nothing in the data strikes me as indicating a particular change in the pattern of property transactions. We will consider carefully the statistics for quarter 1 of 2015 from Registers of Scotland as they become available.

The Convener: The Scottish Property Federation raised concerns about the non-residential rate. It said that the 4.5 per cent rate, as opposed to the 4 per cent rate in the rest of the UK, would have a detrimental effect on the likelihood of decisions being made to invest in Scotland. I put that concern to you some months ago, when you said that it would not make any significant difference, but the Scottish Property Federation's representative said that his personal experience is that the rate is having an impact on investments in the £6 million to £8 million range. Does the Scottish Government have any detailed information on whether that is the case, or does it believe that it will be the case?

John Swinney: No detailed information—or any information—has come to me on that point. I think that we discussed the issue at the Finance Committee meeting on the Isle of Arran, in your constituency, when I set out some of the scenarios that would be relevant. For a £10 million transaction, the increase in the tax charge would be £40,250, which is 0.4 per cent of the total transaction value. I consider that a change of that level is at the margins of the assessment of such a transaction, and I am not aware of any information that in any way contradicts what I said to you when we discussed the issue in your constituency.

The Convener: Thank you. I will now open out the session to colleagues. The deputy convener will be first, followed by Richard Baker.

John Mason: Good morning, cabinet secretary. The Chartered Institute of Taxation commented on sub-sale development relief and the term "significant development"—if a significant development happens within five years, tax is not payable. Are you happy that the term "significant development" will not lead to a lot of wrangles and court cases?

12:00

John Swinney: We have set out a definition of "significant development" in paragraph 7 to schedule 10A of the order:

"significant development" means development that is significant having regard to, among other things, the nature and extent of the subject-matter of the qualifying sub-sale and to the market value of that subject-matter."

There are a couple of points that I would make about that. The first is that we have defined as

clearly as we can what we would consider to be significant. That takes into account the market value of the subject matter and the nature and extent of the development. In an example in which planning consent had been given for the building of 100 houses in a development and only one house had been built, that would clearly fail the test of significant development. If the committee will forgive me, however, I will not start to police where the line should be deployed.

That brings me to my additional point. The wording of the definition says:

"having regard to, among other things".

That is designed to give flexibility to Revenue Scotland to look reasonably and credibly at a situation. If 99 houses had been built, I would say—without creating a precedent in the committee today—that that would feel to me as if significant development had been undertaken; if only one had been built, clearly that would not be the case. Revenue Scotland would have to make a judgment in that range, taking into account market conditions and other factors.

We do not wish to prescribe, and I think that prescription is the next place that we could go to in that definition. We have tried to give as much clarity as possible.

Of course, these matters will ultimately be subject to debate and determination by Revenue Scotland, but I think that we have set out enough detail to inform that judgment.

John Mason: CIOT made another point that is linked to that. It asked whether, if there were external events that were outside the control of the developer during the five years, it would be able to apply for an extension of that period.

John Swinney: No, it could not.

John Mason: Right.

The Convener: Richard Baker has a question.

John Mason: Sorry, convener, could I ask another question?

The Convener: I am sorry; I thought that you were winding up, but in fact you were just getting fired up.

John Mason: That was just my introductory bit.

The question of competitive advantage or disadvantage has been raised by a number of witnesses. I got a slightly confusing picture from the witnesses, because some seemed to say that the tax was extremely important and would affect a development going forward and others said that the tax was only one part of it. How significant do you see LBTT being with regard to whether a residential development goes ahead? Do you think

that it is other factors that will cause a development to go ahead?

John Swinney: LBTT will be one factor in the judgments that are made. I do not think that it will be the central factor; I think that it will be a marginal factor. Much more significant will be questions of the capacity to raise the capital to fund the development and, implicit in all of that, how likely it is that that capital will have to be held on to before it is replenished by sales. All of those factors are much more material to the judgment about whether a development proceeds than the rate of LBTT.

In principle, LBTT is a marginal consideration in whether developments are taken forward. It is certainly not a central factor. In terms of where we are more competitive or less competitive—to use that terminology—the difference in the levels that we are setting out is a marginal factor in the judgments that would be made.

John Mason: We had evidence from SFHA about mid-market rent. Most of us in the committee are sympathetic to the concept of mid-market rent, whereby it is a bit more affordable than the rent would be in the completely private sector. The suggestion was that, in order to encourage mid-market rent, there should be further reliefs to those who are seeking to make that kind of development. I wondered whether, if we are helping that kind of sector, it is better to do it by tax relief or by a direct grant.

We have had a similar debate on whether to encourage eco-friendly housing by relief or subsidy. I am not asking you to commit to supporting mid-market rent, but if we were to do it, what would be the best way of doing it?

John Swinney: I have read the SFHA evidence and I saw some of the dialogue that the committee had with it this morning. Obviously, the Government will always give consideration to propositions and suggestions that are advanced, but I would apply a couple of caveats to that.

One is that I was clear with Parliament and the committee that we did not want to create a relief-strewn bill, if I could call it that. I felt that, throughout the process of the bill, I had firm support from the committee in the judgments that I was arriving at. I was clear with the committee that, when relief was required, genuinely necessary and had firm purpose, it should be granted, but we should not replicate all the reliefs that were available under SDLT, for example, because that would simply replicate some of the difficulties and challenges that existed with SDLT on tax compliance.

We have been going through a debate in the United Kingdom on tax compliance and avoidance. As the committee knows, the

Government has decided to take the strongest possible stance on tax avoidance. Of course, the more reliefs that we have, the more ground is opened up to potential practices that we might not have envisaged at the conception of the legislation.

Therefore, one caveat is that I am naturally cautious about extending reliefs. That is why, when I was in front of the committee at earlier stages, I was reluctant to go into the territory of sub-sale relief. I have been persuaded of the merits of that argument by the industry and we have gone into that in a fashion that I think is consistent with the legislation. We have to be careful about how much we open up the process.

The second caveat is the point that Mr Mason raised that, when we are trying to solve a challenge such as improving the availability of mid-market rent properties, we need to take the most effective intervention to do that. We should not take another intervention because a piece of legislation happens to be in front of Parliament and it seems a good idea to advance the issue, when that may not be the most effective mechanism for stimulating mid-market rent properties.

I would much prefer us to take forward a policy on a more direct financial support mechanism. For example, the national housing trust, which aims to deliver properties for mid-market rent, has been very successful. It involves a very low level of Government financial support and it relies on the private market, but it has been very successful in the delivery of mid-market rent properties. When we have such mechanisms, we should do all that we can to ensure that they are successful.

John Mason: That is great. Thank you.

The Convener: Have you definitely finished now? [*Laughter.*]

John Mason: Yes.

The Convener: We will move to questions from Richard Baker.

Richard Baker: My questions also relate to multiple dwellings relief and the evidence from the Scottish Federation of Housing Associations on homes for mid-market rent, which enable more people to get the housing that they need, so that is a big issue for the progressive approach. We welcome the fact that you have sought a progressive approach through the legislation. However, in three areas, the SFHA says that the changes that are being made are detrimental to schemes for mid-market rent. The costs for housing associations will be higher than those under stamp duty for transactions on homes for mid-market rent, for the purchase of land through

back-to-back sales from a developer and for the purchase of multiple properties.

Given that you said that you want the order to bring more progressivity to the provisions, why did you not ensure that such an important scheme for housing provision would not have a detrimental impact and would, preferably, encourage more mid-market-rent homes to be built? There seems to be a danger that such developments would be largely discouraged if the order goes through as proposed.

John Swinney: I challenge some of the evidence that has been put in front of the committee. For example, Mr Baker posits a particular scenario of land purchases from a developer, but that is one scenario. It does not have to be the scenario by which land becomes available to or is accessed by a housing association to develop mid-market-rent properties.

We have to be careful about the positing of particular scenarios that become arguments for suggesting that somehow a disadvantage is being created, because Parliament has taken the general view that it wants to minimise the risk of tax avoidance. We have to be careful about some of that evidence.

The Government has set out a progressive approach to the delivery of the policy. It is designed to ensure that the payment of tax relates to the value and significance of developments. Some of the issues that Mr Mason raised are more material to whether a development takes its course than is the assumption that an action under LBTT—as I said in my response to the convener, that will be a marginal factor—has any effect on the decisions about taking forward a development.

Richard Baker: The SFHA gives a clear example of buying 20 properties. The impact of LBTT on that might be marginal but, under the provision that you put forward, the cost to the housing association for the purchase of those properties will be greater than that under stamp duty. That seems to be going backwards, not forwards, in encouraging such developments.

John Swinney: LBTT will be a marginal factor in all this. I made the point to the convener that that is all in the marginal territory.

The tax charge might be higher not because of the absence of a relief but because of the proposed rate of 4.5 per cent. The committee has got to be careful where it goes here. If the committee believes that we should start to litter the legislation with reliefs—to provide exemptions—it will open up opportunities for tax avoidance. The committee would run that danger if it followed that line of argument.

We have related the rates much more closely to the size of transactions to encourage and motivate more activity by having a more competitive rate for the lower end of property transactions. That means that there is a higher rate on larger property transactions. If the committee tried to temper that by putting a relief in place, I caution it that it would be going into the territory that it expressly tried to avoid when it scrutinised the legislation some months ago.

Richard Baker: I was not on the committee at that point, so it seems to me that I have carte blanche to litter the thing with reliefs as much as I want. However, I am not suggesting that; what I suggest is on a specific issue. Surely it is not beyond the wit of the Scottish Government, on an issue that involves a housing association—a clearly defined entity in law, which it is difficult to pretend to be, as we heard earlier—to ensure that the legislation is not just beneficial to such purchases but not detrimental to them, compared with the provisions that were in place under stamp duty.

John Swinney: That proposition can be advanced if people wish to advance it, but I am simply setting out to the committee the issues that it would have to consider if it wished to advance those arguments.

12:15

Richard Baker: The Scottish Federation of Housing Associations says that there would be a strong case for an exemption from LBTT for housing associations that pursue such developments. That would be an important way of encouraging their development and it would not be a huge cost to the Scottish Government, given that it would apply in a specific area. What consideration have you given to that proposal? Has there been any dialogue with housing associations on it? I understand your caution, but would you be prepared to consider the idea for the future?

John Swinney: As I said at the outset, the Government is always prepared to consider such issues. I will certainly consider the proposal. In the evidence that the committee heard this morning, no figure was given for the proposal's financial impact. If we were talking about an exemption rather than just a relief, that would affect the estimates that I make about the tax take. That money has to come from somewhere.

The judgments that are being arrived at are about the tax charge that it is appropriate to apply to particular developments. There is flexibility in the legislation to determine whether the tax charge should be varied for one organisation or another. I am certainly happy to discuss that with the SFHA.

The Convener: Mark McDonald has a brief supplementary.

Mark McDonald: Gavin Brown can go first.

Gavin Brown: The cabinet secretary mentioned that the Scottish Fiscal Commission is doing some work on forestalling. Is there a timescale for that work to be completed and published?

John Swinney: The discussions are on-going. We are carrying out further research work based on what the Fiscal Commission has requested of us. The commission will come to its own judgment; that is not a matter for me to get involved in. It would have to set out the timescale for that.

Gavin Brown: So there is no specific timescale.

John Swinney: When the Chief Secretary to the Treasury appeared before the committee, he indicated that he expected the discussions on forestalling to go on into the start of the next financial year. That is later than I would like, but it takes two to have a negotiation. We will carry on the work that is being undertaken with the commission, but the management of that work and any determination that is made about it are matters for the commission.

Gavin Brown: When you gave evidence to us in December, just before the autumn statement, your view was that the LBTT rates that you were setting would have no behavioural impact. We then had the autumn statement, which changed things. Is it still your view that, had we not had the autumn statement, there would have been no behavioural impact at all? Do you put all the forestalling down to the autumn statement, or do you accept that some of it was down to the LBTT rates being different from the existing stamp duty rates?

John Swinney: Individuals base their judgments about property transactions on a wide variety of factors. I do not think that the introduction of LBTT has led to a particularly significant behavioural response, but it is clear that the autumn statement had an additional impact on the market. That brought further uncertainty to the marketplace, which I suspect will be reflected in forestalling.

Gavin Brown: When you were asked about the impact so far, you said that the evidence that you had came from the quarterly house price index, which was published in February and related to quarter 4 of 2014. I was a bit surprised by that. Given that the Scottish Government deals regularly with Registers of Scotland, do you not have figures for January?

John Swinney: I said that there is no published data. When it comes to the official output of Registers of Scotland, the published data is all that I can deal with. I take a close interest in the

property market's performance. I look at a range of information sources, but nothing indicates to me that there is any evidence to substantiate the claim that there has been a change in performance as a result of the introduction of LBTT.

Gavin Brown: We heard evidence earlier from witnesses who believe that, as a consequence of LBTT—if the proposed rates are set—activity at the higher bands of the property market will be depressed, which would have a detrimental impact on other steps of the ladder. That is their view; I assume that the Scottish Government takes a different view, but if they are correct—if that scenario plays out post-April—will the Scottish Government act?

John Swinney: In what respect?

Gavin Brown: If the Scottish property market is hit detrimentally as a consequence of the rates that you have set and if there is a different result from that in the north of England or the midlands, for example—I would treat London separately—will the Scottish Government act and change the rates to help the market to function?

John Swinney: No.

Gavin Brown: No?

John Swinney: No.

Gavin Brown: Okay. I presume that the rates will be reviewed at budget time each year.

John Swinney: That is correct.

Gavin Brown: So your position is that you would do nothing prior to that.

John Swinney: That is correct.

The Convener: Mark McDonald is next.

Mark McDonald: My question was dealt with by Gavin Brown—he asked what I was going to ask about possible impacts. That is what I get for saying that he could go first.

The Convener: Is it that great minds think alike or fools never differ? I am not quite sure.

Motion moved,

That the Finance Committee recommends that the Land and Buildings Transaction Tax (Sub-sale Development Relief and Multiple Dwellings Relief) (Scotland) Order 2015 [draft] be approved.—[*John Swinney.*]

Motion agreed to.

Motion moved,

That the Finance Committee recommends that the Land and Buildings Transaction Tax (Tax Rates and Tax Bands) (Scotland) Order 2015 [draft] be approved.—[*John Swinney.*]

The Convener: The question is, that motion S4M-12346 be agreed to. Are we agreed?

Members: No.

The Convener: There will be a division.

For

Baker, Richard (North East Scotland) (Lab)
Chisholm, Malcolm (Edinburgh Northern and Leith) (Lab)
Gibson, Kenneth (Cunninghame North) (SNP)
Mason, John (Glasgow Shettleston) (SNP)
McDonald, Mark (Aberdeen Donside) (SNP)
Urquhart, Jean (Highlands and Islands) (Ind)

Against

Brown, Gavin (Lothian) (Con)

The Convener: The result of the division is: For 6, Against 1, Abstentions 0.

Motion agreed to.

The Convener: We will suspend the meeting for one minute to allow for a changeover of witnesses.

12:22

Meeting suspended.

12:23

On resuming—

**National Health Service Pension Scheme
(Consequential Provisions) (Scotland)
Regulations 2015 [Draft]**

**Teachers' Pensions Scheme
(Consequential Provisions) (Scotland)
Regulations 2015 [Draft]**

**Police Pensions (Consequential
Provisions) (Scotland) Regulations 2015
[Draft]**

**Firefighters' Pension Scheme
(Consequential Provisions) (Scotland)
Regulations 2015 [Draft]**

The Convener: The next item on the agenda is evidence from the cabinet secretary on four statutory instruments relating to public service pensions. The cabinet secretary is joined for this item by John St Clair, Chad Dawtry and Jim Preston from the Scottish Government. I invite the cabinet secretary to make an opening statement explaining the instruments.

John Swinney: The Scottish Government is currently implementing reforms of public service pension schemes that are required by the United Kingdom Parliament's Public Service Pensions Act 2013. The changes in the instruments that the committee is considering today form part of those reforms. The Scottish ministers have executively devolved responsibility for the schemes. Overall, occupational pension policy remains reserved.

The key terms of the reforms and the timetable for them were set out by the UK Government in the 2013 act. That act also requires instruments that amend primary legislation to be considered under the affirmative procedure.

As the committee knows, in effect, the reforms will close the existing pension schemes on 31 March 2015. That means that the new schemes and important transitional protections for pension rights that have already been built up to that point need to be in place from 1 April 2015.

The instruments before the committee make necessary consequential modifications to the Pension Schemes Act 1993 and the Finance Act 2004 to ensure that the national health service, teachers, police and firefighters pension schemes work as intended within the complex wider framework of pensions and tax law, and that pension scheme members who transfer to the new schemes retain accrued pension rights.

In brief, the proposed modifications that are set out in parts 2 to 4 of each set of regulations are common to each of the four schemes. Additional provisions are set out in part 5 of the relevant instruments for the teachers, police and firefighters schemes.

Under part 2 of each of the instruments, modifications are made to regulations that govern the contracting-out of the additional state pension. Although contracting out will end in April 2016, the new schemes remain contracted out until then. The changes that are introduced in part 2 reflect the UK Government's simplified contracting-out election process for the new schemes for this financial year.

Part 3 makes modifications to the 1993 act, so that members who move from the current schemes to the 2015 schemes are not wrongly treated as deferred members of their existing schemes. Modifications under part 3 ensure that pension benefits that scheme members have accrued to date are revalued correctly, and not as if those individuals were deferred members. A scheme member's right to a cash-equivalent transfer value, to a refund of contributions or to a cash transfer sum applies only when they leave the new scheme. Guaranteed minimum pension safeguards operate as intended, by modifying anti-franking provisions. Those modifications mean that, for those purposes, such individuals do not cease to be active members of their existing scheme until they leave their new scheme.

Part 4 makes modifications to the 2004 act to ensure that members with service in both pre-2015 and post-2015 pension schemes who retire with an ill-health pension do not face unintended tax consequences.

Part 5 of the instruments that deal with the police and firefighters schemes modifies the 1993 act in line with the requirements of the 2013 act to permit active and deferred scheme members to have different pension ages. Part 5 of the regulations that deal with the teachers scheme is designed to reflect, in the short-service provisions of the 1993 act, that different rates of actuarial reduction for active and deferred members are provided for members with a normal pension age above 65.

The changes are very technical modifications to wider pensions legislation. They seek to ensure that teachers, NHS workers, police officers and firefighters get the pensions that they expect without any unexpected effects as a result of potential conflicts with wider pensions and tax law.

The Convener: I have no questions, but the deputy convener does.

John Mason: I have the privilege of being on the Delegated Powers and Law Reform Committee, so I have been at both ends of the discussion. The DPLR Committee's convener, Nigel Don, has written to the cabinet secretary and to this committee about the timing of the laying of the regulations. In particular, he makes the point that the new scheme regulations—other than those for the teachers pension scheme—were laid after the regulations that make consequential provision relating to the schemes. That has caused, and could cause, a bit of a problem. Could you comment on that?

John Swinney: I deeply regret the fact that the Finance Committee's deputy convener is on the Delegated Powers and Law Reform Committee—the issue has flushed that out.

There is indeed an issue here, and although the Government is trying to operate as helpfully as possible, I accept that the situation that we face is not ideal. Essentially, the instruments that are before the Finance Committee today make the required alterations to primary legislation. Those alterations are provided for but they must be undertaken under the affirmative procedure.

The issue became apparent towards the end of last year, and affects pieces of legislation under which there are substantive regulations that the Delegated Powers and Law Reform Committee did not have sight of until after it had sight of the present modifications.

My reason for going through that explanation is basically to say that the regulations that are before the committee today address problems that arose from the interaction of new legislation with old legislation and which were not foreseen when the Public Service Pensions Bill was considered in 2012 and 2013. The provisions are in two quite different spheres of impact.

With regard to the pace of development, we had been working on the substantive regulations and expected them to take their course, but new issues emerged that required the laying of additional instruments.

That is about the best that I can do.

12:30

John Mason: Was the timing under the Scottish Government's control, or was there a timing issue with the UK Government?

John Swinney: The timing of the substantive scheme regulations was a product of UK legislation, but the Scottish Government had to act in a way that ensured that those regulations were in place so that they would be effective from 1 April 2016. In that respect, we have had to take action to get the regulations in place. Subject to parliamentary consent, they will be in place according to the timescale that we envisaged.

The difficulty has arisen as a result of interaction between new legislation and old legislation, which has flushed out some very technical issues that have had to be addressed in the regulations. That is why the regulations have come before the committee in the sequence that they have.

John Mason: One example—which I accept is fairly minor—is that different terms have been used in the different regulations. Regulation 13 in the draft Firefighters' Pension Scheme (Consequential Provisions) Scotland Regulations refers to an "upper tier ill-health pension", whereas elsewhere the word "higher" is used. That is not ideal. Can we have an assurance that it will not happen again?

John Swinney: My officials are meeting the clerking team from the Delegated Powers and Law Reform Committee after this meeting of the Finance Committee to talk through all the issues that have arisen. Mr Mason is correct that both the Minister for Parliamentary Business and I have corresponded with the convener of the DPLR Committee. I would not for a moment suggest that the arrangements with which we are wrestling today are ideal, and I would be very keen to ensure that we did not find ourselves in the same circumstance again.

The issue has arisen as a result of the emergence of new material, and the position had to be rectified to ensure that pensioners maintain existing rights from 31 March into 1 April, which would not have been the case unless we had laid the instruments that are before the Finance Committee today.

John Mason: Okay—thank you.

The Convener: There are no further questions, so I ask the cabinet secretary to move motions S4M-12363, S4M-12364, S4M-12365 and S4M-12366.

Motions moved,

That the Finance Committee recommends that the Firefighters' Pension Scheme (Consequential Provisions) (Scotland) Regulations 2015 [draft] be approved.

That the Finance Committee recommends that the Police Pensions (Consequential Provisions) (Scotland) Regulations 2015 [draft] be approved.

That the Finance Committee recommends that the Teachers' Pension Scheme (Consequential Provisions) (Scotland) Regulations 2015 [draft] be approved.

That the Finance Committee recommends that the National Health Service Pension Scheme (Consequential Provisions) (Scotland) Regulations 2015 [draft] be approved.—[*John Swinney.*]

Motions agreed to.

The Convener: The committee will now publish a short report to Parliament setting out our decisions on all the statutory instruments that we have considered today. At the start of the meeting, the committee agreed to take the next item in private, so I thank the witnesses for their contributions today and close the public part of the meeting.

12:34

Meeting continued in private until 12:44.

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