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Scottish Budget 2017

Finance Secretary Derek Mackay delivered the 2018/19 Scottish Draft Budget on Thursday 14 December 2017 setting out the Scottish Government's financial and tax plans. The announcement had been timed to take place after Chancellor of the Exchequer Philip Hammond delivered the UK Budget on 22 November 2017 in order to avoid 'fiscal and economic uncertainty'.

This letter highlights the Scottish Government's income tax changes which are due to take effect from April 2018 and sets out further proposals for Land and Buildings Transaction Tax, Air Departure Tax and VAT.

Scottish resident

Following the introduction of separate Scottish income tax bands (and rates) it has been necessary to define and identify a Scottish taxpayer. A Scottish taxpayer is someone who is UK resident for tax purposes and has one place of residence which is in Scotland.

Individuals who have more than one place of residence in the UK need to determine which of these has been their main place of residence for the longest period in a tax year. Individuals who cannot identify a main place of residence will need to count the days they spend in Scotland and elsewhere in the UK. If they spend more days in Scotland, they will be a Scottish taxpayer. More detail on the rules are set out in the Appendix.

Scottish Income tax

The Scottish Government has the power to set the rates and bands of income tax (other than those for savings and dividend income) which apply to Scottish resident taxpayers.

Since 6 April 2016 the rates and bands of Scottish income tax have been frozen at 20% and the Scottish higher and Scottish additional rates at 40% and 45% respectively. For 2017/18 the higher rate threshold in Scotland is £43,000 whilst the threshold in the rest of the UK is £45,000. This means that a Scottish higher rate taxpayer will pay £400 more tax in 2017/18 than a UK higher rate taxpayer, being £2,000 at the marginal rate of 20%.

In the 2018/19 Draft Budget the Finance Secretary announced two new income tax bands: a starter rate of 19% for the first £2,000 of income above the personal allowance and a 21% intermediate rate for income between £24,000 and the higher rate threshold. In addition, whilst the basic rate will be frozen at 20% the higher and additional (to be renamed 'top') rates of tax will increase by 1% to 41% and 46% respectively.

For 2018/19 the rates and tax bands applicable to Scottish taxpayers on non-savings income will be as follows:

Scottish Bands	Band name	Scottish Rates
Over £11,850* - £13,850	Starter	19%
Over £13,850 - £24,000	Basic	20%
Over £24,000 - £44,273	Intermediate	21%
Over £44,273 - £150,000**	Higher	41%
Over £150,000**	Top	46%

* assuming the individual is entitled to a full UK personal allowance

** the personal allowance will be reduced if an individual's adjusted net income is above £100,000. The allowance is reduced by £1 for every £2 of income over £100,000

The UK higher rate tax point for 2018/19 has been set at £46,350 (for those entitled to the full UK personal allowance) and the tax rates for non-savings and non-dividend income have been maintained at 20%, 40% and 45% respectively.

For 2018/19 Scottish taxpayers with employment income of £26,000 will pay the same amount of income tax as those with the similar income in the rest of the UK. For higher earners, with pay of £150,000, a Scottish taxpayer will pay an extra £1,770 of income tax than those on similar income in the rest of the UK.

Employers

Employers should be aware that if an employee is classed as a Scottish taxpayer then a special PAYE code (S) will apply and this will be notified to employers and pension providers by HMRC where appropriate.

An employer does not have to make any assessments on taxpayer status. Employers should not change a tax code unless advised to do so by HMRC. Employers of Scottish taxpayers will need to ensure their payroll software has the capability to deal with S codes.

It is important that employers remind their employees of the importance of keeping HMRC informed of their correct address details as this information is crucial in determining whether or not they are a Scottish taxpayer. Taxpayers can check and update their address details through their online Personal Tax Account. For those individuals who have not yet used their account they can register at www.gov.uk/personal-tax-account.

Land and Buildings Transaction Tax and First-Time Buyer Relief

The Scottish Government announced that they will introduce a new Land and Buildings Transaction Tax (LBTT) relief for first-time buyers of properties up to £175,000. The relief will raise the zero tax threshold for first-time buyers from £145,000 to £175,000, and according to the Scottish Government 80% of first-time buyers in Scotland will pay no LBTT at all. The Scottish Government also announced that first-time buyers buying a property above £175,000 will also benefit from the relief on the portion of the price below the threshold.

The Scottish Government announced that they will launch a consultation on the policy before introducing the first-time buyer relief in 2018/19. The relief for first-time buyers paying Stamp Duty Land Tax on first homes in the rest of the UK was introduced from 22 November 2017.

Delay to the introduction of Air Departure Tax

As part of the UK Autumn Budget on 22 November 2017, UK and Scottish Government Ministers have agreed to delay the introduction of Air Departure Tax (ADT) in Scotland until issues have been resolved regarding the tax exemption for flights departing from Scottish Highlands and Islands airports..

Air Passenger Duty (APD) will continue to apply to flights departing from Scottish airports, and HMRC will continue to have responsibility for administering APD in relation to Scottish flights.

ADT was expected to replace APD from 1 April 2018 for flights departing from Scotland. The Air Departure Tax (Scotland) Act 2017 introduced the new tax, the payment of which will be determined by the passenger's final destination and class of travel.

ADT is expected to work in a very similar way to APD, however, the administration will be slightly different in that the air operators will be required to complete quarterly rather than monthly returns. Revenue Scotland will also be changing the way the tax is collected via a digital service (Scottish Electronic Tax System - 'SETS').

VAT assignment

From 2019/20 half of the VAT from Scottish receipts will be assigned to Revenue Scotland. Currently there has been no further information as to the precise method of assignment.

APPENDIX

Scottish Residence

Determining an individual taxpayer's status

Whether an individual is deemed to be Scottish for the purposes of paying Scottish income tax rates will depend on where they live, or reside, during the course of the tax year.

For the vast majority of individuals, the question of whether or not they are a Scottish taxpayer will be a simple one – they will either live in Scotland and thus be a Scottish taxpayer, or live elsewhere in the UK and not be a Scottish taxpayer. Scottish taxpayer status is dependent upon being UK resident for tax purposes - a non-UK resident cannot be a Scottish taxpayer.

Scottish taxpayer status is applicable for an entire tax year, and complications could arise where an individual's residential situation is less straightforward. A series of tests exists in order to help determine taxpayer status in such cases.

The rules governing residence are complex, but an individual who is resident in the UK for tax purposes will be a Scottish taxpayer if they satisfy one of the following tests:

A. They are a Scottish Parliamentarian

B. They have a 'close connection' to Scotland, either through:

1. having a **single place of residence**, which is in Scotland, or
2. where they have more than one place of residence, having their '**main place of residence**' in Scotland for at least as much of the tax year as it has been in any other part of the UK

C. Where no 'close connection' can be established, it will be necessary to apply '**day counting**'.

Main place of residence

As set out above, for those who have more than one place of residence in the UK it is necessary to determine whether they have a 'close connection' to Scotland or another part of the UK.

Central to this process is establishing which has been their 'main place of residence' for the longest amount of time during the tax year. (Note that the criteria are not the same as those governing the election of a main residence for capital gains tax purposes.)

HMRC guidance includes a range of potential indicators to assist with the process of determining a main place of residence for the purposes of Scottish income tax. These include such areas as:

- the presence of other family members
- where an individual's children go to school
- correspondence address for household bills, credit cards, etc
- how residences are furnished
- where the majority of their possessions are kept
- main residence for council tax records
- voting registration address
- local parking permits
- club memberships
- evidence of social activities, such as dining out locally
- address for the registration and insurance of an individual's car
- GP/dentist/optician registrations.

Counting the days

Where it is not possible to identify a 'close connection' to Scotland or any other part of the UK by means of an individual's place of residence, it will be necessary to apply day counting – that is, calculating the number of days spent in Scotland compared with those spent elsewhere in the UK.

Where an individual spends at least as many days in Scotland as the rest of the UK, they will be deemed a Scottish taxpayer. A 'day spent' refers to where they are at midnight on any given day (unless they are 'in transit').