Scottish Taxation

Overview

The UK has devolved some tax powers to the Scottish Parliament. In overview-

- Some income tax powers have been transferred to Scotland. These are detailed below.
- On 1 April 2015, SDLT was replaced in Scotland by Land and Buildings Transaction Tax (LBTT); Scottish Landfill Tax applied from the same date.
- Scottish Air Departure Tax will start in April 2018.
- Aggregates Levy is also to be devolved to Scotland.

There are no proposals to devolve corporation tax, inheritance tax or VAT. Some of the UK's VAT receipts are allocated to the Scottish Budget in place of part of the block grant.

Income tax: Scottish Rate of Income Tax for 2016/17

From April 2016, a Scottish Rate of Income Tax (SRIT) was introduced. The SRIT operated in the following way-

- Each of the (UK) rates of income tax (the basic rate, higher rate and additional rates- currently 20%, 40% and 45%) was reduced by 10%.
- The UK rates, as reduced, were then increased by the SRIT as determined by the Scottish Parliament.

For 2016/17, SRIT was set by the Scottish Parliament at 10%, and so the rates of income tax were the same in Scotland as in the rest of the UK.

Income tax: general position for 2017/18 onwards

Following the Smith Commission, the Scotland Act 2016 granted additional powers to the Scottish Parliament over income tax. Scotland was allowed to set its own rates of tax and tax bands.

Scottish rates for 2017/18

The Scottish Government has proposed to set the Scottish rates of tax in line with those in the rest of the UK, but to start the 40% rate at £43,430 rather than £45,000 which will apply elsewhere in the UK. All other thresholds will be identical to those in the rest of the UK. The maximum annual cost to a Scottish taxpayer over others is £314.

Scottish taxpayers

Scottish income tax applies to “Scottish taxpayers”. In outline, a Scottish taxpayer is a UK resident individual whose place of residence is in Scotland for the majority of the tax year.

Income affected by Scottish rates

The rates of income tax for Scottish taxpayers-

- applies to income from employment, self-employment and pensions and to rental income.

- does not apply to savings and dividend income.

UK only income tax powers

The UK Parliament continues to set-

- the level of the personal allowance.
- the rates of tax on savings and dividend income for both Scottish and non-Scottish taxpayers.
- the rates of capital gains tax.
- tax reliefs and the general structure of income tax and capital gains tax.

Points to note

Some points to note are-

- HMRC continues to administer income tax in Scotland as well as other parts of the UK. It applies the Scottish rates to Scottish taxpayers on their non-savings income and UK rates to the savings income of Scottish taxpayers.
- There is no double tax involved. For instance, the tax rules will not attempt to identify Scottish source income of non-Scottish taxpayers, nor non-Scottish income of Scottish taxpayers. Each UK resident will be either a Scottish taxpayer or not for a tax year, and this will be the sole determinant of what rates apply to that individual for that year.
- The Statutory Residence Test (SRT), which determines whether an individual is UK resident or non UK resident for a tax year, or part of a tax year, is unaffected by the "Scottish taxpayer" test. An individual with a Scottish connection who is deemed to be UK resident under the SRT would then need to determine whether he or she was a Scottish taxpayer.

Additional comments on the Scottish Rate of Income Tax

The possibility of a difference between the basic rate of tax in Scotland and elsewhere in the UK raises practical difficulties in a number of areas. The following is a summary of the currently intended approach, as announced by HMRC-

- *Pension tax relief: occupational schemes*. Under net pay arrangements for occupational schemes, pension contributions are deducted from pay before income tax is calculated under PAYE. This mechanism will give tax relief for Scottish taxpayers at Scottish rates.
- *Pension tax relief: other schemes*. Under other arrangements such as personal pensions and SIPPs, contributions are treated as paid net of basic rate tax. The pension scheme reclaims the tax from HMRC; higher rate and additional rate taxpayers can reclaim further tax relief through self-assessment. On the introduction of Scottish rate tax it is likely, as an interim measure that pension schemes will continue to reclaim tax at UK basic rate for Scottish taxpayers. HMRC will make suitable adjustments for Scottish taxpayers through self-assessments or PAYE.
- *Charitable gifts.* Gifts to charities under Gift Aid are deemed to have been made under deduction of basic rate tax. The charity can claim repayment of the tax deducted; the donor can claim any further tax relief if he is liable to the higher or additional rate of tax. Charities will continue to claim repayment at UK basic rate, irrespective of whether the donor is a Scottish taxpayer; Scottish taxpayer donors will claim any further tax relief by reference to Scottish rates of tax.

- *Interest in possession trusts*. Income from interest in possession trusts is paid under deduction of basic rate tax. The deduction will be made at the Scottish basic rate of tax where the beneficiaries are Scottish taxpayers. Similar principles will apply to income from the estates of deceased individuals.
- *Income from Real Estate Investment Trusts (REITs) and Property Authorised Investment Funds (PAIFs).* Some income from REITs and PAIFs are treated for tax purposes as property income. These property income distributions are made under deduction of basic rate tax. The deduction will be made at the UK basic rate for all recipients. The income will be chargeable to Scottish rates if the recipient is a Scottish taxpayer.

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