GLAECONOMICS

Working Paper 81

Stamp duty in London
A publication for the London Finance Commission

Emma Christie

January 2017

MAYOR OF LONDON

copyright

Published by
Greater London Authority
City Hall
The Queens Walk
London SE1 2AA

www.london.gov.uk
Tel 020 7983 4922

Minicom 020 7983 4000

ISBN 978-1-84781-639-9

Cover photograph

© Shutterstock and Daryl Rozario

For more information about this publication, please contact:

GLA Economics

Tel 020 7983 4922

Email glaeconomics@london.gov.uk

Contents

Executive summary

In 2013, the London Finance Commission (LFC) recommended the devolution of the full suite of property taxes – including council tax, business rates and stamp duty – to the capital. In light of the 2016 recommissioning of the LFC by the Mayor of London, this paper seeks to assist the Commission by investigating and suggesting potential improvements to the stamp duty land tax (SDLT) system in London.

SDLT is a transaction tax that is payable on the purchase of property or land in England, Wales and Northern Ireland. It is based on a system of banding, where higher property values attract a higher rate of tax. Following changes in December 2014, SDLT now operates on a 'slice' nature whereby the tax rate is only applied to the proportion of the property value within the band. During 2015-16, SDLT raised £3,370 million for residential properties and £1,395 million for non-residential properties in London. This represents 46.7 per cent and 42.7 per cent of the total English yields respectively, meaning that London contributed more stamp duty than any other UK region.

However, there are a number of issues with stamp duty. As the tax is linked to property values, the tax yield is invariably linked to the economic cycle. This volatility and unpredictability in the tax take makes stamp duty volatile as a funding stream and therefore, arguably, an unsuitable finance source for projects such as infrastructure investments. Stamp duty also represents a lump sum cost associated with buying a house and as such, reduces the incentive for household mobility, as it raises the cost of moving. Ultimately, this leads to a more inefficient use of the housing stock than would have otherwise been the case. Academic studies have suggested that the previous SDLT system (before December 2014) reduced household mobility by 2-3 per cent at the £250,000 band. Moreover, having previously been first introduced back in the 1600s, the rationale for stamp duty – particularly non-residential stamp duty that effectively taxes an input to the production process – is weaker in the modern era.

Given these issues, the Commission's recommendation for the devolution of SDLT to London government provides an opportunity to implement improvements to the tax, as was the case when the tax was devolved to Scotland and Wales. There are a variety of potential options for reform discussed in this paper, including: setting up an investment fund to mitigate some of the volatility in the yield; introducing a flat stamp duty tax rate; replacing stamp duty with council tax or capital gains tax; and – more radically – introducing a land value tax (LVT).

1 Introduction

GLA Economics is producing a series of research papers examining options for greater fiscal devolution in London to inform the second London Finance Commission (LFC2). The research series examines a number of areas including council tax and a possible new tourism levy, among others. As part of this wider project, this paper focusses on SDLT in London.

In May 2013, the LFC published its report arguing for greater fiscal independence for the capital in order to invest and cater for growth[1]. The report recommended that this could be achieved by relaxing restrictions on borrowing for capital investment within prudential rules, and devolving certain revenue streams, including the full suite of property taxes. Specifically, the Commission[2] stated:

> *"The full suite of property taxes (council tax, business rates, stamp duty land tax, annual tax on enveloped dwellings and capital gains property development tax) should be devolved to London government, which should have devolved responsibility for setting the tax rates and authority over all matters including revaluation, banding and discounts."*

With this in mind, this paper looks at the SDLT system in London, and how it has evolved over recent years. In principle, stamp duty is payable on any documents transferring assets to new owners, but most commonly refers to property. Despite changes to improve the tax, there remain a number of issues with stamp duty, as will become apparent later in this paper. Fiscal devolution thus provides an opportunity to further reform stamp duty such that it works more effectively, especially in a London context.

The following section of this paper provides some background to the current stamp duty system and discusses some of the most recent reforms. Chapter 3 then examines some of the issues associated with the tax, while Chapter 4 provides some examples of how stamp duty (or its equivalent) works in other global cities. Finally, Chapter 5 presents some potential options for reform to the SDLT system, followed by the conclusions.

---

[1] Raising the Capital, The report of the London Finance Commission, May 2013.
[2] Raising the Capital, The report of the London Finance Commission, May 2013, pg. 11.

2 Background

Stamp duty is a historic tax dating back to the late 1600s on the documents that recognise the ownership and transfer of property. Here 'property' covered any asset or item that was capable of being owned, rather than solely buildings[3]. The Stamp Act 1891 limited the registration of property where documents lacked the appropriate stamp, thus requiring owners to pay the tax in order to have their property title acknowledged by the courts[4].

SDLT was introduced on 1 December 2003 as a replacement of stamp duty on documents related to land transactions. It also changed focus away from the actual documents of ownership to the transaction itself. Meanwhile, stamp duty reserve tax – which was introduced in 1986 – applied to electronic transactions in securities.

Stamp duty land tax prior to December 2014

Prior to December 2013, the SDLT system in the UK was designed like 'slabs', in that a higher tax rate was payable on the whole value of the property once the purchase price exceeded certain thresholds. Although various band thresholds and tax rates have been used over the years, between 2006 and 2014, generally, residential properties valued at more than £125,000 and non-residential properties valued at more than £150,000 were liable for SDLT. The associated tax rates are shown in Table 1.

Table 1: Previous SDLT systems in the UK between 2006 and 2014

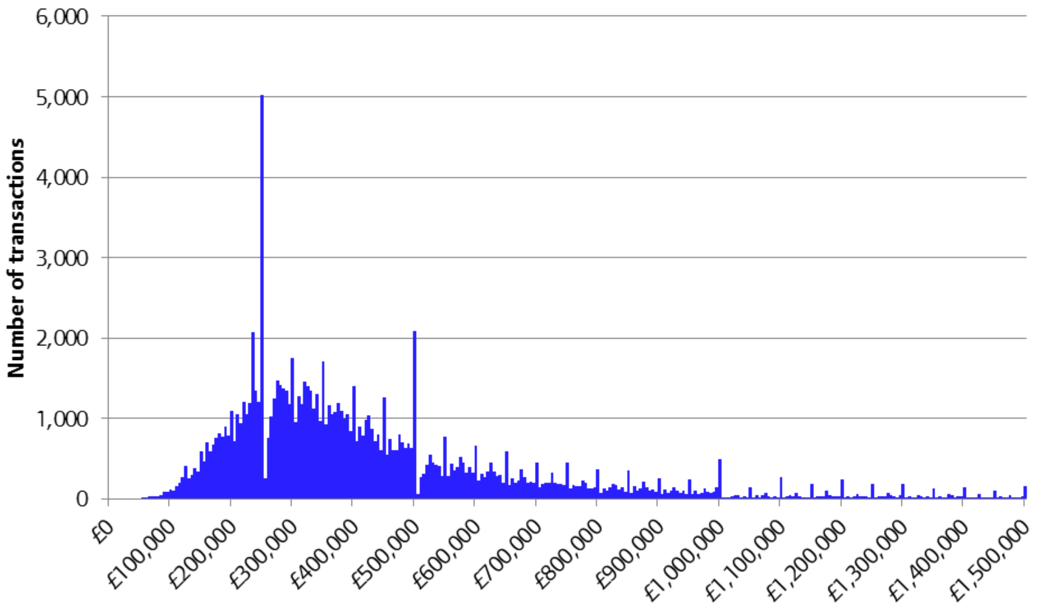
Residential		Non-residential	
Property value	**SDLT rate**	**Property value**	**SDLT rate**
Up to £125,000	0%	Up to £150,000	0%
£125,001 to £250,000	1%	£150,001 to £250,000	1%
£250,001 to £500,000	3%	£250,001 to £500,000	3%
£500,001 to £1,000,000*	4%	£500,001 and over	4%
£1,000,001 and over*	5%		

**From April 2011 onwards. Note: additional rates were payable if residential properties were purchased by corporate bodies. Source: HMRC UK Stamp Tax Statistics.*

One of the issues with a slab nature approach for SDLT is that it created distortions in the housing market. This can clearly be seen in Figure 1 where there are spikes in house sales at particular price points like £250,000, £500,000, and £1 million. These directly relate to the tax band thresholds.

[3] Exceptions included cars and furniture which could have been transferred without paying stamp duty as there were no associated documents.
[4] https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/464298/AnnualStampTaxes-Release-Sep15.pdf

Figure 1: Number of residential property transactions in London by price up to £1.5 million in 2014-15

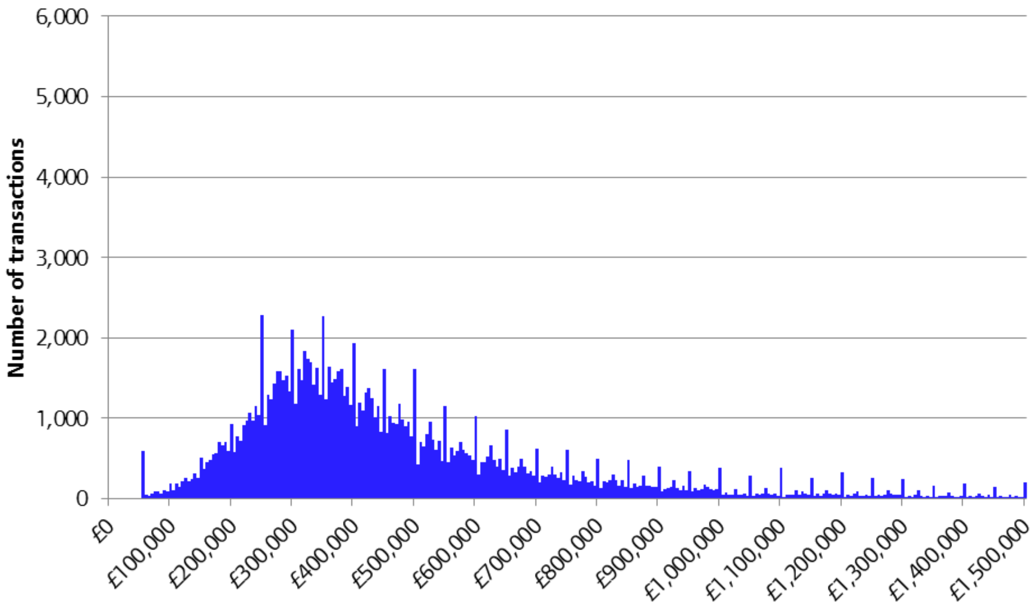


Source: Land Registry Prices Paid Data

Current stamp duty land tax system

A number of reforms to SDLT in December 2014 mean that the current tax system is fundamentally different to previous versions. One of the major differences is the move away from a slab based tax to one based on a graduated or 'slice' basis, where the tax only applies to the proportion of the property value falling within that band. This has the effect of significantly reducing the distortions in the housing market compared with the 'slabs' – see Figures 1 and 2.

Figure 2: Number of residential property transactions in London by price up to £1.5 million in 2015-16



Source: Land Registry Prices Paid Data

The current SDLT tax rates are shown in Table 2. It should be noted that this applies to transactions made in England, Wales, and Northern Ireland; Scotland replaced SDLT with a Land and Buildings Transaction Tax (LBTT), which is discussed in greater depth in Chapter 4.

Table 2: Stamp duty land tax system in England, Wales and Northern Ireland

Residential		Non-residential	
Property value	**SDLT rate**	**Property value**	**SDLT rate**
Up to £125,000	0%	Up to £150,000	0%
The next £125,000 *(i.e. £125,001 to £250,000)*	2%	The next £100,000 *(i.e. £150,001 to £250,000)*	2%
The next £675,000 *(i.e. £250,001 to £925,000)*	5%	The remaining amount *(i.e. £250,001 and over)*	5%
The next £575,000 *(i.e. £925,001 to £1,500,000)*	10%		
The remaining amount *(i.e. £1,500,001 and over)*	12%		

Source: HMRC UK Stamp Duty Statistics

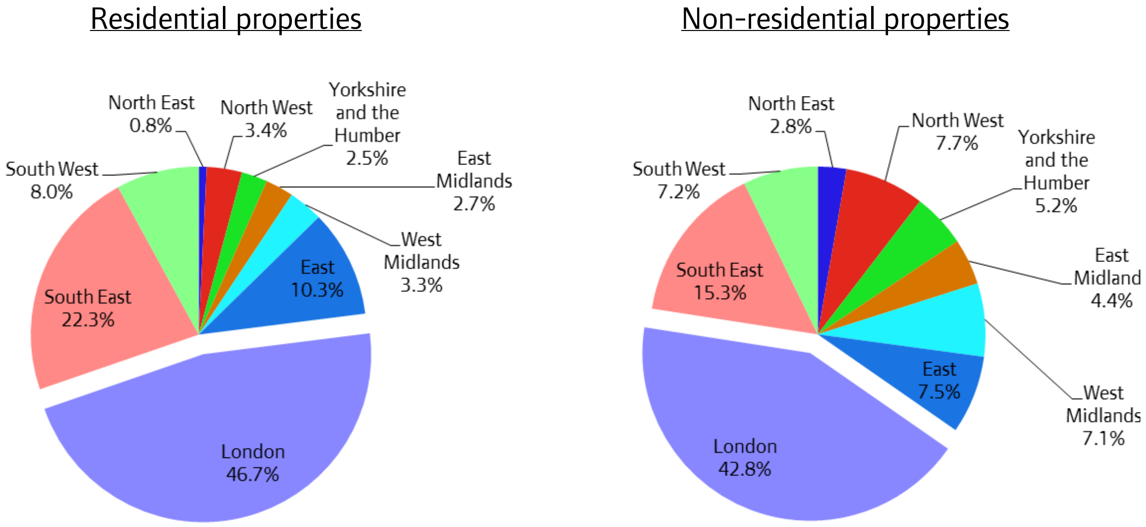
From April 2016, an additional SDLT charge of 3 per cent was introduced and applicable to the purchase of additional residential properties (i.e. second homes) valued over £40,000[5]. Moreover, a special 15 per cent rate is applicable to residential properties valued at £500,000 or more and held in a 'corporate envelope' – that is, transactions undertaken by one or more members who are either a body corporate or a collective investment scheme[6].

[5] Second homes may also face a council tax premium or discount depending on the local authority. See the GLA Economics paper on council tax for more information.
[6] There are some exemptions such as companies acting in their capacity as trustees and property developers.

There are also various SDLT exemptions and reliefs which are outlined in Appendix 1.

Overall, the total yield from SDLT in England in 2015-16, was £7,210 million for residential properties. London contributed the most SDLT of any English region, at £3,370 million, the equivalent of 46.7 per cent of the total. For non-residential properties, the total yield was £3,265 million in England, of which London contributed £1,395 million (or 42.8 per cent).

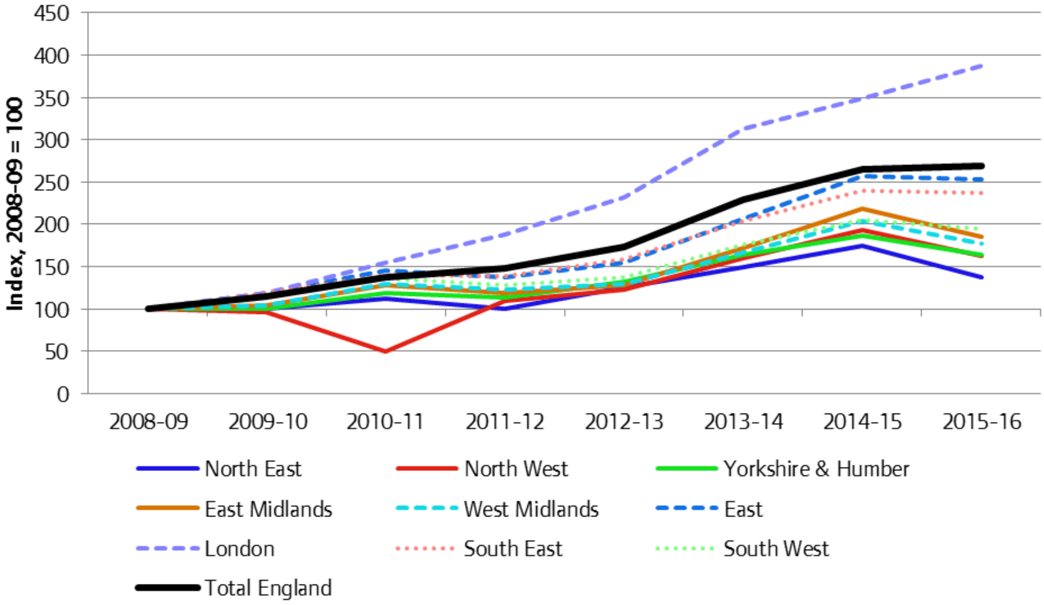
Figure 3: Stamp duty land tax yield by English region in 2015-16



Source: HMRC Annual Stamp Taxes

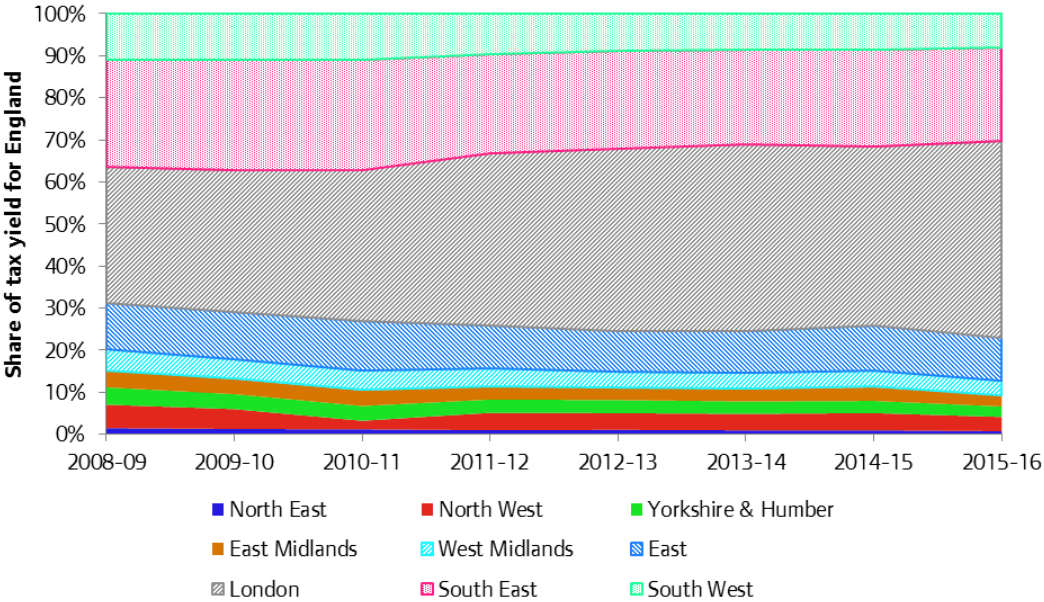
The 2015-16 financial year saw residential SDLT receipts in London increase by £340 million (or 11.2 per cent) on the previous year. In fact, London was the only English region to see an increase in 2015-16. Moreover, between 2008-09 and 2015-16, growth in residential stamp duty collected in London has surpassed all other English regions, as shown by Figure 4. This means that London's share of the total yield for England has increased over time, as shown by Figure 5.

Figure 4: Growth in residential stamp duty tax yield by English region, current prices, 2008-09 = 100



Source: HMRC Annual Stamp Taxes Statistics

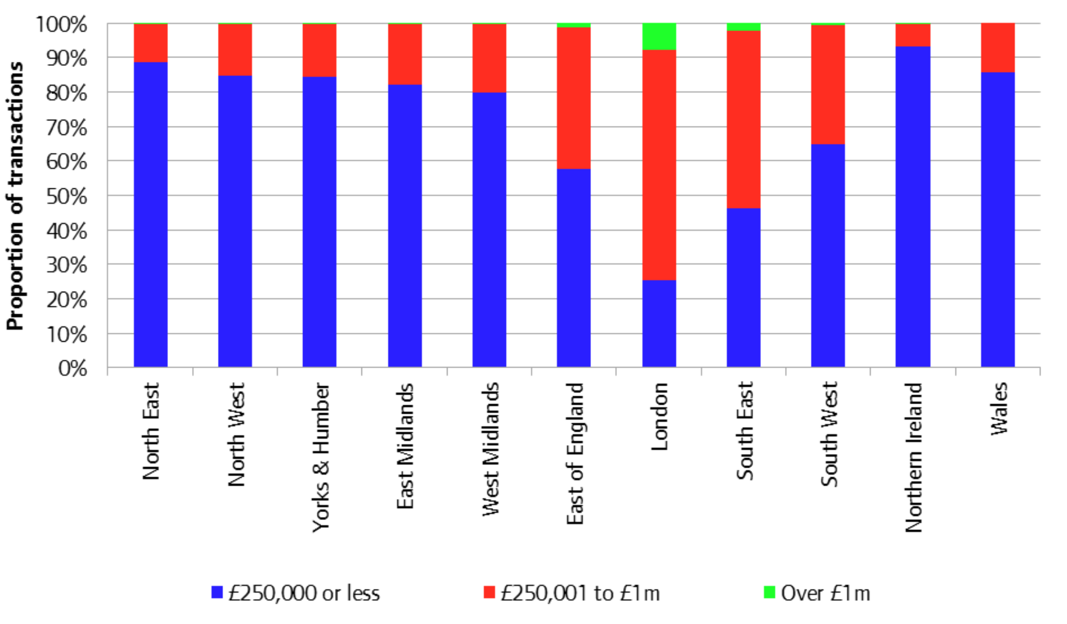
Figure 5: Regional share of residential stamp duty tax yield for England, current prices, 2008-09 to 2015-16



Source: HMRC Annual Stamp Taxes Statistics

The difference between London and England's residential stamp duty tax take is evidence of the differences between the housing markets in London and the rest of England. For example, the vast majority of higher rate properties (i.e. those valued over £1 million) were in London.

Figure 6: Percentage of regional residential transactions by price band in 2015-16



Source: HMRC Annual Stamp Taxes Statistics

The importance of London is further highlighted by Tables 3 and 4, which show that all bar one of the top ten local authorities by residential yield, and all but three by non-residential yield, are in London. Interestingly, Kensington and Chelsea overtook Westminster for the first time in terms of residential stamp duty during 2015-16, though both accounted for 7.1 per cent of the total tax yield for England (or 14.2 per cent in total). In terms of non-residential stamp duty, Westminster continued to dominate, raising 11.6 per cent of the total yield across England.

Table 3: Top ten local authorities with the highest residential stamp duty tax yield in 2015-16

Rank	Local authority	Stamp duty tax yield (£millions)	Percentage of total yield for England, Wales and N. Ireland
1	Kensington and Chelsea	£514m	7.1%
2	Westminster	£513m	7.1%
3	Wandsworth	£218m	3.0%
4	Camden	£205m	2.8%
5	Hammersmith	£153m	2.1%
6	Barnet	£141m	2.0%
7	Richmond upon Thames	£139m	1.9%
8	Southwark	£113m	1.6%
9	Lambeth	£111m	1.5%
10	Elmbridge	£99m	1.4%

Source: HMRC Annual Stamp Taxes Statistics

Table 4: Top ten local authorities with the highest non-residential stamp duty tax yield in 2015-16

Rank	Local authority	Stamp duty tax yield (£millions)	Percentage of total yield for England, Wales and N. Ireland
1	Westminster	£377m	11.6%

2	City of London	£172m	5.3%
3	Islington	£78m	2.4%
4	Camden	£72m	2.2%
5	Kensington and Chelsea	£71m	2.2%
6	Hammersmith	£69m	2.1%
7	Birmingham	£66m	2.0%
8	Tower Hamlets	£64m	2.0%
9	Manchester	£56m	1.7%
10	City of Bristol, UA	£48m	1.5%

Source: HMRC Annual Stamp Taxes Statistics

More detailed breakdowns of residential stamp duty for the London boroughs are provided in Appendix 2.

3 Issues with stamp duty

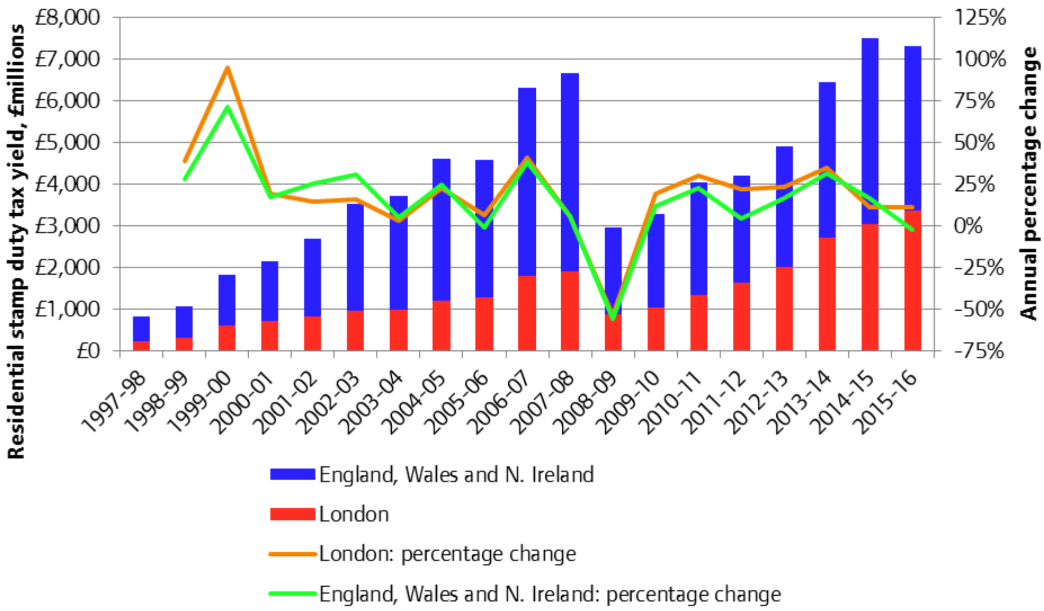
Despite the recent changes to stamp duty, there remain some fundamental issues with the tax system. As such, if stamp duty was to be devolved, as recommended by the LFC, then London government may wish to redress these inefficiencies (as with the other property taxes – council tax and business rates). These issues are discussed in this chapter.

Volatility in the tax yield

The income received from SDLT is dependent on the continual sale and purchase of property. As a revenue source for government, it can be inconsistent and difficult to forecast, creating a potential problem if it were to be used as a funding stream for projects requiring a steady flow of capital, such as infrastructure investment.

Between 1997-98 and 2015-16, the annual absolute change in London's stamp duty tax yield has varied from an increase of £705 million (+34.9 per cent) recorded in 2013-14 to a decrease of £1,025 million (-54.1 per cent) reported in 2008-09. This volatile trend can be seen in Figure 7. Consequently, if stamp duty revenue were to make up a part of London's budget, there would clearly be significant risks resulting from this level of uncertainty.

Figure 7: Residential stamp duty tax yield for London and England, Wales & N. Ireland between 1997-98 and 2015-16, current prices



Source: HMRC Annual Stamp Taxes Statistics

This trend continues even at a local authority level. Both inner and outer London has shown percentage changes of over 30 per cent in recent years. Furthermore, this volatility exists not only between years, but also between financial quarters.

Inefficiency in housing mobility

While the volatility of stamp duty could result in some practical difficulties in managing the proceeds from the tax, probably the main issue associated with SDLT is its distortive influence on the housing market. SDLT reduces the incentive for individuals to move house by increasing the associated costs of moving and so, ultimately, results in a more inefficient distribution of housing than would otherwise be the case.

The Mirrlees Review[7] looking at good tax design found in relation to stamp duty that:

> *"…by discouraging mutually beneficial transactions, stamp duty ensures that properties are not held by the people who value them most. It creates a disincentive for people to move house, thereby leading to potential inflexibilities in the labour market and encouraging people to live (and businesses to operate) in properties of a size and in a location that they may not otherwise have chosen."*

Economic theory on optimal tax policy suggests that tax should be designed in such a way as to reduce inefficiency and minimise distortion of behaviour (unless changing behaviour is the policy objective). As such, any resulting negative behaviour change could be considered as inefficiency in the system or a deadweight loss[8].

In this light, SDLT reduces mobility which results in an inefficient use of the housing stock. Practically, this could take the form of an elderly person choosing not to downsize or an employee not moving to nearer their place of work. Academic research supports this; in relation to the previous stamp duty system, Hilber & Lyytikäinen found that the 2 per cent increase in SDLT at the £250,000 threshold can reduce household mobility by 2-3 per cent[9]. It is likely that similar reductions in household mobility would also be experienced in the current stamp duty system.

This inefficiency is likely to be greatest where the costs of moving are largest. As already discussed and shown previously in Figure 5, London – as an area with a higher number of properties in the higher tax bands – is likely to be disproportionately affected.

Rationale for stamp duty

While other property taxes like business rates and council tax can be considered consumption taxes for local services, the rationale for stamp duty is not so clear[10]. Originally, stamp duty was conceived back in the late 1600s as a tax for recognising the legality of documents associated with assets; however, technological advances mean that these issues with recognising documents and ownership are far less common today, thus weakening the historic rationale for stamp duty. For example, the Mirrlees Review[11] stated:

"[Stamp duty] stems from a time when few other potential taxes were straightforward to implement… but, in the modern era of broadly based taxation, the case for maintaining stamp duty is very weak."

---

[7] Mirrlees, J et al. (2011). Tax by design, Chapter 16, pg. 403. Available at: https://www.ifs.org.uk/publications/5353
[8] The loss of economic efficiency, due to sub optimal allocation of resources, in this case caused by the distorting impact of stamp duty on the demand for housing.
[9] Their research estimates "the effect of the UK Stamp Duty Land Tax on household mobility using micro data", in particular they use self-assessed house values from the British Household Panel Survey against actual sale values of the house and use regression analysis to examine the impact of the jump in stamp duty from the 1 per cent threshold to 3 per cent threshold. Hilber, C. A. L. & Lyytikäinen, T., Housing transfer taxes and household mobility: distortion on the housing or labour market?, Government Institute for Economic Research: Working Papers 47, August 2013.
[10] See for example: Stephens, M (2011). Tackling housing market volatility in the UK, Joseph Rowntree Foundation, May 2011; and Crawshaw, T. (2009). Rethinking housing taxation: options for review, Shelter, Discussion Paper, November 2009.
[11] Mirrlees, J et al. (2011). Tax by design, Chapter 16, pg. 403. Available at: https://www.ifs.org.uk/publications/5353

Moreover, if stamp duty was alternatively considered a consumption tax, then it may make more sense to combine it with other property taxes, such as council tax. This would simplify the tax system – a criterion identified by the Mirrlees Review as being a characteristic of good tax system – as well as remove some of the inefficiencies of stamp duty itself.

Non-residential stamp duty taxes an input

Similar to the issues associated with business rates, non-residential stamp duty can affect a firm's decision about its inputs in the production process. From an economic perspective, business property is an input to production among other factors like labour. Theoretically, a larger commercial property can lead to higher output for example. However, as stamp duty is charged on property values, it can be considered to have raised the cost of using property in relation to other inputs. Therefore, the conclusion that business rates artificially skews activity away from property-intensive production could apply to non-residential stamp duty as well[12].

[12] Mirrlees, J et al. (2011). Tax by design, Chapter 16, pg. 376. Available at: https://www.ifs.org.uk/publications/5353

4 Cross-country comparison

Nevertheless, taxation on asset transactions, in some form, is used by many national and local governments around the world. This section provides a summary of several of these for comparison purposes. It should be noted that, where applicable, monetary values reported in national currencies have been converted into pound sterling using purchasing power parities from the World Bank[13].

Scotland

While historically Scotland shared the same stamp duty system as the rest of the UK, the power over the setting of stamp duty on property purchases was devolved to the Scottish Government from December 2014.

Given this new responsibility, SDLT was replaced with a Land and Buildings Transaction Tax (LBTT) in April 2015. In essence, LBTT in Scotland works in a broadly similar way to the current reformed SDLT system for the rest of the UK. That is, it is a 'slice' system where the tax rate for each band is only applied to the part of the purchase price in that relevant band. However, notable differences between the two systems are the rates of tax and the band thresholds as shown in Tables 2 (for SDLT) and 5 (for LBTT). These differences effectively mean that a residential property valued at £333,000 or more would pay more tax in Scotland under LBTT than in the rest of the UK under SDLT. For example, the average house price in London is £485,000[14] – this would pay £14,250 in SDLT, but this would be £21,850 if the LBTT was adopted.

Table 5: Land and buildings transaction tax system in Scotland

Residential		**Non-residential**	
Property value	**LBTT rate**	**Property value**	**LBTT rate**
Up to £145,000	0%	Up to £150,000	0%
The next £105,000 *(i.e. £145,001 to £250,000)*	2%	The next £200,000 *(i.e. £150,001 to £350,000)*	3%
The next £75,000 *(i.e. £250,001 to £325,000)*	5%	Over £350,000	4.5%
The next £425,000 *(i.e. £325,001 to £750,000)*	10%		
Over £750,000	12%		

Source: Scottish Government LBTT guidance

For second homes or buy-to-let properties with a value of £40,000 or more, a 3 per cent Additional Dwelling Supplement (ADS) is also charged on the whole of the purchase price in Scotland. Therefore, this means that a second home valued at £145,000 would pay £4,350 in total (£0 in LBTT and £4,350 in ADS), while a second home valued at £750,000 would pay £70,850 in total (£48,350 in LBTT and £22,500 in ADS).

It should be noted that property prices in Scotland are generally lower than London. For example, approximately 2 per cent of residential property transactions in Scotland were valued

[13] This process involved first converting the national currency into US dollars (the base currency for the World Bank's purchasing power parities) and then converted again into pound sterling.
[14] https://www.gov.uk/government/publications/uk-house-price-index-summary-july-2016/uk-house-price-index-summary-july-2016

at more than £500,000 in 2014[15]. Comparably, this figure was around 29 per cent for London. Consequently, for the 2015-16 financial year, if London had the equivalent of LBTT, then the LBTT tax take could be around £4,347 million compared with the SDLT yield of £3,770 million[16].

Wales

At present, Wales shares the same system for SDLT as England and Northern Ireland. Under current proposals, Welsh ministers are to gain powers to set rates to raise around £250 million a year from autumn 2017, and will replace SDLT with a land transaction tax. The collection of this tax will be undertaken by a new Welsh Revenue Authority and follows legislation to allow the collection and management of taxes that was passed by the Welsh Assembly in March 2016[17].

Ireland

The Irish system for taxation of property transactions is by far the simplest of those discussed in this paper. As of December 2010, a rate of 1 per cent is charged on the first €1 million (the equivalent of around £825,000) for residential property and 2 per cent on the amount in excess of this. Stamp duty payable on non-residential property is charged at a flat rate of 2 per cent.

Essentially this means that residential property transactions in England valued at £250,000 would pay more tax under this Irish system, but properties worth £250,000 or more would pay less tax. For example, a residential property in London worth £485,000 (the London average house price) would pay £4,850 in stamp duty (1 per cent effective rate of tax) under the Irish system. This compares with £14,250 under the current SDLT system.

Overall, the Irish government collected €1,268 million (the equivalent of £1,072 million) in stamp duty revenue in the 2015 calendar year[18]. That was down from €1,687 million (£1,369 million) in 2014.

Hong Kong

In Hong Kong, stamp duty is charged on the sale or lease of immoveable property (both residential and non-residential) and the transfer of shares. While the latter has a different set of tax rates, there are two scales for immovable property[19]. The scale 2 rates are applicable to residential property transactions acquired by a Hong Kong permanent resident and who does

---

[15] The estimate for Scotland is based on property transactions data from HMRC. This records the number of transactions liable for the LBTT. However, no English regional data is available in this dataset. As such, the estimate for London is based on the Land Registry prices paid dataset. This records the number of property sales that were lodged with the Land Registry for registration. As is noted later on in this paper, there are some differences between the HMRC and Land Registry datasets which is likely due to the different ways of categorising residential and non-residential property. Therefore, the percentages of properties valued at more than £500,000 are used here instead of the actual number in order to take into account the different estimates of the total number of transactions.

[16] This estimate is primarily based on the Land Registry Prices Paid data. Using this dataset, it is estimated that the SDLT tax take in London was approximately £4,522 million and the potential LBTT tax take was around £5,834 million in 2015-16 – a percentage difference of 29 per cent. As noted in the previous footnote and later in this paper, there are some differences between the Land Registry and HMRC datasets. This can explain why the modelled estimate of SDLT tax yield (£4,522 million) is different to the tax take figure reported by HMRC and used in this paper (£3,770 million). To account for this, it has simply been assumed that the impact of LBTT in London would apply to the HMRC estimates of SDLT tax take, i.e. £3,770 million x 129% = £4,347 million.

[17] BBC News (2016). Bill for Welsh property tax replacing stamp duty published, 12 September. Available at: http://www.bbc.co.uk/news/uk-wales-politics-37307106

[18] Irish Tax and Customs (2016). Annual Report for year ended 31 December 2015. Available at: http://www.revenue.ie/en/about/publications/annual-reports.html

[19] GovHK (2016). Stamp duty rates. Available at: http://www.gov.hk/en/residents/taxes/stamp/stamp_duty_rates.htm

not own any other residential property in Hong Kong. The scale 1 rates apply in all other scenarios such as second home transactions. These tax rates are shown in Table 6.

Table 6: Stamp duty tax system in Hong Kong

Property value (HK$)	Scale 1 (HK$)	Scale 2 (HK$)
Up to $2m	1.5%	$100
$2m to $2.176m*	$30,000 + 20% on excess over $2m	$100 + 10% on excess over $2m
$2.176m to $3m*	3.0%	1.50%
$3m to $3.290m	$90,000 + 20% on excess over $3m	$45,000 + 10% on excess over $3m
$3.290m to $4m	4.5%	2.25%
$4m to $4.429m	$180,000 + 20% on excess over $4m	$90,000 + 10% on excess over $4m
$4.429m to $6m	6.0%	3.00%
$6m to $6.720m	$360,000 + 20% on excess over $6m	$180,000 + 10% on excess over $6m
$6.720m to $20m	7.5%	3.75%
$20m to $21.739m	$1.5m + 20% on excess over $20m	$750,000 + 10% on excess over $20m
Over $21.739m	8.5%	4.25%

**This is $2.352 million for scale 2. Note: a Hong Kong permanent resident buying a residential property and who does not own any other residential properties in Hong Kong pay the tax rates shown in scale 2; all other scenarios pay the tax rates shown in scale 1. Source: GovHK*

In addition to these basic stamp duty rates, Hong Kong also has a Special Stamp Duty which is payable if a residential property is resold within three years of the transaction date. The Special Stamp Duty tax rate varies from 10 per cent if the property is resold between 1-3 years of the original purchase date to 20 per cent if resold within six months.

There is also the Buyer's Stamp Duty, which is charged on residential property transactions undertaken by people who are not Hong Kong permanent residents. The Buyer's Stamp Duty is charged on top of the basic stamp duty tax (see Table 6) and is calculated as 15 per cent of the property value.

Broadly speaking, if London had the same stamp duty system as Hong Kong, then residential properties worth £1.9 million or less would usually pay more tax than the current SDLT system. Instead properties worth more than £1.9 million would usually pay less stamp duty. This is on the basis of the scale 1 stamp duty tax rates in Hong Kong and no Special or Buyer's Stamp Duties. For example, based on a property worth £485,000 – the London average house price – they would pay around £14,550 in tax based on the Hong Kong system, in comparison with £14,250 under the current SDLT system.

New Zealand

The New Zealand government taxes residential construction activities and the first sale of new dwellings[20]. However, it does not apply any asset transaction tax for property after its first sale. While this creates some issues – i.e. it increases house prices for new homes (as the tax amount is accounted for in the price) and, as such, offers a windfall gain to existing home owners who bought their house prior to the introduction of the tax – it leaves the 'second-hand' property market far more flexible than that in the UK.

[20] There is no capital gains tax in New Zealand. Income tax is sometimes payable if the property is bought with the intention of reselling.

5 Potential options for reform

While Chapter 3 discussed the issues associated with stamp duty – such as the inefficiency in housing mobility – this chapter sets out several options for reforming stamp duty so that it is more efficient and works better for Londoners.

The impact of these potential reform options have been modelled for London but, given the lack of access to the underlying HMRC data, this analysis is based on the Land Registry Prices Paid data and may therefore be somewhat imprecise[21]. There is also a lack of information on non-residential property transactions and so the analysis focuses on residential sales only.

Option 1: Infrastructure (or other) Investment Fund

Assuming London was to gain control of SDLT, policy makers would need to decide how the funds collected would be managed in such a way as to limit the negative effects of its volatility.

One option for reducing this could be to put revenues raised from collection of SDLT (regardless of its form) into a fund. This 'infrastructure (or other) investment fund' would release a percentage of its reserve capital for spending each year such as to provide a constant stream and mitigate revenue fluctuations.

It should also be noted that when SDLT was devolved to Scotland, the Scottish Government was provided with a cash reserve (within the UK government rather than commercially) to build up funds when devolved revenues were lower than forecast. Since June 2011, they have been able to make discretionary payments into the Scottish Reserve, and now have the power to draw on this fund to smooth spending and manage tax volatility. If London is to receive powers over stamp duty, a similar arrangement could be hugely beneficial. In addition, both Norway and Saudi Arabia already have not dissimilar Sovereign Wealth Funds to achieve this[22][23].

Option 2: Introduce a flat rate of tax

Even with such a fund, further changes to or reform of stamp duty may be desirable. One possibility for reform would be to charge a flat rate tax on all property sales. Arguably, this would be simpler than the existing system but, depending on the rate set, could have consequences for revenue raised.

Table 7 shows the estimated potential revenue raised on London property sales in 2014-15 given various stamp duty flat tax rates. It also shows the expected surplus/shortfall in tax take when compared with the amount currently raised under the 'slice' system. Overall, a flat tax rate of 5.17 per cent[24] would be required in order to raise the same amount of SDLT as the current system in 2014-15.

[21] Following investigations with HMRC it is likely that some of this difference relates to a difference in the 'categorisation' of residential properties by Land Registry compared with HMRC. For instance, Land Registry 'categorises' any house purchase by a company as non-residential, whereas such purchases may be classed as residential for HMRC purposes.
[22] Norges Bank (2016). About the fund, accessed on 6 December 2016. Available at: https://www.nbim.no/en/the-fund/about-the-fund/
[23] SWFI (2016). Public investment fund, accessed on 6 December 2016. Available at: http://www.swfinstitute.org/swfs/public-investment-fund/
[24] The flat tax rate required to be fiscally neutral for England, Wales and Northern Ireland may be different.

Table 7: Revenue from various flat stamp duty tax rates in London during 2014-15

Flat stamp duty tax rate	Estimated tax take (£millions)	Estimated surplus/shortfall in comparison with current tax take (£millions)
1%	£548.9m	-£2,481.2m
2%	£1,097.7m	-£1,932.3m
3%	£1,646.5m	-£1,383.5m
4%	£2,195.4m	-£834.6m
5%	£2,744.2m	-£285.8m
5.17%	**£3,030.0m**	**£0.0m**
6%	£3,293.1m	£263.1m

Source: Land Registry Prices Paid data, GLA Economics calculations

Another benefit of a flat tax is that it could further remove the distortions in the housing market (see Figures 1 and 2 for example). That is because there would be no incentive to have purchase prices at particular price points (i.e. around the SDLT band thresholds). However, the main issue with this form of tax rate is that it is less progressive than the existing system.

Option 3: Replace with capital gains tax

The National Institute of Economic and Social Research (NIESR) has previously described stamp duty as the "worst of all worlds" as it restricts the efficient allocation of housing and labour mobility (previously discussed in Chapter 3)[25]. Unlike other assets, NIESR observed that the income and capital gains from housing is untaxed as neither stamp duty or council tax cover this. As such, they suggest that stamp duty (and, to some extent, council tax) could be replaced by a tax on the sale of a home – a kind of capital gains tax for housing. They also argue that a capital gains tax on housing could dampen the volatility in house prices as the tax would help reduce the gains in an upturn and the losses in a downturn.

At present, capital gains tax in the UK is payable on profit when an 'asset' is sold that has increased in value. For example, a painting bought for £5,000 and sold for £25,000 would represent a profit of £20,000 and be subject to tax (subject to income tax and capital gains tax thresholds being met). While main homes are currently exempt, capital gains tax is payable on property that is let or used for business (even if it is also a main home), as well as all other property[26].

From April 2016, higher rate tax payers have been charged 28 per cent on gains from residential property that is not their main residence and 20 per cent on other assets. For basic rate tax payers, this is based on taxable income which gives a variable tax-free allowance on any gains. If, with gains, the amount falls within the basic income tax band, 10 per cent is payable on additional gains, and 20 per cent is payable above this[27].

Option 4: Roll into council tax

Instead of replacing stamp duty with capital gains tax, it could instead be rolled into council tax. As discussed in Chapter 3, if the rationale behind stamp duty was partly because it is a consumption tax, then it could be combined with council tax that has similar rationale and

[25] Armstrong, A (2016). UK housing market: problems and policies, *National Institute Economic Review*, 235, February 2016.
[26] https://www.gov.uk/capital-gains-tax/allowances
[27] https://www.gov.uk/capital-gains-tax/rates-6-april-2016

objectives[28]. In effect, this would then create a 'housing services tax' which would also bring it more in line with business rates – the equivalent consumption tax for businesses – and create greater equity between residential and non-residential property taxes[29].

Other benefits from rolling stamp duty into council tax would be that it goes some way of simplifying the tax system – an objective of 'good' tax design. It would also encourage greater mobility in the housing market as payments would no longer be 'one-off' but distributed across the population and paid over time.

Despite these advantages, the Mirrlees Review noted that the volatility in stamp duty tax take makes it difficult to say how it can be rolled into council tax[30]. Moreover, any changes to stamp duty is likely to create windfall winners and losers as the tax would largely have been capitalised into property values – that is, the property price accounts for the housing tax. Therefore, some consideration should be given in ensuring any change to stamp duty is revenue neutral.

Option 5: Introduce a land value tax

Another potential option for SDLT reform would be to abolish SDLT, council tax and business rates and replace all three with a land value tax (LVT). This would be a tax payable on the value of the land rather than the valuation of property on that land as is the case at present.

At present, the different effective rates of tax in council tax and business rates as well as the differentiation in stamp duty means the tax system treats residential and non-residential properties differently. The LVT would be payable on all types of land, regardless of its use, and could therefore remove any preferential activity towards a particular land use. Effectively, this would create an equal playing field among the different types of land uses, i.e. residential vs commercial land and the various types of businesses.

The LVT would also cover undeveloped land which currently is not taxed to the same extent as developed land. This could then be beneficial in terms of equity, efficiency and environmental factors. For instance, taxing undeveloped land along with commercial (business rates) and residential (council tax) land ensures that all land users are contributing their share to local finances. Removing the disincentive to improve undeveloped land caused by the various tax relief options currently available would also lead to efficiency improvements; an undeveloped land tax raises the holding (and opportunity) cost of the land meaning it may be more profitable to change its economic use. Consequently, the added supply of land available to develop may reduce pressures to build on green and public spaces, thus having a positive environmental impact. Bringing more land into the property tax system also has the potential to increase the amount of tax raised, all other things being equal.

A LVT, assuming valuations were timely, could also represent an efficient and effective way of capturing the gains in land value resulting from infrastructure investment. Many investments by local authorities, the GLA or central government can help increase land values. At the moment it can be argued that the gains from these investments are not effectively captured by the public sector. A LVT could help alleviate this situation.

[28] Mirrlees, J et al. (2011). Tax by design, Chapter 16, pg. 385. Available at: https://www.ifs.org.uk/publications/5353
[29] See the separate GLA Economics paper on council tax for more information.
[30] Mirrlees, J et al. (2011). Tax by design, Chapter 16, pg. 385. Available at: https://www.ifs.org.uk/publications/5353

Previous LVT studies imply a tax rate of between 0.79 per cent and 4 per cent would be most appropriate[31] but how this might affect total tax revenue is uncertain. That said, LVT in London would likely change the incidence of property tax between commercial and residential property (particularly at higher values of property). Alongside this, there are further practical considerations that need to be made in terms of a LVT, such as:

- how will land values be assessed;
- the frequency of revaluations;
- who would set the tax rate (central or local government); and
- how will the tax revenue be distributed among the various levels of government.

[31] Oxfordshire County Council's survey (2005) reported that a land value tax rate of 0.79% would generate sufficient tax revenue to replace both business rates and council tax. Meanwhile, Muellbauer (2004) suggested a land value tax rate of 2% for commercial land, whilst maintaining half the current business rates. This has been assumed to be 4% if business rates were abolished. Wrightman (2010) also suggested a land value tax rate of 4% (maximum) in a study for the Scottish Parliament.

6 Conclusion

This paper looked at the stamp duty land tax system in London but, in doing so, highlighted a number of issues associated with the tax. Firstly, stamp duty encourages an inefficient use of property, in that it raises the cost of moving and acts as a disincentive to housing mobility. In addition, as it is linked to property prices, tax take follows the economic cycle and is consequently volatile. This makes it hard to forecast and use as a funding stream for certain types of project. Moreover, stamp duty for non-residential property itself is taxing an input to the production process, which could sway activity away from more property-intensive production.

While the reforms to stamp duty in December 2014 tackled some of the previously intrinsic issues with the tax – such as the 'slab' nature which distorted the housing market – there is a case for further improvement. Given this, the devolution of property taxes as recommended by the LFC, provides an opportunity to do improve the overall efficiency of stamp duty.

As such, this paper presented five options for reforming – or, in fact, replacing – stamp duty. This included introducing an infrastructure investment fund, a flat rate of stamp duty, replacing it with capital gains tax for housing or rolling it into council tax, and introducing a land value tax. In looking at these potential options for reform, this paper also looked at how stamp duty works in other countries, such as Scotland which received responsibility for the tax as part of their devolution package.

Appendix 1: Stamp duty exemptions

HMRC charge SDLT on all property and land transactions in the UK which meet certain thresholds. Transactions may qualify for reliefs which reduce or eliminate SDLT paid in the following circumstances:

Table 8: Various stamp duty reliefs and exemptions

Exemption	Conditions:
Multiple dwellings – the transaction or a number of linked transactions include freehold or leasehold interests in more than one dwelling	• The tax rate is calculated by dividing the total paid for the properties by the number of dwellings, the tax is applied to this figures, and then multiplied by the number of dwellings • The dwelling must have a lease of less than 21 years • There is a minimum tax rate of 1 per cent Example: • You buy 5 houses for £1 million • £1 million divided by 5 is £200,000 • SDLT payable on £200,000 is £1,500 • £1,500 multiplied by 5 is £7,500 • But that's less than 1 per cent of £1 million so tax paid is raised to £10,000
Building company buys an individual's home – when they are selling them a new home	• The person must have lived in the property as their main home during the last 2 years • They must buy a new home from the house builder • They must intend to live in the new property as their main home
Compulsory purchases – so that a property development can go ahead, usually done via the local authority	• As there are 2 sales (one to the local authority, one to the developer), 2 amounts of SDLT would normally be payable. In this instance, the local authority is eligible for relief • This relief can be claimed even if the sale isn't made under these powers, so long as development by a third party occurs
Transfer of property between companies – for companies within the same group	• The buyer and seller must both be companies • At the effective date of the transaction, both companies must be members of the same group
Relief for charities – when buying the property for charitable purchases	• This is still applicable if the charity is buying jointly within a non-charity buyer. The charity can claim relief on its share of the property • HMRC can withdraw the relief within 3 years of the transaction if the charity stops being a charity, or uses the property for purposes that aren't charitable
Right to Buy properties – a sale of a dwelling at a discount by a public sector body or where there is a preserved right to buy	• SDLT is calculated on the discounted price that the buyers pays but does not include any additional payments
Registered social landlords	• Most of the board members of the registered social landlord are tenants living in property from the social landlord • The seller of the property is a 'qualifying body' • A public subsidy funds the sale
Other reliefs	• Less common reliefs include First Time Buyers Relief and group, reconstruction or acquisition relief, among others • More information about these is available in the SDLT manual: https://www.gov.uk/hmrc-internal-manuals/stamp-duty-land-tax-manual/sdltm20000

Source: HMRC

Appendix 2: Stamp duty statistics by London borough

Table 9: Residential and non-residential stamp duty tax yield by London borough in 2015-16

Borough	Residential		Non-residential	
	Number of transactions	Stamp duty tax yield (£millions)	Number of transactions	Stamp duty tax yield (£millions)
Barking and Dagenham	3,220	£9m	270	£10m
Barnet	6,630	£141m	580	£28m
Bexley	4,900	£25m	320	£8m
Brent	4,570	£67m	470	£14m
Bromley	7,150	£88m	480	£11m
Camden	3,570	£205m	1,250	£72m
City of London	510	£15m	1,380	£172m
Croydon	7,480	£51m	620	£28m
Ealing	4,950	£81m	620	£25m
Enfield	5,060	£44m	390	£13m
Greenwich	5,580	£53m	380	£15m
Hackney	4,290	£70m	700	£29m
Hammersmith	3,690	£153m	610	£69m
Haringey	3,950	£74m	410	£8m
Harrow	4,010	£50m	340	£10m
Havering	5,400	£32m	360	£10m
Hillingdon	4,970	£47m	470	£33m
Hounslow	4,350	£60m	510	£32m
Islington	3,510	£91m	890	£78m
Kensington and Chelsea	3,800	£514m	630	£71m
Kingston upon Thames	3,190	£54m	360	£16m
Lambeth	6,310	£111m	580	£40m
Lewisham	6,280	£58m	370	£10m
Merton	3,990	£83m	360	£11m
Newham	4,780	£25m	670	£17m
Redbridge	4,290	£38m	310	£5m
Richmond upon Thames	4,080	£139m	440	£21m
Southwark	6,040	£113m	780	£44m
Sutton	4,010	£31m	290	£11m
Tower Hamlets	6,110	£79m	820	£64m
Waltham Forest	4,580	£38m	290	£7m
Wandsworth	8,150	£218m	650	£33m
Westminster	5,450	£513m	2,760	£377m
London total	**158,840**	**£3,368m**	**20,350**	**£1,394m**
Inner London total	66,430	£2,239m	12,480	£1,085m
Outer London total	92,400	£1,129m	7,870	£309m

Source: HMRC Annual Stamp Taxes Statistics

GLAECONOMICS

Greater London Authority
City Hall
The Queens Walk
London SE1 2AA

Tel 020 7983 4922
Fax 020 7983 4674
Minicom 020 7983 4000
Email glaeconomics@london.gov.uk

http://www.london.gov.uk/gla-economics-publications

MAYOR OF LONDON