Reforming Stamp Duty

New ideas to promote home ownership

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ONWARD

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Onward is a campaigning thinktank whose mission is to develop new ideas for the next generation of centre right thinkers and leaders. We exist to make Britain fairer, more prosperous and more united, by generating a new wave of modernising ideas and a fresh kind of politics that reaches out to new groups of people.

We believe in a mainstream conservatism – one that recognises the value of markets and supports the good that government can do, is unapologetic about standing up to vested interests, and assiduous in supporting the hardworking, aspirational and those left behind. Our goal is to address the needs of the whole country: young as well as old; urban as well as rural; and for all parts of the UK – particularly places that feel neglected or ignored in Westminster.

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Thanks

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Data in this report

Data in this report is primarily drawn from the annual UK Stamp Tax statistical release from HMRC, combined with the authors' calculations using semi-elasticities provided by the OBR. In addition a number of ad-hoc statistical releases from MHCLG and other departments were used. For a more detailed methodology please contact the Onward team.

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Summary of the argument

Stamp duty is a bad way to tax owner occupiers. It adds considerable transactional costs to the process of buying a home and thus acts as both a barrier to entry for first time buyers, and an impediment to older homeowners downsizing to release housing stock for families. First levied in 1694 to pay for the war with France, it is now a major drag on the housing market, especially in London and the South East, with knock on effects for labour mobility and house prices.

The only reason for maintaining stamp duty in its current form is that it raises a lot of money for public services. While this makes it difficult to abolish in a way that is fiscally responsible, this is not a very good reason for continuing with a major policy that affects hundreds of thousands of people every year. It is time the Treasury bit the bullet and took most people out of stamp duty. This paper sets out how.

The effects of stamp duty are considerable. A non-first time buyer purchasing a property for £500,000 pays stamp duty of £15,000. This has to be cash funded. If using Help to Buy (which allows a deposit of just 5 per cent) stamp duty can add 60 per cent to the cash cost of buying a new-build home. For many prospective buyers, especially young people, this up-front cash outlay is the limiting factor in being able to buy a house or to move.

Home ownership is an inherently beneficial thing for individuals. Those who own their own home enjoy secure tenure and housing costs for people owning their own home are lower than for those renting. Over the long term, it is financially better to own rather than rent – even if house prices do not rise faster than inflation. And owning a property gives many people a real sense of a place they can call home.

It is no surprise, then, that 86 per cent of the public aspire to own their homes. Yet only 63 per cent actually do – nearly a quarter of our fellow citizens wish to own their own home but do not. Home ownership rates have fallen over the past 20 years, from a high of 71 per cent. The falls are especially acute amongst those in their 20s and 30s, where home ownership rates have almost halved. It is a legitimate – and popular – objective of public policy to help those wanting to own their own homes.

In the last ten years, owner occupiers have also been crowded out by financial investors and second home buyers, often from overseas, who have superior financial firepower. They currently make up around a quarter of all residential sales, and likely even more of new build sales. There is now a good argument to say this is undermining home ownership by crowding out first time buyers and other owner occupiers.

The Government recognises this. It has already abolished stamp duty for first time buyers purchasing properties under £300,000 and cut it by £5,000 for those buying at under £500,000. Several of the candidates in the Conservative Leadership contest have outlined aspirations to reduce the burden of stamp duty. This paper sets out how they could achieve it, recouping some of the costs through more efficient and less distortionary taxes.

We argue that – at a minimum – the Treasury should:

- Abolish stamp duty entirely for *all* purchases of a main home under £500,000 and halve current rates of stamp duty for purchases of a main home over the same amount. This would effectively abolish stamp duty for nine out of ten owner-occupiers.

- This would save a normal family buying an average priced home of £228,000 around £2,080 on their purchase, rising to £12,850 on the purchase of an average London home of £457,000. This is equivalent to half a typical 5 per cent deposit.
- The cost of this is £3.3 billion. This will help more people buy their first home, and make moving house – for a new job, or to downsize or upsize – with a much smaller up-front cost. For expensive properties, where stamp duty is currently charged at a marginal rate of 12 per cent, it is likely that transaction volumes are being suppressed. Halving stamp duty rates may result in a Laffer effect due to an increase in transaction levels.
- To balance the costs of this policy, the Treasury should introduce a number of smaller tax changes affecting other forms of property, where there is broad public support for taxation and a clear case for action. This includes the following eight changes, which collectively raise £3.3 billion.
  - Introduce a one per cent annual tax on the value of homes left empty for more than 6 months in a year. This would raise £645m per annum.
  - Increase the current three per cent stamp duty surcharge on second homes and investment properties to 5%. This raises £790m per annum.
  - Introduce an extra three per cent stamp duty surcharge of non-UK resident buyers of residential property. This raises £540m per annum.
  - Introduce an extra higher band of council tax for more expensive properties. This raises £173m per annum.
  - End all council tax reliefs for vacant and second home property. This raises £75m per annum.
  - Create a new eight per cent (up from five per cent) stamp duty band for the portion of commercial property purchases over £1 million. This raises £682m per annum.
  - Levy stamp duty on residential properties transferred by selling the company that owns them. This raises £175m per annum.
  - Double the Annual Taxation on Enveloped Dwellings. This raises £140m per annum.

If Ministers want to truly capture the dynamic benefits of stamp duty reform, we believe there is a clear intellectual and economic case for going further, although this would mean the package of reforms are no longer cost-neutral for taxpayers. This would mean:

- Abolishing stamp duty entirely on all main residences. This would cost £5.2 billion, or £1.9 billion more than the revenue raising measures proposed above. This should be seriously considered if fiscal room allows, or if ministers identify further revenue raising measures that would fund the £1.9 billion extra cost.

- Home buyers of main residences could be given the option to choose at the point of purchase whether to either (a) pay stamp duty as now and enjoy the Capital Gains Tax exemption on their main property as now or (b) not pay stamp duty on purchase but instead pay Capital Gains Tax on the profit from the sale of their home when they sell it. In the short term, people electing to not to pay stamp duty would cost the Exchequer income, but in the long term might (depending on house price growth) deliver more revenue. The cost of the main residence CGT exemption at present is £27.2 billion per year, whereas main residence stamp duty only raises £5.2 billion per year – although the CGT figure is flattered by substantial house price growth over the past 30 years which may not continue into the future.

Taken together, the changes proposed in this paper will help tilt the playing field back towards owner-occupiers and provide a powerful signal that this Government believes in home ownership.

This would be achieved by cutting stamp duty for owner occupiers and first time buyers, while increasing stamp duty and other taxes for non-UK residents, second home buyers and property investors – who have been crowding out owner occupiers and first time buyers. With home ownership in precipitous decline for fifteen years, there is a clear moral and economic case for policymakers to prioritise homeownership in this way.

Options for reform

Table 1: Options for reducing stamp duty on primary residences

Options for changing stamp duty on primary residences	Estimated cost to the Exchequer per annum*	Number of beneficiaries Per annum	Worked examples			
			£280,000 house		£800,000 house	
			Effective rate	Duty paid	Effective rate	Duty paid
No change	0	0	1.43%	£4,000	3.75%	£30,000
Raise in the exemption limit to £500,000	£2.1bn	770,000	0%	£0	3.75%	£30,000
Raise in the exemption limit to £500,000 and halving of stamp duty rates for properties over that	£3.3bn	850,000	0%	£0	1.88%	£15,000
Raise in the stamp duty threshold to £500,000	£3.8bn	850,000	0%	£0	0.75%	£6,000
Raise in the stamp duty threshold to £500,000 and halving of stamp duty over that	£4.3bn	850,000	0%	£0	0.94%	£7,500
Complete abolition of stamp duty	£5.2bn	850,000	0%	£0	0.00%	0%

* *Costs calculated as if they had been levied on property values and transactions in 2017–18.*

The change highlighted in grey is the one which is immediately recommended, with consideration of complete abolition of main residence stamp duty suggested if fiscal room allows.

Table 2: Options for covering costs of stamp duty reduction

Policy	Estimated additional revenue raised	Notes
A tax of one per cent on homes empty longer than 6 months in each 12	£645m	Data suggests there are 215,000 meeting this criteria. Slightly higher than average estimated value per property.
Raising the surcharge on additional properties from three per cent to five per cent	£790m	This would increase stamp duty rates on the 23 per cent of residential purchases that are for second homes or investment properties. A behavioural change has been allowed for in this estimate, although when the three per cent surcharge was introduced there was no behavioural change.
A new (additional) surcharge of three per cent on non-UK resident purchasers of residential	£540m	Data on foreign ownership and elasticity responses is limited, but the majority of high-value properties purchased by foreign non-resident buyers appear to be in Greater London.
Introduce additional Council Tax band and End empty/2nd Home CT relief	£173m £75m	Exact revenue depends on local council tax rates and distribution of high-value properties in the new bands.
Adding eight per cent non-residential stamp duty band for properties over £1m	£682m	Would only apply to 11 per cent of non-residential stamp duty purchases; the majority are under the £1m threshold. Only applies to the portion of the value over £1 million. Elasticity allowed for.
Introduce stamp charge on change of Ultimate Beneficial Ownership of enveloped properties and double ATED	£175m £140m	These are sound transparency measures as well – by recording Ultimate Beneficial Ownership in the land registry (necessary to track changes in UBO and levy stamp) money laundering through UK residential property will become materially harder.
Total	£3.22bn	

These measures finance the proposal in the previous section to abolish stamp duty entirely on properties under £500,000 and halve current stamp duty on properties worth more than this.

The challenge

How Stamp Duty makes the housing crisis worse

This section summarises the problem with Stamp Duty Land Tax (SDLT) in the UK, and the implications this has for the ability for ordinary people to gain and retain a foot on the property ladder.

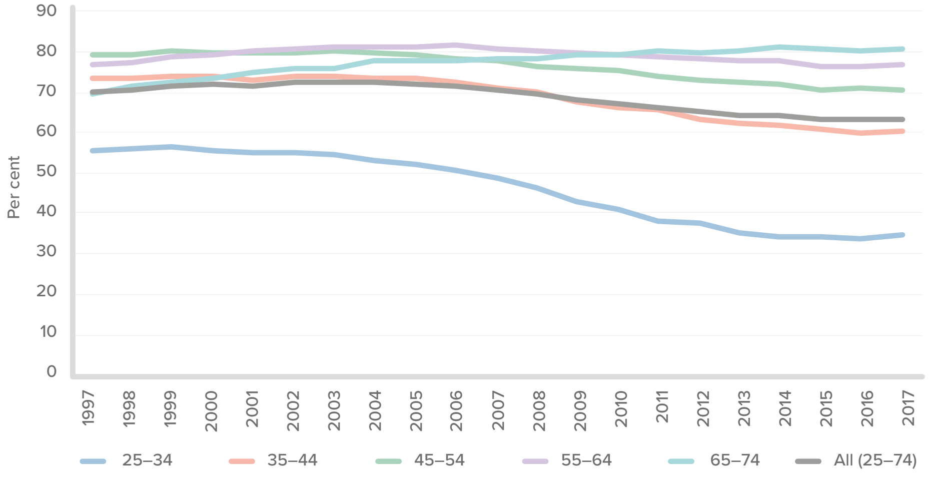
Stamp duty and housing

Home ownership is declining in the United Kingdom

63 per cent of households own the house they live in in the UK,[1] but the rate of homeownership has been declining since a peak of 71 per cent in the early 2000s.

- This means that home ownership in 2017 was similar to levels last experienced in the 1980s. This is primarily driven by declines in ownership by younger generations and especially 35–44 year olds.
- Whilst renting can sometimes be advantageous for flexibility, the main driver of declining home ownership is affordability. In a 2014 poll of private renters, 67 per cent reported that the reason they rented from a private landlord was being unable to afford their own property.[2] A recent review of tenants by a PRS firm found that two thirds of budgeting families intended to buy property at some point in future, but currently rented.[3]
- As shown in Figure 1 below, this trend is particularly acute for specific groups. For example, the homeownership rate for 25–34 year olds has dropped from 55.2 per cent in 1996 to just 34.9 per cent in 2017,[4] a considerably larger decline than other age groups. As shown by Onward's *Generation Why?* Report, this group is substantially less likely to vote Conservative than previous cohorts, in part because of declining homeownership.

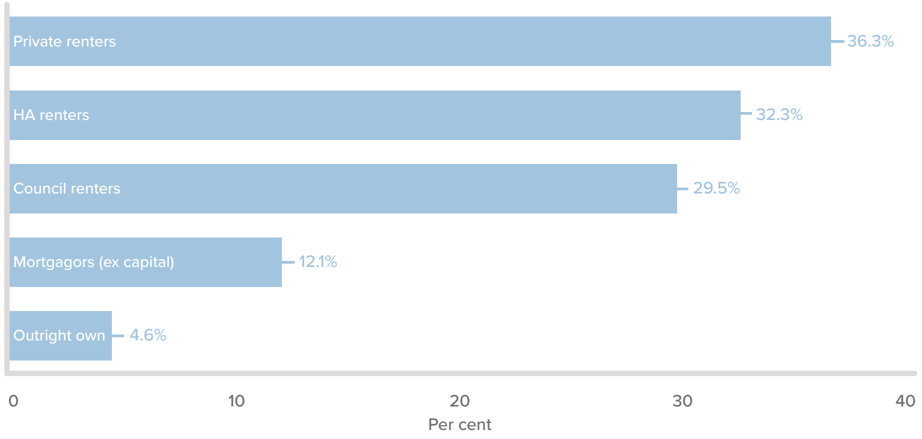
Figure 1: Home ownership by age group (England)



Source: Institute for Fiscal Studies, 2018

- This is despite clear evidence that home ownership brings a number of benefits to those able to buy a home:
  - Those who own their own home enjoy a more secure tenure.
  - Housing costs for people owning their own home are lower than for those renting.
  - Over the long term, it is financially better to own rather than rent – even if house prices do not rise faster than inflation.
  - Owning a property gives many people a real sense of a place they can really call home.
- It is no surprise, then, that 86 per cent of the public aspire to own their homes. Yet only 63 per cent actually do; nearly a quarter of our fellow citizens wish to own their own home but do not.

Figure 2: People renting pay far higher costs for their housing than those who own their own home



Source: Resolution Foundation, "Home Affront", September 2017

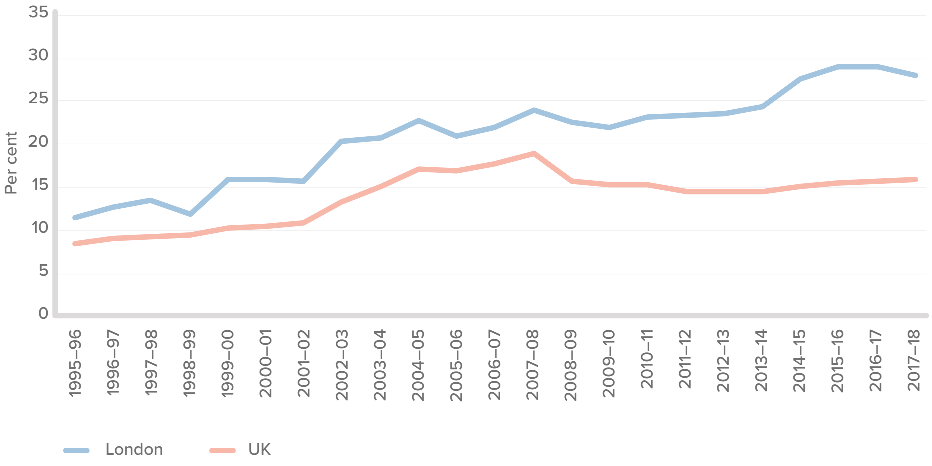
- Affordability is a significant challenge in the parts of the UK with the most economic opportunities. Whilst there are numerous other components to the housing crisis, including lack of demand or poor quality in some areas,[5] it is nonetheless the case that the cost of housing is prohibitively high in some parts of the country. In London, average house prices in an area can range from 9.8 times median wages to 44.5 times median wages, and in the South East the comparable figures range from 7.2 times median wages to 18.6 times median wages.

Figure 3: Housing affordability ratios in Local Authorities (England and Wales), 2018

Source: Office for National Statistics, Affordability ratios for local authorities, England and Wales, 2018

- In practice this means that saving to afford housing is incredibly difficult for young families in England. Across all English regions the number of years taken for the median under-35 year old to save for a deposit has increased substantially in the southern half of the country over the past two decades. But, for young households in the north and midlands, saving for a deposit has become slightly more affordable since the financial crisis.
- In general, the picture is one of house prices racing away from incomes. The number of years it statistically takes to save for a deposit for the median home has increased from eight years in 1995 to 13 years in 2018. In London and the surrounding regions this has risen even further. The number of years needed to save for a deposit rising from ten years in 1995 to 24 years in the capital.

Figure 4: Average number of years it would take to save for a deposit



Source: Onward analysis, HBAI, Nationwide house price index and Land Registry data (1995–2018)

Solutions to the housing crisis will take a long time to have an impact

Whilst a multitude of different factors can affect the price of land and housing, new housing and the land to build it on are the fundamental factors driving rising house prices.

- Estimates suggest between 240,000 and 340,000 new houses are required each year to meet demand, and the Government has pledged to deliver 300,000 homes by the mid-2020s. Despite substantial increases in recent years, and over 220,000 homes being met last year, the market remains some way off price stability.[6]
- As Onward's previous paper *Green, Pleasant and Affordable* notes, the main factor limiting supply is not the lack of available land, but rather the failure of the planning system to deliver well-designed homes in the right places and with the requisite infrastructure. This creates a "vicious circle" of opposition to new development and rising prices.[7]
- Reforms to the planning system, changes to property taxation to limit investment in housing as a speculative asset, and greater power for communities to acquire and build on land can all help address the UK's housing crisis in the long term – and should be pursued by the next Government. In the short-to-medium term, however, more specific policies will be needed to help people realise their dream of home ownership.
- Ministers have recognised this challenge and introduced numerous policies to respond to it. The Help to Buy Equity Loan scheme aims to help ownership through lending for the purpose of purchasing eligible new-build properties and has been judged as a success against its objectives by the National Audit Office,[8] and in 2017 Stamp Duty relief was introduced for first-time buyers.[9]
- In addition, the Government has introduced a number of proposals and policies to help the transition from rental to ownership, including Onward's previous recommendations to reform Capital Gains Tax in order to help renters purchase the home that they live in.[10] These all have an important role to play, but do not address one of the fundamental issues constraining the UK housing market. To make progress in the coming years, more immediate policy changes are needed.

Stamp duty creates an effective barrier to home ownership, both directly and indirectly

Stamp Duty Land Tax is a tax charged in England when property is purchased,[11] and is levied on residential properties above £125,000.

- After changes in 2014 it is now charged on a 'slice' basis, with different rates charged on different portions of property value.[12] In 2017, the threshold was changed for first-time buyers to £300,000 as part of a package to help them get on the housing ladder.[13]

Table 3: SDLT rates for normal and first-time buyers[14]

Standard SDLT rates		First-time buyer under £500,000	
Price band	**Rate**	**Price band**	**Rate**
Up to £125,000	Zero	Up to £300,000	Zero
£125,000 to £250,000	2%		
£250,000 to £925,000	5%	£300,000 to £500, 000	5%
£925,000 to £1.5 million	10%	x	x
Above £1.5 million	12%	x	x

- If a current homeowner bought a house for £350,000, they following SDLT charges would apply:
  - The first £125,000 is not taxed.
  - The next £125,000, from £125,000 to £250,000, is charged at two per cent: £2,500.
  - The next £100k, from £250,000 to £350,000, is charged at five per cent: £5,000.
  - The total equals £7,500, an effective tax rate of 2.1 per cent.
- If a first-time buyer bought the same house, the following charges would apply:
  - The first £300,000 is free.
  - The next £50,000, from £300,000 to £350,000, is charged at five per cent: £2,500.
  - The total equals £2,500, an effective tax rate of 0.7 per cent.
- Whilst SDLT is paid by the buyer, some of the cost or incidence of the tax falls on the seller who has to offer a lower selling price to offset the cost of the tax.[15] A study from the 2008–09 stamp duty holiday in the United Kingdom estimated that approximately 60 per cent of the benefits of the stamp duty tax reduction accrued to the buyer, suggesting that despite this are significant costs that they take on.[16]
- Despite its revenue-raising power, stamp duty creates significant barriers to people moving, meaning that they are less likely to downsize and the available housing stock gets misallocated. This is because stamp duty is a transaction tax which is levied only when property is purchased, and which can therefore be avoided by not buying. Stamp duty is a cash cost (it cannot normally be mortgage funded) and for buyers struggling to put together a deposit can stop them from being able to buy.
- In practice, this means stamp duty causes fewer moves; a 2013 study from Australia found that a 10 per cent increase in stamp duty lowers turnover by 3 per cent in the first year and 6 per cent if sustained over a three year period,[17] and a 2017 study in the UK found that an increase from 1–3 per cent reduced mobility by around 40 per cent.[18]

- This is because the cost of the transaction can outweigh the benefits of moving, therefore meaning people stay put or focus on improving their home. An LSE paper on SDLT suggested that this prevented mobility, contributing to the UK's productivity problem and issues with social mobility.[19] In particular, despite the fact that financial benefits of downsizing will likely outweigh stamp duty,[20] survey evidence suggests that many old people still view it as a barrier to moving.[21]
- As a result, SDLT, combined with high deposit rates, can limit the ability to buy, both by increasing costs, and by reducing the availability of suitable houses. In particular, stamp duty is a cash cost that usually cannot be mortgage funded. Cash costs are often the main barrier to buying a new home. In short, stamp duty reduces home ownership, both directly and indirectly.
- There is a near consensus from academics and economists that stamp duty is in principle a poor tax. The Mirrlees Review, the most comprehensive review of the UK tax system in decades, conducted by the Institute for Fiscal Studies, suggested that the main justification of SDLT was the revenue it raised and that otherwise there was not a clear economic rationale for it. In 2017–18, SDLT raised £12.9 billion in revenue for HM Treasury, from 1.2 million transactions. The majority of this comes from residential tax receipts.

Figure 5: Stamp Duty Land Tax receipts, 2006–07 to 2017–18

Source: Annual Stamp Taxes Statistics Publication, HMRC, 2018/19

Non-owner occupiers entering the market

Owner occupiers are being crowded out by second home buyers, UK based property investors and overseas investors.

- Last year, 23 per cent of residential transactions fell into one of these categories. The introduction of the three per cent stamp duty surcharge for these types of buyers[22] in 2016 did not affect their volumes – they were undeterred.

- Reports suggest that nearing 50 per cent of new build in central London and even in Birmingham[23] and Manchester[24] is being sold overseas to investors, mostly from the far east. They have superior financial firepower compared to UK prospective owner-occupiers and are often pricing them out of the market. We should seek through policy to tilt the playing field more in the direction of owner occupiers and first time buyers.

Box 1: Overseas buyers are taking up around 50 per cent of London new-build stock – even cheaper flats in the suburbs

Examples of Recent Developments sold Abroad:

- **Heygate Estate**, Elephant & Castle. First 51 units of a regeneration project all sold abroad.
- **Baltimore Wharf**, Isle of Dogs 87 per cent of the 2,999 apartments sold overseas.
- **Edgware**. 100 Flats in an Office-to-Residential Conversion. Near the tube station. Average price £300k per flat. 75 per cent sold off-plan in the far-east.
- **Hounslow**. 250 Flats in an Office-to-Residential conversion. Average price £225k per flat. Over 50 per cent sold off-plan to the far-east.
- **Manchester**, 230 flats. Average price £23k per flat. 94 per cent sold to non-UK residents (17 UK, 47 Hong Kong, 26 UAE, 17 Singapore, 8 South Africa, 5 Malaysia, 3 Thailand, 125 a BVI company, rest – Others).

Source: Interviews; The Bow Group.

Solutions

Reducing stamp duty for owner-occupiers

Britain's problem with declining home ownership and private share ownership are well documented. This chapter outlines how stamp duty could be cut for people buying their primary home. It proposed three different options for how stamp duty could be significantly reduced on the places people live – thereby boosting the ability for British people to buy or move houses. The options we explore are:

1. Exempt all primary residences under £500,000 from stamp duty and (potentially) halve current stamp duty rates for properties sold for more than that.
2. Raise stamp duty exemption for primary residences to £500,000 – i.e. have a zero stamp duty rate up to £500,000 for all primary residences under that price – and (potentially) halve the current stamp duty rates for properties above that level.
3. Abolish stamp duty on all primary residences.

These policies would have an annual cost ranging from an estimated £2.1 to 5.2 billion per annum. It is recommended that, at a minimum, we exempt all primary residences sold for below £500,000 from stamp duty and halve the current stamp duty rates on primary residences sold for above £500,000. The cost of this is £3.3 billion.

We suggest a number of alternative revenue-raising options that could be used to cover the costs. These are:

- An annual surcharge on empty properties, levied at one per cent of the property's value.
- Raising the stamp duty surcharge on additional properties from three per cent to five per cent.
- Introducing a stamp duty surcharge on foreign purchasers of three per cent.
- Introducing an additional council tax band to recoup some of the costs on the most expensive properties.
- Ending any council tax relief for vacant properties or second homes.

Adjusting non-residential stamp duty to add an additional eight per cent band for the portion of commercial properties over £1 million;

In addition, we propose some wider adjustments that will help address some of the structural issues with how taxation on properties is levied in the United Kingdom, and in particular to raise money through policies to address the avoidance of stamp duty. Specifically we propose that:

- Where a residential property is owned by a company the ultimate beneficial owner of any property should be registered at the Land Registry, and stamp duty should be levied when this changes, thereby meaning it is charged on enveloped properties when they change hands.
- The rate of annual tax on enveloped dwellings (ATED) should be doubled, thereby increasing the annual charge on residential properties owned through commercial vehicles, rather than by the owner or resident themselves. Existing exemptions should remain.

These changes, taken together, will help tilt the playing field back towards owner-occupiers. This would be achieved by cutting stamp duty for owner occupiers and first time buyers, while increasing stamp duty and other tax for non-UK residents, second home buyers and property investors – who have been crowding out owner occupiers and first time buyers.

Reducing or abolishing stamp duty on Primary Residences

Stamp Duty has continued to exist primarily due to its revenue-raising capabilities. Whilst there have been various calls to abolish it,[25] in 2017–18 it generated £12.9bn for the exchequer; an increase of £1.1bn compared to 2016–17.[26]

- Residential SDLT receipts account for a significant proportion of this, accounting for approximately £9.3bn of SDLT receipts in 2017–18. Whilst the tax may cause economic distortions and worse outcomes, the significant cost of abolishing it has meant that there has been no serious attempt to do so.
- Despite this, some policy moves have acknowledged the issues that Stamp Duty is causing for affordability. In 2017, the Chancellor announced a First Time Buyers' (FTB) Relief on SDLT on properties up to £300,000, with additional relief on properties up to £500,000. This move has already benefited 121,500 first time buyers to the tune of £284 million.[27]
- However, the UK remains some way short of outright abolition and millions of people pay stamp duty every year. This means that most of the distortive effects of the tax persist, including misallocation of housing resources and reductions in labour mobility.
- To reduce these effects, and the amount of purchasers that they impact, we propose significant reductions in stamp duty on primary residences, or its abolition altogether.

Exempting properties under £500,000 from stamp duty

One option is to change policy to ensure that less expensive properties no longer pay stamp duty.

- This would mean granting an exemption for properties under £500,000, meaning that stamp duty is only paid by properties over this amount.
- Given that stamp duty is currently levied on residential properties above £125,000 – this would mean making up to an additional £375,000 worth of the purchase tax free for eligible properties. For those properties above £500,000 the same amount of stamp duty would continue to be levied at the same rate.
- In 2018–19, some 84.7 per cent of the total properties liable for stamp duty were sold for less than £500,000. However, after accounting for additional properties being purchased, this decreased to 56.3 per cent of transactions. This would mean the exemption would cover over half of current transactions that stamp duty is currently applied to.[28] Exceptions would be those over the exemption limit or first-time-buyers purchasing properties as they are already exempt when purchasing properties below £300,000.

- In April 2018 the average detached house in England was worth £367,142.[29] The increase in the exemption would save someone purchasing this house approximately £8,300. This would significantly reduce the costs of moving house, for example to have more space for a family, or to move towards a new employment opportunity.
- Using 2017–18 figures, the stamp duty charged on these properties brought in approximately £2.15bn worth of revenues, or approximately 23.1 per cent of total residential stamp duty receipts. This would mean that the total cost of this policy would be **£2.1bn in total**.
- The dynamic effects of a cut in stamp duty rates would be to increase transactions. Because the rate being charged would be zero this would not result in more revenue directly from these properties, though there may be increased activity which increases prices above the exemption limit. In addition, early figures from 2018–19 suggests that SDLT revenues have fallen slightly in 2018–19 from £12.9bn to £11.9bn. This also means that the total cost of the policy might be fractionally less.
- A variation of this policy could be to instead apply the £500,000 threshold to all properties, creating a 0 per cent rated band for the first £500,000 of all primary residences. In this case we would expect an additional cost of £1.2bn per annum from the component of more expensive properties that would now be tax free. This would bring the total cost of the **policy package to £3.8bn**.

Accompanying the exemption with a 50 per cent cut in stamp duty rates

Exempting primary residences below £500,00 would benefit some 770,000 buyers a year, but the impact would be confined exclusively to those purchasing houses below the £500,000 limit.

- Whilst this is undoubtedly generous, it would not necessarily have the impact of increasing transactions and mobility in the parts of the UK economy where it is arguably most needed.
- House prices in London are significantly higher than this, with the average semi-detached property in London costing £580,900 in May 2018, and the average detached property costing £906,200.[30] Given that this is one of the areas that may be most in need of having homeowners move or downsize to use housing stock more efficiently, it is arguable that a more ambitious policy that also reduces stamp duty for properties above £500,000 might be needed.
- One option is to accompany the rise in the exemption limit with a 50 per cent cut in the stamp duty rates levied on those still paying stamp duty. This would mean, for example, that the five per cent rate above £500,000 would shrink to 2.5 per cent, and the rate charged from £925,001–£1.5m would decrease from 10 per cent to five per cent. Finally, the rate charged on the remaining amount would shrink from 12 per cent to six per cent. Much like the previous proposal, this would only apply to primary residences.

- Using data from 2017–18, receipts from houses worth above £500,000 were worth approximately £5.36bn. However, 44 per cent of those revenues came from the HRAD proportion of residential receipts, meaning that they were not from primary residences. This means that revenue charged on this group generated just under £3bn worth of SDLT receipts (£2.96bn).
- An effective halving of the rate that is paid on these properties would mean foregone revenue, and therefore a cost to the government, of approximately £1.5bn in 2017–18, assuming no behavioural change. This would be in addition to £2.1bn estimated cost of bringing the exemption limit up to £500,000.
- However, one of the features of transaction taxes is to dampen activity due to increased costs. Estimates from the OBR on the responses to changes in stamp duty suggest that a one percentage point increase in stamp duty at a given rate reduces transactions by about 4.5 per cent and prices by about 1.5 per cent for homes worth between £250,000 and £1m, and by about six per cent and 1.5 per cent respectively for homes valued over £1m.
- Applying these figures in reverse, a cut in rate would likely increase the sales of homes and also marginally increase prices. Cumulatively, the large change in rates would mean that we would expect transactions of homes, and the prices they were sold at to rise. We estimate that this would offset some of the lost revenue from the cut in stamp duty, reducing the total cost of the policy to £1.2bn.
- This would mean the total **cost of the policy would be approximately £3.3bn**, comprised of £2.1bn of cost from the raise in the exemption limit, and an additional £1.2bn cost that comes from halving the SDLT rate for primary residences.
- If the threshold was increased on all properties rather than just those under £500,000 and this was accompanied by a reduction of 50 per cent in the rates, this would mean a **total cost of £4.3bn,** a significantly higher figure than if the exemption limit only applied to houses under £500,000.

Abolishing stamp duty on primary residences

The alternative approach is to abolish stamp duty on principal residences altogether.

- This would give a significant tax break to all 854,000 people buying a primary residence each year, including first time buyers who are purchasing a property over £300,000. Crucially, because all primary residences would be eligible, it would completely remove the transaction costs people incur from moving, meaning that housing is much more likely to be allocated efficiently in the future.
- The merit of this approach would be that, compared to other alternatives, the complete removal of transaction costs would accelerate housing sales, meaning that residential properties would be more likely to be allocated efficiently – for example allowing people to move to be nearer their work with greater ease, or to downsize.

- OBR elasticity estimates suggest that a 1 percentage point increase in stamp duty is associated with a 4.5 per cent reduction in transactions. Extrapolating this in the opposite direction, abolishing stamp duty in its entirety could increase house sales amongst properties worth between £250,001 and £925,000 by approximately 22.5 per cent.
- In practical terms that would mean more people in homes that suit them, rather than staying put to avoid stamp duty. To ensure that it was targeted at those living in the accommodation, abolition would be limited to primary residences. Second homes and buy-to-let properties should continue to be subject to current rates, including the three per cent surcharge introduced in 2016.
- The cost of this would be significantly smaller than the £12.9bn from the abolition of all stamp duty. On 2017–18 data this would have meant a cost to the Treasury of **£5.2bn in foregone taxes**. Unlike the previous option, none of the increased activity would cause compensating increases in revenue, as none of the properties would be liable for stamp duty anymore.

Policies to cover the costs of reducing stamp duty

In order to address the shortfall that reducing or abolishing SDLT on primary residences would cause, we propose a number of options to adjust taxation of properties in the UK. The principle underlying these changes would be to reward the use of the UK's housing stock for its primary purpose – providing somewhere to live, and to pay for it by taxing less desirable uses of housing such as speculative investment.

Taxing empty homes

One such use is leaving a property empty. There are an estimated 630,000 empty homes in England,[31] of which 215,000 were empty for over six months.

- Since 2010 there has been a concerted effort to bring empty homes into use[32] and research has shown strong support for tackling this issue across Parliament.[33]
- Internationally there are several examples of successfully taxing empty homes; Vancouver levies a tax of one per cent of an empty property's value, bringing in approximately $38m CAD in 2017, and Australia levies an annual vacancy fee on foreign-owned vacant properties.[34] In the UK, some local authorities such as Croydon also charge a higher rate of council tax on empty homes.[35]
- To incentivise the transfer of empty homes back into use, and to cover a proportion of the cost of abolishing stamp duty for primary residences, the introduction of a one per cent annual tax on the value of empty homes could be introduced. Research released earlier this year suggests that around 3.4 per cent of all properties in England and Wales lacked a permanent resident,[36] which is broadly consistent with the 630,000 figure above. However, it would seem more reasonable to levy a charge only if the property were vacant for more than 6 of the last 12 months (215,000 properties, as per the MHCLG data above) and levy a one per cent tax on the value on them. This would raise **£645 million**.

- Unlike parts of Canada and the US there is currently no tax based on current property value, and therefore no obvious mechanism to regularly identify, value, and tax properties, Councils already levy additional charges on vacant or empty properties. This could be used to identify the relevant properties, which could then be evaluated and the appropriate sum levied on them, initially on a self-assessed basis with a substantial penalty for manifestly inaccurate self-valuations.
- In practice the sum generated may be smaller than £645 million as the introduction of an annual levy on vacant properties would likely encourage some vacant properties to be pressed into alternative use or to be sold. This would undoubtedly be good for maximising the use of the UK's housing stock, but would reduce the revenue raised by the policy.

Raising the surcharge on additional properties from three per cent to five per cent

In 2016 the Government introduced higher rates of SDLT on additional properties purchased, known as the Higher Rate on Additional Dwellings (HRAD).[37]

- This has had a significant impact on stamp duty revenues; additional dwellings transactions accounted for 23 per cent of residential transactions (an increase of 4 percentage points) in 2017–18 and 44 per cent of residential receipts (an increase of 5 percentage points).
- The extra rate is currently 3 percentage points above the current stamp duty rates and levied on the entire price of the property. It is applicable to anyone purchasing a second property that is not their main residence, and was introduced to generate tax revenues to help double the affordable housing budget.[38]
- Despite the increased costs, the number of additional dwellings, or second homes, purchased in the UK rose significantly between 2016–17 and 2017–18. In 2017–18, a total of 252,000 additional dwellings were purchased and charged the surcharge.
- Three per cent of additional dwellings transactions were valued above £1 million in 2017–18, accounting for 37 per cent of residential transactions and 50 per cent of residential receipts within this price band.[39]
- One option for covering the cost of reductions in stamp duty for primary residences is to increase this levy. An increase of 2 percentage points from three per cent to five per cent would mean that, holding behaviour constant, around £1.3bn more revenue would be generated from the sale of additional properties, and the total maximum level of stamp duty for additional homes valued over £1.5m would rise to 17 per cent.
- However, the increased rate would likely reduce demand. Using data from OBR[40] on stamp duty elasticities, we estimated that a tax increase of 2 percentage points over the year 2017–18 would have meant that, after accounting for reduced prices and transactions, £4.9bn would have been raised. This would mean a **£790 million** net revenue gain compared to what the three per cent tax raised that year.

- In practice, the figure is may be greater; so far the responsiveness of second home owners to stamp duty has appeared to be limited, and the HRAD has so far generated significantly more revenue than was initially expected.

Introducing a surcharge on foreign purchasers of three per cent

The 2018 budget proposed a one per cent surcharge on UK properties owned by non-UK residents, driven by concerns that foreign investment in the UK property market has driven up prices for British residents. The consultation period for this proposal ended on 6th May, and the outcome is to be released shortly.

- There are definitely a significant number of properties and transactions that this could apply to. Research from York University and LSE found that 13 per cent of new-build properties sold in London between 2014 and 2016 were bought by overseas buyers. The proportion rose from 10.5 per cent in 2014 to 17.9 per cent in 2016. Overseas buyers accounted for 36 per cent of sales in 'prime' boroughs (the City of London, Westminster and Kensington & Chelsea) compared to 16.2 per cent in the rest of inner London and 5.7 per cent in outer London.
- There appears to be some evidence for the idea that curbing foreign investment in the UK property market could reduce prices and make housing more accessible; research by King's College London University[41] finds that foreign investment has an upward and significant impact on local house prices, with an increase of one percentage point in the volume share of residential transactions registered to overseas companies leading to a 2.1 per cent increase in house prices.
- Data on foreign ownership of property is harder to identify as no official statistics are published. However, estimates from Savills suggest that around 32 per cent of 'Prime' London Buyers are international, with around a third of that group purchasing properties either as second homes, or as investments.[42] Other estimates suggest that 7 per cent of all new and second hand residential sales in Greater London and 20 per cent of sales in inner London were to non-residents.[43]
- We propose a three per cent stamp duty surcharge (in addition to the new five per cent surcharge for non-main residence buyers already suggested above) for non-UK resident buyers of residential property. On the conservative assumption that this would affect 20 per cent of London and five per cent of non-London new build sales, and 2.5 per cent of all second-hand transactions, the three per cent surcharge would raise **£540 million** (assuming that the an overseas buyer is buying units at about twice the general average value, given their preference for prime central London and new build projects).
- The Government's consultation on the surcharge indicated the possibility of sensible exemptions or refunds for foreign owners who actually reside in the properties, ensuring that the UK still remains open for foreign workers. These should be taken forward, but it is right and fair that those who seek to use UK properties as investments should pay a significantly higher price, and that the funds raised should help British people get on the property ladder.

Introducing two additional Council Tax bands

The most significant direct beneficiaries of the reduction or abolition of stamp duty would be those purchasing expensive houses. One option to recoup some of the revenue in a better designed tax would be to partially make up for the cost of the policy through the introduction of an additional council tax bands above on extremely high value properties.

- This would mean that whilst people purchasing the most expensive houses would see a significant reduction in their stamp duty, this would be offset by year-on-year rates of higher council tax.
- We propose that this new band would have a threshold 25 per cent higher than the existing band H. Using government statistics on the number of homes in each council tax band and Land Registry transactions, we estimate that this would mean approximately 103,000 houses in the new upper band. These would be predominantly concentrated in areas with high house prices; London and the South East have over 70 per cent of band H properties, meaning that the same places where most of the benefits of a large change in stamp duty would be felt.
- Multiplying through the number of homes in the new bands by the average extra rate (say an extra £1,700 per year) charged at that level, we estimate this would generate an **additional £173m per annum**. This is consistent with other estimates; the Resolution Foundation found in 2018 that a higher rate council tax bracket above band H would generate £100m, an estimate that is similar, but lower due to the fact that they allocated fewer houses to the upper band.
- In addition, there are a number of discounts that exist on second homes and vacant dwellings, although how a council chooses to treat these is up to the authority. Abolition of these reliefs could save £3.8m and £70.9m from second homes and vacant dwellings respectively, **making £75 million in total**.

Adjustments to non-residential Stamp Duty

One of the characteristics of Stamp Duty on commercial and non-residential property is that the rate charged is currently set at a maximum consistent rate of five per cent on properties over £250,000.

- There is a compelling rationale for this distinction in that businesses will have a clearer rationale for needing larger premises such as office buildings and warehouses. However, this lower rate comes with a large cost, and there is a credible case that can be made for increasing the rate to bring it slightly closer to the one charged on residential properties.
- One option would be to make SDLT on non-residential property slightly more progressive by adding an additional band above £1m at a rate of eight per cent. This would mean that the new set of thresholds and rates would be:

Table 4: Possible rates for non-residential stamp duty

Thresholds	Current rates	Proposed rates
Under £150k	0%	0%
£150k to £250k	2%	2%
£250k to £1m	5%	5%
Over £1m	5%	8%

- This would generate a significant amount of new revenue. By combining the taxable value by the rates charged at each threshold and the number of transactions, and adjusting for changes in behaviour, it is possible to estimate how much this would generate. Our calculations suggest that compared to the existing baseline this would raise an additional **£682m** each year compared to the current SDLT rates.
- Whilst an increase of three per cent to the rate appears large, the change in the effective rate is much lower due to the fact that the eight per cent rate only becomes active after the property exceeds £1m. As an example, a commercial property bought for £1.3m would be charged nothing on the first £150k; two per cent on the next £100k; five per cent on the next £750k; and eight per cent on the remaining £300k. The total SDLT would equal £63,500. Previously this property would have been charged a flat five per cent on the value over £250k, for a total SDLT of £47,500. The effective tax rate on this property increases from 3.65 per cent to 4.88 per cent.
- This would not obviously be a tax on most businesses; only 11 per cent of non-residential SDLT transactions are on properties worth over £1m, meaning that the other 89 per cent would see their purchases of properties unchanged. Of the eligible properties, nearly four in ten would be based in London or the South East, indicating that much of this is driven by the generally high cost of land in those areas.

Improving transparency of property ownership

One way that stamp duty is frequently avoided is the use of companies and other vehicles that purchase the residential property. Whilst a punitive 15 per cent rate of SDLT is now levied on these transactions when the property is purchased by a company, many high-end properties were placed into corporate ownership many years ago, before the 15 per cent SDLT rate was introduced.

Currently, when one of these properties is sold, sale of the property can then be achieved by selling the shares in the company that owns the property. This means that regular stamp duty on the property sale is not paid. Often, the company owning the property is based in a jurisdiction such as the Cayman Islands or British Virgin Islands. This is because the share register in these places is not transparent, and it is a means of disguising the true ultimate beneficial ownership of the properties. So not only is stamp duty lost, but it can facilitate money laundering.

There are two changes that will seek to raise further revenue and also promote transparent disclosure of ultimate beneficial ownership:

- Where a residential property is owned by a company the ultimate beneficial owner of any property should be registered at the Land Registry as on the title deed. When there is a change of ultimate beneficial owner, the price should be disclosed and a stamp duty charge levied as is the property had been sold in the normal way. It is estimated that this will raise **£175 million per year**, assuming a 10 per cent turnover of ownership per year and assuming that only properties worth more than £2 million in corporate wrappers are transferred by way of sale of the company.
- Residential properties owned by companies (and not under development or rental) over £500,000 in value are subject to an Annual Tax on Enveloped Dwellings (ATED) to discourage the practice. ATED ranges from £3,600 per year for properties worth £500,000 to £1 million, up to £226,000 per year for properties worth over £20 million. This tax should be doubled, leading to extra receipts of **£140 million per year.**

Creating the option to pay Capital Gains Tax instead of Stamp Duty

A final option to consider as a medium-term reform is allowing people to choose, at the point of purchase, whether to pay stamp duty or instead choose to forgo the capital gains tax exemption which they currently enjoy.

- Under the current system, the capital gains on an individual's primary residence are tax free. This costs £27.2bn per annum, one of the largest individual tax reliefs.[44]
- There are strong reasons to retain this relief. For one – having made the rules that people structured their purchasing decisions around it could be considered unfair to tax them for retrospective gains that are only just being realised with the sale of the property. Moreover, the concept of a completely new tax is a generally unwelcome and unlikely to be politically feasible.
- However, in many ways Capital Gains Tax would be better than Stamp Duty; for one, it would be levied on a generally less controllable factor (external influences on house prices), rather than on transactions, meaning it is less likely to cause distortions.
- Capital Gains tax is also more likely to fall only on those who can afford it, as it is not levied when there have been no gains in the house price, after accounting for inflation and improvements that the owner has made. Comparatively, even if somebody is downsizing their house, for example due to the death of a partner, SDLT would still be levied.
- One option would be in this case to provide individuals with the option at the point of purchase between paying SDLT or foregoing their CGT exemption at the point where they sell the house. This would mean that if the individual were unable to afford SDLT, they could elect to instead forego a part of the future potential capital gains, in return for paying no SDLT in the present.

- Conversely, if the individual were able to pay SDLT and was bullish about their house price rising, they could elect to pay their Stamp Duty sum and preserve their full CGT exemption. However, given individuals' aversion to immediate costs and the 'no gain, no payment' approach to CGT, it would be highly likely that foregoing some of the exemption would be a desirable option for many.
- From an Exchequer perspective this would mean an immediate cost in terms of foregone revenue from those who made use of the option to not pay SDLT, but long-term access to a new revenue stream as those individuals sell their houses and pay a portion of Capital Gains tax at a later stage. The amount raised in future CGT would clearly depend on the evolution of house prices over the medium to long term, which is inherently difficult to forecast.
- In the immediate term this would not offset the costs of SDLT reduction, and lower rates of SDLT would reduce the incentives to take up this option. However, in the longer-term it could provide a feasible vehicle to gradually move from a taxation system that punishes people moving, and towards one which captures some of the value from future house price increases.

This is an option that requires further modelling, but merits serious consideration.

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