

Tax Devolution in Wales – Land Transaction Tax

Response by the Bevan Foundation

The Bevan Foundation develops ideas to make Wales a better place and improve people's lives. It is independent of government and politically neutral, and is a registered charity. We welcome the opportunity to respond to the consultation on the proposed Land Transaction Tax (LTT).

Preamble

The Wales Act brings a unique opportunity to reform the tax on land transactions.

We welcome the Welsh Government's proposal to continue with a transaction tax. Although many economists argue that a tax on transactions is not 'rational,'¹ we note that a tax on property transfers is the most common property tax in the OECD² not least because it is easy to collect and hard to avoid. Abolishing a transaction tax would also lose revenue. While in theory the lost revenue could be replaced by increases in business rates and Council Tax, neither of these are popular and Council Tax is highly regressive. There is also some evidence that transaction taxes reduce volatility in housing markets.³

The introduction of a new land transaction tax provides a once in a generation opportunity to get the tax on a fair and firm footing. While we understand the Welsh Government wishes to maintain the revenue generated by a tax on land transactions, we suggest there is potential to develop the new tax as part of the wider effort to encourage regeneration and improve the provision of housing in Wales.

Some have argued that responsibility for paying the tax on transactions should shift from the purchaser to the vendor.⁴ This change would mean that investment in land and property, whether by individuals or institutions, is incentivised by being free of tax. Vendors are also typically in funds, realising any increase in land or property

¹ Mirrlees, J. et al (2011) **Tax by Design**. Institute for Fiscal Studies.

² Lawton, K. and Reed, H (2013) **Property and Wealth Taxes in the UK: the context for reform**. IPPR

³ Oxley, M. and Haffner, M. (2010) **Housing taxation and subsidies: international comparisons and the options for reform**. Joseph Rowntree Foundation.

⁴ For example Henderson, G., Lodge, G., Raikes, L. and Trench, A. (2015) **Assessing the implications of a stronger Wales for the west of England**. IPPR

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values. Further investigation of this option should be undertaken to establish if a switch from payment of the tax by the vendor rather than the purchaser could be beneficial to the regeneration of Wales.

Question 1: Do you think the current residential SDLT rates and bands are suitable for Wales?

- *If you think the current rates are suitable, please provide reasons why.*
- *If you think the current rates are not suitable, please provide reasons why and, where appropriate, provide suggestions for alternative rates and bands.*

The current residential SDLT rates and bands are in our view not suitable because they are arbitrary and have no obvious connection with Wales' residential property market or any policy objectives. The rates and bands should be based on the principles of fairness and soundness, should reflect the circumstances in Wales, and should reflect the Welsh Government's policy objectives in respect of housing.

We would suggest:

- **Review of bands:** There should be provision to review the bands regularly to reflect changes in the housing market e.g. by annual uprating. This would avoid increasing numbers of low value purchases being dragged into the transaction tax net as house values rise.
- **The lowest band –** Careful definition of lowest bands and rates can be used to facilitate access to home ownership for lower-income households. We suggest that the definition of the lowest band should be linked to the structure of the housing market (such as – by way of illustration only – the cheapest fifth or similar).
- **Additional bands** - the additional bands should also be linked to the structure of the Welsh residential property market (for example – and again for illustration only – each band being the value of a fifth of transactions). This would avoid having very high value tax bands that are effectively redundant in Wales. The need for simplicity and compliance suggest that a relatively small number of bands – four or five - would be appropriate.
- **Rates** – we strongly support progressive rates, i.e. that higher rates are applied to higher value transactions. There should be a clear rationale for the different rates – there is at present for example no obvious explanation for the doubling in tax rates at £925,000.

The rate applied to the lower bands is key. Housing costs have an important and direct impact on poverty, although the relationship between poverty and

tenure (and in particular owner occupation) is complex.⁵ It is important to stress that home ownership is **not** a solution to poverty, as it is neither necessarily cheaper than other tenures, nor can owner-occupiers access any equity in their property. Nevertheless there is some evidence that owner-occupation offers some ‘corrective’ against poverty for a minority of people, at any point in time as well as over the life course. For example, owning a home outright can reduce the impact of poverty (e.g. in older age) for some people.

We therefore consider that a zero rate on the lowest band(s) would help lower-income households to be able to purchase property to meet their housing needs and would make a modest contribution to the long-term reduction of poverty.

Question 2: Do you think that the 15 per cent slab rate for certain transactions by non-natural persons should continue to operate in Wales following the introduction of LTT? Please explain the reason for your answer.

It is right that purchases of residential properties by companies, investment schemes etc (non-natural persons) pay a higher rate of tax than individuals and households as the purchase is for business rather than residential purposes. The ‘slab’ approach is discredited and should be replaced with a marginal approach, at no detriment to revenue.

We suggest that rather than distinguish by the type of purchaser, residential property bought for letting should be regarded as a commercial transaction and taxed accordingly. This approach would allow LTT to distinguish more effectively between property bought as primary residences by individuals or households and property bought for business reasons whether by an individual or a company (e.g. second homes, buy to let).

Question 3: What would be the key impacts on the residential market in Wales of having a different transaction tax regime from England?

The response to this question depends on:

- a. whether transaction taxes have an impact on the residential market and
- b. what impacts are deemed to be desirable and undesirable.

In our view, difference in itself is unlikely to have a significant impact. Transactions between individuals are unlikely to be affected by a different regime in England as most residential purchases are not ‘mobile’ over a long distance.

⁵ Tunstall, R. et al (2013) **The Links Between Housing and Poverty: an evidence review**. Joseph Rowntree Foundation

There is strong evidence that the residential property market responds quickly to taxation on transactions in terms of activity, prices and timing of purchases.⁶ Some have suggested that temporary tax relief for first time buyers has also been found to have encouraged increased activity in the market in the short- and longer-run,⁷ although the UK Treasury⁸ concluded that the impact was limited. Land Transaction Tax could therefore be a useful tool with which to stimulate the Welsh Housing Market.

Differences between Wales and England are most likely to have an impact where there are cross-border considerations - there are at least two possible areas where this might be significant:

1. **Cross border residential property market:** a study by IPPR North⁹ found that property prices in south east Wales, even in Cardiff, are significantly lower than those in Bristol and the south west. It concluded that a difference in transaction tax regimes would be most unlikely to overcome the price differential and affect cross-border movement or attractiveness to investors.
2. **Residential property investment market:** the differential in property prices between Wales and some areas of England is often suggested to be a key factor in the purchase of Welsh property for investment e.g. holiday homes, buy-to-let property, although we have been unable to identify any data on this.

As with the wider residential market, it is unlikely that a difference in transaction tax regimes would overcome the price differential, although it is possible that some purchases could be redirected to low-cost areas of England. Whether this is desirable depends on the policy objectives.

Question 4: Do you think the Welsh Government should have the ability to change or introduce new rates and bands in LTT with immediate effect? Furthermore, do you think there are other areas of LTT where it would be appropriate for the Welsh Government to make changes with immediate effect? Please specify

⁶ Best, M. C. and Kleven, H. J. (2013) **Housing Market Responses to Transaction Taxes: Evidence From Notches and Stimulus in the UK.**

⁷ Ibid.

⁸ Bolster, A. (2011) **Evaluating the Impact of Stamp Duty Land Tax First Time Buyer's Relief**, HMRC Working Paper.

⁹ Henderson, G., Lodge, G., Raikes, L. and Trench, A. (2015) **Assessing the implications of a stronger Wales for the west of England**. IPPR

The Welsh Government needs the same powers to change LTT as the Treasury does in respect of transaction taxes in England. This includes being able to make immediate changes to rates and bands – either on its own initiative or because of changes made in England. The Welsh Government also needs the power to make other changes e.g. to introduce temporary reliefs or exemptions. There is a case for Welsh Government to be able to make such changes with immediate effect to avoid ‘blight’ on the market.

Question 5: Do you think the definition used in SDLT defines residential property adequately for the operation of the tax and will be suitable for LTT? Please give details of practical problems with the definition and how you think the definition can be improved (either by statute or by guidance).

As a matter of principle we oppose lack of clarity and uncertainty in taxation matters as they increase the risk of avoidance and evasion. The existence of two different definitions of residential property is a recipe for confusion. We would therefore support a clearer definition but do not have the expertise to suggest one.

Question 6: How important is it to have consistency between the tax regimes in Wales and England for non-residential property transactions? Please provide practical examples to support your answers.

- If consistency is important, what key elements need to be consistent e.g. tax structure (marginal or slab, rates and bands, how transactions are taxed)?

The response to this question depends on:

- a. how sensitive commercial transactions are to taxation and
- b. the sensitivity of national and international investors to variation in tax regimes and
- c. the outcomes that the Welsh Government wishes to achieve.

Changes in LTT compared with SDLT have the potential to encourage beneficial investment in Wales and could in theory be a useful tool for the Welsh Government to encourage regeneration. However, IPPR North’s study of the potential impact of changes in taxation on the south west of England¹⁰ found that the market for office space in Cardiff is already more competitive than in Bristol (with lower rents and higher vacancies). It is unlikely that a reduction in transaction taxes would increase competitive advantage in Cardiff compared with the south west. The evidence on retail was too limited to draw conclusions.

We are sceptical of the possible deterrent effect of a different tax regime on investors, simply on the grounds of difference. They will of course prefer consistency but as they manage already substantial differences in other policy areas e.g. planning, they ought to be able to cope.

¹⁰ Op. cit.

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Question 7: Does a slab structure create distortions in the non-residential property market? Please provide practical examples to support your answers.
- If so, would a marginal rate be an improvement on this? Please give details

We are not aware of any evidence on the impact of the slab structure. As the 'slab' approach is discredited a marginal rate is a better approach.

Question 8: What would be the key impacts on the non-residential market in Wales of having a different transaction tax regime from England?

See answers to question 6.

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