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Scrapping Stamp Duty – an interesting and expensive idea

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Industry voices call for government to reform the existing Stamp Duty Land Tax system (SDLT) on a fairly regular basis. Calls to abolish the tax entirely are less common. But that very suggestion came from two rather different quarters this September. The Organisation for Economic Co-operation and Development (OECD) suggested SDLT should be scrapped to encourage more mobility in the jobs market and remove disincentives for potential downsizers, while a report from the government's innovation agency Nesta proposed getting rid of both SDTL and Council Tax, and replacing them with some kind of system that primarily taxes a property based on the value of the land it occupies.

The UK often takes OECD forecasts with a pinch of salt, and the government has no compunction to enact its recommendations. But the Nesta paper – 'Economic Growth and Productivity – the ideas' was put together with the help of John Van Reenen and Anna Valero of the London School of Economics, who are both members of Chancellor Rachel Reeves' council of economic advisers. Van Reenen is the chairman of that council. Reeves is no doubt familiar with the nine 'ideas' in the report. So Nesta's suggestion on property and land taxes perhaps merits closer inspection.

Nesta's core argument is that replacing the current framework with a 'land value tax' would lead to more efficient use of land via quicker and denser development, which would in turn promote economic growth. By increasing the cost of holding undeveloped land, you encourage landowners to use it as productively as possible.

They say this would get rid of land banking – where developers buy parcels of land, acquire planning permission which makes that land more valuable, and then sit on them for years waiting for them to increase further in value. There are currently 1.1 million plots in the UK with planning permission which have not been built on. However, the report is not clear on exactly how introducing a new tax would prevent land banking – presumably the level of tax would need to set pretty high, pitched so as to encourage developers to build and sell swiftly, to pass responsibility for the land tax on to homebuyers. But crucially, the land tax would need to be set at the right level so as not to deter people from buying in the first place, or decreasing the achievable value of these properties to a point which disincentivizes the builders from building. That in itself would be a challenge.

The report also argues that such a tax change would result in denser urban and suburban building. If true, this would be a welcome development. We have long held that the UK could benefit from more low-rise flats of three or four storeys. Low rise flats are appealing to younger people who can only afford limited space and may not have the time or inclination to focus on property maintenance or gardens. They can be great for older people for similar reasons, and as they engender a sense of community and provide living space on one level. And they can't be extended, so you retain the supply of smaller properties for those who need them. Of course, leaseholds, ground rents and maintenance charges all need to be carefully worded and fairly set. But a land tax system which encouraged developers down this route, rather than constructing more and more 'executive homes' with huge footprints could be positive.

Nesta also points out that a land tax could benefit the state when it grants planning permission and develops infrastructure (roads, utilities, public transport etc). Currently, these actions increase the value of the land, which benefits private developers, while the state then bears the cost of maintenance. Developers are obliged to contribute to infrastructure costs, but where, for example,

new roads are not formally adopted by the local authority (which is under no obligation to do so) developers then pass the burden on to homebuyers in the form of 'estate management' or similar fees, over which residents have little control. A land value tax could be a more direct and efficient way of contributing towards infrastructure costs – and thereby returning more value to the state.

The paper's other claims are arguably less thought-provoking. A land tax is no more likely to discourage second homes and foreign buyers than higher SDLT. And suggesting the tax is the primary motivator preventing older people from downsizing is unconvincing. There are very good reasons why 'older' people stay in their family homes. Many simply enjoy the space. Others in their fifties and sixties are increasingly likely to have adult offspring still living at home. And those in their 70s and 80s often want room for visitors and current or future carers. Taxing older people out of their existing homes would be an unfair and politically unpopular piece of social engineering.

In fact, while Nesta's paper contains some interesting elements worth examining, the entire proposal on land tax looks difficult to implement, very expensive and potentially politically damaging.

A core requirement would be agreeing a fair contemporary valuation of land. As the paper points out, current Council Tax bills are based on valuations from 1991. This is a nettle which needs to be grasped – but it will take a brave government to do the grasping. Nesta claims that 'available public data' increases the feasibility of revaluing land across the country. We're not so sure.

Any change would have to be phased in to mitigate payment shock, as many people's tax bills would be very different to their current Council Tax. The most disadvantaged would need financial support from government, which could be expensive.

It would also need a rethink of how local councils are funded without Council Tax and Business Rates revenues. Councils in the more economically disadvantaged parts of the country could be worst hit, as revaluation could lay bare significant differences in land values that have been exacerbated since 1991, so 'some form of redistributive mechanism would be necessary'.

Each of these considerations comes with a hefty price tag. And the proposal also rests on immediately abolishing SDLT, which raised more than £15bn for the Treasury in 2023. A government facing a 'black hole' of £22bn is unlikely to slay that particular golden goose in the foreseeable future, even if longer-term economic growth were a guaranteed outcome – which is not the case.

Nesta itself admits that 'the proposal would likely reduce overall tax revenue' and that the 'short-term transitional support … likely to be necessary to mitigate political backlash … could be very costly.' Surely a policy which risks significant political opposition and cost needs to be justified in terms of clear calculations and expectations of specific advantages and gains, albeit over a longer timescale. But the report does not clarify the potential economic upside or attempt to estimate how much could be saved, or raised, in the long run. On balance, it seems likely that this particular set of ideas on property and land taxation is likely to remain in the notional debating chamber for some time to come.