improving living in scotland

HOMES FOR SCOTLAND

Scottish Parliament Finance Committee
Land and Buildings Transaction Tax Bands & Rates

Written Evidence
October 2014

ABOUT HOMES FOR SCOTLAND

Homes for Scotland is ***the*** voice of the home building industry.

With a membership of some 200 organisations together providing 95% of new homes built for sale in Scotland each year as well as a significant proportion of affordable housing, we are committed to improving the quality of living in Scotland by providing this and future generations with warm, sustainable homes in places people *want* to live.

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PROCESS

Homes for Scotland represents members on a wide range of issues affecting their ability to deliver much needed homes.

Our views are endorsed by committees and advisory groups utilising the skills and expertise of key representatives drawn from member companies.

The evidence below represents our member's views in relation to land and building transactions that occur to facilitate residential development in Scotland.

What should the threshold be for the purchase price of the nil rate band?

HFS is keen for the Scottish Government to bring forward a framework for LBTT that promotes a healthy housing market, allowing movement up and down price levels without any artificial barriers.

Whilst keen to see support directed to first time buyers and those on the lower rungs of the housing market, in achieving a 'revenue neutral' position, we are concerned that raising the nil rate band is going to have a detrimental effect on home buyers purchasing at mid to higher values, thereby creating too much of an imbalance within the market.

We note from the draft Scottish Government budget on 9 October 2014 that the nil rate threshold is proposed to increase marginally to £135k. However, given that the new progressive approach will mean that those buying just over the band thresholds will not be disadvantaged as they are under the existing slab LBTT structure, we do not think that the increase in the nil rate band is necessary and would propose that it remains at £125k

Using an example of a purchase of a home at an average house price of around £160k, under the Scottish Government's proposals for a nil rate band at £135k the buyer will pay £500, which is £1,100 less than they would under the current stamp duty system. Using the same example of a purchase at £160k, but with the nil threshold remaining at £125k, the buyer would pay £700, which is still £900 less than they would pay in stamp duty.

Retaining the nil rate band at £125k will assist in balancing out the impact on mid to higher value purchases which at the moment we see as too heavy, as outlined below.

We would suggest that the nil rate band, along with the other band thresholds, are reviewed against house prices regularly by the Scottish Government. The bands should be adjusted in line with house price inflation to ensure they remain relevant to the Scottish housing market.

What should the rate for the other tax bands be?

We note the rates within the Scottish Government budget as:

- at 2% on homes valued between £135k and to £250k
- at 10% for homes valued between £250k and £1m
- at 12% for homes valued over £1m

We have considered the impact of these rates compared to the existing SDLT on a variety of house prices (see annex 1) and are pleased to note that home buyers purchasing homes under £325k are set to pay less under the new system.

However, we view the rate on transactions over £250k to £1m to be too punitive on the upper-middle market i.e. for buyers purchasing homes from £325k to £500k. This core, upper-middle market comprises aspirational movers and families with changing needs. It should not be assumed that these households are able to raise the additional funds required. Many households have seen the equity they hold in their homes reduce with a reduction in home valuations during the recession, this has had an impact on the availability of funds available to support a house move.

This market segment is critical to the sustained recovery of the housing market and this is particularly so in areas such as Edinburgh, East Renfrewshire and Aberdeen where demand for family housing is high, supply is low and house prices are high. These markets will be badly affected and a reduction in house sales is anticipated as a result.

To ensure the tax is more evenly distributed above the £250k level, we would suggest an additional band between £250k and £500k.

Should there be more or fewer bands and, if so, the rate for any additional tax bands?

We are concerned that the LBTT chargeable on upper-middle value homes is now too high, potentially leading to stagnation within that market segment as outlined above. We would like to see the LBTT more evenly distributed above the £250k band to avoid such a disproportionate burden on mid to higher value purchases.

<u>We would suggest an additional band between £250k and £500k is created and that the rate should be 7%.</u>

The effect of this, and a lower nil rate band of £125k, on a number of house prices is set out within annex 1.

Should the rates and bands be set so that the impact of replacing SDLT with LBTT is broadly financial neutral?

LBTT, as was its predecessor SDLT, is a tax relating to the purchase of land or property which is compulsory, but very few fully understand why it is being paid, or what the money is used for. It would be worth the Scottish Government giving consideration to the potential uplift that could accrue from the economic activity that is generated when a tax on mobility is removed completely.

The Scottish Government has, however, made it clear that they desire a revenue neutral position and our response to each consultation relating to LBTT has been on that basis.

We continue to remind Scottish Government that if Scotland is to secure its fair share of investment and remain attractive it must be competitive and have at least an 'equal playing field' with the rest of the UK. Investment decisions of home builders, many of which operate north and south of the border, will be based not only on the cost of land, but the health of a housing market, to give their funders the confidence that they can achieve a return.

Even within a 'revenue neutral' stance, we have suggested ways that the Scottish Government could do more to support the delivery of much needed new homes in Scotland. The use of deferred payment of LBTT in land transactions, even when the chargeable consideration is known by the home builder, is an example of that (see annex 2 for further details).

Should the lower top rate for non-residential property be lower than for residential property?

The interest of the home building industry in LBTT rates for non-residential transactions relates to the purchase of land for residential development. To ensure the supply of much needed new homes, we are supportive of a lower top rate for non-residential property than for residential property.

Section 59 of the Land and Buildings Transaction Tax (Scotland) Act 2013 defines the meaning of 'residential property' in line with the existing definition under SDLT (see annex 3). It is crucial that the existing definitions remain in place to ensure that the proposed residential rates are not applied to the purchase of land for residential development.

In the main, land purchases for residential development will be of land which is currently not classed as 'residential'. For example, this could include brownfield land that is currently classed as industrial, or greenfield land that is currently classed as agricultural. When the land being purchased is not currently classed as residential, the LBTT chargeable will be based on non-residential rates.

Within the draft budget for 2015/16, the Scottish Government has proposed that LBTT for non-residential transactions will be charged at –

- 3% for land valued between £150k and £350k
- 4.5% for land valued above £350k

Given the value of land for residential use is likely to exceed the £350k lower threshold, this means that in the main 4.5% LBTT will be chargeable on land purchases by the home building industry. With a 4% maximum charge currently in place for non-residential transactions under SDLT, the tax bill under LBTT will be 0.5% higher.

For example, purchase of a site valued at £5m under the existing system would result in a tax bill of £200,000, but under the new system the LBTT system an additional £25,000 would be chargeable.

It could be argued that the impact of the 0.5% increase will be reflected in development appraisals, with the land owners absorbing the additional cost through a reduction in their net price. However there is a risk that vendors may choose not to sell if land values are beneath their aspirations, causing stagnation in the delivery of new projects.

Furthermore, if the increase is implemented, there will undoubtedly be a transitional impact on contractual arrangements that have been entered into already, those which contain minimum price clauses which can not be met, as a direct result of the additional cost of the increased LBTT threshold.

It is crucial that Scotland remains a competitive place to invest and bring forward housing development. A flat increase in the cost of purchasing land for development 0.5% is not helpful and immediately puts Scotland at a disadvantage to purchases of land in England and Wales, where the existing SDLT will remain. If a company was looking at two similar opportunities, one in Scotland and one in England, there is a real danger that Scotland will lose out due to the higher cost.

<u>To support land purchases in Scotland, we would propose that the rate for land valued above £350k remains capped at 4%.</u>

What is the likely impact on the property market and wider economy?

Scotland must remain competitive and the Scottish Government must do what it can to support the housing market and the supply of much needed new homes.

<u>Housing Market Activity</u>

A move to ease the LBTT burden on home buyers at the lower end of the market is welcome and should have a positive impact on housing market activity. With first time buyers considered the lifeblood within a housing market, the knock on effect should be very positive. However, what is being proposed by the Scottish Government is going to have too much of a detrimental impact on middle to higher value homes and, as a result, we would expect to see stagnation in this part of the market. This core, upper-middle market comprises aspirational movers and families with changing needs, a section of the market that is critical to the sustainability of the housing market. To mitigate this impact of what the Scottish Government has proposed, we have suggested an additional band for homes valued between £250k and £500k.

<u>New Housing Supply</u>

Scotland has an acute housing shortage with 465,000 new homes required by 2035, just to keep up with anticipated population growth. Whilst in Scotland we delivered only 15,000 homes in 2013, these stats show that we should be delivering at least 25,000 each year to ensure sufficient supply. The Scottish Government has over recent years taken measures to support housing supply, the most successful being Help to Buy (Scotland) where the value of the investment is £275m over 3 years. We want to see the Scottish Government join up policy streams to ensure all their efforts are pushed towards solving the current housing crises. The Scottish Government should not seek to introduce financial policies that will counter these efforts, at any point of the development process.

The impact of increasing tax payable on most land transactions is concerning. HFS already has trepidations about the ability of Scotland to continue to compete for housing investment with England, given that it is already proving more expensive to build homes north of the border. We would like to see the Scottish Government use devolved powers within its gift to encourage investment, for all the benefits it can bring to the wider economy.

Importance of Reliefs

Whilst this evidence relates to the rates and bands for LBTT, we must not ignore the importance of ensuring that the reliefs brought forward within the legislation are appropriate and practical. We have acute concerns about the impact of the proposed multiple dwellings relief on Scotland's ability to strategically grow a quality, professionally managed private rented sector, and also on the plans for a sub-sale relief which has the potential to erode the important role of a lead developer. We have responded in detail to the Scottish Government proposals and eagerly await the outcomes of the consultations carried out.

We understand that the Scottish Government will be keen to differentiate its new policy from the existing SDLT structure, but it is important to remember that, fundamentally, the new-build housing markets in England and Scotland are similar and interlinked. Both have suffered severe structural harm and damage as a result of the financial crash. Both have housing outputs that are at near all-time lows, whilst need and demand continue to rise. Both have similar levels of home ownership and aspirations for home ownership. Both have the same UK-wide home builders delivering the vast majority of all new homes in each country. Both have the same lenders providing mortgages and development finance. And both would be looking to attract institutional investment to grow the private rented sector and finance the building of additional homes.

In bringing forward the legislative framework for LBTT, we would urge members of the Scottish Parliament to challenge the detail of LBTT proposals to ensure every aspect is about enabling investment and encouraging an increase in residential development in Scotland.

Support policy agendas

Furthermore, we would be keen for the Scottish Government to relate the new LBTT regime with other policy priorities. It is our view that it is simply an opportunity missed if they do not. Within its Sustainable Housing Strategy the Scottish Government has stated that they want to see a market premium on warm, high quality, low carbon homes with lower running costs because these attributes are valued by lenders, consumers and surveyors. In achieving this, the Government acknowledges the need for the market to fully reflect the benefits of 'greener' housing.

We believe that the Scottish Government should use LBTT to influence the market for energy efficient homes by linking the amount payable to the Energy Performance Certificate (EPC). When a property is marketed for sale both sellers and buyers have access to an EPC. This mandatory certificate allows comparisons of homes for sale across the market, encouraging buyers to take account of the energy efficiency of the home in their choices. Whilst the amount saved by the customer will not off-set the additional costs incurred by the builder in delivering a higher efficiency home, it would introduce a much needed incentive to help create market demand for energy efficient homes.

Annex 1 – comparison of LBTT payable on house prices compared to SDLT

Example House Price	**Current SDLT**	**SG draft budget – 2% from £135k up to £250k, 10% over £250k & 12% over £1m**	***HFS proposal – 2% from £125k up to £250, 5% over £250k to £500k, 7% from £500k to £1m, 12% over £1m***
£125,000	£1,250	£0	*£0*
£150,000	£1,500	£300	*£500*
£175,000	£1,750	£800	*£1,000*
£200,000	£2,000	£1,300	*£1,500*
£225,000	£2,250	£1,800	*£2,000*
£250,000	£2,500	£2,300	*£2,500*
£275,000	£8,250	£4,800	*£4,250*
£300,000	£9,000	£7,300	*£6,000*
£325,000	£9,750	£9,800	*£7,750*
£350,000	£10,500	£12,300	*£9,500*
£450,000	£13,500	£22,300	*£16,500*
£550,000	£22,000	£32,300	*£25,000*
£700,000	£28,000	£47,300	*£40,000*

Annex 2 - Example of support for home building within a revenue neutral position - Deferred payment

In most land transactions the purchasing price will be contingent on planning or may be uncertain where the price mechanism is linked to house prices/builders sales revenues. Recognising that this is the way that most land transactions work, the SDLT system contains a facility for deferred payment when the 'chargeable consideration' is not yet determined.

Home builders agree to drip feed the land owner on an agreed timescale in arrears. The deferred payment arrangement allows builders to defer the payment of stamp duty in line with the land payment to the land owner.

The Scottish Government has acknowledged the importance of this and has consulted on the basis that the subordinate legislation coming forward for LBTT will include the ability for home builders to apply for deferment in the same situations as they would currently under SDLT. Given that this arrangement is already in place under SDLT, it will be cost neutral for both the business community and the Scottish Government.

However there is an opportunity for the Scottish Government to better support the home building industry in Scotland, whilst still achieving revenue neutrality. HFS has proposed that the option to utilise a deferred payment is also made available to builders even when the chargeable consideration is known.

For example, if a builder had an agreed land deal for £20m payable in 5 equal instalments over 5 years. Currently they would have to pay £4.8m at the date of entry i.e. the first land payment plus the SDLT which is due on the *total* amount. We would suggest that it would be more equitable for the LBTT to be phased in the same way as the land payment to allow the builder to pay £4,160k every year i.e. the £4m land payment plus the LBTT due on each phased amount.

The deferment of the tax aligned to the actual contracted land payments, rather than the current front loaded requirement, would be most helpful to those schemes with marginal viability, as well as the general business cash flow benefit to the industry.

If full deferment is not acceptable then we have asked the Scottish Government to consider introducing partial deferment in transactions where the chargeable consideration is known, for example splitting the LBTT liability into two payments.

With the upfront costs involved in delivering a residential development making it difficult for some home builders to access development finance, this is one way that the Scottish Government could look to support the industry without any cost to the public purse. The arrangement would remain cost neutral for the Scottish Government with the same amount of tax being paid, just on a slightly different timescale.

Annex 3 - Meaning of “residential property” in Land and Buildings Transaction Tax (Scotland) Act 2013

(1) In this Act “residential property” means—

(a) a building that is used or is suitable for use as a dwelling, or is in the process of being constructed or adapted for such use,
(b) land that is or forms part of the garden or grounds of a building within paragraph (a) (including any building or other structure on such land), or
(c)an interest in or right over land that subsists for the benefit of a building within paragraph (a) or of land within paragraph (b).

(2)Accordingly, “non-residential property” means any property that is not residential property.

(3)For the purposes of subsection (1) a building used for any of the following purposes is used as a dwelling—
(a)residential accommodation for school pupils,
(b)residential accommodation for students, other than accommodation falling within subsection (4)(b),
(c)residential accommodation for members of the armed forces,
(d)an institution that is the sole or main residence of at least 90% of its residents and does not fall within any of paragraphs (a) to (f) of subsection (4).

(4)For the purposes of subsection (1) a building used for any of the following purposes is not used as a dwelling—
(a)a home or other institution providing residential accommodation for children,
(b)a hall of residence for students in further or higher education,
(c)a home or other institution providing residential accommodation with personal care for persons in need of personal care by reason of old age, disability, past or present dependence on alcohol or drugs or past or present mental disorder,
(d)a hospital or hospice,
(e)a prison or similar establishment,
(f)a hotel or inn or similar establishment.

(5)Where a building is used for a purpose specified in subsection (4), no account is to be taken for the purposes of subsection (1)(a) of its suitability for any other use.

(6)Where a building that is not in use is suitable for use for at least one of the purposes specified in subsection (3) and at least one of those specified in subsection (4)—
(a)if there is one such use for which it is most suitable, or if the uses for which it is most suitable are all specified in the same paragraph, no account is to be taken for the purposes of subsection (1)(a) of its suitability for any other use,
(b)otherwise, the building is to be treated for those purposes as suitable for use as a dwelling.

(7)In this section “building” includes part of a building.

(8)Where six or more separate dwellings are the subject of a single transaction involving the transfer of a major interest in, or the grant of a lease over, them, then, for the purposes of this Act as it applies in relation to that transaction, those dwellings are treated as not being residential property.

(9)The Scottish Ministers may, by order—
building is, or is not to be, use of a building as a dwelling for the purposes of subsection (1),
(b)amend or repeal subsection (8).

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