

Residential LBTT & ADS Full Year Report

Scottish Housing Market

Summer 2020



Residential LBTT Up Year-on-Year But Future Outlook Uncertain

Like the rest of us, the Scottish Government's property tax (Land & Buildings Transaction Tax, or LBTT) has had a bewildering last few months. This Briefing looks at the residential part of LBTT based on housing market transactions.

Ostensibly, things look positive - in 2019/20, the number of LBTT returns reached over 105,000, up from just under 104,000 for the same time a year earlier; an increase of 1.2%. The total value of LBTT tax revenues to 2019/20, excluding its sister tax Additional Dwelling Supplement (ADS), totalled £288 million, 10% up on the previous year. The greater increase in revenue, ahead of transactions, reflects the flattening of housing market activity over 2019/20 while prices continued to rise. As the new tax year started in the shadow of the Covid-19 lockdown, the outlook for LBTT revenue in the coming years is highly uncertain and looks likely to be significantly down.

In broad terms, rising house prices and transaction activity in the past few years have supported rising LBTT revenues for the Scottish Government (see Fig.1). However, this growth has not always been consistent as political factors, such as Brexit, have impacted on market sentiment. Fig. 2 shows the year-on-year fluctuations in LBTT transactions and revenue. There was already a slowing down in transaction numbers from the end of 2019, which turned negative at the start of 2020.

With the latest figures now reported, we can see the first impacts of the Covid-19 lockdown, with overall revenues for April and May down c.67% on the year before (Fig.3.). With the housing market effectively closed during April and May, it would be expected any revenues will be minimal for what is usually the buoyant Spring market. It will be difficult for 2020/21 revenues to recover all ground lost after this despite the recent announcement of the recent LBTT holiday which we reflect on later in this briefing.



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Fig.1 LBTT & ADS revenue had been rising due to price & transactions growth
LBTT Tax Revenue by Month (£m)

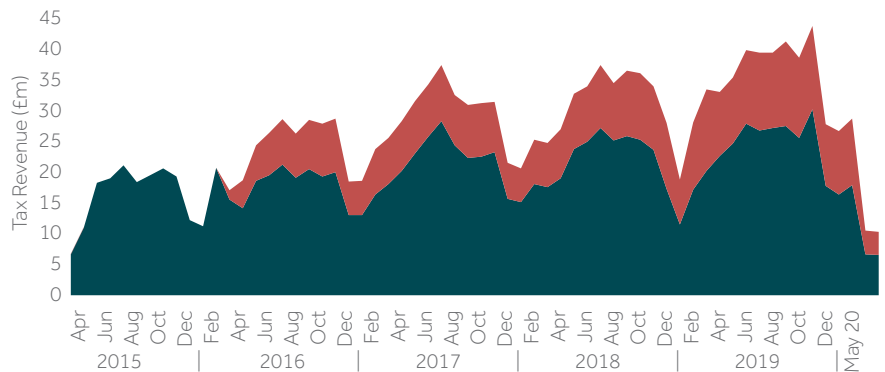


Fig.2 Annual growth in LBTT transactions turned negative in March 2020

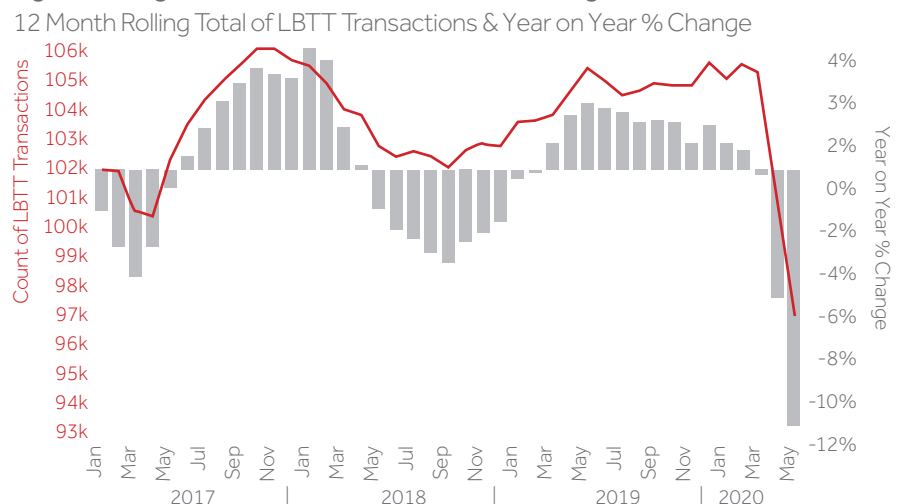
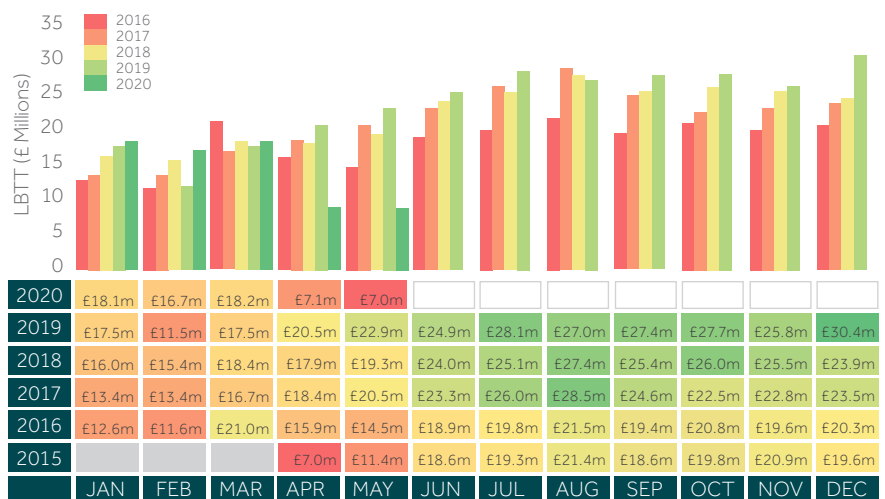


Fig.3 LBTT revenue in April / May 2020 was down -67% year-on-year as a result of Covid-19
LBTT excluding ADS declared due by month and year



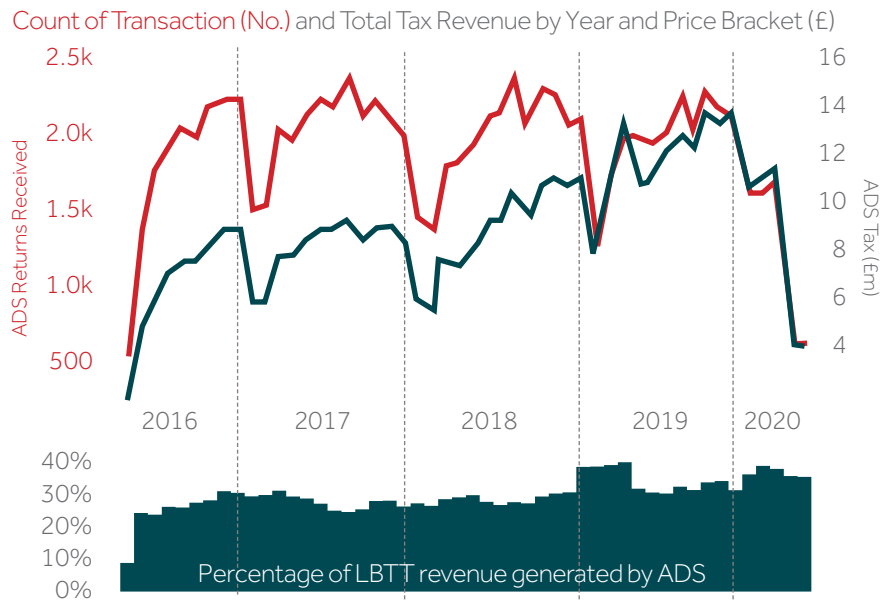
ADS's Starring Role

Since its introduction in 2016 and rate increase in 2019, the ADS on second home purchases has played a significant role in driving LBTT revenues for the Scottish Government. In 2017/18, ADS revenue exceeded £100 million for the first time. While ADS revenue figures still need to be finalised for 2019/20, as a proportion needs to be reclaimed, revenue will likely remain over £100m.

When first launched, this tax typically accounted for around 25% to 30% of total residential LBTT revenues, but over 2019/20, this proportion has increased to average around 34%.

The investment markets in the major cities play an important role in generating ADS and market uncertainty as well as changes in the rental sector, including short-term rental demand, may see revenue dramatically impacted over 2020/21.

Fig.4 ADS revenue has been rising in recent years



ADS has accounted for almost 40% of LBTT revenue in some months

Prime sales hold both risk and reward

The banding structure of LBTT places a heavy weighting on revenue generation on transactions above £325,000. Over three-quarters of revenue collected in 2019/20 came from these higher value transactions, although this market only represents a relatively small proportion of all transactions, typically less than 10%.

For the Scottish Government, while this tax structure is good politics, with 45% of house sales not subject to any LBTT in 2019/20, any fluctuations in the market above £325,000 opens up the potential for a substantial impact on

annual revenue. This can be especially true in periods of weaker market activity or uncertainty, when discretionary purchases, which are often higher value, drop off.

With the fuller impact of the Covid-19 lockdown yet to manifest, this weighting of tax revenue may contribute to a more significant drop in annual revenues than in housing transactions. Since the introduction of LBTT 5 years ago, the higher value Edinburgh market has been more sluggish than the wider Scottish market, or comparables like Glasgow (see Fig.5).

Fig.5 Edinburgh has seen slower growth

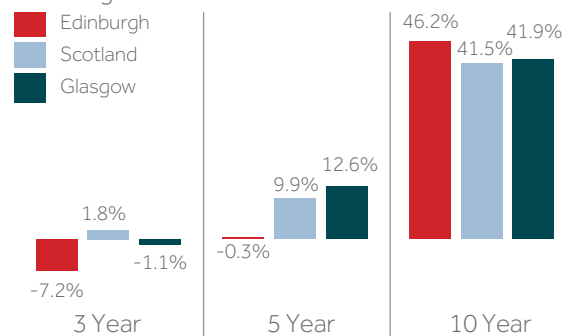
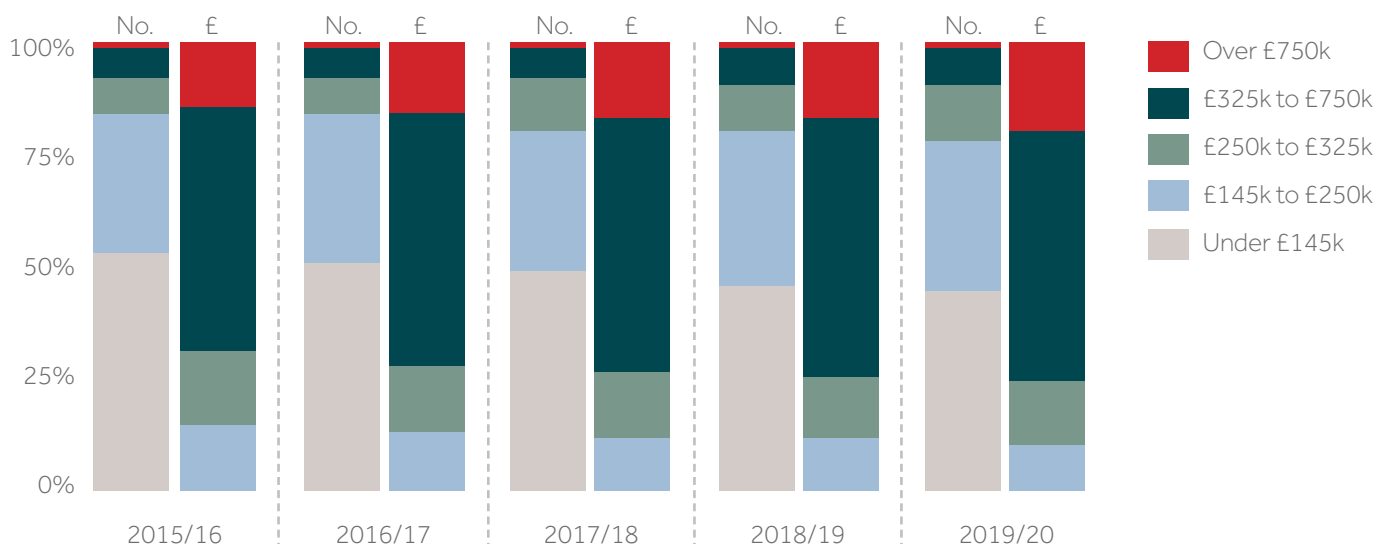


Fig.6 Despite accounting for around 10% of sales, transactions over £325k contribute over three quarters of LBTT revenue (2019/20)

Count of Transactions (No.) and Total Tax Revenue by Year and Price Bracket (£)



Revenue Forecasts and Covid-19

As Fig.7 illustrates, the difference between forecast revenues and actual tax take has varied significantly since the introduction of LBTT in 2015/16. This was most acute in the first year of the tax, when behavioural changes saw many transactions rushed through before the tax's introduction.

The Covid-19 lockdown represents the first major upheaval in the market since the introduction of LBTT and, as the 2008/9 downturn showed, such events can significantly impact government revenue. To see our latest market forecasts click [here](#).

In the wake of the recent LBTT holiday announcement by the Scottish Government, The Scottish Fiscal Commission has released the costing for this policy implementation ([link here](#)) which estimates a -£33m change on total LBTT revenue in 2020/21 and a -£15m change during 2021/22.

Fig.7 LBTT revenue peaked in December 2019

Revenue Scotland Forecasts : Tax Revenue from SDLT & LBTT against

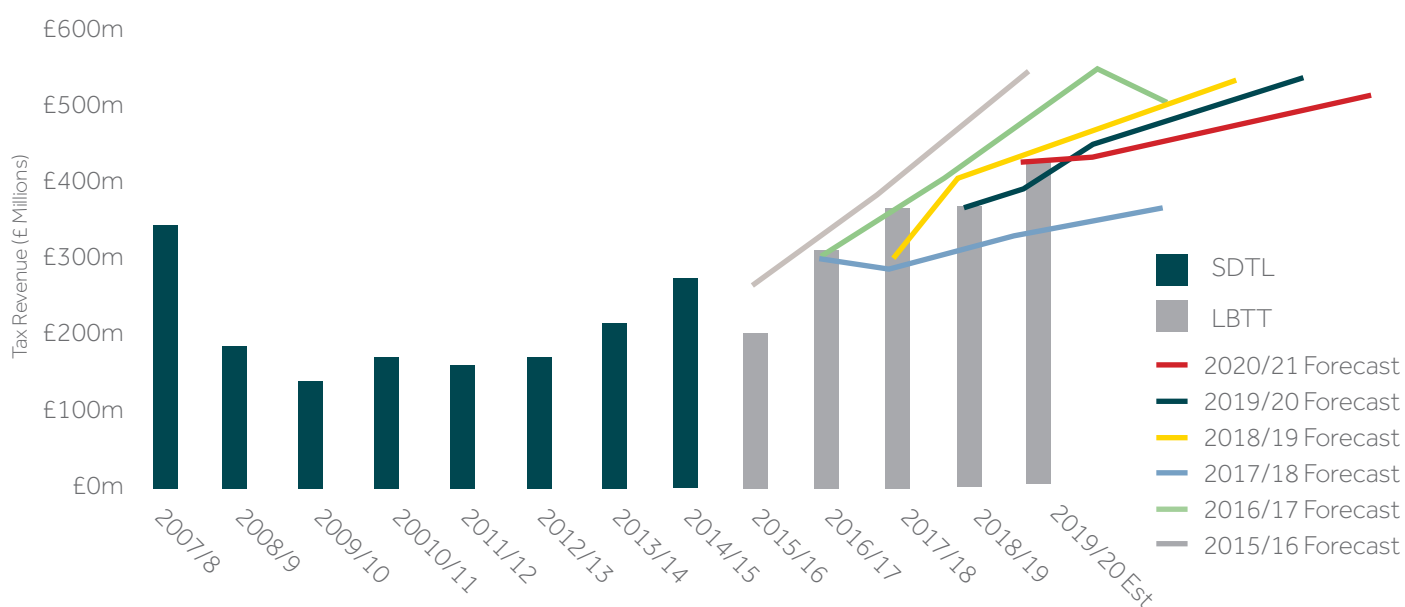


Fig.8 The Covid-19 Lockdown looks set to materially impact LBTT revenue in 2020/21

LBTT Residential Returns by Week

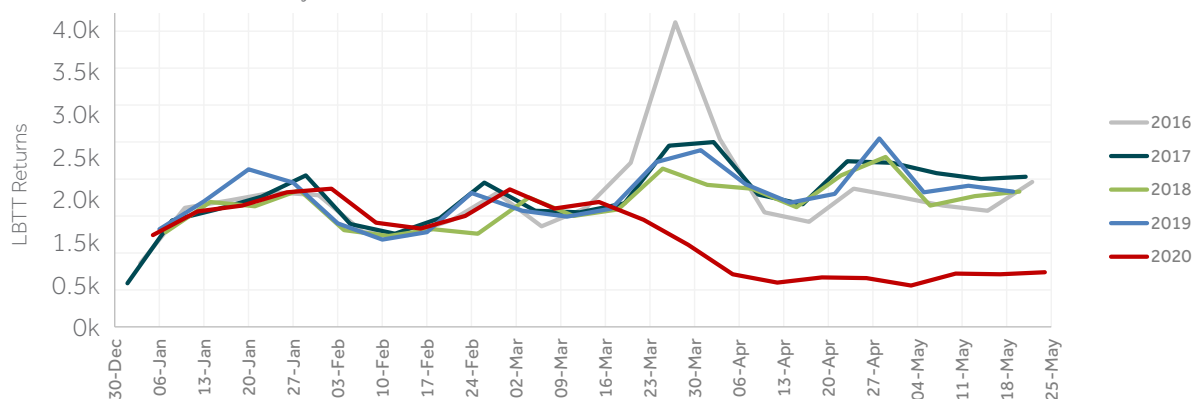


Fig.9 The Scottish Fiscal Commission estimates the cost of holiday on LBTT revenue to be -£33m over 2020/21

Effect of policy change on Residential LBTT

	2020/21
Static Cost	
Effect of raising threshold	-£60m
Saving from First Time Buyer relief	£5m
Saving from other relief	£2m
Behavioural Response	
Price Effect	£4m
Transaction Effect	£3m
Forestalling	£6m
Total Cost	-£39m

Effect of behaviour on ADS Revenue

	2020/21
Gross ADS	£8m
Repayments	-£1m
Net ADS	£7m

Source: Scottish Fiscal Commission
 Figures may not sum because of rounding.

Changes Happening

On 8th July, the Chancellor of the Exchequer announced an immediate SDLT 'holiday' in England & Wales, which raised the threshold from £125,000 to £500,000 on properties bought, producing an average saving of £4,500 and up to £15,000 for purchases over £500,000. This raising of the threshold is time limited (to 31 March 2021) and is therefore to encourage people to buy (and sell) property in the near future to help to give the housing market and wider economy a lift.

The Scottish Government responded later that week and announced its own LBTT 'holiday', which raised the nil threshold to £250,000 and came into effect for transactions from the 15th July 2020. This essentially wipes out the 2% payable on the £145,000 to £250,000 threshold, saving all buyers 2% of the difference between £145,000 and their purchase price in this band, and buyers over £250,000 have a saving of £2,100. It is estimated that this will take 80% of buyers in Scotland out of LBTT. It is also time limited to end of March next year.

The consequential arising from the Chancellor's announcement were also used to further boost the First Time Buyers Home Fund in Scotland (a shared equity scheme to support first time buyers access the housing market) by £50 million.

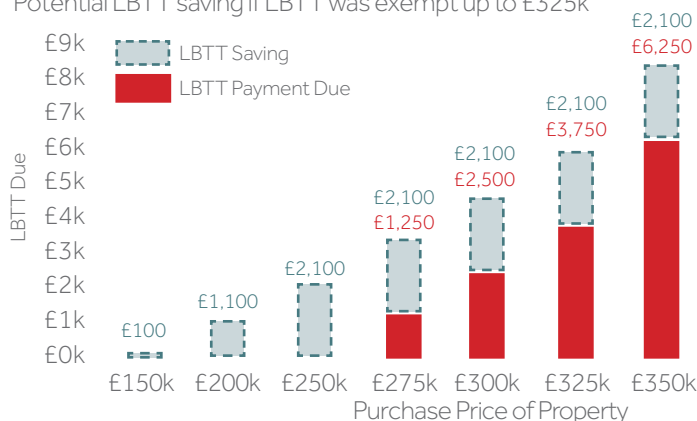
Although such holidays will be costly – the Scottish Fiscal Commission estimates it to be around £39 million in Scotland, it will stimulate other economic activity in the residential sector, helping to boost employment, business rates, VAT receipts, etc. During a crisis as big as Covid, the Government has to act to stimulate activity as much as it can or the recession we are experiencing will simply worsen.

There could be alternative measures looked at:

- **Reducing or removing LBTT for older buyers.** This may encourage older people to move from often under occupied properties to more bespoke properties and allow for families to have greater access to more suitable housing product in the cities in particular.
- **Further raising the threshold for first time buyers, or removing the from LBTT altogether.** FTBs are the lifeblood of the market and help to create market chains more effectively than any other buyer type.
- **Gather firm evidence to support tax bandings to maximise revenues.** It has been a subject of much debate about whether the Scottish Government's current bandings stifle market activity in the middle to upper ends of the market and whether adjustment of these bands could boost market activity and raise revenue. This requires direct market evidence to underpin SFC's behavioural models. Rettie & Co has suggested to the Scottish Govt and SFC that primary research with house buyers and sellers in Scotland is the only way to capture such evidence reliably.
- **Tie LBTT to energy efficiency of homes.** Perhaps a more long-term reform could be to encourage people to buy energy efficient property (and therefore to incentivise sellers to make their property more energy efficient) by reducing the LBTT bill for the more energy efficient properties and raising it for the less energy efficient.

Fig.10 LBTT savings under £250k LBTT Holiday

Potential LBTT saving if LBTT was exempt up to £325k



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