Sustainable Housing Policy in Scotland: Reforming Devolved Property Taxation

Kenneth Gibb* and Chris Leishman**

*University of Glasgow/UK Collaborative Centre for Housing Evidence

**University of South Australia/UK Collaborative Centre for Housing Evidence

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Executive Summary

Key Messages

- Housing tax reform is a necessary component of wider Housing to 2040 programmes goals – but has not made any material progress to date.
- Council Tax and Land and Buildings Transaction Tax are both in different ways flawed and in need of reform for multiple public policy reasons.
- This report examines the two taxes in detail, makes the case for reform, undertakes econometric modelling to support an automatic valuation approach to regular revaluation, a process by which revaluation for a different property tax or even land value tax might also be based.
- A deliberative citizen's panel found that, rather than be unwilling to contemplate changing Council Tax, our participants favoured reform, and the majority were willing to look more closely at fundamental reform.
- While we narrow down possible approaches and undertake a balanced review of a selection of recent proposals to reform property taxation, we conclude that this is the beginning not the end of a wider civic conversation and debate about the future of housing taxes, local government finance and Housing to 2040.

What the project is about

Housing to 2040 is a wide-ranging strategy, both in terms of its vision for housing but also in terms of the many actions proposed. These proposals include more cumulative longer-term aspects of reforming the housing system. This often ends up in the hard to deliver box, and for which more fundamental work designing the proposals is undoubtedly required. Tax reform falls squarely into this category. In the current Parliament, all that was proposed within Housing to 2040 was to undertake critical reviews of the two key devolved housing taxes: Council Tax (CT) and Land and Buildings Transactions Tax (LBTT).

Diagnosis

If we take the two Scottish housing taxes together, they do not contribute positively to important goals regarding housing market efficiency (e.g. as a well-run market-shaping tool of policy); neither do they support greater equality and reduced housing-related poverty (McCauley, 2022)[1 2] . They also do not make the contribution they could do to supporting Scottish public finances and releasing funds for more progressive sustainable and resilient goals. Nor do the housing taxes as they currently operate, support the goals of Housing to 2040 as regards the de-speculating and stabilising of the housing market. In the case of Council Tax it is also at the heart of several challenges associated with our system of local government finance.

There are several widely held criticisms of the Council Tax:

It is regressive because the property value banding system which causes higher value properties to be taxed at a lower rate, proportionately, than lower valued property. More graphically, the Commission on Local Tax Reform (2015, 2.3) said 'People in the most expensive homes pay no more than 3 times the tax on the lowest value homes, even though we estimate those homes, on average, are now worth around 15 times as much. That means people in less expensive homes are paying a higher proportion of their property's value in Council Tax than those in the most expensive homes'. The Burt Review in 2006 was the first detailed examination to indicate that Council Tax bills as a share of income (benefit support excepted), fall as income rises, especially at higher levels of incomes.

In Scotland and in England the Council Tax has not undergone a general revaluation since its inception more than 30 years ago. The growing separation of the tax base from the current level and distribution of property value is widely criticised. Recent research (Scottish Local Tax Commission appendix 2) suggests that as many as half of properties are now in the 'wrong' tax band because the market has shifted structurally over the intervening period. Also, every property built since that 1991 valuation requires to have its value estimated for 1991 prices. Moreover, the 1991 valuation was done via an inexpensive drive-by process which was questioned in terms of its accuracy.

Evidence for England shows that, regionally, council tax, as a share of current property values, is higher in lower valued house price regions than high value regions – in other words Londoners pay less of their property value in tax than northern regions. This also means that government grant to local authorities is distributed less progressively than would be the case if the tax base in high value areas was not depressed as it is by the Council Tax bands. The same principles will apply contrasting high and low value property markets in Scotland.

The Council Tax also retained specific features of the preceding Community Charge – such as discounts for single adults and certain exemptions (e.g. students), which introduces a degree of arbitrariness into the tax liability.

Turning to LBTT, the economics profession has long been clear about its opposition to property transactions taxation like Stamp Duty Land Tax and LBTT. The 2011 Mirrlees review of taxation for the Institute of Fiscal Studies argued that taxes specific to property sales deter those sales and hence damage labour and housing mobility to the detriment of

1 We define tax progressivity as tax liability taking an increasing proportion of household income as one moves up through the income deciles of the distribution of income. Regressivity suggests an inverse version where lower income take up higher tax liabilities as a proportion of household income.

2 McCauley 2022 Reform Scotland

economic productivity and household utility. The efforts to produce progressive tax structures (increasing with sales value), the use of exemptions and nil rates for first time buyers inevitably also interact and distort market segments. This has been exacerbated by regular tinkering with tax rates and exemptions by previous UK Chancellors of the Exchequer and Scottish Finance Ministers.

The other difficulty with LBTT is that it needs to be accurately forecast by the Scottish Fiscal Commission to help the Scottish Government plan its budget. There are three moving parts: predicting the volume of transactions (both house sales and properties sold falling into the Additional Dwelling Supplement category); forecasting the level and distribution of house prices for those properties transacting; and, estimating the effects of possible different tax rates, as well as the existing tax rate structure, including reliefs, on revenues (as a result of the first two variables).

The Promise of Reform

Housing tax reform offers, first, the prospect of using fiscal tools to help shape the housing market and improve its efficiency. We also recognise, second, the rising importance of housing wealth as a site of inequality and the failure to recognise the many problems that the concentration of housing wealth brings, which is an important additional reason to use these levers progressively to reform tax and potentially raise revenue for housing and other redistributive ends. Third, creating a wider property-based tax base in Scotland offers public finance opportunities and scope to reduce reliance on more elastic income tax.

Two other important reasons for reform are, first, that the existing taxes are problematic in important ways and, as many previous and recent studies, commissions and programmes of work have shown, they do, objectively, need to be reformed. Second, Housing to 2040 sets out an ambitious desire to stabilise real house prices in Scotland, to reduce the dependence on property as a store of wealth, and to de-speculate the housing market. Tax levers are an important (necessary though not sufficient) set of interventions to help make progress with that agenda.

It is undeniable that there is a considerable gap between ambition and actual policy proposals, and that has led us to focus in this report on housing tax reform. However, it is also a critical potential area for both redistribution and housing market improvement, to help deliver a well-functioning housing system. A theme running through this discussion is the recognition of how difficult effective reform in this area can be to deliver. Also, in response, there is a need to think hard about presenting, framing and persuading around the case for reform (see Slack and Bird, 2015).

Researching Reform

The project first conducted a review of the property tax reform literature going back to the short-lived Community Charge (poll tax) but also considering specific Scottish and international debates about tax reform (see: Gibb and Christie, 2015; 2019; Slack and Bird, 2015). The study also examined contemporary reform proposal ideas and, in so doing, distinguishes between moderate reform of council tax as opposed to more thoroughgoing replacement of the council tax (and indeed also of Land Buildings Transactions Tax).

To help us better understand the reform agenda and the aspects of politics and public policy that hinder or prevent reform, the project team undertook a programme of economic modelling of different tax reform ideas. First, the team used a tried and tested method to revalue the Scottish property tax base for individual capital values. We found, as a result, that a revenue neutral national (or proportional) property tax rate would be approximately 0.46% and that a revenue neutral land value tax (LVT) rate would be approximately 1.43%. The redistributive impacts of the LVT would be more pronounced than the council tax revaluation or the proportional property tax. This is logical given that the spatial variation in property values is more significant than spatial variation in construction or development costs. Finally, we find that a revenue neutral LVT designed only to replace the land and buildings transaction tax (LBTT) would be approximately 0.32%.

Finally, the team convened a deliberative citizen panel at the beginning of June 2024 to better understand how a cross section of citizens understand and evaluate how local taxation, local services and housing come together, what the trade-offs are, and whether there is a preferred way forward. The team also met with an expert panel of housing sector experts and leaders to both diagnose the current arrangements and debate alternative reform proposals.

Conclusion on Ways Forward

The report argues for abolition of both Council Tax and LBTT. They would be replaced by a split tax combining a revenue-neutral, regularly revalued proportionate property tax, wherein the local element, replacing Council Tax, would be set locally and retained by local councils, but a supplementary added tax rate, also based on revalued capital value would be paid to the Scottish Government to replace lost LBTT revenues – the latter element would only be paid by all owner occupiers and private landlords. A deferral scheme would operate for both tax elements alongside a continuing national low-income rebate scheme.

We also stress that we are departing from recent reform proposals in the literature by not supporting a new property tax that would only be paid by owners of property. One of the criteria we judge property taxes by in the local governance sphere is their contribution to local democratic accountability. We are sufficiently worried about the downsides of not charging tenants (regardless of the arbitrary effects of partial capitalisation of tax by some private landlords on to rents) for local government services that we conclude that we need to remain with a household based and not property owner based local property tax. This would not apply to the revenue element replacing LBTT which we do think should be paid by owners of property only (and on a revenue-neutral basis, initially).

Finally, we would stress that these conclusions are only provisional ones, but we are convinced they are the right direction of travel. They should form the beginning of a civic conversation, public debate and a larger Citizen's Assembly deliberative process to analyse and discuss our proposals and, quite possibly, arrive at superior ones. But we really cannot wait any longer not taking tax reform forward for both housing taxes. Such reform can contribute to a more stable and less speculative housing market in Scotland - but would only be part of what would need to be a multi-faceted series of reforms. However, the other redistributive and housing system-enhancing functions of housing tax reform and to the case for bringing forward reform.

1. Introduction

This is one of two reports seeking to reinvigorate complementary and critical parts of the Housing to 2040 Scottish housing strategy. This report focuses on the reform of devolved housing taxes. The companion report examines the Affordable Housing Supply Programme.

Housing to 2040 was the product of three years of inclusive consultation with the housing sector in Scotland. It delivered an ambitious and comprehensive programme of housing reforms over 20 years and more, geared to meeting affordable housing need, to raise standards and rights across the housing system, to pilot housing's contribution to meeting net zero, to end homelessness, and much more besides. At its heart were fundamental principles: implementing a well-functioning housing system, progressively realising the human right to adequate housing, and reducing housing's role as a store of wealth and as a speculative asset. Housing to 2040 was also closely aligned to fundamental purposes of public policy: UN sustainable development goals, reducing child poverty, and inclusive economic prosperity.

These ambitions and the scope of the strategy as an inter-departmental cross-government approach were widely welcomed, though the pace of intervention and the lack of detail on implementation, co-ordination, monitoring and calibration were concerns from the outset[3] . Unfortunately, work to progress this programme has proven susceptible to external shocks (Covid-19, Brexit and global inflation) and internal factors (such as significant budgetary reversals in 2023-24 and 2024-25, but also the unanticipated impacts of government policy).

Recognition of the severity of the problem is reflected in thirteen local authorities and now the Scottish Government describing the situation as a housing emergency[4]. Most observers would agree that the Housing to 2040 strategy is in significant difficulty, and with it the ambitious goals to elevate the housing system so that it can make a sustainable long-term contribution to prosperity, meeting housing need, and reducing poverty and inequality.

1.1 What we looked at

The UK Collaborative Centre for Housing Evidence (CaCHE) has undertaken an innovative research project seeking to both understand the challenges facing two key parts of the strategy, and to offer a range of solutions and reform ideas to help recapture the earlier momentum and make a sustained contribution to achieving the key goals of the programme. Our aim is to assist the work of Scottish Ministers and the newly established Housing to 2040 delivery board and their interim review of the strategy.

We did not examine equally the more than one hundred actions in the strategy's route map; instead, the research focused on two contrasting but critical components of the strategy: developing 110,000 social and affordable homes to contribute to meeting affordable housing need across Scotland; and the reform of devolved housing tax levers to improve the function of the housing system and reduce housing-related inequalities. The former is in immediate crisis and the latter has not really started but both are critical to outcomes concerning the economy, fairness and the wider public policy system. The rest of this report focuses on the second of these two themes i.e. property taxation reform.

Housing to 2040 is a wide ranging and comprehensive strategy, both in terms of its vision for housing but also in terms of the many actions proposed. These proposals represent both immediate or short term, but also more cumulative longer-term aspects of reforming the housing system. The latter category is also often in the harder to deliver box, and for which more fundamental work designing the proposals is undoubtedly required. Tax reform undoubtedly falls into this category. In the current Parliament, all that is proposed within Housing to 2040 is to undertake critical reviews of the two key devolved housing taxes: Council Tax (CT) and Land and Buildings Transactions Tax (LBTT).

Our reasoning for choosing this area of the strategy as a focus is as follows. First, housing tax reform offers the prospect of using fiscal tools to help shape the housing market and improve its efficiency. Second, the rising importance of housing wealth as a site of inequality and the failure to recognise the many problems that the concentration of housing wealth brings, is an important reason to use these levers progressively to reform tax and potentially raise revenue for housing and other redistributive ends. Third, creating a wider property-based tax base in Scotland offers public finance opportunities and scope to reduce reliance on more elastic income tax. These are the hypotheses we examine in what follows.

Two other important reasons for reform are, first, that the existing taxes are problematic in important ways and, as many previous and recent studies, commissions and programmes of work have shown, they do, objectively, need to be reformed (an argument developed in the next two chapters). Second, Housing to 2040 sets out an ambitious desire to stabilise real house prices in Scotland, to reduce the dependence on property as a store of wealth, and to de-speculate the housing market[5]. Tax levers are an important (necessary though not sufficient) set of interventions to help make progress. It is an undeniable fact that there is a considerable gap between ambition and policy proposals, and that has led us to focus on housing tax reform. However, it is also a critical potential area for both redistribution and housing market improvement, to help deliver a well-functioning housing system. A theme running through this discussion is the recognition of how difficult effective reform in this area can be to deliver. Also, in response, there is a need to think hard about presenting, framing and persuading around the case for reform.

3 Gibb and James, 2021

4 As of end September 2024: Aberdeen, Argyll & Bute, Angus, Dumfries & Galloway, Edinburgh, East Renfrewshire, Glasgow, Fife, Scottish Borders, West Dunbarton, West Lothian and South Lanarkshire councils have declared a housing emergency locally, along with the Scottish Government.

5 See principles 2 and 3 in the Vison and Principles Housing to 2040 document

1.2 What did we do?

The project first conducted a review of the property tax reform literature going back to the short-lived Community Charge (poll tax) but also considering specific Scottish and international debates about tax reform (see: Gibb and Christie, 2015; 2019; Slack and Byrd, 2015). This review also set out the policy framework and context within which these reform debates take place (and are constrained). The study also examined contemporary reform proposal ideas and, in so doing, distinguishes between moderate reform of council tax as opposed to more thoroughgoing replacement of the council tax (and indeed also of Land Buildings Transactions Tax). To help us better understand the reform agenda and the aspects of politics and public policy that hinder or prevent reform, the project team undertook a programme of economic modelling of different reform ideas. Finally, the team convened a deliberative citizen panel at the beginning of June 2024 to better understand how a cross section of citizens understand and evaluate how local taxation, local services and housing come together, what the trade-offs are, and whether there is a preferred way forward. The team also met with an expert panel of housing sector experts and leaders to both diagnose the current arrangements and debate alternative reform proposals.

This report is structured into 7 chapters. The next chapter (Chapter 2) sets out the policy context, presents the current devolved tax arrangements in Scotland and common criticisms of the status quo. Chapter 3 does two things: first, it sets out criteria by which to judge property tax reform ideas; second, it take the reader through the modern history of tax change in Scotland, going back to the demise of the domestic rates and through to more recent debates over council tax reform. Chapter 4 outlines several contemporary ideas for reform. Chapter 5 sets out the new property tax modelling carried out on a unique Scottish property valuation database. Chapter 6 reports on the citizen panel on property tax reform carried out in June 2024. Chapter 7 summarises and concludes with key messages about the relevance of this question to housing to 2040 and the wider benefits of reform but also thinking hard about overcoming the political and practical difficulties of property tax reform.

2. Policy Context and Overview

2.1 Background

The set of housing taxes potentially relevant to Scottish households are wide-ranging. They include Capital Gains Tax associated with land sales, second residences and properties owned for business purposes (but not primary owner-occupied residences, which are exempt). They also include VAT on repairs and improvements (though not new build), and property aspects of Inheritance Tax liabilities. There are also many taxes associated with businesses working in the residential sector. In practice this cluster of taxes is reserved to Westminster. The only taxes not reserved are the Council Tax (CT), which was part of the 1999 Devolution settlement to pay for local government services, and Land Building Transaction Tax (LBTT), the Scottish version of Stamp Duty Land Tax, which was devolved as part of legislation in 2012 and introduced two years later.

In 2012, localism legislation in Westminster ended the GB-wide system of Council Tax Benefit, localising the scheme in England and devolving it to Scotland and Wales. At that time, Scotland decided to set up a Scottish wide scheme along similar lines to the pre-existing benefit called the Council Tax Reduction Scheme (CTRS). It remains in operation today, providing rebates on council tax for lower income, often older, households. For completeness, it is worth adding that the other benefit counterpoint to housing taxes, Housing Benefit/Universal Credit for social tenants and Local Housing Allowance, other than discretionary housing payments, remain reserved to Westminster). While not further discussed here, any comprehensive discussion of housing policy in Scotland in the round needs to factor-in the dominance of demand-side subsidy and the costs and benefits of their devolution, bearing in mind the need to have control over the main supply and demand levers of affordable and lower income housing policies across Scotland (Gibb, 2024).

2.2 Council Tax

Council Tax is the principal source of revenue under the control of Scottish local authorities, although, as we shall see, council tax rates have been frozen or capped by central government for most of the period since 2007. In recent years, across Scotland, Council Tax has raised 19-20% of local government revenue, which amounted to £2.73 billion in 2022-23[6].

As in England and Wales, Council Tax is structured around bands based on property values. There are eight Scottish-specific bands which are each a fixed percentage of Band D – see Table 1. The chief effect of the banding is to dampen the relationship between tax payment and relative property value, especially for higher valued properties, although this was somewhat mitigated by increases to the higher bands (as a percentage of band D) introduced in 2017, following the Government's response to the Scottish Local Tax Commission. The other key feature is that Scotland, as England (but not Wales), has never had a general revaluation and the tax base remains at the 1991 initial valuation of the scheme (more modern built homes and more recent transactions of properties are assigned a 1991 value for council tax purposes).

Table 1 The Council Tax in Scotland (current arrangements)

Tax band	Price range (1991 values)	Weight relative to band D= 100	Average Scottish Charge 2023-24
A	<£27,000	0.67	£944
B	£27,001-35,000	0.78	£1,102
C	£35,001-45,000	0.89	£1,259
D	£45,001-58,000	1.00	£1,417
E	£58,001-80,000	1.31	£1,861
F	£80,001-106,000	1.63	£2,302
G	£106,001-212,000	1.96	£2,774
H	>£212,000	2.45	£3,470

Council Tax replaced the Community Charge ('poll tax') in 1993 as a politically acceptable hybrid of a property value tax (i.e. the attractiveness of property as an immovable tax base compared to mobile people), whilst retaining a service-charge element from the poll tax as a tax on all households and not just owners of property assets. Since that time, there have been growing calls from commentators (if not national politicians) for a regular comprehensive revaluation, as well as efforts to review the tax and seek its reform and even abolition[7].

In practice, the only reforms of note in Scotland were to widen the band multipliers for high banded properties in 2017, and at the same time provide additional support for low-income households caught with higher bills due to the 2017 changes through adjustments to the Council Tax Reduction Scheme (CTRS). Alongside these band weighting changes, the decade-long freeze on Council Tax was loosened, first as an annual cap on increases, until discretion was wholly returned in 2022-23. However, **in the Spring of 2023, there was a consultation exercise which proposed further increasing the weights of the highest bands. This was subsequently abandoned. Instead, after announcements made at the SNP national Conference in October 2023, the decision was unexpectedly taken to reinstate the freeze for 2024-25.**

The Council Tax freeze was a particularly popular policy

6 Scottish Government 2023 Local Government Finance Statistics 2022-23. Note that the local percentage raised by council tax varies considerably across local authorities.

7 E.g. Burt Inquiry, 2006; Commission on Local Tax Reform, 2015

with households but stored up problems of different kinds the longer it continued. In the Scottish 2011 election, the freeze was found to be the most popular policy pursued by government in exit surveys. However, it cost an additional £70 million each year to keep Council Tax to 2007-08 levels for nine years – cumulatively fully £3.1 billion was required to be added to local government block grants. And it was far from progressive since it benefitted higher band taxpayers the most. It also erodes local government democratic accountability by removing voter choices over local spending and tax decisions.

The CTRS in Scotland supported about a fifth of households in chargeable dwellings in 2023-24 and spent of the order of £387.6m in that financial year, an average of £850 per year for the more than 461,000 recipients.[8] The scheme is targeted at people on low income – below a capital requirement (£16,000) and for people qualifying for Universal Credit or related legacy benefits and the guarantee credit element of pensioner credit. The scheme also has a taper of withdrawal as income rises (set at 20%). Inevitably, the different means-tested supports interact increasing complexity. Scottish Government statistics (ibid.) indicates that around a third of recipients are aged over 65, one in six are lone parents and 57% of recipients live in the 30% most deprived local areas. Recipients living in properties with bands E to H can, since the 2016-17 reforms, receive further reductions compensating for the increased weights in higher bands then introduced. All single adult households receive a discount on their council tax bill.

There are several widely held criticisms of the Council Tax:

- It is regressive because the design of the property value banding system causes higher value properties to be taxed at a lower rate, proportionately, than lower valued property. Table 1 above shows that a property in Band A pays a bill of 2/3 of band D though a property in the upper third of band D is worth twice the upper value of Band A (on valuation grounds). A top-rated H banded property has a bill that is just under 2.5 times the bill of a band D property, but the estimated 1991 value for Band H is at least more than four times the mid-point of band D. More graphically, the Commission on Local Tax Reform (2015, 2.3) said '*Even by its own test of charging households, amounts based on the value of the property they live in, the present Council Tax system falls short. People in the most expensive homes pay no more than 3 times the tax on the lowest value homes, even though we estimate those homes, on average, are now worth around 15 times as much. That means people in less expensive homes are paying a higher proportion of their property's value in Council Tax than those in the most expensive homes. And all charges are based on not what the property is worth now, but what it was worth in 1991. For newly built homes, an estimate must be made of what it would have been worth in 1991.*
- In Scotland and in England the Council Tax has not been generally revalued since its inception more than 30 years ago. The growing separation of the tax base from the current level and distribution of property value is widely criticised. Recent research (Scottish Local Tax Commission Appendix 2) suggests that as many as half of properties are now in the 'wrong' tax band because the market has shifted structurally over the intervening period. Also, every property built since that 1991 valuation requires to have its value estimated for 1991 prices. Moreover, the 1991 valuation was done via an inexpensive drive-by process which has always been questioned in terms of its accuracy.
- It is also apparent from evidence covering England that, regionally, Council Tax, as a share of current property values, is higher in lower valued house price regions than high value regions – in other words Londoners pay less of their property value in tax than northern regions[9]. **This also means that government grant to local authorities is distributed less progressively than would be the case** if the tax base in high value areas was not depressed as it is by the Council Tax bands. The same principles will apply contrasting high and low value property markets in Scotland. Looking at England, Nanda (2021, fig.3, p.7) illustrates that as property value increases, Council Tax rates fall. Also, (figure 4, p.10) shows that average Council Tax payments fall as a share of property value when mean local authority house prices increase. In other words, lower value properties pay higher rates of council tax.
- The Burt Review in 2006 was the first detailed examination to indicate that Council Tax bills as a share of income (benefit support excepted), fall as income rises, especially at higher levels of incomes.
- The Council Tax also retained specific features of the preceding Community Charge – such as discounts for single adults and certain exemptions (e.g. students), which introduces a degree of arbitrariness into the tax liability.
- The combination of these factors led the Scottish Government to tinker with upper value tax bands' weightings (and augment the Council Tax Reduction Scheme to compensate lower income households). However, it stopped short of a general revaluation and moving any further in the direction of a closer relationship between tax bills and current property value. **Revaluation to current capital values would be a simpler and more progressive way to tax housing wealth. Additionally, the return to freezing Council Tax further erodes local government accountability for setting taxes.**

2.3 Land Buildings Transactions Tax

Table 2 sets out the different tax rates that are formally liable on home purchasers when they buy a home. Land & Buildings Transactions Tax (LBTT) has a progressive structure in that it rises as a percentage of sales price as that value increases. It also has a zero tax rate starting band and has an exemption level for first time buyers up to a higher threshold. Unlike the earlier version of Stamp Duty, which had a slab structure (i.e. you paid the relevant highest marginal tax rate based on purchase price on all of the liable purchase price), purchasers pay progressive elements at each applicable tax rate ('slice') and only the highest marginal rate on the uppermost

8 https://www.gov.scot/publications/council-tax-reduction-scotland-2023-2024/pages/2/
9 Leishman et al, 2014

component of value.

In 2021-22, Scottish LBTT raised £827m (including £161m from Additional Dwelling Supplement (ADS) - see below)[10]. Scotland introduced its tax bands, reflecting lower Scottish values just before the UK Treasury introduced its new (non-slab) tax bands in 2013. Note that the tax take is larger than the annual investment in the affordable housing supply programme, even though the LBTT revenue is not assigned to any housing-related programme.

Table 2 Structure of LBTT, Scotland

Price band	LBTT Tax rate
<£145,000	nil
£145,001-250,000	2%
£250,001-£325,000	5%
£325,001-£750,000	10%
>£750,000	12%

Notes

(1) First time buyer main residence relief or nil rate up to £175,000

(2) Additional Dwelling Supplement adds 8% to liable LBTT for second or additional homes

The other major change to LBTT was the introduction of the Additional Dwelling Supplement (ADS) which levies a higher tax rate (a flat rate basis regardless of value added to the standard LBTT liability) on second properties and landlord purchases. HM Treasury came up with this idea to support potential first-time buyers by reducing the competitiveness of landlords purchasing properties within the reach of potential owners. This also had the effect of deterring landlords from investing in a context where access to a mortgage and high deposit requirements were increasing demand for private renting (the same logic applied to 'supporting' first time buyers' by offering them partial exemptions from LBTT). Scottish ministers chose to emulate this policy along with the rest of the UK. Subsequently, Scotland increased the ADS rate from 4% to 6% (the highest such basic rate in the UK), and agreed to increase the tax rate from April 2025 to 8%.

The economics profession has long been clear about its opposition to property transactions taxation like Stamp Duty Land Tax and LBTT. The 2011 Mirrlees review of taxation for the Institute of Fiscal Studies argued that taxes specific to property sales deter those sales and hence damage labour and housing mobility to the detriment of economic productivity and household utility. The efforts to produce progressive tax structures (increasing with sales value), the use of exemptions and nil rates for first time buyers inevitably also interact and distort market segments. In Scotland, for instance, there has been much commentary on the bunching effects of moving from the 5% to 10% tax rate when properties go over the £325,000 price and which also leads to property sales grouping just below the value that signals a rate increase. This has been exacerbated by regular tinkering with tax rates and exemptions by previous UK Chancellors of the Exchequer and Scottish Finance Ministers going back at least to Gordon Brown and as recently as the Covid-19 period.[11]

This transactions tax is far from economically and socially neutral in its effects. The above criticisms have led some critics to call for its outright abolition, arguing that the direct and indirect economics benefits would justify the tax cut.[12] Abolishing LBTT would probably lead to rising house prices as the removal of the tax reduces the cost of purchase and would stimulate demand. LBTT raises significant revenue for a Scottish fiscal system that requires its budget to balance – so it is not credible to imagine that it could simply be abolished. Some other form of preferably property-related tax would need to fill the gap, moderate the capitalisation effects on house prices, and meet the requirements of the rules for new devolved taxes.

The other difficulty with LBTT is that it needs to be accurately forecast by the Scottish Fiscal Commission to help the Scottish Government plan its budget – and there are important constraints and consequences on Government that means that this degree of forecast-ability is a non-trivial consideration (i.e. the need to borrow to make up short falls in revenue). Essentially, there are three moving parts: predicting the volume of transactions (both house sales and properties sold falling into the ADS category); forecasting the level and distribution of house prices for those properties transacting; and, estimating the effects of possible different tax rates, as well as the existing tax rate structure and tax reliefs, on revenues.

10 Revenue Scotland (2022) Annual Summary of the Trends in Devolved Taxes. https://revenue.scot/news-publications/publications/statistics/annual-summary-trends-devolved-taxes-2021-22/land-buildings-transaction-tax

11 We note that Whitehead, et al (2024) have advanced a proposal for a 100% concession on SDLT for over 65s buying property to encourage down- or right-sizing to better balance households and housing stock.

12 Nanda, 2021

3. Property Tax Reform

3.1 Introduction

In this chapter we think about how we might assess the need for property tax reform. We do this by examining a range of widely used criteria to assess the fitness of property taxes. Here, we identify five themes that will be used in the rest of the report. The next part if this section complements our discussion of criteria by drawing on international evidence about the characteristics of effective property tax reform. We then move on to look at the history of the property tax reform debate in Scotland.

3.2 Five Criteria for Good Property Taxes

There is no standard set of criteria to judge good property taxes though there are multiple criteria that have been deployed over time by reforming governments (Gibb, 1988) (see relevant green papers in 1981, 1986 and 1991 as well as various commissions of inquiry identified in the references to this report).Typically, they include reference to the technical and fiscal feasibility of a proposed or current tax (including how it fits into wider systems of local government finance and service delivery), fairness in multiple guises is highlighted, as is a discussion of democratic local accountability. Several of the lists of criteria for a good tax also include minimising wider distortions and unintended consequences often relating to economic and market effects (as well as positive spillovers that might arise from a reform). In this section we examine five criteria that are adopted in what follows.

1. Housing system improvement. Does the proposed property tax contribute to the wider goals of housing system improvement? In Housing to 2040, the Scottish Government is clear that the strategy aims to contribute to the whole purpose of a developing a well-functioning housing system and that reform of devolved property taxes may contribute to the vison and principle of de-speculation and stabilisation of housing prices and private rents and facilitate the diversification of savings and wealth holdings away from property. Housing to 2040 does not adequately define what is a housing system, let alone a well-functioning one. These ideas originated in Scotland through Local Housing Systems Analysis (see O'Sullivan, et al, 2004).

A contemporary perspective on a well-functioning housing system, which CaCHE authored, can be found in the recent Homes for All English housing strategy from the Church of England and Nationwide Foundation (pp.24-26). Table 3 summarises and paraphrases the main components. Housing policies and reforms move the system to the desired goal if they are compatible and consistent with the system incorporating the 18 elements set out in the table below. The components are divided into three: the quality of homes; the functioning of the housing market; and the outcomes of the housing system. Thus, a well-functioning housing system moves towards a progressive realisation of high minimum standards, energy-efficient, affordable, tenure-neutral homes. The nation builds enough homes to meet needs and demand, in places where people want to live and this includes sufficient good quality social housing, high quality private renting and sufficient temporary accommodation for those in urgent need. The aim is a housing system where the different elements work together rather than in opposition so that homelessness is largely ended, and where house prices and rents move in the long term with the general level of inflation in a neutral fashion, stabilising markets. In such a world, housing contributes to economic productivity and regional economic development. The housing system complements key policy systems like social care, pensions, health and social security. Housing systems do not amplify social division by increasing inequalities, exclusion or discrimination.

Our immediate question from this criterion is whether existing devolved property tazes are contributing to or inhibiting the development of this well-functioning housing system? Do existing taxes encourage energy efficiency, housing affordability, stable housing markets, reduced wealth inequality, better working social care and pensions systems, a better-functioning economy, or more liquid and accessible housing e.g. access to home ownership? Similar questions can be asked of alternatives or reforms to the current arrangements for CT and LBTT.

Table 3 A Well-Functioning Housing System

Homes	The housing market	The housing system
People live in homes of high minimum standards and provide stable adaptable, secure environments	We build enough homes to meet existing need and newly arising needs and demands, including sufficient accessible homes	The different parts of the housing system work together rather than against each other.
Homes provide thermal warmth and energy efficiency	Sufficient homes are in places where people want to live, and communities have an influence on design and development	Homelessness is rare, brief and non-recurring
Homes are affordable in terms of cost to income and residual income	There is sufficient good quality social housing which is a platform for lower income households to build their lives	House prices and rent rise over time in a more stable or orderly fashion, close to or at the rate of general inflation
Genuinely affordable choices for housing exist throughout the life course	There is a thriving high-quality PRS which balances security and affordability with decent rates of return for landlords	Housing contributes to and does not inhibit economic growth or performance and housing policy is more integrated into levelling-up and spatial balance strategies, facilitating labour mobility
Home ownership should be possible more widely but is not the only measure of housing success or quality	Mortgage regulation is such that the home ownership sector is more accessible but still stable and financially sustainable	Housing complements other vital social systems such as social care, health care and social security
Housing is regardless of tenure well designed, secure and affordable and residents feel they can exercise meaningful degrees of control	Temporary accommodation is available to those who need it for short periods, and it does not disempower them	Housing system structures and processes do not amplify social division e.g. discrimination, exclusion and wealth inequalities

Source: Church of England and Nationwide Foundation (2024) Homes for All: A Vision for England's Housing System[13]

2. Fairness and Inequality Reduction. Asking whether our property taxes are fair begs several questions. Fairness in terms of the housing impacts can cover several dimensions of inequality. Thinking about the tax as a burden on household income - is the perceived tax burden progressive, proportional or regressive as a percentage of income as we, for instance, look at different income deciles? Do we consider this in isolation from the tax system as a whole? For the Council Tax, how fair is the correspondence between tax bills and the consumption of local government services? How effective is the council tax reduction scheme in helping low-income households mitigate the tax burden? For LBTT how fair is the proxy of house price for wealth or income in presenting purchasers with a graduated tax that increases payments as property value rises (and are those increments or bands fair)? Is it fair that all landlords face the same, across the board, 8% hike in LBTT?

The original logic of a local property tax was that property values were enhanced by good local services (good local government performance is capitalised into higher prices) and hence it is fair that property owners pay more. This also implies that local property taxes are a consumption tax on local households relating to local public service consumption, but that they can be, secondly, considered as a tax on wealth held in property. Housing wealth is lightly taxed in the UK (e.g. the modest contribution housing makes to inheritance tax with its high levels of exempt wealth holdings, and the exemption of primary residences for capital gains tax purposes). **This means that local property taxes could play (and could be designed to perform) a role in taxing wealth held in housing and thus both redistribute wealth and generate additional taxable resource for redistributional purpose and/or offer opportunity to redefine the Scottish tax base.** More generally, economists have long argued that **failure to tax investment aspects of a tradable asset like land and property can lead to over-investment in that asset, greater speculation and destabilisation, as well as more inequality, housing-related poverty and exclusion from access to housing and impaired social mobility.**

3. Furthering Local Democratic Accountability. Local elections allow different parties to promote their own policy platforms, approach to local government and what they ask voters to pay through their local tax bills. Particularly in the 1980s, this notion of local democratic accountability was viewed as one of the key criteria for a good system of local taxes. Does the tax link higher (lower) spending to higher (reduced) tax bills? Are forms of tax signal able to do this more directly? This was important for the Community Charge, which wanted to use the grant system to create a local price for a standard level of local services and in which dissatisfied voters could vote out a high spending - low service value combination. They could also vote with their feet and move to a better fiscal combination elsewhere (with big deterring effects on the origin council's spending ambitions). This is one

13 The paper was authored by CaCHE researchers: Alex Marsh, Kenneth Gibb and Alice Earley

ex post rationalisation of why the Major government did not alter the poll tax grant system underpinning the new Council Tax to retain these conservative budgetary incentives.

The political narrative since 1993 has continued to be one of centralisation and reduced discretion for local government. This was most clearly seen with the introduction and long-term retention of the council tax freeze in Scotland – **a policy that was expensive to the tax payer overall, served to most benefit higher property value households over time, but also one that undermined the voter-councillor fiscal connection.** While it might be argued that local tax payers do not know enough about what their taxes pay for, this is also true of central government revenues and, in any case, is in no way a necessary or desirable unchangeable fact of citizen-government relationships[14].

We note that the recent reemergence of a council tax freeze retains the assumption of control over local government by Holyrood and remains a strong populist policy platform (and one deeply unpopular with local government). This is in part about how local taxes and finance fit into the wider central-local relationship over power, resources, agency, and control over who provides and leads on different services. This criterion is where we recognise that we cannot look at council tax in isolation from these wider relationships, institutions and principles. It also raises questions and trade-offs for reform ideas e.g. that property taxes should only be paid by property owners and where that leaves the accountability between tenants and payment for council services consumed (and voted for).

4. Fiscal and wider Public Policy Goals. LBTT is a form of Stamp Duty – a tax designed to have a **100% take up or collection rate because it is associated with the legal act of transferring property ownership. LBTT raises close to a billion pounds a year in a devolved fiscal system that must balance its budget each year.** This is intrinsically difficult to forecast because of the moving parts that determine the tax take. Moreover, the design of a transactions tax like LBTT may reduce labour mobility and damage the economy by reducing opportunities to take up jobs in growing parts of the economy, and, at the same time, push up rents in local rental markets. If future policy seeks to alter LBTT - to reduce it, change it in different ways, or abolish it – the tax revenue lost must be found in other ways. This is also of course an opportunity to be creative and thoughtful with a different property tax base, perhaps one based on recurring charges rather than only at the point of transaction.

While we have not seen a system level change to local government finance since the late 1980s, the interconnected nature of taxes and grants makes a strong case for a serious examination and **phased transition** to new arrangements (assuming one can come to a consensus around the critical elements). What would be the overall size of the grant in aid package from central to local government? A key role played by grant is to equalise resources – reflecting differences on both local need for services and different capacities to pay (local tax bases vary). What progress can be made here without running into fiscal difficulties overall? Is there a case, as those in favour of more localist reforms propose, to return non-domestic rates revenue to local government (they are currently essentially a flat rate or national tax on businesses returned to local government as a per capita grant) and, to return rate-setting to local government? This would reduce the gearing on Council Tax and increase local accountability; it would also increase discretion for local government about how they incentivise local business and economic development. Once these large finance building blocks are settled, it is then that a more coherent approach to local tax reform might proceed in a sustainable way.

These are big strategic decisions that require long term policy debate, design and implementation that goes well beyond a single Parliamentary term and consequently requires a 'big tent' approach and inclusive consensual support (including from HM Treasury around fiscal framework implications). But **if one is to take a long-term resilient approach to local taxation then it needs to be consistent with a sustainable system of local government finance.**

5. Technically feasible taxes. Devolved property taxes are relatively attractive because they have a degree of technical soundness, provided they are implemented to maximise this aspect of the tax in question. We have seen that taxes on immobile property are harder to avoid and easier to collect than e.g. poll taxes or indeed taxes on income. Stamp duty-based taxes are easy to collect because they fall at the point of legal transaction. However, property is an asset class wherein value changes and does so in a relatively volatile and uncertain way. This is why regular general revaluation is important to retain the link between tax base and value but also to allow the tax base to be buoyant - tied to grow with broader economic change (noting that the cost of local services increases with inflation); otherwise, tax rates have to endlessly rise to accommodate rising costs. Revaluation was in earlier generations, and crucially in the 1980s and 1990s, perceived as a difficult, expensive and electorally damaging process. Internationally (not just in Britain) this led to long delays and failure to carry through regular periodic revaluations even when they were statutory. However, the advent of big data and automatic valuation systems has revolutionised property valuation for tax purposes, and many of the age-old technical concerns are now significantly mitigated. This also means that more radical reforms, e.g. land value taxation, are also now more practically possible and much less a theoretical proposition only.

Clearly, any tax must deliver high rates of collection and fiscal certainty for those involved. The tax base should be stable, cost-effective to deliver and minimise evasion (Gibb, 1988). Regular revaluation is essential, but it also has positive externalities. Thus, if one lived in in a system where annual revaluation was the norm, this would have a major impact on what economists call price discovery - flooding the market with current valuations of all properties and leading to better informed market actors (and not just agents). As we discuss in the next chapter, data technology advances also mean that is becoming possible to routinely extract robust land value

14 We note the recent increase in Scottish councils consulting voter/taxpayers with choices over how spending cuts could be allocated to specific services, and indeed, the uptake more generally in community budgeting in different forms.

estimates from the capital values of properties too.

If we look at these five criteria together (housing system improvement, fairness and inequality reduction, furthering local democratic accountability, fiscal and public policy goals, and technically feasible taxes), it should be clear that they are connected, interdependent and need to be considered in the round. We will attempt to do this throughout this report, starting with a brief review of contemporary ideas about property tax reform.

3.3 Contemporary Literature: Delivering Property Tax Reform

In the last two decades, there have been several important studies that have contributed to our understanding of tax reform regarding the two taxes, in terms of making the case for feasible reform and outlining the difficulties in persuading politicians and the public that these are feasible, implementable and wise reforms. Here, we acknowledge the work done on a proportional property tax (Nanda, 2021, and earlier from the Burt Review), on land value taxation, on stamp duty (e.g the Mirrlees review) and the stimulating papers by John Muellbauer (2023) and Tim Leunig (2024). These are all reviewed in the next chapter. Here we focus on the international research by Slack and Bird (2015) that looks to common problems and their possible solutions in the delivery of property tax reform.

The troubled history of local tax reform in Britain has led many contemporary politicians to simply place meaningful local tax reform out of reach. This status quo thinking goes back to the demise of Domestic Rates in the 1980s, and the Scottish rates revaluation and ratepayers' rebellion in 1985, seen as a major source of demand for a non-property based domestic tax with which to fund local government. Later, over-cautious lessons were drawn from the disaster of the poll tax, something exacerbated by making everyone pay a minimum contribution and the error of moving from a tax base using property to the much less reliable one of people. It also led to a desire to find a political solution, the Council Tax, with much more interest in de-escalating the issue rather than developing a good and resilient system of local government finance and renewed central-local government relations. In fact, most of the 'poll tax' system, except for the actual tax, remains in place.

Property taxes are intimately related to the wider context of local authority finance. If the tax base (property values) oscillates over time because values in the market rise and fall, this creates problems for local government who are not normally able to borrow to meet shortfalls and hence they are obliged to adapt through higher tax rates. This is analogous to the Scottish Government having limited powers to borrow for shortfalls induced by forecasting errors in revenue tax take. This also brings to the fore the trade-offs between tax-raising powers, ability to borrow and strengthening local financial accountability to taxpayers. While we make much of the need to improve fairness in our housing taxes, we also want such taxes to enhance housing market efficiency, support the public finances and sharpen accountability between tax setting authorities and taxpayers.

The local tax base varies across council areas and does so on a per capita basis. This is why we need systems of grant that equalise resources to reduce post code lotteries; this is also why we need to reflect in grant that needs differ and services do not just depend on population size. We should also bear in mind that ultimately grant also comes from taxpayers, in this case national (Scottish taxpayers) as opposed to local bill payers. There will be trade-offs, but these will need to be surfaced and debated transparently.

Table 4 Slack and Bird Challenges and Proposals around Effective Property Tax Reform

Issues & Problems	Promising Approaches	Less Promising Approaches
Salience: property tax is more noticeable than other taxes	Conjoin tax reform with improvements in local services; withhold tax at source or other payment options; phase-in changes	Set revaluation limits; cap or freeze the property tax
Liquidity Constraints: imperfect association between taxpayer incomes and property taxes, especially for seniors	Offer tax deferrals for seniors; provide more payment options; phase-in changes	Set assessment limits; cap or freeze the property tax
Perceived Regressivity: taxes higher as a percent of income for low-income taxpayers	Offer property tax credits; offer tax deferrals; bundle with other tax reforms; package with expenditure changes; provide low income housing exemptions	Implement banding
Volatility: potentially large swings in taxes for some taxpayers (not an issue with Council Tax but potentially with other property taxes)	Conduct annual revaluations; index the tax base; provide taxpayer education; communicate in an understandable form; phase-in changes	Set assessment limits; cap or freeze the property tax
Presumptive Tax: tax base is inherently arbitrary	Provide taxpayer education; conduct public consultations; make revaluation appeal process accessible; phase-in changes	Allow self-assessment for revaluation; implement classified property tax rates; set progressive tax rates; set revaluation limits; cap or freeze the property tax
Inelasticity (a problem for local governments, not taxpayers): taxes do not increase with growth	Conduct annual revaluations; index the tax base; phase-in changes	

Source: derived from Slack, E and Byrd, R (2015) Table 2

As outlined in Table 4 above, Slack and Bird (2015) identify six fundamental problems that those reforming property taxes must confront. These are: salience – relative to other taxes, taxpayers are disproportionately aware of property taxes they face; liquidity constraints – lower income, often older households struggle to pay taxes based on capital values i.e. they may be cash poor but asset rich; perceived regressivity faced by low income taxpayers; volatility – poor design can generate large annual swings in tax payments; presumptive taxation – the property tax is regarded as lacking legitimacy with taxpayers as a tax base and is seen as arbitrary; finally, the tax base is inelastic or non-buoyant and does not necessarily rise with economic growth.

Slack and Bird suggest (right column Table 4) several property tax reform ideas unlikely to prosper and therefore to be avoided. These include: not revaluing regularly and comprehensively; moving from a value base to a banded value base; limiting, capping or otherwise attenuating revaluation to protect and make revaluation more palatable politically; capping or freezing property tax bills; adopting self-revaluation methods; or, establishing progressive tax payments structures within the tax liability of the property tax (as opposed to a single proportional tax rate, as with Nanda, 2021). **They also generally favour the practice observed in many countries outside of the UK of adopting several low incidence property and non-property local domestic taxes, as opposed to reliance on a single tax with a higher implied tax burden.**

The middle column of Table 4 suggests a range of policy proposals to help reform property taxes:

- Regular, eventually annual, revaluations (possibly indexed annually between revaluations) with an accessible appeals process (drawing on technological advances such as automatic valuation and exploitation of big data);
- Link tax reforms to public service improvements and expenditure programme changes;
- Provide tax deferrals, offer property tax credits, and other payment options to ease taxpayer difficulties;
- Phase-in tax change and dampen the maximum annual impacts on taxpayers;
- Exempt low-income housing below a certain level of value;
- Provide coherent and impactful taxpayer education and communications on tax and local government spending.

These ideas are important steps in evaluating proposals for reform of property taxation. It should also be said that progressivity should be assessed in relation to the total tax burden households face and not simply one tax or sub-set of the totality (McCauley, 2022). Tax reform proposals also have to cohere with the Scottish Government's own tax framework and be consistent with the devolved financial framework operating between Scotland and the UK.[15]

15 A Framework for Tax (Scottish Government, 2021)

3.4 A Short History of Property Tax Reform in Scotland

Land buildings and Transactions Taxes

Stamp duty Land Tax (SDLT) is an ancient transaction tax associated with the transfer of ownership of assets, both financial and physical and have come to be an important transactions cost in the sale of land and property. Stamp duty's design was heavily criticised in the 1990s because it was both a relatively high incidence tax and hence impacted negatively on housing mobility. One consequence of its burden on purchasers was that it was frequently tinkered with by successive chancellors, particularly from Gordon Brown onwards but continuing with Osborne and Sunak. Governments introduced temporary and otherwise later reverse reliefs on stamp duty to increase turnover during the Covid-19 pandemic, to favour specific regions, to reduce the burden on first time buyers, and raising additional tax through stamp duty to reduce demand for purchase by Buy to Let investors.

A second key feature of Stamp duty was its traditional slab structure (Andrew, et al, 2003). Until it was reformed in the first half of the 2010s, payment liability was in a progressive form i.e. as the property sale price increased, purchasers move into higher tax liabilities. However, unlike for example, income tax, the purchaser paid all their tax at the highest liability associated with the actual price of the property. In other words, these was no reduction for the first portion of the liability wherein properties below that threshold paid no tax; there was also no benefit on paying lower tax increments on the succeeding bands. Reforms introduced by the Coalition Government swept the slab approach away, such that purchasers paid a tax liability based on the sum of whatever they were liable for each proportion of the property, as with income tax. This reduces liability overall but remains progressive in the sense that the tax liability remains higher, the higher is the value of the property. While this is an improvement on tax liability and progressivity grounds, it remains the case that any such tax with a non -zero liability still impedes mobility. It is also important to recognise that such progressivity critically depends on the rates and bands used and how often the bands are uprated in the light of general house price inflation. Note also, finally, that the Additional Dwelling Supplement is not progressive in the way just described – instead it is a flat rate (slab) added to the normal stamp duty liability for landlords and other second property owners (and is high in Scotland, 8% from 2025-26).

In Scotland following the 2007 Scottish election and advent of an SNP minority government, the UK parliament conducted an inquiry to provide additional powers that would, it was thought, satisfy growing demands for constitutional change (as was the case after the 2014 referendum). Finally, in 2012, new tax powers were created, and one major reform was to devolve residential stamp duty, now called Land and Buildings Transactions Tax (LBTT). LBTT also eschewed the slab structure and constructed a progressive set of liabilities rising from zero to successive higher tax payments that grew with increased property values but with each paid on the successive elements of the property value, like income tax. There were reliefs for first time buyers, and subsequently, additional dwelling supplement was added (also devolved) when this was introduced by the UK government. Scotland has lower house prices than the rest of the UK, so it set different tax rates across more moderate priced bands, but the Scottish overnment also decided to make their tax rates and bands more progressive than in the rest of the UK, leading to further tax competitive changes made by the UK Government. Scotland also introduced and retains a higher rate of additional dwelling supplement than elsewhere in the UK. Scotland followed the temporary Covid-19 reliefs on LBTT as introduced in 2020 by the UK Government (generally considered to be unnecessary to maintain prices and turnover – Pawson, et al, 2022).

As with all taxes, issues remain over the incidence and effects on economic behaviour associated with such transaction taxes, but also as with other taxes, there are more precise questions about the schedule of tax rates and their associated property value bands (e.g. clustering of offers over prices in order to try to keep sales prices below a band threshold), as well as exempted value bands for low cost properties and specific tax reliefs, as well as the treatment of private landlords. As we will find in the next chapter, writers seeking to reform LBTT/SDLT see it both as a tax that can be combined with council tax but also if retained can be incentivised in different ways e.g. providing tax reliefs associated with green retrofit outcomes.

Local Taxation

We have the Council Tax because of the politics of reforming the Domestic Rates and its temporary ill-fated successor the community charge (poll tax). Here we briefly outline the history of this process (see Gibb, 1988; Butler et all, 1994; Hollis, et al, 1991; Gallagher et al, 2007– for much more detail).

Domestic Rates, a local tax on the rental value of homes of renters and owners, to be regularly revalued (in theory if not practice), had been around for hundreds of years on the UK before modernisation around both sides of the turn of the 19th to 20th centuries. Along with municipalisation processes, local government finance took on its more familiar shape of local taxes along with grant from central government for equalising resources (local rateable values of domestic and non-domestic property) and needs equalisation reflecting the different economic, social and demographic circumstances of local populations.

The relationship between local and central government had long been uneasy but conflicts arose over the relative powers and discretions held. Despite local government being elected, it has also been constitutionally a creature of the UK Parliament and large subventions from London (and Edinburgh) have also meant that to an extent local government has acted as central government's agent providing specific services. Where local government was at odds with central government either for party political reasons or because of local issues, this in part led to a sense in the 1960s and particularly the 1970s (when the Layfield Commission reported), that clear resolution of the relationship between central and local government, the functional distribution of service and authority for such services, the geography of single or two tier local authorities[16], and broader funding questions (along perhaps also with the most efficient geography and structure of local government) needed clarity and long term settlement. **This never happened and the fundamental Layfield reform debate choice between centralising versus localising local government remains both critical and unresolved.**

These issues flared up much more aggressively with the election of the Thatcher government and a combination of pointed conflict with specific Labour councils, the use of financial and legislative powers to curb spending and discretion on the part of local government, as well as underlying political problems with imminent revaluation in Scotland and considerable political opposition through rate payer associations, local politicians and media (Hollis, et al, 1991; Butler et al, 1994). Home ownership was increasing, rate payers believed that higher valuations led automatically to higher bills (and did not consider the key role of both grant and the locally set rates or tax rates in determining actual bills).

By 1984 the Thatcher Government was clear that rates should be replaced with a 'better' tax alternative and this was accelerated by the experience of the Scottish revaluation proposed for 1985. In 1986, a new model of local government finance, Paying for Local Government, was launched as a Green Paper: reforming and simplifying grant, changing non domestic rates to a tax that would be centrally pooled and returned to councils as a population-driven grant, and the Community Charge, a poll tax, replacing the property tax. The shift to the new person-based tax was to be introduced over ten years but instead of offering 100% rebates for rate payers on very low incomes, households on the lowest incomes would still be expected to make a 20% minimum contribution. It was recognised in the Green Paper that removing the property tax would have an effect raising house prices but government argued on fairness grounds that the tax was really a highly visible average price of local services and people could shop around and move elsewhere or vote down their council if unhappy. There was still social security (albeit capped at 80% of the charge) but government did not accept the criticisms over the poll tax nature of the charge, arguing that it is the overall tax burden that matters.

After winning the 1987 general election the Thatcher Government pushed forward legislation on local government finance reform and critically did away with the proposed transition phase of 'dual running' and instead opted to introduce it in Scotland in one go in 1989 followed by the rest of the country (but not Northern Ireland where the status quo was retained) in 1990.

The introduction was disastrous, contributed to the demise of Mrs Thatcher and left considerable scars to this day about committing to wholesale reform of local taxation. The critical problems were twofold:

- The tax base was inherently much more mobile; there was significant non-payment problems compared to the near 100% collection and payment through a property tax base. This led to 'missing millions'. In the 1991 census as well as existential revenue shortfalls for councils. The poll tax was not technically feasible.
- The fairness argument was comprehensively lost by the government, as witnessed by a comprehensive rejection of the policy by commentators and other political parties, and, of course, through mass non-payment, demonstrations and rioting.

The new Major government pledged at the end of 1990 to quickly come up with a replacement tax that would neutralise the problem, utilising a sharp increase in VAT to fund shortfalls in revenue, and Michael Heseltine was put in charge of the rapid development of what became the Council Tax, introduced in 1993. It bears repeating to note that the rest of the grant and non-domestic rates systems did not change so that the council tax operates within the local government finance system to this day in a way essentially the same as the Community Charge (with band D tax bills taking on a similar role).

The new tax was a banded capital value tax wherein properties were valued at 1991 prices and then allocated one of 8 bands (the majority in the bottom four bands). With no expectation of a general revaluation (a political fix to avoid the difficulties experienced in the 1980s), all subsequent sales or new supply would be revalued for council tax purposes to 1991 values. That this 'fix' could not be sustained as housing markets evolved and prices changed was at best seen to be a problem for a future government.

The council tax was seen to be more palatable for three essential reasons:

- Fixing tax bills to relatively constrained proportions of band D was seen as an important way, along with not generally revaluing, to protect owner interests and moderate their tax bills. The unfairness of this and its contribution to encouraging greater wealth inequality only became generally apparent as time wore on.
- 100% social security help was restored to those on lowest incomes.
- Discounts and exemptions were carried over or extended from the community charge system, perceived to also support single adult households and students, among others.

An important wider implication of the council tax system was that it increased the process of gearing or leverage – **over time the proportion of local government revenues raised locally has shrunk, meaning that with grant relatively fixed, any 1% increase in total spend would need to all come from council lax. Thus, if council tax raised 20% of total revenues, a 1% increase in spend needs a 5% increase in CT.** Both the Thatcher and Major governments saw this gearing effect as an important way to reduce excessive spending increases by local government.

16 Scotland has moved from two tier authorities based around larger regions in the 1970s to a single tier array of 32 unitary authorities, of vastly different sizes, and distinctly non-functional boundaries in the mid 1990s. We note that England under the new UK government intends to move over two years to single tier authorities (alongside more combined mayoral authorities).

However, this all meant subsequently that it was easier for the UK government to use grant in aid to enact austerity cuts on local government and for devolved governments like Scotland after 2010, to pass on Barnett consequentials form UK budget cuts to councils too. In both cases, local government struggles to escape the blame for these cuts.

Remarkably, introduced more than 30 years ago, this system remains largely unchanged (bar a Welsh revaluation in the 2000s which introduced two additional top rate bands, and Northern Ireland's continued exceptionalism with its proportionate property tax, confusingly called the 'Rates)', the preference for imposing council tax freezes from the centre, especially in Scotland, and the willingness to tinker with the weights on higher bands in Scotland after the 2015 local tax commission created a climate for some measure of reform). Wales also introduced two higher bands. While there have been commissions in England and Wales, official and non-official in status, and plenty of commentators writing about council tax reform, very little has changed. Below we concentrate on Scottish council reform discussions, focusing on: the Burt review in 2006, the initial SNP tartan tax plan, the council tax freeze and concordat, before looking at the 2015 commission on local tax reform and its aftermath. We also shed a little light on the contemporary position in Wales which remains of much interest.

After the second Scottish Parliament was elected in 2003, an inquiry into local taxation was established under the chairing of **Sir Peter Burt**. It reported in 2006 founded on a strong diagnostic analysis that stands the test of time. The Inquiry was very critical of council tax, the failure to revalue, also evidencing its regressivity in terms of tax bills as a share of income and came down strongly against multiple local domestic taxes. Instead, **it favoured abolition of council tax to be replaced by a tax on household properties based on a fixed percentage (locally varied) of regularly revalued capital value.** The then First Minister Jack McConnell rejected the reform out of hand, before it was even published, apparently on grounds of the anticipated unpopularity of such a proposal a year before a tight general election in Scotland.

Nonetheless, **the same proposal was developed and carried through in Northern Ireland afterwards, keeping the same name 'the Rates' but in effect a revalued capital value based tax set at a combined national and locally-set tax rate.** Politically this worked because the revaluation was undertaken at the beginning of a price bubble prior to the GFC and tax payers perceived that by the time the tax was introduced the valuation was already out of date and more acceptable. It also helped that for most of this period Northern Ireland was under direct rule from Westminster. Subsequently, there has been no further revaluation and the Northern Ireland government also introduced an absolute cap on household payments, attenuating the link to property values at the upper end of the price distribution (something criticised explicitly by Slack and Bird, 2015). Despite these criticisms, Northern Ireland remains proof, in a peculiarly challenging setting (bearing in mind the Community Charge was never countenanced for Northern Ireland), that a more traditional (proportional) capital value tax can work in a UK setting.

The SNP won a minority government in 2007 and acted to investigate the feasibility of their manifesto commitment to use the 3% incremental income tax available to them in the 1998 Scotland Act (the so-called tartan tax) as a Scotland-wide replacement for the council tax. Hitherto, the SNP had avowedly supported a local income tax. However, it quickly transpired that such a move would raise insufficient finds and was unpopular with local government. It was quickly dropped. Later in the same parliament the Scottish Government negotiated a concordat with local government which provided certain additional freedoms to end ring fencing in agreed areas e.g. supported housing, in return of a council tax freeze funded from the Scottish government budget. This then went on for nine years and was electorally very popular (and cumulatively very expensive).

After the 2014 referendum outcome and the appointment of a new first minister, the next programme for government announced an all-party commission on local taxation[17] focused on reforming/abolishing council tax and recommending whether to end the freeze. This was to report in time for the 2016 election wherein the parties would provide their commission-informed positions on these questions in their party manifestos. **The Commission ultimately recommended (majority position) the ending of the tax freeze and the replacement of council tax with a locally varied regularly revalued capital value tax (the key proposal of Burt) but with a local income tax supplement (a combined tax proposal also made by Gibb and Christie in their Policy Scotland submission to the Commission)**. In the manifestos, Labour, Lib Dems and the Greens also favoured abolition of the council tax with various forms of capital value tax to replace it. But the Conservatives and the SNP proposed much more modest adjustments, neither of which included a revaluation. With a minority government re-established the new SNP government decided to increase the weights on higher banded properties and provide some additional benefit support for low-income households in higher banded properties. It remains an odd situation that having set up a reform commission, the government chose to reject its findings with little more enthusiasm for reform than McConnell had shown in 2006 (perhaps for similar reasons?).

Nothing more happened till the Scottish Government in 2023 announced a consultation over further re-weighting to higher bands as in 2016 (see Gibb, 2023). Then at an SNP conference the then new first minster Humza Yousaf announced a new council tax freeze for 2024-25 without consultation with local government. While the re-weighting consultation was dropped the controversial freeze went ahead. It is worth noting that **Wales did undergo a revaluation of council tax in 2003 adding two new highest bands, and is presently reviewing more fundamental reform including a further revaluation to be implemented by 2028 and on a four-year cycle thereafter along with possible further re-bandings and review of discounts**

17 Co-chaired by the relevant minister and the chair of COSLA, all parties were represented except for the Scottish Conservatives.

and exemptions (passed in the Welsh Senedd, July 2024).

Key takeaways for contemporary discussion of tax reform:

- The recurring importance of the political context and electoral acceptability perceptions of decision-makers
- Evidence that capital value taxes can work
- Revaluation can be done successfully
- Government leadership and commitment as well as consensus building is essential
- We still have a largely unreformed council tax in Scotland and England.

4. Contemporary Housing Tax Reform Debates

Tax reform has a spectrum of possibilities that range from no change and modest reform of the existing system of council tax (e.g. general revaluation or adjustment to exemptions and discounts, etc.) through to more thorough-going embracing alternative local taxes such as a capital value tax, often described as a proportional property tax, or involving elements of land value tax. As we shall see one needs to look closely at these proposals and think through their design and implementation. It is also conceivable that tax reform might be combined e.g. reforming council tax and land building transactions tax. **Below we look at a selection of three related recent proposals in more detail: John Muellbauer's 2023 proposal for a green land value tax to replace council tax, Tim Leunig's (2024) hybrid tax proposal; and, the notion of a proportional property tax, as led by Fairer Share and by IPPR, among others. In turns this leads us back to the identification of critical trade-offs that any reform proposition needs to identify and address.**

4.1 Contemporary Reform Options

Split Rate Green Land Value Tax Proposal

The paper by John Muellbauer (2023) builds on earlier work on property tax alternatives. It is written through the lens that rising land prices are important drivers of the housing market. Muellbauer has multiple objectives which are about shifting property tax from transactions taxes to recurring taxes on land, providing incentives to support the shift to net zero and to make this distributionally acceptable through both a transitional reform and a comprehensive deferral scheme to resolve the cash poor asset rich problem. He argues that well-constructed land taxes can support economic efficiency and wider productivity. They can help regional housing markets and economies, and that market value-based taxes (i.e. with regular general revaluation) support financial, macro and regional economic stability, incentivising housing supply both through the inescapability of land value tax and by de-speculating markets and reducing the amplitudes of cyclical volatility. A further central feature of his proposal is to provide tax discounts for energy efficient homes, in the long-term bringing down societal energy costs.

Muellbauer's tax proposal in summary would look like the following. The proposal is for a split rate tax , along the lines of the Mirrlees' (2011) review which argues for an efficient land value tax which are good for paying for economic and social infrastructure (given that they increase local property values through land value uplift) but additionally adds a tax on the building or structure itself as a form of consumption which should be taxed in an efficient system and presumably could in principle allow non-owners of property to contribute to funding local public services (though this is not his intention; rather he seeks to tax owners of property only). The tax element on buildings would receive the green discount element for energy efficient buildings, and Muellbauer proposes a zero rate for carbon neutral buildings (p.10). He also proposes a tax allowance on the land value element (m2 not parcels) for the first X% of land value. Note, however, that Muellbauer assumes elsewhere (p.12) that property taxes are passed on by landlords to tenants in the form of higher rents but because the LVT on apartments is comparatively lighter, they should still benefit from the tax change.

Muellbauer argues (p.12) that a proportional property tax, and especially one with higher rates on land, is necessarily progressive for household disposable income [taking account of imputed income going to owner occupiers] and can be made even more progressive through tax allowances'.

A key argument is Muellbauer's deferral proposal. He points out that countries such as 24 individual US states (who operate means-tested deferral schemes for the retired) (p.8), Canada, Denmark and Ireland operate tax deferral schemes that address the cash poor asset rich or liquidity problem households can face, which has the added benefit of reducing the need for other less efficient mechanisms such as delaying revaluations or relying on a wide class of tax exempt groups. Muellbauer recognises that many of the systems in place around the world do not work well and have low take up. He therefore proposes a simple and broader based scheme eligible for all households headed by a person who is of retirement age. If they choose to defer the tax, the taxing body registers a proportionate or equity share interest equal to the unpaid tax each year and this would be settled only when the property is transferred or sold on, and this could be incentivised with discounts for cash payments. Clearly, government will be able to take out low cost secured lending backed by these equity share should there be temporary shortfalls in revenue.

Muellbauer proposes a split rate tax on land and buildings with a green discount attached to the latter. How does land value taxes (LVT) and land structure property taxes compare against his criteria? Muellbauer (pp.20-21) refers to a paper by Cheshire and Hilbert (2021) which makes this comparison. They argue that an LVT is more difficult to value and administer than a property tax, but the LVT is better on efficiency and economic stabilisation grounds. They also favour LVT on distributional grounds because land is more unequal than property. They do however concede that a property tax is better on revenue-raising, ease of transition, public acceptability and on grounds of simplicity. Muellbauer contends that his split rate tax encompassing the building element captures some of these benefits and is therefore superior to a pure LVT but acknowledges that it is more complex to a have a dual or split tax.

Going back to the poll tax, we know that effective transition to new tax arrangements is important. Even with an automatic valuation system, a public education programme and the deferral scheme, there still needs to be phasing-in of the new tax. Muellbauer proposes a three year phase in of 2/3 old tax, 1/3 new tax; 2/3 new and 1/3 old in year two and in year three only the new tax. Bearing in mind the longer transition periods of the original plans for the community charge (10 years) and for the English social sector rent reform in the 2000s (12 plus years) wherein the latter damped possible maximum rent increases during the transition – three years might be incautious, though this will be an empirical problem regarding the gap between respective tax bills and their distribution, as well as a political acceptability question.

Key takeaways:

Transition to net zero through incentivised property taxes are key.

Stresses the resource allocation, stabilisation, productivity-enhancing and regional economic impacts, as well as the benefits of moving away from transactions taxes and widening the tax base towards recurring annual property taxes (and a degree of localising business property taxes).

The tax would have a relatively complex split structure between land and structures elements. The tax would be liable to all owners of domestic property, owner-occupier or landlord.

There is a focus on liquidity issues around deferral systems, transitioning over three years to the new tax, and making the case for greater emphasis on taxing land.

The author sees the tax as close to the proportional property tax discussed below. There are also several points of agreement with Slack and Bird (2015) on what makes a good tax and the ways in which this proposal meets several of the criteria set out in Table 4 above.

Proportional Property Tax

Organised around the fairer share campaign and previously advocated by bodies like IPPR , the proportional property tax (PPT) has become a coherent alternative to the status quo. It seeks to combine revenue from Council Tax and Stamp Duty Land Tax (or LBTT in Scotland) with a common percentage on regularly revalued capital values of properties paid by their owners. Here we look at the case they make for the tax, how it will work in detail and we also assess important trade-offs against the tax criteria we discussed earlier in section 3.2. Note that what follows is based on English data and English local government and housing markets only.

Nanda (2021) and the Fairer Share Manifesto (2021) provide the basis for characterising the PPT proposal. Nanda reaffirms that in a context of large increases in housing wealth especially in southern Britain that disproportionately benefit older generations and the already wealthy, the council tax is out of data and unfair, generating regional unequal outcomes, for example, property owners of high value properties in the south east of England can pay the same council tax bill as those in the lower property value north of England. Nanda reiterates the inefficiency of stamp duty for housing market mobility and efficient turnover.

In addition, the Fairer Share Manifesto notes (2021, p.5) that: 'Council Tax places the heaviest burden on the young, low-earners and those living in less prosperous parts of the country, who typically live in modest properties, while benefiting wealthy homeowners and those fortunate enough to own multiple properties. Property values have skyrocketed for the asset rich and Council Tax bills have increased but average incomes have stalled'. Fairer Shares estimates (p.10) that the effective CT property tax rate is 0.2% in the south east but 0.7% in the north east. They also stress the unfairness of non-revaluation and the structure of banding that means that those on low bands pay proportionately more of their property capital value in tax than those on the highest bands. Younger and lower income adults are concentred in lower bands, so they pay higher effective tax rates. They also, like Nanda, stress the inefficiencies of stamp duty – reducing housing mobility also means not moving to jobs and lost economic opportunity for individuals and society. They also connect the consequences of unreformed property taxation to the housing crisis in the sense of supporting housing wealth and price inflation assisting the plateauing and reduction of home ownership especially for new, younger cohorts, adding to pressures in the PRS and reducing incentives to downsize and thereby better match homes to households.

Nanda set out what property tax reform would seek to achieve. **It should help to address cumulative housing wealth inequality. It should address regional inequality. It should support fiscal devolution, increasing the share of local government control over finances in a partnership with central government and making more decisions locally** where information on context is strongest. **There is also an economic case that should be addressed: better use of the existing stock, reaping agglomeration economies through supporting new supply in higher demand areas and increase productivity by supporting infrastructure across lower value regions.** A reformed property tax should also mitigate regressivity with respect to regions but also to the extent that council tax design is to an extent regressive with respect to incomes. Stamp duty abolition should also increase mobility (Nanda, p.15, quotes Hilber & Lyytikäinen (2017) who model increasing SDLT by 2% overall which generates a reduction in household mobility of a little less than 40%). Property tax reform should also support housing affordability, noting that moving to a PPT should reduce effective tax rates in the north while increasing them in the south, but noting that these will be capitalised in to house prices so that first time buyers in the south will face lower prices as a result (p.15)[18].

The Fairer Share Manifesto suggests (p.11) five principles and eight key reforms to introduce the PPT. The principles are (to paraphrase):

- 1. Taxation should be based on actual housing wealth and the burden should be borne proportionately on housing wealth.
- 2. The PPT should be simple to understand, hard to avoid and easy to administer.

18 Nanda quotes Hilber 2015 whose review of house price capitalisation studies finds that most tax changes are largely if not wholly fully capitalised into house prices ie a change in the form of a property tax increase reduces house prices. (2021, p.19). This is also the logic that suggests the abolition of domestic rates replaced by s poll tax will put upward pressure on house prices (depending on income and substitution effects).

- 3. The PPT should be redistributive like income tax, with wealthier regions supporting other parts of the country paying for public services (a form of resource equalisation).
- 4. The PPT should be related to a household's ability to pay.
- 5. The PPT should encourage the more efficient use of land, buildings, towns and cities.

The eight key reforms which provide much more detail on the design principles of the PPT, involve:

- 1. **The Council Tax band system should be replaced with a simple Proportional Property Tax, charged as a fixed flat percentage of property value.** They recommend a (revenue-neutral) flat rate of 0.48%, with a higher rate of 0.96% for second, empty and non-resident owned homes.
- 2. **Stamp Duty Land Tax (SDLT) on owner occupied property should be abolished.** SDLT should nonetheless remain in place for second home and non-resident buyers.
- 3. **At the point of transition to PPT, any increase in local property tax would be capped at £100 a month for primary residences**. The transitional protection would disappear at point of sale - buyers would then benefit from the removal of Stamp Duty.
- 4. **Property tax should be collected not from tenants, but directly from owners, who are in a better position to pay.** This would bring England into line with international practice and reduce administration for councils).
- 5. **A deferral mechanism should be introduced for those owners genuinely unable to pay.** Tax and a modest interest charge could be paid at a later date or, if need be, upon sale of the home, thereby avoiding the debt issues that have plagued the collection of Council Tax.
- 6. **Property taxation should be made simpler and fairer by abolishing the majority of reliefs and exemptions, including those for single occupants, second homes and empty homes.**[19] These reliefs complicate the system and have unintended negative consequences.
- 7. **A revaluation of all residential property must take place as soon as possible, with annual revaluations thereafter.** Improvements in technology make this much more feasible than in the past. Properties should be taxed on their average value across the last three years, to ensure that increases in property value are subject to taxation.
- 8. **Property tax should apply to undeveloped plots of land that have received planning permission from the local council.** This would discourage developers who purchase land and refrain from building while they wait for the value of the plot to increase.

Fairer Share argue that a move to a PPT in England would generate the following benefits (among others):

- 18 million households pay less tax i.e. 75% of households would be better off
- [All] 8.7 million tenants would no longer be liable with the 'obligation' passed to their landlord.
- Each year all purchasers would no longer pay SDLT (estimated at 750,000 buyers), increasing housing market activity by more than £3 billion per year.
- 1.4 million second, empty and undeveloped properties (with planning permission) would be brought into the taxation system.

Fairer Share argue that the tax revenue from the PPT should be split between local government and central government reflecting the original sources of the two elements PPT is now paying for. They would like to see some of the central resources being redistributed locally (and of course central government is still providing the lion's share of revenue for local government). The assumption regarding the local component of PPT is that local voters should be able to hold local government accountable for local spend and tax decisions – this implies that the local element of the tax rate is indeed variable and so while revenue neutral for the country as a whole, there is scope for local authorities to vary the local element of PPT rates: '*Councils are given power to flex the rate of PPT that gives them their PPT allocation. Councillors could make decisions to increase or decrease the rate on their PPT allocation, much like councillors can make decisions to vary Council Tax now*' (p.14).

Critically Fairer Share recognises that shifting the property tax base to current capital values relative to 1991 council tax values redistributes the tax base across the country and does so in favour of the wealthier south east of England. This requires resource equalisation either from (or a combination of) redistribution of central government grants to offset the changing tax base or pooling and redistributing PPT revenue from tax base rich councils. As they say this is a long-standing principle of central-local government finances throughout the UK but is a major restructuring of the current system (which is still based on the community charge grant and tax funding model). It would also be supported by localising non-domestic rates across the country.

Fairer Share also considers the 25% who are expected to face higher bills and made need mitigation (noting that none of these, formally, will be renters). Mitigation would involve:

- £100 cap on increases until first move (when the benefit of SDLT abolition kicks in).
- The use of their version of a deferral mechanism until point of next sale of the property
- Other options include: allowing councils the discretionary power to design their own mechanisms to help low income residents through the way PPT operates (clearly with limits set by their principles set out above but perhaps similar to current local rebate systems under council tax); this could also include greater use of discretionary housing payments for those struggling to pay PPT; they also **suggest offering generous discounts to social**

19 The Manifesto also argues that the spare room subsidy or bedroom tax ought to be abolished at the same time.

landlords for operating at high levels of energy efficiency.[20]

Looking at the design in more detail and comparing back to our criteria and the Muellbauer proposal, leads to a number of key trade-offs, decisions and issues that remain to be considered.

First, the tax is on owners only and unlike Muellbauer, the Manifesto is silent on issues of economic incidence and passing on of PPT in whole or in part through higher rents. Nanda (2021, p.29) argues that the evidence elsewhere citing support from Mirrlees, et al, 2011, Tax by Design) suggests that most of the economic incidence will remain with owners of property. This is a rather heroic assumption and one sensitive to the precise design of the tax, the competitiveness of rental housing markets and landlord behaviour. At best we need more rigorous empirical work on this specific critical question.

Second, recognising the issues of resource equalisation but also local democratic accountability, the Fairer Shares Manifesto favours local tax setting for the local element of PPT, whereas Nanda is more nuanced on this question. A question does remain and is likely to arise in debates about the introduction of PPT – concerning the non-tax-liability of tenants and their right to vote in local elections that set local tax rates (actually a very old argument). These are treacherous waters and one immediate response, apart from broader principles of democracy and rights, would be note that most local government revenues come from the national tax payers, and tenants are still part of that constituency though income tax, NICs and VAT.

Third, the focus on owners changes the liquidity and cash poor dimension of the support offered for low-income taxpayers, reducing the need for a national rebate system (which remains in place in Scotland) but requires a number of mitigations led by the deferral scheme. This proposed deferral scheme does not have the detail of targeting associated with Muellbauer's proposal (or his greater analysis of challenges regarding interest costs and the like). But clearly there is scope to develop something solid out of these two approaches.

Fourth, the PPT transition scheme is based around capping increases in bills until first move in the housing market (again made more plausible because of the focus on owners only) – as opposed to Muellbauer's three-year transition phasing. Again, there is no reason why both systems might not apply at the same time. It remains important to cost the effect of transitional schemes form a local government revenue point of view especially as the housing market and tax base evolves dynamically over time (although this will itself be a temporary issue for revenue).

Fifth, **taxing undeveloped land with planning permission through the PPT is an interesting incentive to promote new supply** and provide the same sorts of benefits commonly attributed to Land Value Tax. Again, this is an area where the incentive is probably more important that the direct revenue take associated with it, even though the numbers are potentially large, at least initially. **Clearly, by bringing new supply forward through the acceleration of completions will generate a larger PPT tax base.** Given the new UK Government's ambitious plans with housebuilding, this also has important tax base consequences for local government.

Sixth, while there is considerable discussion of the capitalisation effects of property tax changes and their impact on house prices there is less consideration empirically of the effects the abolition of SDLT on house prices i.e. pushing up prices where the impact is largest and offsetting some of the gains of replacing Council Tax with the PPT. This is another area where further modelling is required.

Leunig's (2024) Fairer Property Tax Proposal

The most recent contribution to the debate on property tax reform, with echoes of the PPT (but with significant differences), comes from Tim Leunig writing for the Onward think tank (Leunig, 2024). Leunig wants to abolish the stamp duty land tax and spreads the required tax revenue more broadly, while also replacing council tax. He proposes a two-part or 'horizontal' split tax with an annual national tax to replace SDLT (levied on owner-occupied homes only) above a minimum of £500,000 set at 0.54%, with a supplement of 0.278% for properties worth more than £1 million (thus achieving revenue neutrality with SDLT). The payment would rise annually linked to inflation. At the same time, the council tax replacement would be levied on properties valued at under £500,000 operating with a minimum annual payment for all of £800 – rates would be set locally by councils with a 0.54% rate offering revenue neutrality. The local tax would only apply to property owners not residents. Initially, a form of algorithmic modelling would values properties based on sales price data individual records, thereafter uprated by the ONS house price index; properties over £500,000 have the same tax rate equally applied so there is no need to revalue them, according to Leunig.

Leunig argues for this horizontal split because it keeps the more volatile tax source (SDLT) with national government which has better capacity to handle uncertain buoyancy. Leunig recognises that actual tax bills will divert from the revenue neutral assumption because of spending needs and the vagaries of the performance of the housing market nationally and locally. It will also be critical how government chooses to help cash poor households mitigate their property tax costs. One of the interesting features of the thesis developed in this paper is the author's concern with the unfairness of regional variations in tax bills and wishing to reduce this, and at the same time reduce the demands on valuation by the practice of the £800 minimum charge (which is the equivalent of all properties worth less than £180,000) and the cap at £500,000. The author argues that looking at the distribution of local authorities before and after the proposed reforms, only 36 councils would have a rise or fall of more than 25% of revenue and that his might be more readily accommodated, presumably through forms of resource equalisation via central government. Leunig is bullish about the feasibility of these reforms, especially regarding the council tax.

20 One wonders whether this might also be extended to private landlords to incentivize investment in energy efficiency where it is arguably more needed?

4.2 Conclusions

In the last chapter we found that the historical picture, international evidence and the different practices found in the UK – all suggest that **property tax reform is possible, it has economic and fairness benefits as well as tilting us more towards a well-functioning housing system. It also builds on wider arguments from OECD and elsewhere about restructuring a widening of the tax base focused more on land and property wealth.** It also suggested that well thought through and communicated reform policy design can be publicly palatable and politically acceptable. In this chapter we see that contemporary proposals reflect green incentivising agendas as well as seeking to overcome the now familiar problems with both council tax and transactions taxes, through split tax proportional property taxes. These proposals are well advanced in providing a solid basis for reform provided the trade-offs and challenges set out at various points in this chapter can be addressed.

We come back to these points in the conclusion but before that in the next chapter we return to Scotland and use a unique modelling approach to the valuation of the Scottish property tax base to assess empirically key aspects of the reform agenda, questions that have been our focus such as revaluing the council tax base, introducing a land value tax and also make brief reference to an estimated proportional property tax (not in this case including LBTT).

All of the authors considered recognise that revaluation, let along the tax change proposed may cause capitalisation effects on house prices i.e. higher tax bills post change or revaluation reduce prices and vice versa for lower tax bills. It also suggests that where supply is not elastic and responsive to price changes, relative tax cuts may indeed lead to higher prices and if it is a tax on owners specifically this will be passed on to a greater extent if inelastic supply pertains to that market, to tenants. This follows recent evidence assembled by IFS, Hilber and by others (Hilber and Vermeulen,2016; Koster and Pinchbeck, 2022, Adam, et al, 2025). We note however that these are quite complex conceptual and empirical problems to allow us to reach definitive conclusions on precise price and rent effects but this is an important distortion and should feature in any evaluative assessment prior to any major tax reforms.

5. Modelling Aspects of Property Tax Reform in Scotland

5.1 Introduction

This chapter explains the process by which alternative Scottish property tax reform scenarios can be examined using a quantitative (modelling) methodology. The overarching purpose of the modelling is to create a database that is representative of Scotland's residential dwelling stock in its entirety, and to populate that database with up-to-date market values. The mid-point of 2023 (i.e. end of June) is chosen as the valuation date for the purpose of this exercise.

The chapter first sets out the distribution of council tax subjects within Scotland and summarises the current council tax band limits and associated tax liabilities. It then moves to explain the data sources used to build the revalued dwelling stock database and provides a summary of the econometric results obtained from the modelling exercise itself. Finally, the chapter reports the results of a simulation designed to predict the principal distributional impacts of reforming the council tax. It begins by calculating the market value band limits for each council tax band under the current system that would effectively deliver a Scotland-wide revenue neutral revalued council tax base. The simulation is also used to calculate the required tax rate of a flat rate national (proportional) property tax that would be revenue neutral for Scotland overall (but note this does not include revenue for LBTT) and conducts a simulation for a land value tax proposal. In each of these scenarios, there are distributional impacts, which are summarised later in the chapter.

This chapter demonstrates that the analytical and data foundations for a more automatic form of valuation and regular general revaluation, and indeed the principles to develop a land value tax base (at least of domestic properties), are perfectly feasible. The results also provide implications for assessing the property tax reform choices and trade-offs to be confronted.

5.2 Methodology

In an ideal world, options for reforming the council tax would be informed by a dataset comprising the market value of all residential dwellings matched to the incomes and socio-economic characteristics of those individuals and their households occupying those dwellings. Such a dataset would allow the interrogation of practically any combination of property and/or income tax reform scenarios.

Unfortunately, no such database exists. Instead, this project has developed a dataset designed to closely match Scotland's residential dwelling stock and has implemented several modelling steps designed to predict the market value of each dwelling. This approach permits council tax and property tax reform scenarios to be examined and, as mentioned in the introduction, this includes a land value tax (LVT) scenario. For the sake of brevity and to side-step the need to repeatedly describe the final dataset, we refer to it as SCOTPMOD hereafter (Scottish property tax model).

SCOTPMOD is developed from two principal datasets which are:

- 1. Zoopla listings data, for all of Scotland and covering the period 2018-2023
- 2. Energy Saving Trust Home Analytics data (EST)

Each of the datasets contains a great deal of information on the characteristics of residential dwellings at the unit level (i.e. each record in these datasets describes a dwelling at a particular address). The econometric modelling which follows on from the assembly of these datasets is designed to produce results that can be generalised to the point that it yields the current market value of any dwelling (using a so-called 'hedonic' model). The hedonic model disaggregates dwelling transaction prices, asking prices or rents to 'attribute' prices, such as price per bedroom, price differences for each property type, locational premia, and so on. A good hedonic model can therefore be used to predict the price of any dwelling given information on its location and other characteristics.

The Zoopla listing data includes information on listing price, and contains numerous variables describing the location, size, type, age and so on, of every dwelling in the dataset. The Zoopla data were supplied under license by the Urban Big Data Centre, University of Glasgow, for the purpose of this project.

It is important to note that the Zoopla data includes listing price rather than transaction price. This is a limitation because there is no guarantee that transaction prices will be the same as listing prices in all cases. In practical terms, they are likely to be close enough to mean that any bias introduced to the modelling process will be minimal. A second limitation of the dataset is a more serious problem. The listings data contain postal addresses but are not geocoded and cannot be matched directly with a unique dwelling identifier available in other data sources. In an ideal situation it would be possible to match each record in the Zoopla datafile with Ordnance Survey open UPRN data, for example. We explain how this problem is overcome a little later in the chapter.

Zoopla data were processed to remove duplicates and to allow a merge with the Scottish postal address file (2023, February version). This operation permitted the transactions to be geocoded, and for Council and Datazone boundaries to be added to the data. There were 231,101 transactions available for hedonic modelling after these data operations.

The second data source referred to earlier is the EST Home Analytics dataset, which is freely downloadable. It contains a wide array of variables that are of interest for the purpose of modelling energy efficiency. However, given that property type, bedrooms, public rooms, floor area and locational variables are also included, it is possible to merge the data with hedonic coefficients and, subsequently, predict property value. There are 1,493,155 records after cleaning (mainly consisting of removing cases with missing values). Given that there are approximately 2.67M dwellings in Scotland, the EST dataset represents a better than 50% sample, but it is important to acknowledge that there is still scope for sample selection bias.

To summarise, Zoopla data contain the information on listing prices necessary to build the hedonic model which forms an important part of SCOTPMOD, but the dataset only covers the years 2018 through 2023, and there are 231,101 observations to be used in the analysis. The EST dataset is much larger (1,493,155 observations) but does not contain any information on dwelling price or value. The analysis therefore follows the following high-level steps:

- Zoopla data are used to estimate the hedonic (econometric) model;
- The model results are used to populate the much larger EST dataset with predicted market prices/values;
- A process is followed to ensure that the EST dataset can be scaled up from 1,493,155 observations to represent the 2.67 million residential dwellings that are subject to the council tax.

5.3 Estimation of the hedonic model

The hedonic model is central to the ability of SCOTPMOD to simulate property tax reform impacts. It has been used for this purpose before – notably by Leishman et al (2014) – a final report on a previous Joseph Rowntree Foundation project, and by Hincks and Leishman (2021) who examined council tax revaluation and reform in Wales.

The hedonic model is applied in an innovative way, by following a two-step process set out by Leishman (2009) and subsequently used by Hincks and Leishman (2021) to simulate a council tax revaluation (and various other scenarios) in Wales. The process begins with a simple model (an ordinary least squares or OLS hedonic model). The OLS model is simply used to identify outliers, but the coefficients and model performance are summarised in the technical appendix (table A1). After coding a series of local authority specific intercepts, the model performance is reasonably good with an adjusted R square of 0.66.

The OLS estimation is used to identify outliers, defined as observations generating an absolute residual greater than 2.32 (i.e. 1% of cases assuming the data are normally distributed). This procedure is followed because including errors arising from variable mismeasurement, coding errors or typographical errors can introduce bias to the model. It is a reasonable supposition that a small number of observations that create very large prediction errors contain erroneous variables or suffer from the omission of important determinants of market value.

The second step is to estimate a more refined model known as the hedonic multi-level model (see Leishman, 2009, if more detail is required). In brief, it allows parameters to vary spatially. For example, the model can include a Scotland-wide attribute price for a feature such as a detached house, but it can also include a local authority specific and even a datazone-specific price for this attribute. This more flexible specification allows us to include time series 'random effects' defined at the level of the local authority, the level of property type, and the level of the Datazone. This specification assumes that:

- There are annual and quarterly time trends, but these vary between local authority area;
- There is a different intercept or 'premium' for each combination of local authority and datazone;
- There is a different intercept or premium for every defined property type.

The estimation results are shown in technical appendix (tables A2 and A3). For more technical readers with an interest in the methodology, please note that the results are interpreted as two separate parts. Table A2 shows the Scotland level coefficients or attribute prices. Table A3 provides a summary of the variation in attribute prices at the 'levels' defined above (so-called 'random effects'). The random effects cannot be read directly from the results but can be predicted as a post-estimation procedure. The results in A3 summarise the variance within the estimated random effects.

As a final check, a new OLS hedonic model can be estimated using the original set of predictors, but this time augmented by the newly created variables (random effects). This is done as a demonstration and to allow comparison with the first version of the model. The results are shown in technical appendix table A4. The adjusted R square of this demonstration model is 0.8975 (compared to 0.6622 for the original model) and the RMSE is 0.21778 (compared to 0.39697 for the first model). This is clearly a high level of predictive power and shows that the model is suitable for matching to EST data and subsequent property value prediction. In other words, the final model was subject to rigorous testing which gave us a high level of satisfaction that the model generates sufficiently reliable property values for the purposes of this study.

5.4 SCOTPMOD

As discussed in the introduction, SCOTPMOD is assembled by merging the hedonic model coefficients, as summarised in Table 8, with the EST dataset. By multiplying out the EST variables by the coefficients exported from the modelling process, a predicted market value can be generated for every dwelling in the EST dataset. However, as noted earlier, EST contains just under 1.5M records, while there are circa. 2.67M residential dwellings in Scotland at the June 2023 valuation date. If the 1.5M EST records were an entirely random selection from the 2.67M residential dwellings in Scotland, then we could simply re-scale the EST dataset. It is more likely that the probability of a dwelling being contained with EST is related in some way to its size and location, the logic being that smaller dwellings transact more frequently than larger ones. In addition, some household types (such as younger families or recent graduates) are likely to move home more frequently than older, more established household types. Thus, the type of dwelling typically occupied by such households will trade more frequently. There are almost certainly many more socio-economic factors and processes at play which mean that the 1.5M EST records are not a perfect proxy for the 2.67M dwellings in Scotland's residential dwelling stock.

To control for this problem, the distribution of dwellings by size and council location was examined and compared to the pattern that can be observed in the EST data. The 2011 census was used for this purpose because the small area level results from the 2023 census were not available at the time of the research. Table 9 shows the 2021 pattern.

Table 9 Distribution of properties by number of rooms and Council (Census 2011)

	All households	One room	Two or three rooms	Four or five rooms	Six or more rooms
Aberdeen City	103371	669	26395	52239	24068
Aberdeenshire	104714	265	11171	44050	49228
Angus	51616	212	8084	25109	18211
Argyll & Bute	40125	211	5521	19795	14598
Clackmannanshire	22734	158	3250	12450	6876
Dumfries & Galloway	67980	213	7518	34666	25583
Dundee City	69193	536	16347	38229	14081
East Ayrshire	53919	243	6672	32530	14474
East Dunbartonshire	43473	160	4439	19803	19071
East Lothian	42905	189	6002	22823	13891
East Renfrewshire	37225	134	4018	16331	16742
Edinburgh, City of	223051	1676	52552	115532	53291
Eilean Siar	12576	37	1065	5470	6004
Falkirk	68732	256	8191	40283	20002
Fife	160952	640	19968	90188	50156
Glasgow City	285693	4244	82180	162818	36451
Highland	102091	528	10922	49534	41107
Inverclyde	37434	342	7069	22106	7917
Midlothian	34978	128	3527	20964	10359
Moray	40062	105	4361	19268	16328
North Ayrshire	62498	304	9071	36129	16994
North Lanarkshire	145998	905	20457	90607	34029
Orkney Islands	9725	38	1182	3975	4530
Perth & Kinross	64777	265	9127	30342	25043
Renfrewshire	80902	638	15998	44636	19630
Scottish Borders	52498	171	7421	25548	19358
Shetland Islands	9950	50	1077	4367	4456
South Ayrshire	51286	214	7144	26240	17688
South Lanarkshire	139188	716	20098	77626	40748
Stirling	37566	159	4704	18195	14508
West Dunbartonshire	42167	341	8110	26274	7442
West Lothian	73398	314	8716	42148	22220

On a council-by-council basis, the proportion of residential dwellings in each size band (1, 2-3, 4-5, 6+) in the EST dataset was compared to the Census 2011 proportions. This allowed the creation of sampling weights that simultaneously ensure the correct SCOTPMOD distribution by room size band, and that the scaled number of dwellings in SCOTPMOD sum to 2.67M.

5.5 Estimation of the construction cost model

To explore the potential for a land value tax (LVT) hereafter, a simple model of housing construction costs was estimated using data supplied on license by Emap-Glenigan. The coefficients of the model are summarised in Table 10.

Table 10 Construction cost model results

Variable	Unstandardized Coefficients	T statistic	Sig.
Constant	0.31619364	20.612	***
UNITS	0.03968026	88.681	***
units2	-0.00013054	-51.637	***
Pre 2016	-0.52230554	-21.059	***
Year_2016	-0.36970390	-14.177	***
Year_2017	-0.39636523	-15.016	***
Year_2018	-0.41337147	-15.955	***
Year_2019	-0.38545914	-15.457	***
Year_2020	-0.31739073	-11.667	***
Year_2021	-0.18879280	-7.064	***
Year_2022	-0.02340282	-0.861	
Population density	0.00001481	3.426	***
Population density sq.	0.00000000	-3.028	***
No. flats	-0.00609392	-7.874	***
No. flats sq.	0.00003788	6.336	***
Adjusted R Square	0.783		
F statistic	1660.222	***	
N	6442		

The dataset used to estimate the model is a subset of the Emap-Glenigan dataset. The data are extracted from planning application records and include several useful variables including the estimated value of the construction contract (i.e. construction costs), the type, size and location of development. There are flags indicating whether each application includes houses, apartments, commercial space, funding type and tenure. The data are also geocoded which, in turn, permits the records to be matched with variables external to the dataset. In this case, population density and squared population density have been added, and these proxy for some of the spatial conditions that affect construction costs - notably urban density and rural remoteness. Prior to estimating the model, the estimated total construction costs are re-based using a construction cost index and converted to natural logarithms to linearise the data.

The results show that construction costs increase with development size, unsurprisingly, but that costs rise at a decreasing rate. In other words, there are economies of scale at work. There are separate coefficients for housing and apartment developments. In fact, the coefficients suggest that there are diseconomies of scale for apartment developments. Overall, larger developments have greater efficiencies, but these efficiencies drop away quickly for larger apartment developments. The population density variables are also significant, and the coefficients suggest that construction costs are higher in more densely populated urban areas, but that the rate of increase falls as density rises.

Overall, the model performs well empirically, despite its simplicity. The adjusted R square suggests that the model explains 78% of variation in construction costs between projects, which is a fairly high explanatory power.

5.6 Simulation results

Table 11 summarises the SCOTPMOD output, both with and without sampling weights. The median value is predicted to be £156,000 without weighting, or £199,000 with the use of sampling weights. This compares to £189,000 (average) reported by the ONS or £184,000 geometric mean reported by Scottish Government in the Scottish Housing Market Review. But, the SCOTPMOD mean is much higher than other sources at £241,000. This clearly warrants further investigation, but it probably reflects the fact that estimates of both average and median prices based on transaction data suffer from the sample selection bias issues discussed above (larger, higher value properties transact less frequently than other property types or price niches).

Table 11 The predicted value distribution in SCOTPMOD

Predicted value	Mean	P5	P25	P50	P75	P95
Unweighted	195,000	77,000	106,000	156,000	239.000	450,000
Weighted	241,000	83,000	126,000	199,000	316.000	545,000

The 2022/23 total council tax take in Scotland was approximately £2,873M. SCOTPMOD places the total value of the residential dwelling stock at £621.64Bn, which implies a that a flat rate national property tax would be revenue neutral at 0.462% of total property value.

SCOTPMOD can be used to assess the upper valuation limits on revalued council tax bands that would give a revenue neutral outcome. Table 12 shows the 1991 band limits and shows the proportion of dwellings in each band for Scotland overall. By running a query to find the same proportions as shown in the bottom row of Table 12, the revised band limits for a revalued council tax base can be found, and these figures are summarised in Table 13.

Table 12 Current (2023) distribution of dwellings by council tax band

Valuation band ranges (1991 values)	Under £27k	£27k to <£35k	£35k to <£45k	£45k to <£58k	£58k to <£80k	£80k to <£106k	£106k to <£212k	Over £212k
Proportion in band	19.25%	22.44%	16.26%	13.95%	13.88%	8.32%	5.35%	0.55%

Table 13 Council tax band upper limits that deliver the same number of dwellings in each band A=H as the current system (2023 count)

Band	Upper limit
A	118,426
B	175,036
C	225,725
D	288,434
E	396,221
F	512,811
G	800,672
H	N/A

As Table 13 clearly shows, the uplift in property values since 1991 has been very significant. Yet, when the implied growth rates are calculated the position is less dramatic. Band A properties (in 1991 terms) grew in value by an average 4.7% per annum of the 32 years of the study period while the value of properties in bands B through F grew by approximately 5.1% per annum over the period. The highest value properties in bands G and H saw their values grow by approximately 4.2%. Of course, the more important story is a spatial one in the sense that different parts of the country have seen quite different cumulative changes in property value over the 32 year period. This is perhaps best summarised in Tables 14 and 15 which show the distributional impact on Council Tax revaluation.

Table 14 Predicted number of Council Tax subjects by band, following revaluation[21]

	A	B	C	D	E	F	G	H
City of Edinburgh	14576	25263	85271	28552	36766	25092	24545	3771
East Lothian	2547	5105	7911	8904	10962	7758	6663	1031
Midlothian	224	2722	11938	5142	11761	5556	5335	273
West Lothian	6976	15014	19496	14280	15473	9328	1551	53
Fife	27754	44200	31408	30992	30986	8362	1797	0
Scottish Borders	276	5460	5160	11649	13220	7610	12610	1862
North Lanarkshire	47288	40950	30420	22325	13152	1878	116	0
South Lanarkshire	33920	44702	14407	24707	26046	8538	1566	0

21 We have selected eight local authorities for illustrative purposes that broadly match the Edinburgh City region and Lanarkshire, the areas we focused on in our sister AHSP analysis

Table 15 Predicted gross revenue ignoring benefit, concessions, 2nd home surcharge under the current, revalued and flat rate property tax scenarios (GBP millions).

Council	Revenue under current banding and weighting	Revenue under revalued CT with same weights	Flat rate (Proportional) property tax
City of Edinburgh	404.38	405.50	332.94
East Lothian	84.29	92.15	79.59
Midlothian	70.01	81.22	64.16
West Lothian	113.11	62.77	97.45
Fife	240.06	234.94	178.87
Scottish Borders	80.58	114.40	104.12
North Lanarkshire	190.30	193.57	125.64
South Lanarkshire	202.39	212.24	147.69

The second column of Table 15 shows the Council Tax revenue for each of the council areas chosen for this study under the current Council Tax arrangements. This acts as a comparator for the third column which shows the predicted gross revenue under a revalued Council Tax as predicted by SCOTPMOD. The picture that emerges is one of relative stability for the City of Edinburgh and North Lanarkshire, but a significant increase in total property value for East Lothian, Midlothian and Scottish Borders. The increase in value in South Lanarkshire compared to North Lanarkshire is modest by comparison. However, relative to the rest of the Lothians, West Lothian has seen a sizeable reduction in its share of Scotland's total Council Tax base. In other words, property values have risen more slowly there than elsewhere in the study area, and most residents would like to see a significant downward shift in Council Tax liability following a revaluation.

The final column of table 15 shows the predicted total tax take in the event that the Council Tax were abolished in its entirety and replaced by a national (Scottish) proportional property tax – a first approximation to a proportional property tax (with respect to Council Tax only, and not including LBTT). This is, of course, a revenue neutral simplification because there are alternative arrangements that would allow local variation, much in the same way as the Council Tax was originally intended.

The analysis assumes a single or nationally-set tax rate. The distributional impacts predicted by SCOTPMOD are much more pronounced than a simple reform of the Council Tax and this, in turn, suggests that there have been significant shifts in the shape of the capital value distribution, and the differential spatial patterns in value change, have occurred since 1991. These patterns require further investigation and testing, but the suggestion from the results is that the 'middle' of the price distribution has increased in value by a greater degree since 1991 than the higher price points of the distribution. The differential growth of prices in the middle of the distribution has not been high enough for properties in the middle to 'overtake' the value of properties higher up the price distribution. But, the effect is sufficient to mean that the aggregate value of property in the middle of the price distribution has increased more than the aggregate value of property in the higher points of the price distribution.

Land Value Tax

We now turn to the LVT and provide some comparison with the simulated Council Tax revaluation and national/ proportional property tax illustrations.

The LVT is designed as a residual site value (RSV) model. For each dwelling the SCOTPMOD we estimate the value of the land occupied by that dwelling. This process follows a number of steps. First, we estimate the construction costs associated with a 'typical' housing development and apartment development. This uses the construction cost model summarised in Table 10. The Glenigan data reveal the mean and median size of new housing and apartment developments in Scotland, as shown in Table 16.

Table 16 Descriptive statistics based on Glenigan data for Scotland

	Dwellings		Site_area (hectares)	
	Mean	Median	Mean	Median
Private housing development	57	40	3.76	1.93
Private apartment development	40	26	1.04	0.37
Land required for 1 house	482.5 sq. m.			
Land required for 1 flat (assuming 6:1)	80.4 sq. m.			

We therefore assume that a typical housing development includes 40 dwellings and a typical apartment development includes 26. The quantity of land required for these hypothetical development types is calculated and set out in the bottom of Table 16.

Next, the construction cost model is used to predict the cost per hectare of developing (a) housing and (b) apartments in the precise location occupied by every dwelling in SCOTPMOD. Given that the characteristics of the hypothetical developments is fixed at 40 or 26 depending on development type, the variation that occurs in construction costs is driven by the fact that population density varies spatially. In effect, the construction cost model provides two development cost estimates for every Datazone in Scotland.

Finally, we select the appropriate construction cost estimate based on dwelling type in SCOTPMOD. For apartments, the hypothetical apartment development project cost is selected. For all other property types the housing development project cost is selected.

Development value is predicted using the hedonic model results shown in Table 8. The difference between predicted development value and predicted development cost becomes the predicted land value. Although the modelling assumes development sizes of 40 or 26 dwellings for housing or apartment projects respectively, the final residual site values (RSVs) are scaled down to the amount of land occupied by one dwelling before being attached to each case in the SCOTPMOD database.

Table 17 Summary of simulation results [22]

Local authority	PPT take	Share of Scotland total	LVT take	Share of Scotland total
Glasgow City	236,688,684	8.34%	271,974,531	9.59%
North Lanarkshire	136,372,612	4.81%	24,460,946	0.86%
South Lanarkshire	152,499,935	5.38%	63,342,224	2.23%
City of Edinburgh	386,041,028	13.61%	808,602,911	28.50%
East Lothian	74,155,648	2.61%	105,891,543	3.73%
Midlothian	47,000,946	1.66%	56,627,233	2.00%
West Lothian	101,871,210	3.59%	87,469,550	3.08%

Table 17 compares the headline results from the simulation of a proportional property tax (PPT) and land value tax (LVT) using SCOTPMOD. The tax rate for both the PPT and LVT are set to ensure revenue neutrality in relation to the 2022/23 council tax take (£2.837 Billion). This derives an PPT rate of 0.46% and an LVT rate of 1.43%. Table 17 summarises the implications for local authorities in the study area. Given that the geographical variation in construction costs is much less pronounced than the geographical variation in property values, there is a strong redistributive impact from lower to higher priced places when moving from the PPT to an LVT. To a lesser extent, there is also a redistribution from less to more urbanised places. The analysis predicts that households in North and South Lanarkshire benefit from an LVT while households in East and Mid Lothian would be worse off. But, the stand-out prediction is that the City of Edinburgh gains a very substantial increase in Scotland's total tax base. This is also shown quite clearly by a comparison of Figures 1 and 2 – thematic GIS produced maps of the spatial patterns of PPT and LVT tax take.

22 The choice of illustrative LA, all in the central belt, is a convenience that allow us to show both table 17 and the details of the maps in figures 1 and 2.

Figure 1 Spatial distribution of total PPT take

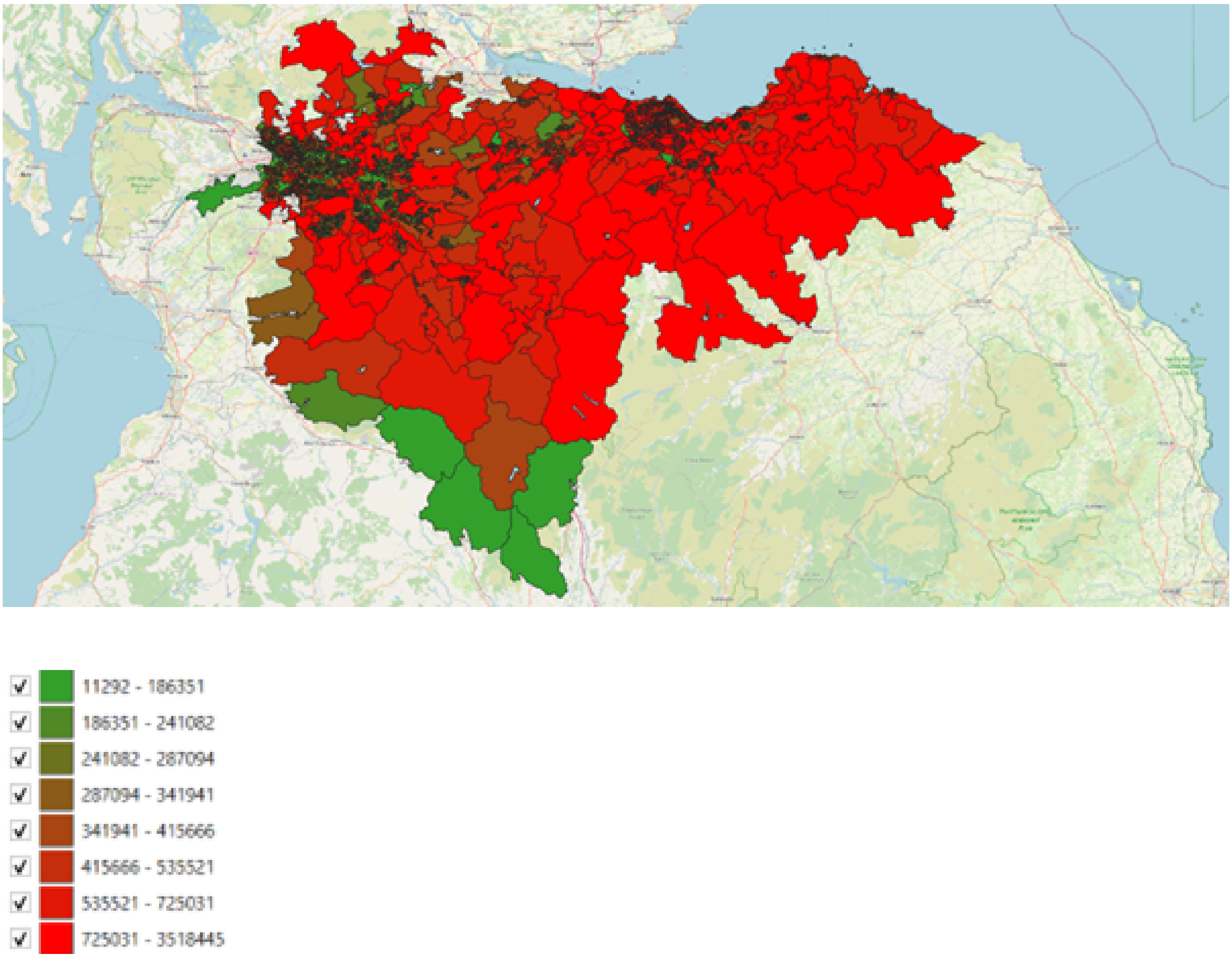
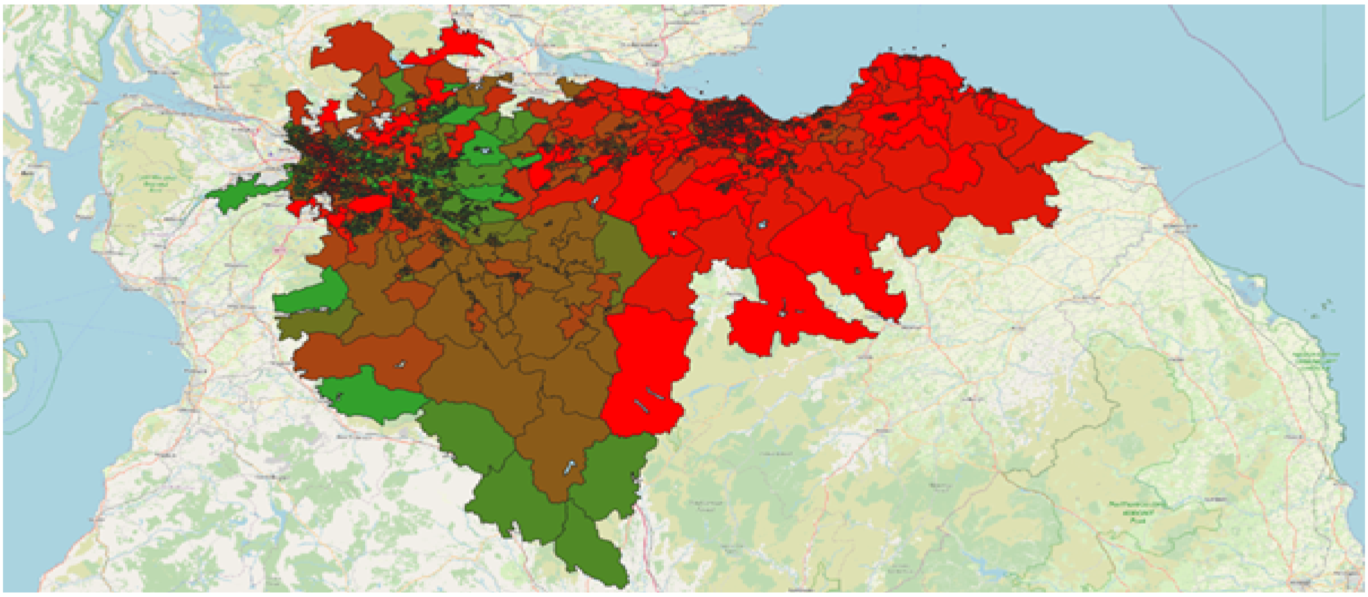
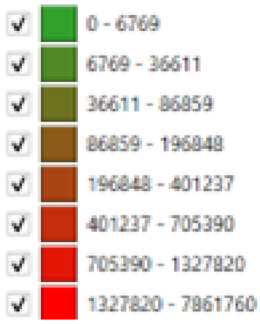


Figure 2 Spatial distribution of LVT take





5.7 Conclusions

To conclude, the scope of the analysis is limited by the fact that information on the current Council Tax band assigned to each dwelling was not available to the research. It is therefore not possible to draw any conclusions about the redistributive impacts of revaluation, or to provide estimates of the number of dwellings moving up or down bands within Scotland. Instead, we provide two scenarios for comparison with the baseline option of revaluing the council tax base. **We find that a revenue neutral national property tax rate would be approximately 0.46%[23] and that a revenue neutral land value tax rate would be approximately 1.43%. The redistributive impacts of the LVT would be more pronounced than the council tax revaluation or the NPT.** This is logical given that the spatial variation in property values is more significant than spatial variation in construction or development costs. **Finally, we find that a revenue neutral LVT designed only to replace the land and buildings transaction tax (LBTT) would be approximately 0.32%.** This figure is based on the most recently available from Scottish Government (£537.5M in 2022/23 including the £172M element from additional dwelling supplement).

The wider implications of this new evidence are, first, that the analysis demonstrates that it is perfectly possible to use existing data sets and modelling techniques to provide a robust revaluation of the Scottish domestic property tax base. Technically, it is also apparent that this could be regularly updated and even done so on an annual basis as is the case elsewhere in the world where automatic valuation models are adopted. Second, it is possible to use construction data and further modelling with these data sets to construct a plausible land value tax base. The provisional results developed here provide a reasonable basis by which to conduct distributional and other analyses of a land value tax.

A third implication is that we can assess the distributional implications on a similar all-residents basis how a revenue neutral tax would work if it was a proportionate property tax, or a land value tax (and they could readily be combined in ways similar to Muellbauer's proposal), as well as identifying the implied percentage revenue neutral land value tax only as a replacement to raise the same revenue as an abolished LBTT. Clearly, the LVT either as an LBTT replacement or standing instead of the Council Tax could be billed only to property owners.

23 Almost identical to the assumption used in the Fairer Shares PPT in England

6. Citizen Panel Evidence[24]

6.1. Introduction

We have seen that despite widely held concern with property tax arrangements in Scotland and the UK, there remains a strong political sense that governments feel it is too risky and politically costly to embark on meaningful reform. A key reason for this is the sense that there will be too many losers in a redistribution of the tax burden and that this will be difficult to introduce and electorally costly. It is often said that the public are not supportive of tax change especially where it concerns property.

Is this really true? We decided to test this by selecting a broad-based citizen's panel to examine current ideas regarding Council Tax reform. This was developed from the research team and the funder discussing different models of deliberative testing of public policy ideas, and a growing belief in the power of deliberative mini publics to help debate fully the nature of a policy issue in a reasoned and objective way, which gives space for the citizens to build consensus or recognise where it does not exist. We have seen recently, the impressive use of citizen assemblies in Ireland to stimulate reform on social issues where political parties benefited from the deliberative steer of a well organised representative assembly. Collectively, we drew on our own experience and that of other colleagues, plus direct subject knowledge to develop a two-day intensive citizens' panel in Glasgow in June 2024.

6.2. Method, Approach and Reflections

Our approach was informed by prior discussions held with Dr Oliver Escobar (University of Edinburgh) and Fiona Garven, formerly Director of the Scottish Community Development Centre. This led to the appointment of an independent facilitator, Kaela Scott, who co-designed the programme with us and led the event through the two days of presentations and discussions. We worked with Taylor McKenzie Market Research Services to recruit a wide-ranging group of 20 Greater Glasgow panellists differentiated by age, gender, race, tenure, socio-economic group, employment status and household types. The group were each provided with a modest financial incentive to say thank you for their taking part, they were thoroughly briefed beforehand and 19 turned up and participated for the full two days (a weekend at the beginning of June). The meeting was held in the CaCHE offices in Bridgeton, Glasgow.

The structure of the event, co-ordinated by the moderator/facilitator, took the form of short presentations led by Ken Gibb presenting factual material and answering clarifying questions across six sessions over the two days, interspersed with 'table' sessions and plenary discussions including votes, as we moved through the agenda (see below). There was extensive use of flip charts, note-taking, post-its and group report backs. Three tables were led by Deborah Hay, Paul Zealey and Lewis Forsyth – each discussion session started from the presentation before and adopted a common set of discussion themes for each session. Gibb and Scott floated between the three groups; Scott kept the discussion lively, on time and on topic throughout.

Holding the event over two consecutive days was tiring but it helped with recall, retention and participation for those involved. The pre-briefing was useful because people came to the event with their specific knowledge of what they paid in council tax, their sense and experience of local government services and a diverse sense of many of the salient issues we explored in the panel. We were struck by how hard they worked, the genuine sense of wanting to better understand specific issues, and a willingness to build on the consequences of conclusions reached (e.g. the Council Tax has flaws, so what should we do about it?).

A critical aspect of this deliberative approach was to first set out material about Council Tax and what others have said is important to understand about it, including what might be considered its flaws, before giving the panel plenty of space to deliberate on what they made of these ideas, to seek further information for the presenter and the table chairs, before arriving at their own conclusions or seeking further elaboration – in a cumulative learning process. We were careful throughout not to influence the direction of travel and to leave that to the panel as they debated the different points.

The structure of the event was as follows: day one was concerned with understanding the existing system and the challenges of keeping or changing it; day two: evaluating options for reform.

6.3. Main Findings

We consider here the broad direction the deliberations took as we moved through six discussion sessions, dividing up the findings as the group moved from review of the current system to discussions around possible reform and what it would need to achieve.

Discussion 1: the existing system

The summary table below (Table 18) aggregates discussion points raised across the three discussion tables: it should not be read as suggesting that participants were much more negative about the current system, than positive. There were mixed views at this stage, but while the positives raised were largely the same across tables, there was a greater diversity of negative points. Furthermore, it should not be inferred that any given point was uniformly shared.

24 The material used in this chapter include a working note of the citizen panel assembled by Deborah Hay from JRF, the presentation materials used in the panel by Kenneth Gibb, as well as further reflection on the panel by the authors after the event.

Table 18: Views about the Current System

POSITIVES	NEGATIVES
• Familiarity: 'it works'	• Based on 1991 valuations/ out of date
• Clarity exists about how it works	• Perpetuates wealth inequality
• Better than the Poll Tax	• Would revaluation actually raise more money?
• 25% single person discounts & exemptions	• Premiums on second & empty homes
• Student exemptions	• Perceived unfairness – e.g. on working adults or those on low incomes
• Raises reasonable amount of funds	• Perceived arbitrariness for different liability at different times e.g. What is 'substantially furnished'?
• Provides local jobs (services/ admin)	• Not integrated effectively with welfare benefits (UC)
• Flexibility of payment options (e.g. you can pay over 10 or12 months or annually)	• Don't know what it's used for/ where it goes
• Not an unreasonable amount	• City centre more expensive than suburbs
• Higher value properties do generally pay more	• Non-payment chased aggressively & sanctions = extreme (e.g. having to pay full liability immediately)
	• Separates rents and rates (used to be included together)
	• Council tax rebates for asset rich/ cash poor
	• Complexity of Council Tax Rebate
	• Taxes residential liability (not property ownership)
	• Not clear whether it's a property tax or a payment for services
	• Stacking of property taxes
	• 50% discount for empty homes (incentivises this)
	• Inconsistency across LA/ Scotland/UK
	• Poor relationship with local services quality

Discussion 2: Fairness

After support from the facilitator to discuss, test and consolidate important dimensions of fairness, the five key principles participants wanted to see in a fair system of local property taxation, were agreed:

- 1. A clear relationship with / strong link to high quality services
- 2. Property tax should be based on up-to-date property valuations
- 3. The tax must take account of ability to pay and offer protective exemptions
- 4. The tax must be predictable, certain, efficient and trusted
- 5. There should be a fair transition from current to new system.

These principles also provided us with helpful over-arching themes and potential trade-offs or fault lines to be negotiated.

Discussion 3: responding to the challenges of reform

Our participants emphasised the need for:

- Education and awareness raising to help the public understand how the current system works and the degree to which it simply doesn't make sense, along with what happens in other contexts (supported by a discussion of the international evidence e.g referring to Slack and Bird, 2015).
- Effective communication of what is a complex area - different people have varying levels of understanding about local taxation in practice.
- Building sufficient clarity and consensus across both the

public and among politicians that any reform both can and should be done.

- Need for a stable political consensus – cross party; beyond political cycles; requiring a formal convention/committee to push through.
- Addressing the 'hangover' from the poll tax (no-one wants to be punished - and political resistance to reform is understood if not accepted).
- (Addressing any) Perceived brake on aspiration (e.g. access to home ownership).
- Convincing the public – pragmatically, it was felt that this in part needs to be about extra pounds in your pocket.
- Better outcomes as a result of future reform – which link to better local services or housing outcomes.
- Speed/ time reform takes – recognition that this can be slow and asks what happens differently in the short and long term (and are there transitional arrangements?).
- Trust – both the need for it and the absence of it in elected representatives (and, presumably, officers).
- Whether property is seen as 'wealth' by all or not (and if not that the tax is simply the price for local services consumption).
- Understanding change is scary for many taxpayers/citizens and, consequently, there may be no appetite for change (especially during a cost of living crisis or where people might have to pay more or where the media and others create fears about change -panellists stressed the potential role of the media more widely in reform debates).
- Transparency/ opacity – the need for reforms to be transparent, clear against an opaque background generally on tax; currently we cannot see where the money goes/ what it buys.
- Winners and losers – which includes a broader set of concerns for society as a whole but is also personal: 'it's all about me, me, me'.
- Being able to respond to different needs – different households, different geographies across Scotland, different needs across UK.
- Cost of reform – which has to be understood, explained and planned for.

Discussion 4: what principles should underpin reform?

Our panel said reform should be:

- Data-driven: evidence based and transparent.
- Fair and seen to be fair: by citizens and local authorities/ service providers.
- Proponents need to articulate a clear case for change: what and why should be well communicated.
- Implementation of change must deliver sufficient resources to run improved, quality services right across Scotland.
- Reform should build trust and local accountability: good services, good value for money.
- Reform should relate well to ability to pay (and consider exemptions) – and fit with the earlier identified principles of fair local taxes (discussion 2).

Discussion 5: alternative tax ideas

When asked to reflect on what they heard, participants shared the following – see Tables 19 (incremental reform) and 20 (the specific example of a proportionate property tax).

Table 19 Incremental Change

Positives	Negatives
Not huge change	What's the evidence of positive impact on services?
Discounts are very positive	It's still a hybrid tax (service and asset)
Only 41% affected and 8% went down – useful to know it can go down, as well as up	Costs of transition – what were they?
Based on up to date, accurate, property valuations	What does success actually look like?
More tax bands make it more progressive	Not enough tax bands – too limited an impact on the housing market
Works and has been seen to work	Re-valuing too often means some are paying more and more in absolute terms
Undertaken during period of political stability/continuity	

Regarding incremental change only – panellists thought that it could address some of the challenges identified above because would not be a huge change, it has been seen to work (compared to the Community Charge), the earlier Scottish evidence suggested revaluation was not a one-way street in terms of outcomes, and it was possible to add bands.

On the negative side, it was not clear what impact this would have on services provided, not clear what the cost of revaluation, etc would be, that the banding system was still nonetheless, problematic and regular revaluation still clearly worried some panellists. So, it was not completely clear how well incremental change would relate to the underlying fairness principles, nor how it would relate to the low-income rebates system, or how it would interact with second and holiday homes, let along other property taxes (e.g. LBTT). Panellists were unaware of, but encouraged by, the principles of automatic valuation and use of big data that has made regular revaluations much easier elsewhere and indeed was part of the evidence used by the Commission in Scotland in 2014-15.

Discussion 6: A proportionate property tax (PPT)

The Panel saw different positives and negatives about a PPT (Table 20) – also see the Fairer Share model discussed in chapter 3 of this report). On the positive side, some were reassured i.e. not everyone would be significantly affected by the revaluation, some were comfortable with regular updating of valuations, and favoured the tax on all domestic property owners, including 2nd and holiday homes. They also liked combining the tax with LBTT in a single payment. Positive arguments were also made regarding progressivity and fairness in terms of the English model applied as a national tax rate.

For those expressing more negative views, the factors stressed included: the interaction with renter behaviour i.e. would it encourage more to rent; would the tax be passed on to tenants fully or in part; was it fair to remove exemptions and discounts; would a deferral scheme work or have unintended consequences; and, to the extent that the Fairer Share PPT is a national tax [the discussion recognised that the tax rate could be national or locally set – as discussed in different versions of the PPT case] - what does this mean for local democratic accountability and incentives to improve local service quality?

Table 20 View on a Proportionate Property Tax

Positives	Negatives
Equitable – consistent either at council or national level	Might encourage more people to rent, to avoid tax
Up to date and annual (mandatory) re-valuations, keeps things up to date	Why would landlords pay? Landlords should not pay for local services they don't use (or are paying for elsewhere)
Tax on 2nd homes, empty homes and non UK resident owners	Removal of exemptions and discounts (No consideration of high value asset/low income household)
Takes pressure off renters from paying Council Tax/ only paid by the asset owner	Burden could be transferred to tenants in higher rents – could regulation address this?
Replaces stamp duty ('a tax on moving')	Deferral idea should be monitored/regulated to avoid abuse/ tax avoidance
Progressive	Not equitable – areas that raise the most, will they keep their money?
	No local accountability – what is the function of a LA if it's a national tax? Delivery arm of /subordinate to the national state.
	Could put landlords off buying more properties because of liability (including social landlords?)

Deliberation and Voting

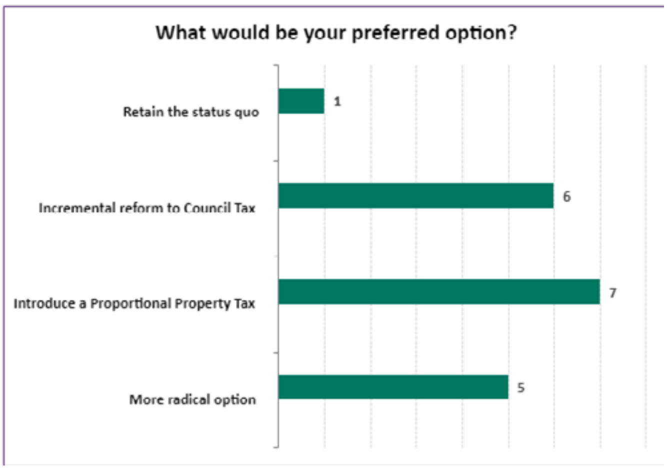
We asked, first, what the citizen panel considered is most important about any new system (the conclusions are ranked below in order of importance, high to low):

- 1. It is fair and seen to be fair – people are at the heart of reform design
- 2. Equal and fair exemptions or support to mitigate payments related to people's ability to pay
- 3. Transparency and clarity (people know what they are liable for)
- 4. Data-driven (up to date, accurate, objective)
- 5. Simple, consistent approach
- 6. Proportionate not excessive or extreme
- 7. People are well informed about the proposal and there is a commitment to education about it
- 8. A clear social contract (what we pay, what we receive and political accountability)
- 9. Tax raised needs to be able to deliver quality services.

These nine characteristics or necessary conditions of a reformed system can be interpreted as stressing ability to pay, simplicity and proportionality, convincing voters/taxpayers through programmes that involve them and provide clarity and explanation. They also imply a concern to retain local democratic accountability and a clear link between tax paid and quality or acceptability of local services.

We held a series of votes on reform that asked whether (1) Whether there should be Council Tax reform? (2) If so, should reform be incremental and within the Council Tax system as understood? (3) How achievable is incremental reform? (4) Are they in favour of more radical reform i.e. the PPT? (5) How achievable is the PPT? (6), Finally, what is your preferred reform? A strong majority wanted reform of the council tax system and slightly more were willing to embrace more comprehensive reform than incremental reform. Three on five opted either for PPT (the most supported route) or something more radical (25% opted for something more radical such as taxing land).

Figure 3 Final vote



Panel Conclusions

Pretty quickly, when faced with how Council Tax is currently calculated and on what basis, citizens accepted there were serious flaws and problems with Council Tax and they were keen to see something with greater fairness at its heart. There were different views about what that new system might look like and no shortage of challenges and trade-offs with an alternative system either.

Some struggled initially with the idea of using property wealth instead of an income-based measure to 'pay' for local services and how to balance affordability, with the number of residents in a home and their circumstances. Protections that took account of ability to pay, especially for the elderly, disabled, low income and in some cases, single person households, and phased in increases were very important.

Some also worried about how to balance the revenue likely to be raised in wealthy areas (where there would be high value assets) and that likely in areas of higher deprivation (lower value assets) but where high quality services would be even more important in addressing inequality. Mechanisms to re-distribute some funds to low value areas could undermine the accountability of the local authority in setting rates and delivering services.

By the end of the two days, there was a clear majority in favour of reform – but the level of support for incremental reform versus an entirely new system of proportional property taxation was much closer. Especially as we couldn't look in any greater detail at the interactions between different elements – what's the impact on transactions, overall burden and distributional impact of both a proportionate property tax and eliminating LBTT.

Given the discussions about how important political will might be, there was a feeling that improving the existing system was more achievable (at least initially) than moving to a proportional property tax. A proportional property tax was 'just' more popular but was felt to be markedly less achievable or politically likely. The importance of making any change 'worth it' in the form of raising more money, improving local services, improving the fairness for those on lower incomes, was held to be valuable.

There were key fault lines and trade-offs that need to be fully explored, concluded and strong cases for change developed: (1) Should a reformed local tax be on owners or households – how feasible would it be to exempt renters? (2) Should the local tax be expanded to replace the revenue lost by abolishing LBTT? (3) How would resources be equalised across Scotland given the locally varied tax bases (different levels of property values)? (4) How would the reformed system signal unambiguous relationships between tax payments and the quality of local services, supporting local democratic accountability? (5) Can this reform provide the foundations to alter the composition of the Scottish level tax base and shift it more towards property wealth?

6.4. Wider Reflections for this Study

The citizen's panel was a constructive experience for researchers and panellists alike. It reassured us that **there is appetite for change and that the model of a considered deliberative process combining explanatory short sessions and plenty of space for discussion and debate, led by the panel, can produce a demand for reform** and a willingness to consider rational redistributive reform based around principles of fairness. It also, clearly identified fault lines and difficulties that need to be comprehensively addressed in the inevitable trade-offs that come in designing local tax reform in practice.

We also note that some of the shibboleths preventing local tax reform have less currency than is often believed – **regular revaluation is not technically so difficult to put it beyond us; a clear programme of communication, information and debate can greatly increase citizen interest and appetite for the area even though it is about tax reform; people are interested in supporting local democratic accountability and connecting tax bills to local services; but, nonetheless, reform needs to be simple, clear, feasible and deliverable, with space for help for lower income households.**

This panel was diverse in demographics, experience and viewpoints and was run over two days. In some ways, the 'arc' that our citizens went on – starting off likely to favour income based measures and ending up wanting a more proportional property tax – was similar to those in the previous, more involved processes. However, we should be cautious in jumping to too many specific policy conclusions - the 'sweet spot' might have been somewhere between the two (income-based v reformed property tax proposals). We did work at pace within a compressed timeframe in a complex policy area, and recognise that under other circumstances, the panel would have benefitted from a longer time in session and more preparation, but we also accept that we would have probably lost the valuable intensity of the weekend's focus that undoubtedly deepened the quality of the sessions.

The key takeaways from reflecting on the citizen's panel, what we recommend for a national conversation on property tax reform, are as follows:

- It is not the case that citizens and voters are intrinsically opposed to tax reform when they have the space to understand and debate fully what are complex public policy issues. **Framing that debate and proving clear communications on policy option and also the cost of business as usual, is fundamental to making preferred reform routes work.**
- **Replacement with a new property tax is preferred to incremental change to the Council Tax. While the PPT was the most popular options it was favoured by just a third of delegates and 25% favoured something more radical.** This is interesting in that it charts a journey from a more income-based ability to pay idea about tax reform initially moving over the course of the deliberative meeting towards a better form of property tax.
- The PPT has fault lines that need to be dealt with – while **there was favour found regarding a tax on capital value, there remained a lack of consensus over whether (and how) tenants could be exempted and the implications for private and social landlords. There were also fault lines concerning the national (and more localised version of such a tax** (i.e. given individual LAs rate-setting powers within a resource

equalisation framework). Third, **there needs to be clarity over both the role of additional revenue raising by the PPT if LBTT is abolished in its current form, as well as how the various forms of deferral and low-income supports are to operate.**

7. Conclusions

7.1. The Case for Reforming the Council Tax and LBTT

If we take the two Scottish housing taxes together, they do not contribute positively to important goals regarding housing market efficiency (e.g. as a well-run market shaping tool of policy); neither do they support greater equality and reduced housing-related poverty. They also do not make the contribution they could do to supporting Scottish public finances and releasing funds for more progressive sustainable and resilient goals. Nor do the housing taxes as they currently operate, support the goals of Housing to 2040 as regards the de-speculating and stabilising of the housing market. This final section starts from this diagnosis and provides a clear steer on recommendations for reform. But these are provisional conclusions, which we hope can form the basis for further Scottish civic debate – about the housing system, property taxation, public finances and how we pay for local government.

7.2 What are the principal trade-offs when contemplating tax reform?

We examined different criteria with which to think through local tax options. We focused in Chapter 2 on housing market improvement (towards a well-functioning housing system); fairness and inequality reduction; furthering local democratic accountability; fiscal and wider public policy goals; and, technical and feasible taxes. Not all of these criteria may be equally-weighted and one's preferred tax may not score well on all of them. If we are to trade-off such criteria, we need to be upfront about it and defend our conclusions. Is the reform fundamentally about improving housing taxation and issues of inefficiency and wealth inequality or a better way to fund local services and which priorities local democratic accountability?

There are also unintended consequences to consider e.g. the fact that altering property taxes in different ways can be capitalised into property values, either raising or lowering them. For instance, removing LBTT may increase property values. At the same time if landlords not tenants are responsible for payment of the tax will it be passed on to tenants, and to what extent?

At the same time property tax reforms will have redistributive consequences. Winners and losers will be found both vertically (e.g. across the income distribution) and horizontally (by housing tenure or place). What options are there to lessen the burden by transitioning to any new tax arrangements, over what time period, and damping the year on year impact of the tax to potential losers. We also need to consider how tax relates to the distribution of taxation as a whole and not just look at it in a vacuum.

Apart from capitalisation of individual property values, there will be wider Impacts on housing market outcomes, for instance, the one-off consequence of the first general revaluation redistributing tax burdens and impacting on willingness to pay for properties changing because of the tax reform (Adam et al, 2025). There will also be changes to the relative values of market segments, hitherto distorted by the council tax valuation hiatus.

Historically, revaluation has provided politically difficult to undertake and to manage and in part this was a technical issue relating to the cost and time and capacity required to make revaluation work. This has been significantly reduced by big data and technology developments which make automatic revaluation a much more low-cost and de-risked activity, as is apparent where it is already operating and where the work described in Chapter 5 here demonstrates.

Part of the repeated unwillingness of political parties to concretely act on the unpopularity of current property taxes is the assertion that this is hugely unwelcome to citizens, taxpayers and property owners. Our citizen panel deliberative process discussed in depth in Chapter 6 clearly and carefully about what the current taxes do and the possibilities of different gradations of reform, making it clear that this perceived unwillingness is not the case (at least amongst our participants).

A further important, fundamental trade-off is to decide whether property tax reform should be designed so that all households pay or whether it should only be the owners of property (owner-occupiers and landlords). Is the latter fair and how would we prevent landlords passing the tax on to tenants? Should tenants not make a contribution to pay for local services?

These trade-offs and challenges must be resolved or at least a defensible position arrived at when considering which tax reform path is to be chosen.

What recent history tells us regarding contemporary discussion of tax reform:

- The recurring importance of the political context and electoral acceptability perceptions of decision-makers (including perceptions about how well the payment for local government services are democratically accountable).
- There is plenty of evidence (including from Northern Ireland) that proportionate capital value taxes can work.
- Revaluation can be done successfully (as we saw in Wales and Northern Ireland) but it needs to be de-politicised, efficient and credible.
- Government leadership and commitment as well as consensus building are essential.

7.3. Recommending Ways Forward and Overcoming Resistance to Change

We conclude[25] that, first, while reform is we believe necessary, we would rule out piecemeal reform of Council Tax e.g. thinking that it is sufficient to make a one-off general revaluation and further, more or less arbitrary, adjustments to bands and the weights applied to those bands.

Second, we are convinced of the desirability of abolishing LBTT and funding the revenue lost through recurring property taxation spread across a wider tax base than purchasers making transactions.

Third, we consider that regular, possibly annual, revaluations are both desirable and now much more feasible and cost-effective through automatic valuation principles.

Fourth, the principal reform is to create a new annual property tax that rases revenue for local government services and the replaced LBTT. Our general position on its design set out immediately below is informed by the analysis in Chapter 4 from the recent proposals from the proposals developed by Fairer Share, (and like-minded supporters) John Muellbauer and Tim Leunig. **Our approach would be to inflect the Fairer Share Proportional Property Tax with an awareness of points raised by the latter two proposals, but also to recognise our own concerns raised in previous chapters.**

What do we specifically propose:

- 1. Phase-in a proportional property tax over 3-5 years and during this transition cap the maximum annual increase in payments anyone has to face as a result of the tax change.
- 2. Operate a deferred payment scheme along the Muellbauer lines to help cash-poor owners.
- 3. Institute a regular, eventually annual general revaluation of properties – it is likely that the extra market information this provides would have wider efficiency and liquidity benefits by improving market decision-making.
- 4. Abolish LBTT and raise the revenue from all private owners of residential property (owner-occupiers and landlords) only.
- 5. Allow local government to set the local element of the new tax (the Scottish government would set the rate for the element raising the LBTT foregone revenue at a national common rate of tax, with parallel arrangements for other countries within the UK). The variation in property values by region, e.g. west to east Central Scotland but more broadly too, will require resource equalisation and redesign of local government grant funding to accommodate the redistribution in tax base compared with that under the Council. Resource equalisation reflecting the different regional values of property should be investigated through review of the local government finance grant system, including non-domestic rates (see point 7 below).
- 6. Include a green discount for high energy efficient properties
- 7. Localise non-domestic rates income to local authorities, i.e. keeping the yield of local non domestic rate income but also including local rate setting of the tax poundage, to reduce the gearing on the local domestic tax and make councils responsible and accountable for a larger share of their income[26].
- 8. As suggested by Fairer Share, tax undeveloped land held with planning permission for housing development – in this way the reform can capture some of the benefits of land value taxation without the complexity of developing an entire new tax infrastructure.
- 9. Over time this will offer the policy space for the Scottish government to increase the share of its wider fiscal tax base deriving from land and property rather than (mobile and more elastic) earned income.
- 10. There should be thorough economic and equalities impact assessments of these proposals. Alongside this, there needs to be widespread debate, education and public discussion about the narrow and wider issues discussed here, and this should include a formal citizen's assembly to assess these ideas in the round alongside Parliamentary scrutiny.

Clearly, if policy is to immediately move to combining the two current taxes into one was not deemed feasible, it would be perfectly possible to first pursue reform as outlined of the Council Tax alone. However, we remain of the view that LBTT needs to be reformed and preferably removed as a transaction tax (but the revenue would still need to be found).

The largest area for contention for us (and for the citizen's panel) remains the question of whether owners only or all households ought to pay the new tax. There is essentially a trade-off here between the housing economics arguments and housing wealth inequalities of present tax arrangements and moving to a more suitable current capital value tax arrangement, as against the need to ensure that tenants as residents retain a connection to paying for local services that they have a vote over. The argument in favour of owners only is essentially about the inequity of their current favourable treatment (especially those in high property value regions) but also that charging only owners of residential capital would be more in line with international practice, as is often claimed (though it is not always mentioned that most other countries have multiple local taxes on household tax units – we just have the one in the UK, bar the recent advent of tourist taxes).

What arguments might we marshal in favour of all households

25 We reiterate that these are our findings and conclusions and do not represent the views of the funder of this work.

26 As laid out in the Scottish Local Government Finance Statistics 2023-24, p.39, Non Domestic Rate Income (NDRI) identified by 'local authorities [do] retain all of the NDRI collected in their area. However, the contributable amount that they report is notionally pooled and then redistributed to councils as the distributable amount of NDRI, allocated to each local authority in proportion to each one's most recent prior year NDRI mid-year estimate'. But this is base don the national rate poundage set by the Scottish Government. Proposal 7 suggests simply doing away with the notional pooling and redistribution and allowing councils to set their local tax poundage (rate) for the non-domestic sector.

being liable?

- Solidarity and local democratic accountability – all households pay the council tax and poll tax and rates before them – this has long been considered an important way in which all households pay for local services and vote for local elected councillors. Is it acceptable to have a proportion of households not paying tax but receiving local services and potentially voting as free-riders? This was a strongly argued issue in the 1980s and surely would arise and challenge the reform case now. This was the view of several of the citizens' panel who were clear that the tax has to link local services to payment and voting. Implicitly, recommending residence and not ownership-based property taxes was also the view held by Burt and by the 2015 Commission. At one level, how one feels about this issue depends normatively on how centralist or localist one considers democratic and fiscal arrangements should be.

- We also note that the Tax by Design Mirrlees review suggested a tax on housing services/consumption as part of their benchmark idealised tax system – this could readily be reconstructed as a tax paid by all households on the rental value of the building and which could be sensibly be set for tenants for the consumption of local services. Equally Muellbauer's split tax non-land building component could also operate in the same way, though that is not what he proposes.

- Muellbauer and Fairer Share recognise that landlords will likely seek to pass through the tax to tenants in their rent. This may mean that in tight rental markets, tenants are obliged to pay extra to secure a home. This will play out in an arbitrary and inconsistent fashion and will be also a function of how competitive rental markets are. It would be naïve to think this would not happen. However, we lack convincing evidence on the extent and nature of such rent capitalisation and cannot rest on just assuming it applies across the board.

- It might also be argued that tenants already contribute to local government finance through general taxation. While this may be true, tax raised from VAT or income tax may find its way from the general revenues back to local government but it is a very indirect link to council spending platforms at elections. Moreover, we would follow Hollis et al (1991) who distinguish in their model of local government finance a distinction between local government acting as an agent for national government on redistributive and needs based services (which should be funded from national grants and taxation) while local spend on amenity and facility services (local parks, recreation, the bins, etc.) should be funded from local taxes. It is perfectly possible to distinguish spending on these different service classes and identify local spending platforms accordingly.

- Less discussed, though raised in the citizen's panel, is the impact of owner liability-only taxes on social landlords' finances who would now be responsible for paying the tax, too. What will they have to reduce to pay this additional burden? More broadly, social landlords are in a different governance position in terms of their ability to simply push up rents in response to this notional local tax obligation. This has not been explicitly thought through by proponents of owner-only property taxes,

- If private and social tenants were paying the new tax, then there would be a clear case to retain a low-income rebate scheme alongside the deferral scheme for owners. The case for this on progressivity grounds, and as suggested in chapter 4 above, would help tenants in higher property value markets.

We think therefore that the local charge should be levied on all households but the national charge for the LBTT revenue element should be paid by private owners (owner occupiers and private landlords) but not social landlords or tenants.

In conclusion to our recommendations, we propose a form of proportional property tax but on balance we think there is a localist accountability case to give further consideration that tenants might contribute. It makes more sense to spread the revenue previously raised by LBTT to owners of property only.

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Technical Appendix

Table A1		First step estimation results
Variable	Coefficient	P
constant	11.06172	***
Bedrooms	0.281938	***
Bedrooms2	-0.0097012	***
Floors	-0.070973	***
Floors2	0.0181346	***
Baths	0.127032	***
Baths2	-0.0087672	***
Receptions	0.0456178	***
Receptions2	0.0049935	***
q1	-0.0218115	***
q2	-0.0132484	***
q4	-0.0100596	***
y2018	-0.1900909	***
y2019	-0.1722017	***
y2020	-0.1424913	***
y2021	-0.0872347	***
y2022	-0.0351866	***
Bungalow	0.3589521	***
Cottage	0.2441573	***
Country house	0.7149774	***
Detached bungalow	0.4089001	***
Detached house	0.3659028	***
End terrace	0.0249351	***
Link detached	0.2808228	***
Council are	1.060863	***
Adj. R sq.	0.6622	
RMSE	0.39697	

*** significant at 1%; ** significant at 5%; significant at 10%

Table A2		HMLM results (main effects)	
Variable	Coefficient	z	P>z
Constant	11.85162	96.24	***
Beds	0.265478	237.18	***
Beds-squared	-0.01	-83.28	***
Floors	-0.01063	-3.05	***
Floors-squared	0.002746	1.78	*
Baths	0.06229	45.95	***
Baths-squared	-0.00188	-7.71	***
Receptions	0.016273	11.04	***
Receptions-squared	0.008821	26.71	***
Outlier	-1.13074	-40.28	***
Wald chi-sq	130359.9	***	

*** significant at 1%; ** significant at 5%; significant at 10%

Table A3	HMLM results (random effect variances)	
Random-effects parameters	Estimate	Std. err.
Property type: Identity		
sd(_cons)	0.486675	0.087729
Council: Independent		
sd(q1)	0.010842	0.001793
sd(q2)	0.002955	0.00221
sd(q4)	0.008841	0.002529
sd(y2018)	0.154908	0.006863
sd(y2019)	0.141496	0.006577
sd(y2020)	0.106482	0.00533
sd(y2021)	0.059137	0.003447
sd(y2022)	0.028581	0.004118
sd(_cons)	0.239789	0.009329
DZ11: Identity		
sd(_cons)	0.266762	0.00134
sd(Residual)	0.217105	0.000345
LR test	3.00E+05	***

*** significant at 1%; ** significant at 5%; significant at 10%

Table A4 sets out the final model, which is estimated as a robustness check, and to demonstrate the high level of explanatory power which is obtained by combining the earlier estimations.

Table A4		OLS demonstration model	
Variable	Coefficient	Std. err.	P>t
Beds	0.289563	0.001199	***
Beds-squared	-0.01243	0.000137	***
Floors	-0.00987	0.003595	***
Floors-squared	0.000913	0.001661	
Baths	0.063729	0.001497	***
Baths-squared	-0.00256	0.000272	***
Receptions	0.006175	0.001737	***
Receptions-squared	0.010307	0.000398	***
q1	-0.0107	0.001508	***
q2	-0.00616	0.001673	***
q4	-0.00322	0.001646	*
y2018	-0.18305	0.002593	***
y2019	-0.15887	0.002552	***
y2020	-0.12374	0.002542	***
y2021	-0.07721	0.002567	***
y2022	-0.02458	0.002556	***
Bungalow	0.489493	0.00324	***
Cottage	0.376683	0.004342	***
Country house	0.893183	0.017463	***
Detached bungalow	0.617696	0.002948	***
Detached house	0.60482	0.002361	***
End terrace	0.179954	0.002475	***
Link detached	0.452904	0.009488	***
Council	0.005312	0.005791	
r1	0	(omitted)	
r2	0.405597	0.099745	***
r3	0.872009	0.859275	
r4	0.337177	0.149066	**
r5	0.143316	0.023025	***
r6	0.228787	0.026128	***
r7	0.149908	0.027469	***
r8	0.157918	0.036282	***
r9	0.25091	0.039065	***
r10	0.995312	0.005494	***
r11	1.051593	0.002044	***
constant	11.04579	0.003725	***
Adj. R sq.	0.8975		
RMSE	0.21778		

*** significant at 1%; ** significant at 5%; significant at 10%