

# CIH Scotland's submission on taxation



## Evidence submitted by CIH Scotland Call for Evidence: A Scottish approach to taxation 30 September 2016

### **About CIH**

The Chartered Institute of Housing (CIH) is the independent voice for housing and the home of professional standards. Our goal is simple – to provide housing professionals with the advice, support and knowledge they need to be brilliant. CIH is a registered charity and not-for-profit organisation. This means that the money we make is put back into the organisation and funds the activities we carry out to support the housing sector. We have a diverse membership of people who work in both the public and private sectors, in 20 countries on five continents across the world including over 2,000 in Scotland.

Further information is available at: [www.cih.org](http://www.cih.org)

### **CIH contact:**

Ashley Campbell, Policy & Practice Manager

[ashley.campbell@cih.org](mailto:ashley.campbell@cih.org)

## 1. General comments

- 1.1 The housing sector in Scotland must be supported by a well functioning system of taxation in order to be able to deliver the homes and services that people need.
- 1.2 Taxation plays a clear role in the funding of affordable housing and housing services through direct subsidy from the Scottish Government for the development of new homes via the Affordable Housing Supply Programme and Council Tax to fund local services. Developer contributions towards affordable housing and essential infrastructure, while outwith the taxation system, warrant scrutiny alongside the Scottish Government's review of taxation and the planning system.
- 1.3 Taxation also dictates, at least to some extent, people's access to different types of housing in different places. For example, through Land and Buildings Transaction Tax and variations in Council Tax rates which can price people out of certain markets or locations.
- 1.4 The idea of a Land Value Tax (LVT) has been explored by many as a means of preventing the boom and bust cycle of the housing economy and preventing the artificial inflation of land prices to the detriment of housing supply and affordability. In the context of the devolution of powers over taxation and looking at Scotland's taxation system as a whole, we believe that this idea merits further consideration.
- 1.5 It is important to note that the issue of taxation as it relates to the housing system is closely linked with a number of other policy areas which are currently under consideration by the Scottish Government and so cannot be considered in isolation. Land reform, the review of the planning system and the creation of a new social security system for Scotland must all be considered alongside any changes to taxation.
- 1.6 In this evidence submission, we will focus on:
  - The high level outcomes we think should be achieved from a well functioning taxation system in Scotland.
  - Issues with the current system that need to be addressed in order to achieve these outcomes.
  - Suggestions for areas that require further consideration or research.
- 1.7 We would also like to highlight the fact that no single measure can achieve the outcomes we think the taxation system should be contributing to. Throughout this submission, we suggest a range of options which could contribute to a better housing system but we do not suggest that any of these alone can provide all of the answers.

## 2. Outcomes of a well functioning taxation system

- 2.1 In CIH Scotland's view, a well functioning taxation system should contribute to achieving the following outcomes for the housing sector:

- Outcome 1 - Scotland's housing needs are met, including the supply of affordable housing and provision of essential infrastructure.
- Outcome 2 - Local services that support communities and help people to live independently are adequately funded.
- Outcome 3 - People can afford to contribute to the tax system as their circumstances allow.

2.2 Achieving these outcomes will contribute to the Scottish Government's ambitions to create a fair and transparent taxation system but will also have a wider impact. They will help to achieve targets relating to housing and homelessness, social security and tackling inequality.

2.3 Achieving these three high level outcomes will also contribute towards the Scottish Government's vision for Scotland aligning with the following National Outcomes<sup>1</sup>:

- We live in well designed, sustainable places where we are able to access the amenities and services we need.
- Our people are able to maintain their independence as they get older and are able to access appropriate support when they need it.
- Our public services are high quality, continually improving, efficient and responsive to people's needs.

### 3. CIH Scotland Taxation Outcome 1 - Scotland's housing needs are met, including the supply of affordable housing and provision of essential infrastructure

3.1 The housebuilding industry went into decline following the economic downturn with completions decreasing substantially from 2008. While recent years have seen a slight increase in completions, there is clear evidence that we are not building enough homes to meet current needs.

3.2 Recent research commissioned by CIH Scotland, Shelter Scotland and SFHA concluded that 12,000 affordable homes must be built each year to meet housing need<sup>2</sup>. This does not take into account the need for more homes in other tenures. Industry body Homes for Scotland has called for a total of 25,000 homes to be built across Scotland each year<sup>3</sup>. Last year just less than 16,000 homes were built across all tenures<sup>4</sup>.

3.3 At best, a lack of suitable housing supply results in increased prices and limits people's choices about where they can live or what type of home they can live in. At worst, it can mean living in unsuitable housing which can have a negative impact on people's mental and physical wellbeing,

<sup>1</sup> <http://www.gov.scot/About/Performance/scotPerforms/outcome>

<sup>2</sup> [http://www.cih.org/publication-free/display/vpathDCR/templatedata/cih/publication-free/data/Affordable\\_housing\\_need\\_in\\_Scotland](http://www.cih.org/publication-free/display/vpathDCR/templatedata/cih/publication-free/data/Affordable_housing_need_in_Scotland)

<sup>3</sup> <http://www.homesforscotland.com/Portals/HomesForScotland/Documents/2015/HFS%20manifesto%202015/01014%20HFS%20MANIFESTO.pdf?ver=2015-11-02-154209-277>

<sup>4</sup> <http://www.gov.scot/Topics/Statistics/Browse/Housing-Regeneration/HSfS/NewBuildAllSector>

education or employment opportunities. For over 28,000 households last year, a lack of suitable accommodation resulted in homelessness<sup>5</sup>.

- 3.4 The Scottish Government has committed to delivering 50,000 affordable homes over the next five years, 35,000 of which will be for social rent. We welcome this commitment to increasing the supply of affordable housing but there are many challenges to be overcome in order to meet this target. Some of the current issues which act as a barrier to the supply of new homes and could potentially be addressed by changes to the taxation system in Scotland are outlined below, along with suggestions for actions which require further exploration.

### Land availability and affordability

- 3.5 The availability and cost of land suitable for developing new homes can act as a barrier, particularly for affordable housing providers who can find it difficult to compete financially with larger commercial developers.
- 3.6 Land which is zoned for housing but not being developed can lead to delays in delivering new housing, force up the price of land and consequently the cost of housing. A research piece from Savills explains how the value of land for residential development is linked to the housing market. The price of development land is linked to the likelihood of achieving a sale price of new build homes which will allow for appropriate profit levels. When land is bought up front, the assumed sale price for the homes is set and developers will only build and sell homes when this price can be achieved<sup>6</sup>.
- 3.7 There is currently no incentive to develop homes on land which can increase in value while remaining undeveloped unless the development of said land would achieve higher profits through the sale of homes.
- 3.8 We acknowledge that private developers will always seek to maximise profits and that this is part of a free market economy. However, we do feel that further exploration needs to be given to options that could help to encourage the delivery of new homes and curb the inflation of land and housing costs such as the introduction of Land Value Tax (LVT).
- 3.9 There are a number of different models for LVT but all are based on the premise that land owners are taxed on an assessed value of the land that they own. This could be set nationally or locally and tailored to different land classes.
- 3.10 A pilot of LVT carried out in Glasgow in 2009<sup>7</sup> identified a number of potential benefits including incentivising best use of land while preventing urban sprawl and land banking. However, transition to a system of LVT would mark a significant shift in the way that local taxes are calculated (the liability resting with the land owner rather than with the resident as with current Council Tax arrangements) and how services are funded. The Glasgow pilot also highlighted risks

<sup>5</sup> <http://www.gov.scot/Topics/Statistics/Browse/Housing-Regeneration/RefTables/RefTables>

<sup>6</sup> [http://pdf.savills.com/documents/2015-06-04ValueofLand.pdf?\\_ga=1.123115467.1370847782.1473333650](http://pdf.savills.com/documents/2015-06-04ValueofLand.pdf?_ga=1.123115467.1370847782.1473333650)

<sup>7</sup> [http://www.andywrightman.com/docs/Glasgow\\_LVT.pdf](http://www.andywrightman.com/docs/Glasgow_LVT.pdf)

with the implementation of LVT, not least the fact that there is little evidence of LVT working within the UK.

- 3.11 The analysis of the pilot highlighted specific issues for consideration including the risk of LVT being passed onto tenants through rent increases, difficulty in identifying land owners and the complexity of the system potentially making it difficult for tax payers to understand. However, the report does conclude that none of the issues arising from the pilot would be insurmountable and that LVT should not be discounted as an option for local tax reform. The report called for a series of detailed national pilots, including localised targeted LVT on derelict land, to be carried out.
- 3.12 Most recently, the idea of LVT has been explored by the Commission on Local Tax Reform appointed by the Scottish Government in 2015. The Commission concluded that while a system of LVT showed promise, further analysis must be carried out to assess the likely benefits of general and targeted LVT<sup>8</sup>.
- 3.13 We support the Commission's recommendation for further research into LVT, how this could work in Scotland and how it could potentially work alongside other taxes. In addition, the possibility of any unintended consequences of LVT should be fully explored. For example, charges levied on derelict land could affect social landlords who are in the stages of preparing for development or where development is planned but delayed for some reason. It would be counter productive for any change in taxation to have a negative impact on the supply of affordable housing.

#### Funding for affordable housing and infrastructure

- 3.14 The future of developer contributions through Section 75 (S75) must also be considered within the scope of this review and alongside the review of the planning system, the results of which were published earlier this year.
- 3.15 The planning review<sup>9</sup> recommendations criticised over reliance on S75 in some areas and also pointed to the fact that the regulations are not uniformly applied across different local authority areas and can lead to significant delays in the planning process. The use of S75 also relies on private developers bringing projects to the market in their own time. These factors raise the question of whether S75 provides the best mechanism to contribute to the development of affordable housing and provision of essential infrastructure.
- 3.16 The planning review recommends that the use of S75 is scaled back and that the system is amended to make it more streamlined. We agree that the use of S75 should be retained but could be improved and that the purpose of S75 needs to be more transparent. This should help to speed up negotiations between developers and local authorities. However, it must also be acknowledged that S75 does play an important role in the development of affordable housing and provision of essential infrastructure. If its use is to be scaled back, we must first establish how developments currently supported by S75 will be delivered in future.

<sup>8</sup> <http://localtaxcommission.scot/download-our-final-report/>

<sup>9</sup> <http://www.gov.scot/Resource/0050/00500946.pdf>

- 3.17 A revised system should make use of S75 alongside better strategic partnerships and joint ventures involving public authorities identifying and preparing land supply in their areas to compliment anticipated supply through S75 contributions.
- 3.18 The planning review also recommends consideration of options for a regional infrastructure levy to be developed and then consulted upon. As the review states, this would need to take into account lessons learned from the establishment of the Community Infrastructure Levy in England and Wales. This is an option worth considering alongside options for LVT as outlined above.
- 3.19 When considering the provision and funding of infrastructure, another approach which should be explored is Land Value Capture (LVC). LVC acts to prevent unearned profit for landowners who would otherwise benefit financially from the provision of infrastructure in the vicinity of their land without having to contribute anything themselves.
- 3.20 Under LVC, the uplift in the value of land created by the provision of infrastructure is captured by the local authority and can contribute to covering the cost of the initial infrastructure investment. LVT can also be used as a mechanism to tackle the perceived unfairness of landowners profiting from undeveloped land. At the same time this lack of development can push up the cost of housing or provision of other amenities generating further profit for landowners and developers.
- 3.21 The case for the introduction of LVC and the potential benefits for the economy and the housing system are set out in a report published by the Centre for Progressive Capitalism<sup>10</sup>. Again, this approach could not be considered in isolation. Implications for the planning system, the housing sector and local taxation must all be taken into account.

## Making best use of existing homes

- 3.22 The development of new homes is essential to meeting housing needs but we must also ensure that existing homes are fit for purpose, that they are warm and energy efficient and that we are making best use of existing buildings.
- 3.23 The latest Scottish House Condition Survey<sup>11</sup> shows that 35% of households in Scotland are living in fuel poverty and 36% of households are in urgent disrepair. Poor quality homes that are hard to heat can lead to poor health and contribute to poverty.
- 3.24 The Scottish Government's commitment to make energy efficiency a National Infrastructure Priority is a welcome step in the right direction but making progress on fuel poverty and energy efficiency will require investment from the private as well as the public sector. The Existing Homes Alliance Scotland (ExHAS) estimates that in order to bring the majority of homes in Scotland up to EPC standard C will require £450 million per year of public investment underpinned by £600 million of private funding each year for the next 10 years<sup>12</sup>.

<sup>10</sup> <http://progressive-capitalism.net/2016/06/bridging-the-infrastructure-gap/>

<sup>11</sup> <http://www.gov.scot/Topics/Statistics/SHCS/keyanalyses/LAtables2014>

<sup>12</sup> <http://existinghomesalliancescotland.co.uk/policy/parliamentary-briefing-taking-scotland-forward-2-june-2016/>

- 3.25 Currently, VAT is charged for all repairs and maintenance work. This does not provide any incentive for private landlords or home owners to invest in their properties.
- 3.26 According to the Scottish Empty Homes Partnership, there are around 34,000 long term empty private sector homes in Scotland<sup>13</sup>. Bringing these back into use as affordable housing could go some way to meeting housing need. While the Partnership has had some success in supporting owners to bring their homes back into use through grant and loan funding, this is another area in which a reduction in VAT for renovations would provide an extra incentive for the owners of empty homes.
- 3.27 We recommend that VAT should be reduced for repairs, maintenance or renovations of existing homes. This would help to encourage investment in improving our existing homes, making them fit for purpose. We understand that EU tax regulation has prevented this suggestion being taken forward in the past but with the transfer of some taxation powers to Scotland and the prospect of withdrawal from the EU, we feel that this proposal should be revisited.

## Land and Buildings Transaction Tax Additional Dwelling Supplement

- 3.28 Land and Buildings Transaction Tax (LBTT) is applied to the purchase of all residential homes in Scotland over £145,000. In addition to the basic LBTT, a supplement of 3% for additional dwellings (second homes or buy to let homes) over the value of £40,000 was introduced in April this year.
- 3.29 When LBTT was introduced, the legislation provided specific reliefs for Registered Social Landlords (RSLs) when acquiring homes. The policy memorandum cited the important role made by RSLs in the housing market<sup>14</sup>. No such relief was included for local authorities which play just as important a role in the provision of housing as RSLs.
- 3.30 Local authorities may seek to acquire existing homes for a number of reasons:
- To increase the supply of affordable housing in an area.
  - Management and maintenance of their own housing stock (particularly where right to buy has led to mixed ownership).
  - Targeted intervention to improve the quality of housing or management in an area characterised by poor conditions or antisocial behaviour.
- 3.31 Further information is available in our evidence submission to the Finance Committee in August this year<sup>15</sup>. The Association of Local Authority Chief Housing Officers (ALACHO) submitted more detailed evidence of the financial impacts that this tax is having on local authorities. They

<sup>13</sup>[http://scotland.shelter.org.uk/\\_data/assets/pdf\\_file/0004/1271767/Scottish\\_Empty\\_Homes\\_Partnership\\_Annual\\_Report\\_2015-16.pdf](http://scotland.shelter.org.uk/_data/assets/pdf_file/0004/1271767/Scottish_Empty_Homes_Partnership_Annual_Report_2015-16.pdf)

<sup>14</sup>[http://www.parliament.scot/S4\\_Bills/Land%20and%20Buildings%20Transaction%20Tax%20Bill/b19s4-introd-pm.pdf](http://www.parliament.scot/S4_Bills/Land%20and%20Buildings%20Transaction%20Tax%20Bill/b19s4-introd-pm.pdf)

<sup>15</sup><http://www.cih.org/resources/PDF/Scotland%20Policy%20Pdfs/Land%20and%20buildings%20transactions/26%2008%2016%20CIH%20Scotland%20response%20LBTT%20FINAL.pdf>

estimate that LBTT charges could cost the Affordable Housing Supply Programme (AHSP) in excess of £2.5 million over the next five years<sup>16</sup>.

3.32 It does not make sense for the taxation system to act as a barrier to local authorities providing affordable housing or seeking to improve the quality or management of housing. We recommend that local authorities be exempt from LBTT charges for the provision of affordable housing in line with exemptions in place for RSLs.

#### **4. CIH Scotland Taxation Outcome 2 - Local services that support communities and help people to live independently are adequately funded**

4.1 Local services in Scotland are partly funded by Council Tax which is based on the value of residential property as assessed in 1991. Last year, just over £2 billion was raised through Council Tax in Scotland<sup>17</sup>.

4.2 It has been a longstanding intention of the SNP Government to revise the system of local taxation which is based on outdated property valuations and does not reflect individuals' ability to pay. Council Tax has been frozen across Scotland since 2007 while options for local taxation have been considered. In 2015, an independent Commission on Local Tax Reform was appointed by the Scottish Government. Evidence and options for changes to the system were reported in December 2015<sup>18</sup>.

4.3 In response to the report, the Scottish Government announced that the Council Tax freeze will be lifted from April 2017, allowing local authorities to increase rates by up to 3%, and that households living in more expensive homes (bands E-H) will pay more. There are no plans for revaluation of properties and therefore Council Tax will remain based on values of properties in 1991.

4.4 To support households that cannot afford to pay Council Tax, the Scottish Government will increase the child allowance within the Council Tax Reduction Scheme (formerly Council Tax Benefit) by 25% and target relief to around 54,000 low income households living in more expensive homes who will see their Council Tax increase because of the changes to higher rate bands.

4.5 While the end of the Council Tax freeze will allow more flexibility for local authorities to increase income, there will be restrictions on how the additional funding can be used. The Scottish Government has stated that an additional £500 million, to be raised through increasing Council Tax for bands E-H over the life of the parliament, will be invested directly into education.

4.6 The Scottish Government's response does not address the fundamental issues with Council Tax – that property values are outdated and that taxation based on the value of property does not reflect individuals' ability to pay. In addition, it is not clear that changes will allow local authorities enough flexibility to adequately fund services based on local needs and priorities.

<sup>16</sup> [http://www.parliament.scot/ALACHO\\_Submission.pdf](http://www.parliament.scot/ALACHO_Submission.pdf)

<sup>17</sup> <http://www.gov.scot/Resource/0050/00501590.pdf>

<sup>18</sup> <http://localtaxcommission.scot/download-our-final-report/>

- 4.7 The recommendations of the Commission on Local Tax Reform should be revisited. The issue of local taxation should also be considered within the context of wider taxation reform issues such as whether a form of LVT or LVC should be introduced. There are also implications for the design and delivery of a new social security system for Scotland and these are explored in more detail below.
- 4.8 If the Scottish Government does intend to keep the current Council Tax structure in place, we would recommend at the very least a revaluation of properties be carried out to reflect changes in the market that have taken place since 1991. Revaluation was carried out in Wales in 2005 presenting an opportunity for the Scottish Government to take lessons from the process.
- 4.9 Consideration should also be given to Council Tax banding to improve proportionality and reduce the differences between bands for similarly priced properties. The issue of Council Tax banding was addressed by the Commission and again, we would recommend that their findings be revisited.
- 5. CIH Scotland Taxation Outcome 3 - People can afford to contribute to the tax system as their circumstances allow**
- 5.1 One of the Scottish Government's stated principles that will underpin the approach to taxation is that it should be proportionate to individuals' ability to pay. We agree that this is a sound principle and should be reflected throughout the taxation system in Scotland. As stated above, the current system of local taxation, Council Tax, is not proportionate and does not reflect individuals' ability to pay.
- 5.2 We welcome the Scottish Government's approach to supporting low income households to pay their Council Tax by funding the shortfall in benefits created when Council Tax Benefit was replaced by the Council Tax Reduction (CTR) scheme. However, an ideal system would be one which is based on an amount that is affordable rather than reliance on a benefit and mitigation measures to cover the shortfall. Around half a million households in Scotland are currently supported through CTR<sup>19</sup>.
- 5.3 We know from experience in other areas of welfare reform such as the introduction of the 'bedroom tax' that long term reliance on a benefit to cover a shortfall is not ideal. There are a number of issues with this approach:
- It relies on the individual or household making an application.
  - There is no guarantee that funding for benefits will always be available or will always be enough to support all households who need it. For example, in the context of support being provided to help cover Council Tax liability, the Scottish Government has pledged to target support at households affected by the increase in Council Tax for bands E-H but has set a maximum of £25,000. It is not clear how this will be distributed<sup>20</sup> or for how long this funding will remain in place.

<sup>19</sup> <http://www.gov.scot/Publications/2016/06/4798/downloads>

<sup>20</sup> [http://www.parliament.scot/ResearchBriefingsAndFactsheets/S4/SB\\_16-28\\_Scottish\\_Government\\_proposals\\_for\\_Council\\_Tax\\_reform.pdf](http://www.parliament.scot/ResearchBriefingsAndFactsheets/S4/SB_16-28_Scottish_Government_proposals_for_Council_Tax_reform.pdf)

- If funding for CTR is subject to further welfare reform cuts in future, the Scottish Government may not be able to continue to fully mitigate the impact which would leave low income households vulnerable to increased household bills.

- 5.4 The situation in England presents a stark example of these risks. The cuts to funding introduced with CTR have not been fully mitigated and nearly 75% of local authorities now require all residents to make some contribution to their Council Tax. Nearly one in five require over 20% of the charge to be met, even by those on the lowest incomes. Research conducted by Policy in Practice found one local authority charging a minimum payment of 45% meaning a single Jobseeker on £73.10 per week would be expected to spend around 10% of their income on Council Tax<sup>21</sup>.
- 5.5 Again, we acknowledge and welcome the fact that there is far greater support for households in Scotland but it is worth bearing in mind the consequences that can arise if support is eroded.
- 5.6 The Commission on Local Tax Reform recommends that a new system should be designed to minimise the need for complex relief schemes, and ensure that any relief schemes are straightforward to understand and administer.
- 5.7 We agree with these principles and urge the Scottish Government to consider options for a system based on ability to pay. Support should be available as required but ideally this should not be the default position.

## 6. Closing remarks

- 6.1 We welcome the opportunity to contribute to this debate on the future of taxation in Scotland. As outlined above, we see real opportunities for the Scottish Government to explore a range of options for taxation with the potential to support a wide range of objectives.
- 6.2 We look forward to further engagement and discussion on this subject.

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<sup>21</sup> <http://policyinpractice.co.uk/nearly-75-of-councils-to-cut-ctrs-budgets-this-april/>