



Transfer taxes and household mobility: Distortion on the housing or labor market?☆



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ABSTRACT

We estimate the effect of the UK Stamp Duty Land Tax (SDLT) – a transfer tax on the purchase price of property or land – on different types of household mobility using micro data. Exploiting a discontinuity in the tax schedule, we isolate the impact of the tax from other determinants of mobility. We compare homeowners with self-assessed house values on either sides of a cut-off value where the tax rate jumps from 1 to 3 percent. We find that a higher SDLT has a strong negative impact on housing-related and short distance moves but does not adversely affect job-induced or long distance mobility. Overall, our results suggest that transfer taxes may mainly distort housing rather than labor markets.

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1. Introduction

Most developed countries impose a tax on transactions of property and land. This tax – in North America often labeled ‘land transfer tax’ and in Britain ‘stamp duty’ – increases the transaction costs associated with the sale of a property and therefore in-

creases the costs of moving for homeowners. This cost increase can be expected to negatively affect the propensity to move. Thus, the tax is prone to have adverse effects on housing and labor markets. Households may not live in the type of dwelling and the location that most closely match their preferences. Similarly, individuals may be less willing to accept new jobs that are not within commuting distance or they may decide to hold on to a current job that is a less good match than another available job further away. Given these potential adverse effects caused by mismatch in housing and labor markets, the question of whether, and to what extent, the tax reduces household mobility is highly policy relevant.

Transfer taxes and in particular the UK Stamp Duty Land Tax (SDLT) – commonly referred to as ‘stamp duty’ – have long been criticized by economists as being inefficient. [Mirrlees et al. \(2011\)](#) highlights the fact that the SDLT “creates a disincentive for people to move house” (p. 403) and the adverse consequences of this on the functioning of housing and labor markets. To date, however, little is known about the *nature of the moves* (short vs. long distance or housing- vs. job-related) that are most strongly adversely affected. This is the key focus of our study.

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The UK stamp duty scheme in place until December 3, 2014 provides an ideal setting to explore the impact of transfer taxes on mobility decisions. This is partly because the tax liability was quite substantial, at least for more expensive housing (the top rate until December 3, 2014 was 7 percent, levied on the entire purchase price), and partly because the stamp duty liability jumped sharply at various cut-off values, providing various 'discontinuities' that can be exploited empirically.¹ Our analysis focuses on a discontinuity – or 'notch' – where the stamp duty jumps particularly strongly. This notch – at £250k – allows us to isolate the impact of the stamp duty from other determinants of mobility.

Basic economic intuition and simple theoretical considerations suggest that different types of moves may be differentially affected by the stamp duty. This is because benefits from moving are likely larger for more momentous – employment- or life event-related – mobility shocks than for more gradual changes in life-cycle circumstances – which typically move homeowners away incrementally from their optimal location and housing consumptions. Our theoretical considerations yield three empirically testable predictions: (i) At the house value cut-off of £250k, as a consequence of the tax notch, household mobility should decrease; (ii) The adverse impact of the notch should be greater for (more incremental) short distance moves than for (more momentous) long distance ones; and (iii) The adverse effect should be greater for (more gradual) housing-related than for (more momentous) job-related moves.

To test these predictions, we use data from the British Household Panel Survey (BHPS) and compare homeowners with *self-assessed house values* on either side of the cut-off, while controlling for flexible but smooth functions of house values. Consistent with our theoretical priors, we find that the SDLT has a significant negative effect on household mobility. Moreover, this adverse effect is confined to short distance moves and to moves that are housing-related. We find no significant effect on job-related moves and we find little evidence that the stamp duty adversely affects moves that are triggered by major 'life events' such as divorce or retirement. We document these key results both visually and using rigorous regression analysis.

Our core estimate indicates that the 2 percentage-point increase in the SDLT reduces the annual rate of mobility by 2.6 percentage points. This is a substantive effect given that the estimated counterfactual mobility rate in the group affected by the tax rate increase is only 7 percent. It equates to a 37 percent decrease in mobility. The corresponding welfare loss in the form of distortions in the housing market is very substantial. Based on our central point estimate, simple calculations imply that the welfare loss associated with the rate increase from 1 to 3 percent could be in the range of about 40 to 80 percent of the additional revenue generated by the tax increase.

In conducting our analysis we faced a number of empirical challenges. Some of these are specific to our underlying data and research design. A key concern is that homeowners with higher underlying propensity to move may be better informed about the stamp duty and may therefore be more likely to report the cut-off value rather than a value slightly above (i.e., sorting of homeowners close to the cut-off could partially drive our findings). Another potential sorting mechanism is that households that are interested in moving may attempt to keep the value of their house below the cut-off by neglecting renovation. To address these potential sorting issues, we drop households that self-report the cut-off value (or values very close to it) in a robustness check. Our results become less precise but the key findings regarding differential impacts of the stamp duty on different types of mobility remain clear. We also carried out a battery of 'balancing tests' to check for sorting of

households with different characteristics around the cut-off. In addition, we perform a robustness check where we limit the sample to households who responded in the survey that they would like to move. For this sub-sample, sorting based on unobserved willingness to move should be a lesser concern. Our key findings are robust to all these checks.

Overall, our results confirm the findings of the previous literature that transfer taxes are highly distortive in that they substantially reduce mobility. The main novel contribution of our study is that we demonstrate that these distortions are largely confined to short distance and housing-related moves.

Two strands of the economics literature motivate our analysis. The first strand is the existing literature on the impact of transfer taxes on household mobility. Transfer taxes are an important part of housing transaction/moving costs and they are the most important component directly determined by policy makers. Despite this, little is known about their effect on mobility. On the theoretical side, [Lundborg and Skedinger \(1999\)](#) modify [Wheaton's \(1990\)](#) seminal search model of the housing market by adding transfer taxes into the framework. They derive that the lock-in effects of the tax reduce welfare, with the adverse effect being larger at low vacancy rates and smaller with a buyer tax. The latter is because the buyer tax-induced price reduction dampens the negative effect on search effort caused by the tax. [Nordvik \(2001\)](#) analyzes the mobility effects of transfer taxes in a theoretical dynamic life-cycle model of housing demand. He finds that a transfer tax rate of 2.5 percent decreases the number of moves by the model household over the life cycle from three to one, implying substantial dead-weight losses.

On the empirical side, [Van Ommeren and Van Leuvensteijn \(2005\)](#) provide indirect evidence on the mobility effects of transfer taxes using individual panel data for the Netherlands. They estimate a competing risks hazard model of moving to renting or owning with house values as an explanatory variable and use a theoretical model to infer the effect of transaction costs. Their results suggest that a 1 percentage-point increase in the value of transaction costs—as a percentage of the value of the residence—decreases residential mobility rates by at least 8 percent.

[Dachis et al. \(2012\)](#) utilize the introduction of land transfer taxes in Toronto to estimate their effect on the housing transaction volume and prices with a Differences-in-Differences approach, comparing market outcomes across the boundary of the affected area.² According to their estimates, a 1.1 percent land transfer tax led to a 15 percent decrease in transactions in the first eight months after the introduction. The implied welfare loss relative to an equivalent property tax is about \$1 for every \$8 in tax revenue.

Discontinuities in transfer tax schedules have recently attracted increasing attention as a source of insight into how the tax affects market outcomes. Most closely related to the present paper, [Best and Kleven \(2015\)](#) utilize (i) administrative data on all property transactions in the UK, (ii) the discontinuities in the UK schedule to study price responses and (iii) changes in the tax schedule over time to study the effect on the transaction volume. [Best and Kleven \(2015\)](#) provide evidence of a strong negative price effect. In addition, they document that a temporary 1 percentage-point cut in the tax rate – due to the 2008–9 stamp duty holiday on houses worth between £125,001 and £175,000 – led to a 20 percent increase in transactions. The bulk of this impact is explained by a long term reduction in sales rather than the timing of purchases.

[Besley et al. \(2014\)](#) exploit the same 2008–9 stamp duty holiday to estimate the incidence of a transaction tax on housing. Their key findings are twofold. First, around 60 percent of the "surplus" due to the tax holiday accrued to buyers. Second, the tax holiday

¹ The reform from December 3, 2014 removed these discontinuities.

² See also [Dachis \(2012\)](#) for follow-up work using a longer data period.

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