Spatial Economics Research Centre

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Does stamp duty stop people moving house?

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People buying a home in the UK have to pay stamp duty on the transaction. Stamp duty-type taxes are one of the oldest forms of taxation – dating back to 1624 – and have long been criticised by economists as being inefficient.

The central case against the stamp duty is that it hampers household mobility. The 2011 Mirrlees Review neatly summarises this argument:

"By discouraging mutually beneficial transactions, stamp duty ensures that properties are not held by the people who value them most. ***It creates a disincentive for people to move house****, thereby leading to potential inflexibilities in the labour market and encouraging people to live […] in properties of a size and in a location that they may well not otherwise have chosen."*

To date little is known about whether the stamp duty does in fact hamper mobility and if so, by how much. In a new SERC Discussion Paper [pdf], my colleague Teemu Lyytikäiner and I provide some answers.

UK stamp duty - or to use the official name, 'Stamp Duty Land Tax' – is an odd tax in that the tax rate jumps dramatically at certain thresholds. For example if you buy a house at t price of £250,000 you pay 1% of the value, or £2500 stamp duty tax. But if you buy a house that costs £1 more, you pay £7500 tax (3% of £250,001).

We exploit this 'anomaly' in our empirical analysis. Specifically, we use a Regression Discontinuity Design type analysis to study whether and to what extent the disincentive to mc translates into lower household mobility.

We find that the overall effect is very substantial. A two percentage-point increase in the stamp duty from 1% to 3% reduces household mobility by around 40 percent. A closer loc reveals interesting additional insights: the stamp duty does not appear to significantly affect labour-related longer distance moves, probably because the benefit associated with th move for these types of moves is greater than the cost, which includes the stamp duty.

So the piece of comforting news is that the stamp duty may generate little mismatch in labour markets. Essentially, people who get a new job far away are likely to move anyway.

However, there is also a piece of bad news: The stamp duty has a very strong adverse effect on short distance moves, which are typically housing related. This suggests that the stamp duty likely has very detrimental effects on the functioning of local housing markets – the stamp duty induces substantial misallocation of dwellings because households do r adjust their housing consumption in order to avoid the stamp duty. This imposes a hefty welfare cost on the society as a whole.

All of this suggests that the stamp duty is highly inefficient from an economic point of view. In this light, the recent introduction of the 'mansion tax' of 7% for properties over £2m is albeit popular, a move in the wrong direction.

Wealthy households, whose children have moved out for example, may opt to stay in their mansions in order to circumvent the tax. Yet, in the absence of the tax, they may well ha preferred to 'downsize'. It may even pay for them to keep their properties empty for longer periods of time. Both responses are legal but inefficient. A smarter intervention would be land value tax, or a tax on property consumption – both of which would be much less distortionary, and much harder to avoid.

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