# "A Mansion Tax Is An Idea Whose Time Has Come"

More than at any other point in recent history, a mansion tax is an *idea* whose time has now come. However, significant barriers remain to define and execute this idea effectively. Even the label 'mansion tax' is a magnet for controversy and political opposition. This essay will outline the reasons why taxing the most expensive properties will be increasingly important for generating revenue and for addressing inequality. It will also explore the barriers to effective implementation and offer a solution based on
reforming existing property taxes instead of just imposing a single new tax on high-priced properties.

## The case for increasing the taxation of high-value properties

All forms of taxation will need to be reviewed as the country faces its largest decline in annual GDP in 300 years and record levels of national debt, each a direct result of the Covid-19 pandemic[1]. In addition, structural issues such as healthcare and social provision for the UK's ageing population, and climate change, will put further pressure on government finances.

Under this review, taxes on wealth must become a priority to tackle rising inequality. A recent ONS study reveals that the richest tenth of the UK population saw their wealth rising at more than three times the rate of that of the poorest 10%[2]. The same study reports that property contributes more than a third (35%) of all wealth held in the UK.

An increasing proportion of this property wealth is generated from inheritances. The Office for Tax Simplification reports that out of 591,197 deaths, only 21,850 estates paid inheritance tax in the 2018/19 financial year[3]. These taxes are disproportionally paid by middle-income earners who do not use trusts and other avoidance strategies that are now standard among the wealthy. The untaxed transfer of wealth to the next generation accelerates social inequality. Large homes and land holdings are widely viewed as an unfair intergenerational tax management system for the richest in society.

Effective tax rates are also higher for income from work versus income from wealth. Researchers at the LSE and Warwick University found that for the 2015/16 tax year, the average person with £10 million in taxable income and capital gains paid an effective tax rate of 21%, much less than the tax paid by people living solely from a £30,000 salary[4].

Similarly, a study by City University of income and taxation in the period between 2011 and 2018 concluded that while job income was taxed at an average of 29.4%, wealth from house-price increases and pensions had been taxed at just 3.4%[5]. The author says that there may be an untapped resource of an additional £174 billion if income and wealth effective tax rates were aligned.

One important way to address revenue shortfalls and inequality would therefore appear to be a new tax on the most expensive properties, ie. 'mansions'. This would have the added advantages of impacting only a small proportion of the population and normalising higher taxes on unearned income.

## Execution challenges of a mansion tax

If it were that simple, of course, it would probably have been done already. So what are the key barriers that must be overcome if a mansion tax is to generate significant revenues while also impacting inequality?

**Transparency of property prices and value** — For a mansion tax to function effectively, there must be a visible price/value point that makes it clear which homes are 'mansions' and which ones are not. This is important because recent purchase and sales data is only available for a limited number of properties. Council Tax bands are progressive but are still based on 1991 house prices. Valuations based on these outdated rates can be challenged, but very few people do so.

An updated, fair and clear evaluation system covering all higher value properties would need to be established by the Government's Valuation Office for a mansion tax to work. The issue of transparency is so fundamental that it could be considered a deal-breaker for a mansion tax if no valid system is put in place ahead of implementation. The question must be asked: is this possible?

**Annual tax versus one-off payment** — Unfortunately, there is no simple solution to the question of whether a mansion tax should be a one-off payment or an annual charge. An annual mansion tax payment is likely to generate more revenue in the long term than a one-time payment at the time of the transaction. This does reduce the spending power of the property owner, although this is less likely to impact the very wealthy. Annual taxes may also hit cash-strapped groups such as mortgage holders and pensioners as described below.

**Thresholds —** A mansion tax payment threshold would have to be low enough to encompass a sufficient number of homes to generate significant revenues, but would also need to avoid penalising people with lower overall wealth. For example, in areas such as London and the Southeast, where house prices are highly inflated compared to the rest of the country, many people own expensive homes but may not be financially secure due to large mortgages. Similarly, pensioners who bought homes a long time ago at very low prices may have since seen the value of their homes skyrocket while they remain on low incomes. Both of these groups would struggle to pay an annual property tax. However, these groups could easily pay higher capital gains tax at the time of sale or through the inheritance tax paid on their estates.

**Cliff edges and distortion —** Regardless of what threshold is set for a mansion tax, it will inevitably become a cliff edge and distort buyer and seller behaviours. Homes valued around the threshold will gravitate in price to just below the threshold to avoid incurring the tax. In some cases, people may choose to rent out their property instead of selling it. Others may choose to hold property within a trust structure to minimise taxation.

A study of New York's mansion tax, established in 1989, highlighted that the extra 1% imposed on the transaction of properties valued at over $1 million led to an estimated elimination of 0.7% of the total transactions and created bunching of prices below and above the threshold[6]. Interestingly, the original flat rate has since been replaced with progressive rates up to a maximum of 3.9% on properties of $25 million or more[7].

**Ease of avoidance** — A fundamental characteristic of inequality is that the wealthy have access to expert advisors and the financial flexibility that allow them to avoid taxes, regardless of the structure of these taxes. If a mansion tax becomes payable on £2 million houses, the wealthy may easily buy three homes valued at £700,000 to avoid the tax. This disincentive for the wealthy to own fewer, more expensive homes could lead to an inflated housing market.

## The way forward: Reform all existing property taxes

As demonstrated above, there are many barriers to the effective implementation of a mansion tax, despite the indisputable need for just such a tax on higher value properties. There are enough potential implementation pitfalls for a mansion tax to become just like inheritance tax, ie. to make no real impact on inequality.

A more pragmatic approach would therefore be a systematic reform of *all* forms of property taxation with the goal of impacting the top 10% of properties. This end-to-end reform of several property taxes, including stamp duty, council tax, capital gains and inheritance tax, will minimise the challenges and limitations for each individual measure because they could be managed as a whole. The use of digital tools for assessment, calculation and payment will need to be at the heart of reform. Tax simplification and ease of payment will encourage and enable payment and compliance.

This reform of property taxes must identify opportunities to reduce costly avoidance measures to increase both revenues and fairness. A gradual phasing out of trusts and complex tax mechanisms would be an obvious, albeit controversial step to take. They have no place in a society that is serious about tackling inequality.

Economists like Thomas Piketty have long argued that equality is bad for everyone, including the rich. While a hard core may never accept the logic of this argument, it is an idea that is no longer considered radical. At Davos this year, an international group of wealthy individuals calling themselves the Patriotic Millionaires lobbied for higher taxation on wealth[8]. Changing perceptions on inequality should result in stronger support in the future for more progressive taxes on all wealth, including so-called 'mansions'.

## REFERENCES


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