



Spatial Economics Research Centre

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Business Rates: Hoorah! But Watch Out for Housing!

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At last we have had a serious and radical policy change that really can improve one element of our dysfunctional, policy-induced development morass. As we showed in our [2008 paper](#) the move to convert Business Rates into a purely and transparently national tax largely removed the incentives for Local Authorities (LAs) to permit commercial development. This increased the costs of office space substantially more than any feasible level of business rates might ever have done. Because it just induced an even greater shortage of supply.

Now we have a [radical government proposal](#) to make Business Rates a local revenue resource. This is splendid news, given how we showed that the present reluctance of LAs to allow office development combined with the Alice in Wonderland complexity of our planning system, amounted to a tax on office space of up to 800% and, even in a struggling city like Birmingham, of 250%.

Cheaper office space means more jobs and a more competitive service sector. People may argue rents are only a small fraction of business costs but, as we recently showed in [another paper](#), the exact location and selection of sites makes a big difference to total factor productivity - at least in retail. Giving LAs a real incentive to permit commercial development also means businesses - with the exception of retail, which is still straitjacketed by Town Centre First policies - will have a freer selection of sites and micro-locations.

Sadly, however, there is a down side to this positive policy change. We all know we have a real housing crisis. Housing starts in England continue to wobble around their post 2007 crisis level and are still about a quarter down on their immediate pre-crisis levels and at less than half the level every informed observer argues is the minimum necessary. Consistent with this, the latest English Housing Survey showed a continuing rise in age for first time buyers with the proportion of 25 to 34 year old owner occupiers falling from 59 to 36% over 10 years; and for the first time ever, more owner occupiers did not have mortgages than did. In other words all the evidence shows that house building is not significantly rising from what was a 100-year peacetime low in 2010, that the supply and affordability crisis gets worse and the redistribution of housing wealth to the elderly continues.

The only policies on offer to address this crisis are what might be called magic; there is more than enough snake oil in all parts of the political forest but since the Conservatives are in power let us focus on theirs. There is the 'Starter Homes' initiative, [tweaked at the Party Conference](#), and the Housing Minister promising that [1 million houses will be built by 2020](#). Neither begins to address the fundamental problem. This is [lack of supply](#): supply of land put houses on and the supply of space building upwards could deliver (building above 7 stories is frighteningly difficult - see the map [here](#)).

So we have promises and hare-brained schemes that will hardly increase the net building of houses at all. Since they go together with boosts to demand via, for example, Help to Buy, in the absence of a radical change to free up land supply, [demand side measures mainly increase prices](#). So given the radical change in incentives the new policy on Business Rate revenues represents, what should we expect to happen? Well obviously LAs - desperate to have more money from [Google](#) to fund their services to non-residents and to make up for the [deplorable](#) and for housing is in effect [almost perfectly unresponsive](#) because of our [planning system](#) and [NIMBY pressures](#), this means they will divert land to commercial development and away from housing. This is despite government policy trying to transfer commercial buildings and land to housing! Economics and history show that if you tell people to do one thing but pay them to do another, they tend to follow the money. So a very good policy change from the perspective of the supply of commercial space threatens to freeze out even that little land available for housing. So the net effect will be to undermine the Starter Homes initiative (not so much a policy anyway - just political grandstanding) and help make housing yet more unaffordable.

The Government has shown courage to spur commercial development. It is now all the more important policy makers show similar - or even more - courage to tackle the housing crisis. Both the British tax and planning system are hopelessly inadequate to deliver enough new homes. Replacing the Council tax (and the stamp duty) with a proper local property (or better: land value) tax could create the necessary incentives for LAs to offset for the effects of the Business Rates Retention to reduce land for housing and could even lead to [more housing construction net](#). And, on the margin, since better designed land and housing taxes would be both more equitable and improve the efficiency with which land was used, there would be additional benefits. Tax reforms alone, however, cannot solve the housing crisis entirely. The planning system is far too deeply flawed for that. The sad reality is nothing short of a radical overhaul of our planning system can have any [real effect](#). Now that would create a lasting political legacy. There's a thought for the current Government...

Posted by [Neil Lee](#) on [Sunday, October 25, 2015](#)

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Benjamin said...

We don't have a lack of supply of housing. If we did we wouldn't see such high levels of vacancy and under occupation. We would also see mass homelessness, but we don't.

Affordability issues are symptomatic of problems with the very foundations of our economic system. It's that which needs tackling, not planning that protects our urban and country environments.

High land values are a good thing. They show efficient exploitation of agglomeration effects, which is why land values are highest at the network hub of successful city centres.

Not only is this unethical, but the resultant free lunch of imputed rents and excessive inequality produces deadweight losses.

We could therefore kill several birds with one stone by replacing all damaging taxes on output with land and other economic rents instead.

The resultant drop in house prices and the re-distributional effects from such a shift would mean a four fold increase in housing affordability, as a ratio of discretionary income, for an average working UK household.

We'd also get optimal efficiency in our land/property market, and a level playing ground between the regions, taking demand for housing away from London and the SE.

The "housing crisis" sorted without any loss of welfare from scrapping existing planning regulations.

We only have a Greenbelt to contain urban sprawl because we don't have an efficient land/property market.

If Hibler and Cheshire really want to solve seemingly irreconcilable problems like housing affordability, protecting green areas and regional inequality, they'd be vociferously campaigning for a 100% Land Tax. Nothing else.

Instead, they choose, presumably for ideological reasons, to blame State regulations for all our ills. In doing so they recommend policies that will only make our property market even more inefficient.

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