

THE CASE FOR SHIFTING FROM STAMP DUTY TO RATES AND LAND TAX

**Submission to the House Standing Committee on Tax and Revenue
Inquiry into Housing Affordability and Supply**

Yogi Vidyattama and John Hawkins

National Centre for Social and Economic Modelling,

University of Canberra

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Introduction

The problem of housing affordability is most acute for the over 100,000 homeless Australians and low income people renting in the private market. But the aspect of housing affordability that attracts most attention is the challenge facing young aspiring home buyers. While young people are facing an increasingly long wait until they can afford to buy a home, it still remains their strongly preferred option.¹

There are many factors that make home purchase difficult.² The reports of two parliamentary committees contain good discussions of many of these that are still relevant today.³ Unfortunately many supposed fixes just boost demand and push up prices, making affordability worse.⁴ At a political level, the basic problem is that most measures that significantly improve affordability imply reducing house prices, or at least causing them to rise less. This is going to be politically ‘courageous’ when about two-thirds of voters own homes. As John Howard said in 2004, ‘I haven’t found anybody stopping me in the streets, shaking their fists and saying “John, I’m angry that the value of my house has gone up” ‘.⁵

This submission will concentrate on one possible way that governments can allow housing supply to match better housing demand. It advocates the gradual replacement of the existing very large one-off stamp duties (also known as transfer or conveyancing duties) on home purchases⁶ with increases to the annual taxes on land (either state government land taxes or local government rates).

Such a tax switch is currently being implemented by the ACT Labor-Greens government. The NSW Liberal-National government released a consultation paper with its 2020 budget about such a move. NSW Treasurer Dominic Perrottet has claimed the reform would mean ‘more than 300,000 NSW residents could achieve their dream of home ownership and Gross State Product could increase by 1.7%’.⁷ The move has reportedly been supported by the Liberal chair of this committee while Labor’s federal shadow treasurer has said he has ‘an open mind to changes of this nature which could make the tax system fairer and improve labour mobility and access to housing’.⁸ So the political stars may be aligning to allow this tax reform to achieve a broad consensus of support.

¹ Sissons and Houston (2019), Hoolachan et al (2017).

² For example, the Reserve Bank governor this month referred to zoning and planning restrictions and inadequate investment in public transport as contributing factors; *House of Representatives Economics Committee, Public Hearing Hansard*, 14 August 2020, p 5.

³ Senate Select Committee on Housing Affordability in Australia (2008) and Senate Economics References Committee (2015).

⁴ Vidyattama and Hawkins (2021).

⁵ Cited by Tiffen and Gittins (2009). Megalogenis (2006, p 177) noted that ‘Gough Whitlam and Malcolm Fraser are the only two prime ministers since records began in 1960 to fight elections immediately after presiding over a capital loss for home-owning voters. Both were punished with massive defeats’.

⁶ There are also stamp duties or similar on other transactions but these are outside the scope of this submission.

⁷ www.nsw.gov.au/sites/default/files/2021-06/property-tax-progress-paper-june-2021.pdf

⁸ Cranston and O’Mallon (2020), who seemed so enthused they referred to Mr Perrottet as the ‘NSW premier’.

Stamp duty on sales of homes is a very inefficient tax

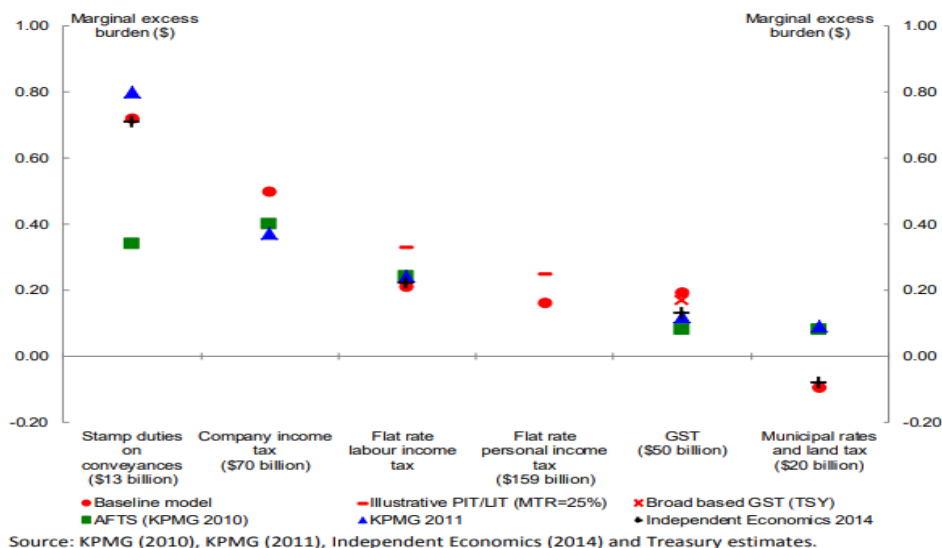
A statement often attributed to Louis XIV’s finance minister, Jean-Baptiste Colbert, is that ‘the art of taxation consists in so plucking the goose as to obtain the largest possible amount of feathers with the smallest possible amount of hissing’.⁹ Stamp duties often involve hissing without yielding any feathers.

Suppose a neighbour of the committee chair who lived and worked in Narrabeen in Sydney’s northern beaches was offered an attractive job in Cronulla in Sydney’s south. The trip from Narrabeen to Cronulla involves about 1½ hour’s drive, or over two hours by bus and train, each way.¹⁰ Faced with this commute, he thinks about selling his house in Narrabeen and buying an equivalent in Cronulla. But current NSW stamp duty on a \$1 million house is around \$40,000.¹¹ This may lead him to stay living in Narrabeen and either not take the better job or gird himself for a long daily commute. Either way, the stamp duty has made him worse off, without raising any revenue at all for the government.

This does not just impose costs on the individual but on the economy as a whole. As the Reserve Bank governor said this month, stamp duty is ‘a tax on mobility — on people moving location. If we’re looking for an economy that’s dynamic and vibrant, we want to remove taxes on mobility’.¹²

A Treasury working paper reviewed the efficiency cost of a number of taxes. It concluded ‘the most efficient tax captured in our model is a hypothetical broad-based land tax, similar to municipal rates’.¹³ The least efficient was stamp duties. The authors noted that a similar conclusion had been reached in other studies. Chart 1 summarises estimates of the efficiency costs per dollar of revenue raised of different taxes, with the different symbols representing different studies. There is a clear consensus that stamp duties are the least efficient and rates and land tax the most efficient.

Chart 1: Comparison of marginal excess burden estimates



Source: Cao et al (2015, p 54).

⁹ For example, The Economist (2014).

¹⁰ [Trip planner | transportnsw.info](http://tripplanner.transportnsw.info)

¹¹ www.revenue.nsw.gov.au/taxes-duties-levies-royalties/transfer-duty

¹² RBA Governor Phil Lowe, *House of Representatives Economics Committee, Public Hearing Hansard*, 14 August 2020, p 5.

¹³ Cao et al (2015, p 53).

Stamp duty also discourages ‘empty nesters’, whose children have left home, from downsizing to a smaller home that better matches their requirements. It therefore prevents young growing families moving to a larger home that suits them. Stamp duties may also encourage first home buyers to buy a larger house than they need at the time to avoid paying further duty should they require a larger home as their family grows.

There is also a fairness aspect. Stamp duties impose a big tax on people who need to move homes. It acts as a tax on divorce, or a tax on relationship breakdowns.

From the states’ viewpoint, another disadvantage of stamp duties is their volatility. When real estate markets soften, both prices and the number of transactions decline, leading to a slump in tax revenue. Land taxes would be a more steady foundation for longer-term budgeting.

A broadly supported reform

There is broad support among academic economists for the switch from stamp duties to land tax. Examples include Coates, Daley and Chen (2018), Eslake (2020), Freebairn (2020), Holden (2020), Ong and Wood (2016), Smith (2015), Stewart (2011, 2016), Uren, Li and Cho (2021) and Wright (2015). Daley and Coates (2015) estimated that ‘shifting from stamp duty to a broad-based property tax would... add up to \$9 billion annually to GDP’. The Henry Tax Review in 2010 and the report of the Senate Economics References Committee (2015) both supported a transition from stamp duties to land taxes.

Indeed, when prime minister, Malcolm Turnbull commented:

If you were to replace stamp duty on property transactions, and replace it with a land tax, a general land tax, there isn't a tax economist or theorist in the country that wouldn't tell you that would be a good move, because taxes on transactions like sales of property obviously inhibit trade, they slow down economic activity. Everyone understands that.¹⁴

Modelling the impact of the ACT reforms

TTPI and NATSEM (2020) used a microsimulation model, drawing on data from the ABS *Surveys of Income and Housing*, to analyse the ACT reforms.¹⁵ Allowance was made for stamp duty concessions under the Home Buyer Concession Scheme, available to low income households buying houses below a price threshold, and the Pensioner Duty Concession Scheme. It was assumed that a potential home buyer needed sufficient assets (savings plus any equity in their current home) to pay a 10 per cent deposit, stamp duty and the lender mortgage insurance premium, with allowance for any concessions or first home owners grant for which they are eligible. (In practice, a majority of recent first home buyers borrow more than 80 per cent of the value.) It was also assumed that home buyers needed sufficient income to meet the loan principle repayments as well as interest, essential food and clothing, income tax, rates and so forth.

The result was the gradual move from stamp duty towards land taxes would have allowed an additional 2,300 households to afford a home. About three-quarters of these would be first home buyers and there would

¹⁴ Malcolm Turnbull, interviewed on ABC *Insiders*, 7 February. www.abc.net.au/insiders/the-prime-minister-malcolm-turnbull-joins-insiders/7146776

¹⁵ See Tanton et al (2011) and TTPI and NATSEM (2020) for more information about the modelling approach.

include single parent families. While the number of home purchases increased the most for middle and high-income earners, there were also additional purchases by those in the lowest income quintile. Ranking households instead by wealth, the largest increase in purchases was by those in the second-lowest quintile. Those in the lowest quintile did not have enough savings or equity to benefit.

It is possible that there is a partially offsetting rise in house prices when stamp duty is reduced. This would lower the estimated number of additional households able to purchase homes as a result of the reform. The reform package would have to induce additional annual price rises of over 2 per cent before it no longer increases home ownership.

The impact on the progressiveness of the tax system is unclear.

The transitional issue

There is a transitional problem in making the switch. Those who have just bought a house and paid stamp duty on it will not be happy if they then have to also pay a higher land tax. One response, adopted in the ACT, is to have a long phase-in. The ACT plan will take twenty years to complete. Having started in 2012, it is now almost half complete. While homebuyers who bought (and paid stamp duty) a long time ago have since benefited from rising house prices, some still grumble about increased land tax.

The NSW Government's proposal is instead to offer homebuyers a choice. New buyers can choose either to pay the upfront stamp duty or opt for the property to be thereafter subject to an annual land tax. A possible problem with this is it may involve an even longer transition period. Furthermore, if buyers have a good idea of how long they will stay in their new home, and rationally choose the option that is cheaper for them, governments will lose revenue and some buyers will still be reluctant to move from their properties.¹⁶

A better alternative might be to introduce a land tax immediately but give recent buyers a partial credit for the stamp duty they have paid.¹⁷

The case for federal government support

It has been argued above that the switch from stamp duties to land taxes would increase efficiency and increase GDP. This in turn would increase income and company tax collections for the federal government. There would therefore be an argument for the federal government to make incentive payments to the states to encourage them to undertake this reform. For fairness, and to avoid punishing good behaviour, these payments should also be made to the ACT (and NSW if it has started down the path by then).

¹⁶ Fairbairn (2020).

¹⁷ Fairbairn (2020).

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