



REAL ESTATE INSTITUTE OF AUSTRALIA LTD

**REAL ESTATE INSTITUTE OF AUSTRALIA SUBMISSION
TO PRODUCTIVITY COMMISSION INQUIRY INTO
FIRST HOME OWNERSHIP**

References:

- A. Productivity Commission Discussion Draft into First Home Ownership dated 10 December 2003
- B. Real Estate Institute of Australia Submission to Productivity Commission Inquiry into First Home Ownership dated 16 October 2003

BACKGROUND

1. The Productivity Commission Discussion Draft, at Reference A, has been released with a request to Inquiry participants, including the Real Estate Institute of Australia (REIA) to comment on the Commission's analysis and preliminary findings, prior to the Commission preparing its final report to Government.
2. The REIA welcomes the Discussion Draft as being a document that has well covered the major issues affecting housing affordability and the REIA supports a number of the conclusions and suggestions.

PURPOSE

3. The purpose of this submission is to provide comment on the Productivity Commission Discussion Draft at Reference A, particularly on issues relating to:
 - a. home affordability,
 - b. regulation of property investment advice,
 - c. social benefits of home ownership and implications for society and government,
 - d. stamp duty,
 - e. land tax,
 - f. taxation,
 - g. negative gearing,
 - h. First Home Owners Grant Scheme (FHOGS),
 - i. access to superannuation, and
 - j. the way ahead.

ISSUES

Home Affordability

4. The REIA concurs with the Commission's conclusions at Reference A regarding the reasons behind the rising house prices over the last few years,

particularly that the dominant source has been the general surge in demand. Reasons are well documented and can be seen at Reference B Paragraph 16. The fact is that home affordability has declined significantly.

5. Reference A concludes that the housing market is cyclical and subject to price fluctuations, and noted that whilst different segments of the market are influenced by broader market trends and economic pressures, home loan affordability has decreased.

6. Reference A Page XIII concludes that “while measured affordability has declined considerably – generally and for first home buyers – it is unclear where it stands historically... In the Commission’s view, the best that can be said is that affordability in many parts of Australia is now likely to be approaching, if not passing, the lowest levels of the last cycle”. The REIA considers that this may not be the case.

7. Current indicators show that affordability may continue to trend downwards because the reasons behind the high price of housing generally show little likelihood of change in the foreseeable future. For example, continued sound economic fundamentals such as relatively low interest rates, low unemployment and business and consumer confidence. Other factors such as the influence of baby boomers, accessibility of housing finance, and changing demographics are likely to continue in the near term.

8. The recent REIA Swinburne University population study shows that, in terms of demographics, the demand for housing is likely to increase significantly, thereby affecting house prices. See Reference B Paragraph 19.

9. However, at Reference A Page 53, the Commission concludes “... that population pressures have not been a major driver of the strong upswing in house prices across Australia. (but).. Overall immigration policy obviously needs to be determined by broader considerations”. Further, at Page 9, the Commission noted that “... over time, the regions may act as a natural safety valve if affordability problems in the cities become particularly acute... (but) ... is a complex issue that cannot be satisfactorily resolved in an inquiry of this sort”.

10. The REIA agrees with the Commission that further inquiry is needed. Moreover, a strategic framework should subsequently be developed which will help shape policies. The REIA proposes the following:

- a. Regional policy should be developed by governments focussed on housing in a nation-wide perspective to take account of issues such as affordability, infrastructure, sustainability, and socio-economic development.
- b. It is clear that such an initiative is a long term prospect, which together with other issues to be covered in this paper including social benefits and implications for governments, would benefit from a broad coordinated planning strategy.
- c. Such a strategy should be developed by the federal Government in conjunction with State and local governments, under the auspices of a

federal Government housing portfolio at Ministerial level. This strategy would provide a planning framework to account for demographic changes, regional and urban development, and contribute to the broader socio-economic development of Australia.

Regulation of Property Investment Advice

11. One major reason for the increase in house prices has been the availability of finance. In this context, at Reference A Page 45, the Commission notes that “like innovation in lending products, increased competition for customers has generally benefited home buyers. However, there is a concern that the incidence of imprudent lending, and misleading investment advice to consumers, is increasing”. Further, “In the Commissions’ view, the current housing boom has highlighted the importance of appropriate regulation of lending practices and property investment”. “However, such regulation is not without risks and potential costs. For example, regulation that significantly reduced the scope for mortgage brokers and property advisors to respond flexibly, and expeditiously to the needs of clients could disadvantage rather than benefit homebuyers”.

12. A national working party, including the ASIC and ACCC, has been established by the Ministerial Council on Consumer Affairs to examine national regulation of property investment advice. It does not appear to have a Terms of Reference at this stage, but clearly in the joint communiqué announced on 1 August 2003, the review was brought about by “... concern at the operation of marketeers and property investment advisers and the detrimental impact that they have on unwary customers”. The REIA is previously on the public record supporting Government initiatives which stop deceptive and misleading practices such as those alleged in media reports about some property investment seminar spruikers. Real estate practice is already extensively regulated by State and Territory governments, and it must comply with provisions of Commonwealth legislation including investment advice under the Financial Services Reform Act, Privacy Act, and Trade Practices Act. The particular limits for provision of financial advice by licensed real estate agents are specifically well covered under the Financial Services Reform Act.

13. Accordingly, the REIA proposes that the Commission make a clearer distinction of the problem regarding the objectives of the Working Party, so that real estate agents are not inadvertently and unnecessarily further regulated as a result of general views expressed by the Commission.

Social Benefits of Home Ownership

14. The REIA supports the Commission’s findings that home ownership “... enhances both economic performance and social capital”, and that the provision of rental housing is still a very important part of socio-economic well-being.

15. Home ownership in Australia is high compared to some other developed countries in the world, eg about 15% higher than France and 30% higher than Germany. The consequent social order and comparative security of living in Australia is the envy of many countries.

16. The socio-economic benefits of home ownership are indisputable. However, a report from the Committee for Economic Development of Australia (CEDA) in December 2001 entitled “Future Directions in Australian Social Policy” has indicated ... “concerns about the widening divisions and inequalities in Australian society, an increasing burden on individuals to cope with new uncertainties and risks, and a questioning of the balance between reliance on the market as a distributive mechanism and a role for government in risk prevention and mitigation, social investment and social protection.” Indicatively, the report stipulated that the home purchase rate among the generation cohort of 25 to 34 year olds has dropped by 10% in the period 1981 to 1996. Similarly, the 2001 Census shows that overall home ownership rate amongst all Australians has dropped from 69% in 1986 to 67% in 2001. Additionally, the Council of Australian Postgraduate Associations stated that “there had been little research on the social or economic impact of student debt so far”, but there is a strong likelihood that this would affect home ownership. Noting that the majority of first home buyers are aged in their twenties and thirties, the Commission might consider that further inquiry is warranted on this point.

17. The percentage of homes being purchased is falling as a result of declining home affordability, and private renters have increased in the last 20 years. See Reference B Table 1.

18. The period starting at 1980 with high affordability resulted in the highest home ownership over a 30-year period. This culminated in 1986 when affordability clearly diminished. The improvement over the two-year period 1992-1994 was not enough to sustain an increase in overall home ownership. Whilst Reference A notes the cyclical nature of housing demand and prices, the trend of low affordability cannot be rationalised as simply a short term phenomenon. Therefore, are many future young Australians to be denied home ownership and all the socio-economic benefits that go with it?

Implications for Society and Government

19. The REIA supports the objective of self-funded retirement particularly with respect to home ownership. Reference A does not appear to cover some major issues regarding the implications of home ownership for society and government.

20. Inter alia, the Commonwealth Government is broadly committed to the socio-economic development of Australia through a prosperous economy with policies that promote business development and self-funded retirement in order to ultimately help reduce reliance on Government support and the taxpayer. Self-funded retirement explicitly assumes home ownership. In the absence of home ownership, a retiree would need a superannuation fund of \$250,000 @ 5% pa, simply to rent modest accommodation at \$250 pw. This is beyond the scope of many Australians.

21. In the Commonwealth Government Report of May 2002, it was stated that: “While the population of labour force age is projected to grow by just 14%, the number of people aged 55 to 64 years old is projected to increase by more than 50% over the next two decades.” The proportion of the population aged over 85 years is expected to treble by 2042. Home ownership will play an increasingly important part in reducing Government expenses related to the health of an aging population.

22. Home ownership also contributes to self-funded retirement because it reduces housing costs in later life. This in turn results in lower take up rates of the age pension and relieves some of the burden on the Government of supporting an ageing society, particularly in the context of a shrinking tax base. Home ownership for the older generation means that they have low cost housing in retirement and an asset which can be used to obtain entry to retirement villages and nursing homes. If affordability of housing continues to decline, people now under 45 years old will find it more difficult to enter the property market. This implies that as retirees, they may have significant housing costs with implications for their lifestyle and increased dependency on Government.

23. Importantly, home ownership as part of self-funded retirement provides choices to individual Australians in terms of their lifestyle, and spending discretionary income which might otherwise be needed for rent. This lifestyle and increased discretionary spending is welcomed by individuals in their aspirations for retirement, and helps to support the wider community, eg tourism, retail and leisure sectors of industry.

Supply of Land and Houses

24. The REIA supports the Commission's general finding that the processes for supply of land and homes should be reviewed (by State and local governments) to improve efficiencies in order to help improve housing affordability.

25. In the REIA submission to the Productivity Commission, at Reference B, the REIA advocated benefit in Governments at the federal, State, and local levels working within the framework of a broad coordinated planning strategy. At Reference A Page 102, the Commission's "... preliminary view is that a national strategic planning framework would have difficulty accommodating urban and regional diversity".

26. The REIA reiterates the need for a broad nation-wide approach coordinated by a federal Government Housing Minister, which would acknowledge the importance of State and local governments addressing urban and regional diversity at local level. The nation-wide approach would address housing in the context of:

- a. regional policy to take account of immigration and demographic issues,
- b. affordable housing schemes such as the one advocated by the Australian Housing National Research Consortium,
- c. broad sustainability and environmental issues, and
- d. taxation reform (to be covered later in this paper).

Stamp Duty

27. The REIA advocates that stamp duty should be abolished, or at least indexed to account for thresholds in rising house prices. At Reference A, the Commission noted the inefficiency and inequity of stamp duty as follows:

- a. the escalation of stamp duty,
- b. the States apply stamp duty on top of GST,
- c. stamp duty is an inefficient tax compared to other taxes such as payroll tax and GST,
- d. stamp duty is essentially a mobility tax on moving residence and therefore a barrier to more efficient utilisation of the existing housing stock, and
- e. stamp duty increases the deposit gap or necessitates higher mortgages.

Whilst the REIA would agree with the Commission's view at Reference A Page 59 that "... stamp duties could only have a marginal direct impact on price trends...", it should be clear that stamp duty directly affects the affordability of homes for first home buyers, because of the deposit gap or need for increased mortgages.

28. Australia ranks the fifth highest nation in OECD countries in respect of its reliance on property taxes. Governments in Australia now collect nearly as much from property taxes as they collect from motor vehicles, general payroll taxes, and gambling taxes combined as shown at Reference B Table 3.

29. The significance of the reliance of the States on property taxes as a component of revenue from total State taxes and as a component of total State revenue is unjustified and discriminatory. Some States collect up to 30% of their taxes from property.

30. At Reference A Page 77, the Commission concludes that "... it is clear that land tax, payroll tax and the GST are all potentially more efficient ways of raising revenue than stamp duties" and acknowledged the input provided by a report from Access Economics which was commissioned by the REIA. Essentially, stamp duty should be eliminated or at least substantially reduced.

31. Notwithstanding that States are dependent on property taxes for revenue, there are economic benefits from a reduction of these taxes across the board. In the report commissioned by the REIA in 2000 ("The Economic Case for Cutting State Taxes on Real Estate"), Access Economics compared the net economic benefits estimated to be derived from a reduction of \$100 million in each of a range of different State taxes benchmarked against the net economic benefits from a \$100 million reduction in State payroll taxes. The key findings of the report were that:

- a. Reducing stamp duties on conveyances of non-residential property would result in gains to economic welfare, economic activity and investment many times greater than the gains from reducing payroll taxes by the same amount.
- b. Reducing any of the State taxes on property individually would provide economic benefits greater than the benefits that would be achieved by reducing payroll taxes by the same amount.

32. At Reference A Page 80, the Commission concludes that "... the case for indexing stamp duties is not compelling. Indeed, attempting to develop effective methods of indexation could divert attention from the need to replace stamp duties with more efficient forms of taxation". The REIA concurs that there is a compelling case to replace stamp duty. However, the REIA contends that any measure to reduce the burden of stamp duty will potentially help more Australians to become home owners in the shorter term, with all the attendant benefits of ownership.

33. Short of abolition, the current inequitable impost of stamp duties can be relieved by indexation. Because stamp duty scales have not been adjusted to reflect the recent increases in house prices, the percentage of stamp duty that is payable is increasing faster than the percentage increase in house prices.

34. The REIA commissioned Econtech to conduct a study of stamp duty on residential property. Econtech concluded that indexing the stamp duty by 20% would ensure that the FHOGS maintains its relative value. A comprehensive submission with modelling on stamp duties provided by the Real Estate Institute of Victoria to the Victorian Government in September 2002 proposed two alternative approaches to developing a stamp duty scale. One is based on dividing the sales for the previous year or for the previous four years into percentiles (at 10%, 20%, up to 90%) and establishing fixed stamp duty rates within each percentile category. The second method uses percentiles (e.g. at 20%, 40%, 60% and 80% in their model) to define the categories based on the previous year's sales history (or the previous four year average) and sets rates within categories that are progressive. See Reference B for a more detailed analysis.

Land Tax

35. At Reference A Page 77, the Commission suggests that "... in contrast to stamp duties, comprehensive taxation of land, based on unimproved values, is generally acknowledged as having efficiency advantages... It is also likely to provide a more stable revenue stream for governments than stamp duties". This suggestion is a concern for the REIA for the following reasons:

- a. land tax will provide a disincentive to already diminishing yields on residential investment properties, thereby potentially reducing properties for rental and causing rents to increase (for example, in some inner city areas, land tax already represents an impost of 40% of rent return after tax),
- b. self-funded retirees will potentially have land tax imposed on their meagre income with consequences for their life-style and well-being,
- c. many asset rich/cash poor self-funded retirees will have retired in areas where they have lived all their lives (inner city) or retired for lifestyle (coast) where high property values would significantly reduce their income or force them to move to more affordable areas, thereby also incurring associated change-over costs, and further limiting their lifestyle choices,

- d. land tax continues to discriminate against the people who would have sacrificed income over the years in order to own a home or investment, and
- e. there is no ongoing holding tax for other assets such as shares.

Other Taxation Issues

36. The REIA supports the statement at Reference A Page 81 in which "... the Commission considers that efficiency, equity, certainty and transparency would in principle be improved if taxes on taxes and multiple levying of tax were eliminated". It is deplorable that governments impose a tax on a tax.

37. The REIA concurs with "... the Commission's view, removal of stamp duties, and their replacement by more efficient forms of taxation, should be a priority. Many of these require more study than is possible in this inquiry". The REIA advocates that such a study should be in the context of a broad review for taxation reform.

38. In 2000, Access Economics provided a report for the Business Coalition of Tax Reform (of which the REIA is a member) titled "Business Tax Reform at the State Level: A Brief Overview of Unfinished Business After the New Tax System". This report essentially ranks the inefficiency of State taxes in order of priority in three groups: firstly, as stamp duties on non-residential conveyancing; secondly, stamp duty on residential conveyancing and land tax; and thirdly, payroll tax.

39. Property taxes are inequitable. Property taxes are fundamentally narrow-based wealth taxes which discriminate against property owners, particularly potential first home owners. Property taxes are aimed only at the property market (commercial and residential) and they affect small business, tenants, home owners, investors and self-funded retirees. Payroll tax is the most broad-based, stable, and robust State tax as shown in the report by Access Economics in 2002.

39. A review could be included as an extension of the review of the Intergovernment Agreement on the Reform of Commonwealth-State financial Relations of June 1999 (IGA) as part of the introduction of the New Tax System. There were a number of taxes identified for review by 2005 including stamp duty on non-residential conveyances. The objectives of the reforms set down in the IGA include the elimination of a number of existing inefficient taxes which are impeding economic activity. The Commission has identified other inefficient taxes such as stamp duty on residential property which should be reviewed and eliminated.

40. As part of the Business Coalition for Tax Reform, the REIA has provided governments with a proposed Terms of Reference for this review which should be conducted as an independent project.

Negative Gearing

41. The REIA concurs with the Commission's view at Reference A Page 88 that changing negative gearing on housing investment would have a range of detrimental flow-on effects to renters, other asset classes, and investment opportunities for

individuals. The rationale for negative gearing is that investors are entering into a business venture which might include buying a property for wealth creation. This is balanced by Capital Gains Tax if a profit is made when the property is sold. Negative gearing is not designed solely for the purposes of saving on tax. The profitability of a negatively geared investment depends on the ability of the investor to repay the mortgage and also depends on after-tax capital gain.

42. Negative gearing assists all income levels and is a key instrument to assist the wealth-creation process in a range of investments rather than only property. It is now much easier for would-be investors in residential property to get a start, since banks require very little capital to back negatively geared loans, and lines of credit have given investors access to funds that previously were not so readily available.

43. Investment in property does have an impact on overall house prices including the market for first home buyers. However, REIA supports the retention of negative gearing as a tax concession for investments in real estate property along with other asset classes for investment and business. Removal of negative gearing would discriminate against the real estate industry as does the retention of stamp duty on real property under the *ANTS*, and it would remove an important incentive to assist Australians to create wealth by investing in property to create wealth including self-funded retirement for their benefit and the benefit of the nation.

44. There are few opportunities for the average Australian, particularly PAYE wage earners, to create wealth to improve family life and prepare for retirement over many years. Wealth is created primarily by investment. Wealth gives people financial freedom and the ability to make life-style choices including education for children and self-funded retirement. Residential property is a relatively straight-forward asset class that most Australians understand and which offers rewards, particularly over the longer term. Unlike other asset classes, residential property offers equity which the individual can build upon. Negative gearing is an essential element of this opportunity.

45. Overall, there should not be any housing-specific changes to negative gearing (including depreciation) in the absence of wider tax review. Negative gearing should not be changed. However, if a review is proposed by the Commission, it should be a broad review of taxation including the interaction between provisions for deductibility of expenses (especially depreciation), negative gearing, capital gains tax, and general income tax structure – so that all asset classes are covered in the review, rather than only property.

First Home Owners Grant Scheme (FHOGS)

46. The REIA notes at Reference A Page 47 that “... while the FHOGS has brought forward some housing demand and has increased prices somewhat, its overall effect has been small”. The REIA supports the Commission’s view at Reference A Page 150 that “... although originally introduced to help compensate for the effects of the GST, the current FHOGS has characteristics that would be desirable in any ongoing assistance scheme for first home buyers:

- a. it is relatively simple and cheap to administer; and

- b. because grants are not tied to type of dwelling or to location, it provides flexibility for families to purchase houses that best suit their needs and preferences.

Indeed, if governments wish to continue to provide assistance to first home buyers, then the current FHOGS provides an appropriate basis for delivering such assistance”.

47. However, the Commission’s view is not supported, that “.. a deficiency in the present arrangements is their lack of targeting”. Simply, FHOGS is a fixed dollar grant that has not been adjusted as house prices have risen. It now makes a smaller contribution to the cost of purchasing a home compared to when it was first introduced. Thus, the relative value of the FHOGS has been reduced as house prices have risen.

48. If the FHOGS is indexed to the rise in median house prices, the grant will rise in line with the increase in price. This will prevent the relative value of the FHOGS from falling as a result of the booming property market. As shown in Table 1, indexing the grant means that the actual value of the grant would rise to over \$10,000 today. As such, the FHOGS would make a bigger contribution to offsetting the cost of buying a home for first home buyers. As shown in the Table, because the FHOGS is not indexed, the purchase of a new home today costs first home buyers around \$4,000 more than when the FHOGS was introduced in 2000.

Table 1: The Effect of Indexing the FHOGS

| | % increase in median house price | FHOGS- no indexation | FHOGS- indexation | Difference in FHOGS |
|------------------------|----------------------------------|----------------------|-------------------|---------------------|
| Australia ^a | 56.4% | \$7,000 | \$10,911 | \$3,911 |

^a Estimated from a weighted average of the increase in house price in each State since July 2000

49. Affordability indices that measure the affordability of housing do not take into account the FHOGS. When the grant was introduced it had a big impact on the number of first home buyers in the property market. The impact has lessened since then because the FHOGS relative value has decreased and its contribution to buying a home has been eroded.

50. The FHOGS should continue to apply equally to both new and established homes in order to provide choice to first home owners, ensure an equitable approach to home ownership, and not unduly skew one part of the marketplace.

51. At Reference A Box 10.1, the Commission has proposed modifications to the FHOGS. Implicitly, this endorses retention of the scheme as a means for governments to fulfil their long-standing commitment to encourage first home ownership. The first three suggestions are:

- a. applying a means test or both means and asset tests,
- b. adjusting the value of the grant according to income, and

- c. placing a cap on the value of the home.

52. Each of these three suggested modifications is a laudable attempt to target the lowest income earner and needy but they all fail to account for the real problem with the FHOGS – the value of the grant at \$7,000 has been, and will continue to be, significantly eroded by the increase in house prices. Additionally as part of asset/means testing, Government would need to develop specific proposals which account for potential practical shortcomings including the following:

- a. People who may have accumulated some other asset(s), eg a small parcel of shares, through prudent investment and who have relatively low incomes, may be forced to sell the asset(s) at a time not of their choosing in order to qualify for the FHOGS, and thereby possibly lose the benefit of that asset(s). In some cases, they will have accumulated the asset(s) to provide a home deposit.
- b. It is difficult for Government to decide an equitable level of income as a threshold because house prices vary so much between, and within, the States and Territories.
- c. The FHOGS did have the effect to bring forward some first home buyers. This was fortunate for them because otherwise the capital cost would have been greater, and the relative value of the grant much smaller, had they waited.
- d. A cap placed on the value of the home could not be consistent across, and within, all States and Territories; or for the different types of dwellings within the housing sector, or for the different family/personal circumstances of individual home buyers.

Even if these potential shortcomings were to be addressed, the real problem would remain to be addressed, ie the relative reduction in the value of the FHOGS.

53. A straightforward, consistent and relatively administratively simple approach is to index the FHOGS so that it remains useful. Payments for capital cities could be based on indexed values of the grant derived using REIA quarterly median house prices, and for regional areas, the indexes could be based on quarterly median house prices published by the State REIs. See Reference B for a detailed analysis of the case for indexing FHOGS.

Access to Superannuation

54. The REIA advocates that further detailed consideration be given to a scheme for early access to superannuation, including the examination of the benefits and implications of such a scheme.

55. Superannuation has an inherent contradiction in that young people must save earnings for their retirement but they may not be able to pay for a home now, and may not have a home when aged. Access to superannuation could help to bridge the

deposit gap. A recent report by Professor Julian Disney of the University of NSW commissioned by the REIA shows that this proposal could be examined to address a range of contemporary social concerns in Australia regarding affordability of education, health, housing, household debt and wealth generation.

56. Early access to superannuation for property purchase would promote home ownership in Australia and could alleviate the impact of a decline in affordability of home ownership. It could help first home buyers secure sufficient funds to pay deposits for home ownership, could provide some security in the event of severe difficulties in meeting mortgage payments (for example, if interest rates rose dramatically), and could allow home ownership to be an achievable goal for low-income earners in a high-cost housing market.

57. An early access scheme to superannuation could be targeted at people who would not otherwise be able to achieve full home ownership before or upon retirement. This could involve, for example, restricting access to first home buyers with incomes below a specified maximum, and limiting withdrawal amounts. Current rules which allow early access to superannuation due to financial hardship could be expanded. Future superannuation entitlements could be made available as security for loans for home purchases.

58. Potential concerns about early access to superannuation eroding retirement income could be addressed through promotion of strategies to unlock the value of retirees' homes through reverse mortgages or similar schemes and limits placed on the amount and timing of access to superannuation funds.

The Way Ahead

59. The Commission has conducted an extensive review of affordability for first home ownership and has comprehensively identified many issues which have contributed to the problem. The Commission has suggested further inquiry should be conducted on a number of issues including inefficient taxes and ways to improve the FHOGS.

60. The REIA advocates that the federal Government establish a forum at Ministerial level including federal Government, State/Territory Governments, and industry representatives to follow up on the Commission's report so that specific improvements can be identified and recommended to Governments for adoption. A nation-wide, whole of government approach with involvement by industry is essential to providing outcomes.

SUMMARY

61. Overall, the REIA considers that the Productivity Commission has provided a comprehensive report on the very important and complex issue of home affordability. The REIA proposes that:

- a. the FHOGS be indexed linked to account for rising house prices,
- b. negative gearing be retained for property,

- c. taxation arrangements be reviewed in the context of the Intergovernment Agreement on the New Tax System,
- d. federal Government establish a Minister for Housing and a nation-wide housing strategy be developed,
- e. the land and housing processes be reviewed, and
- f. a national housing forum of governments and industry be established to progress the Commission's report.

Prepared by:

Secretariat
Real Estate Institute of Australia

6 February 2004



REAL ESTATE INSTITUTE OF AUSTRALIA LTD

**EXECUTIVE SUMMARY OF REAL ESTATE INSTITUTE OF AUSTRALIA
SUBMISSION TO PRODUCTIVITY COMMISSION DISCUSSION DRAFT
OF FIRST HOME OWNERSHIP**

BACKGROUND

1. The Real Estate Institute of Australia (REIA) provided a submission dated October 2003 to the Productivity Commission Inquiry into First Home Ownership issues paper of September 2003. The Commission provided a draft discussion paper in December 2003 and this paper summarizes the REIA response to the Commission's paper.

OVERVIEW

2. The REIA generally considers that the Commission has provided a comprehensive report on the very important and complex problem of low home affordability. There are some issues of note.

ISSUES

Property Investment Advice

3. The REIA suggests that the Commission make a clearer distinction of the problem regarding the objectives of the government national Working Party which is to examine national regulation of property investment advice. The Working Party is concerned with marketeers and property investment seminar spruikers. Of itself, real estate practice is already extensively regulated by State and Territory governments, and it must comply with the provisions of Commonwealth legislation including investment advice under the Financial Services Reform (FSR) Act. The particular limits for provision of financial advice by licensed real estate agents are specifically well covered under the FSR Act.

Declining Home Ownership

4. The socio-economic benefits of home ownership are clear. Home ownership in Australia is falling, particularly in the age group 25 to 34 years old. The Commission's draft discussion paper does not appear to cover all the implications of this for society and governments. Governments advocate self-funded retirement but self-funded retirement assumes home ownership. Declining home ownership means that retirees may have significant housing costs with implications for their lifestyle and increased dependency on Government.

Federal Government Minister for Housing

5. The issues surrounding home affordability are complex and diverse. Further, and ongoing, attention is important. Therefore, the REIA advocates that the federal

Government appoint a Minister for Housing to work with State/Territory Governments and industry to:

- a. develop a nation-wide strategy to take account of issues such as affordability, demographics, regional and urban development, affordable housing, taxation reform, infrastructure, sustainability, and socio-economic development; and
- b. review the supply process for land and houses, in conjunction with local governments.

Stamp Duty

6. The REIA agrees with the Commission's finding that stamp duty is inequitable and an inefficient tax. State governments should not charge stamp duty on GST – tax on tax is iniquitous. It is clear that stamp duty directly affects the affordability of homes for first home buyers, because of the deposit gap or need for increased mortgages. Property taxes are fundamentally narrow-based wealth taxes which discriminate against property owners, particularly potential first home buyers.

7. Stamp duty should be abolished as part of the Government review of the Intergovernment Agreement in the New Tax System which is promised by 2005. In the shorter term, stamp duty should at least be indexed so that the thresholds account for changing house prices, in accordance with the model suggested by the REIA.

Land Tax

8. The Commission's suggestion that land tax is a more efficient taxation alternative to stamp duty is a major concern to the REIA. Land tax will provide a disincentive to already diminishing yields on residential investment property thereby potentially reducing the supply of property for rental and causing rents to increase. Self-funded retirees will have land tax imposed on their meagre income with consequences for their well being including forced sale and move to more affordable areas to live. Land tax continues to discriminate against the people who would have sacrificed income over the years in order to own a home or investment. Additionally, there is no ongoing holding tax for other assets such as shares.

9. There are more efficient and equitable alternatives to stamp duty and land tax which should be considered as part of a review of taxation proposed previously by the REIA.

Negative Gearing

10. The REIA concurs with the Commission's view, that changing negative gearing on housing investment would have a range of detrimental flow-on effects to renters, and investment opportunities for individuals. Negative gearing is a key instrument to assist the wealth-creation process in a range of investments rather than only property. Negative gearing should not be changed. But, any review should be done in the context of all taxes such as capital gains tax and income tax; and all asset classes.

First Home Owners Grant Scheme (FHOGS)

11. The REIA notes the Commission's finding that the FHOGS has increased prices somewhat but its overall effect has been small. The fact is that the relative value of the FHOGS has decreased significantly as a result of rising house prices. The REIA proposes that the FHOGS be indexed to the rise in median house prices; and continue to be applied equally to both new and established homes in order to provide choice to first home buyers, ensure an equitable approach to home ownership, and not unduly skew one part of the marketplace.

12. Other options for modifications to the FHOGS identified by the Commission have some practical shortcomings, including that house prices vary so much across Australia and with different sectors of the market.

Access to Superannuation

12. Access to superannuation could help bridge the deposit gap for first home owners. The REIA advocates that further detailed consideration be given to a scheme for early access to superannuation.

THE WAY AHEAD

13. The REIA generally supports the coverage of issues and findings by the Commission in the draft discussion paper. The REIA proposes that the Commission give further consideration to issues including:

- a. property investment advice,
- b. declining home ownership,
- c. federal Government Minister for Housing and development of a nation-wide strategy on housing including supply of land and housing,
- d. stamp duty,
- e. land tax,
- f. negative gearing,
- g. First Home Owners Grant Scheme, and
- h. access to superannuation.

14. The REIA also proposes that Government establish a national forum of governments and industry to ensure the Commission's work is used as a basis on which to develop specific recommendations for governments so that we can improve home affordability.

Prepared by:

Secretariat
Real Estate Institute of Australia

6 February 2004