Response to Inquiry into Land Transfer Duty Fees

APRIL 2023

AUTHOR: The Real Estate Institute of Victoria Ltd.

Introduction

The Real Estate Institute of Victoria Ltd. (REIV) is the peak professional association for the real estate sector across metropolitan and regional Victoria.

REIV members specialise in a range of real estate areas, including residential, rural, commercial and industrial leasing and sales, auctions, business broking, buyer advocacy, property management, owners' corporation management, and property valuation. REIV represents more than 80 per cent of businesses registered to carry out these services.

Real estate businesses employ more than 15,000 people in Victoria in a market that handles around $76 billion in transactions annually, totalling 20 per cent of Gross State Product. The significance of property related taxes to the Victorian economy makes REIV a major stakeholder in this discussion.

This submission outlines the REIV's position regarding land transfer duty fees, also referred to as stamp duty. It addresses each of the items listed in the motion agreed to by the Legislative Council on 22 February 2023. These items, and the REIV's respective responses, are detailed below.

Economic context

The property industry's contribution to the Victorian economy is significant; larger than the mining, agriculture, and manufacturing sectors combined.

Residential, commercial and industrial property owners and their tenants directly contribute billions of dollars in stamp duty, land tax and other state government charges, accounting for more than 40 per cent of government revenue.

The REIV strives to work with government collaboratively, to ensure that informed regulatory policy is developed that delivers certainty and fairness to all sector participants. With certainty and fairness, buyers and sellers, renters, and rental providers, selling agents, property managers and valuers, and marketing and media, have a level playing field to perform well.

REIV notes that the Inquiry into Land Transfer Duty Fees seeks to investigate issues around land transfer duties including potential transitioning to alternative taxation forms. This submission utilises extant research and draws upon the experience and expertise of industry members.

Recommendations snapshot

The REIV recommends that the Victorian government replaces Stamp Duty on land transfers with a broad-based tax.

A broad-based tax will:

- Create more efficient and equitable taxation distribution that enables greater housing accessibility.
- Provide a more stable and predictable government revenue source.
- Avoid the inefficient and disproportionate effects of house price bracket creep due to increasing median house prices.

In addition to the replacement of stamp duty with a broad-based tax, the REIV recommends:

- Refining first-home buyer incentives that better reflect market reality. Stamp duty concessions are largely ineffective as median house prices rise.
- Introduce a staged transition to a broad-based tax. The REIV would support a staged progression of the removal of stamp duty, consistent with the average buy-sell cycle of around 11 years.

The REIV acknowledges that it is critical for the State that taxation revenue levels be maintained. To this end, the REIV urges the Victorian government to invite stakeholders and experts to contribute to a road map that supports home ownership while maintaining an important tax income stream for the State.

Terms of Reference

1. Analysing the current situation regarding the land transfer duty tax and, reviewing:

(a) Impacts on labour and capital mobility:

Modelling has shown that stamp duty reduces mobility. It impacts mobility in multiple ways:

- Relocation for employment
- Relocation for personal preference
- Downsizing or upsizing based on housing requirements.

House price bracket creep has created an excessive burden upon home buyers. Stamp duty for the median priced house, currently sits at approximately 48.9% of average income.

Fluid mobility of skilled labour is a significant contributor for economic growth. Stamp duty increases the cost of moving. This can reduce labour mobility as people may choose to remain where they are rather than pursue job opportunities elsewhere due to the costs associated with relocation, of which stamp duty is a significant component. This lack of skilled labour clearly has a negative effect on productivity within the economy.

Existing homeowners are discouraged from moving due to significant costs and typically consider the financial costs and benefits of staying put, renovating or moving house. When homeowners decide to remain in accommodation that may no longer be best suited to their needs, housing supply for other buyer categories is affected. This in turn is considered to prevent the efficient up-sizing or down-sizing of housing across the market, creating a shortage of housing suitable for stage of life requirements.

(b) Revenue predictability:

The very nature of land transfer tax is dependent upon market activity and performance. Levels of market activity ebb and flow, generally in response to economic fluctuations and the various forces placed upon a free market. Recent examples include limitations on real estate activity during COVID lockdowns and increases in interest rates. These factors, amongst others, influence individual decisions to engage, or not engage, with housing markets, which in turn impacts government revenue.

Downturns within the economy have a negative impact on households, often resulting in pressure upon governments to support struggling households. At times when Victorians may require greater government support, the State would likely experience reduced revenues. A slowing property market, including housing, results in reduced revenue for government placing further fiscal pressure on government. In other words, when households are in need, government revenue is likely to also be impacted making meaningful policy intervention more difficult.

Table 1, below, highlights this point. The column titled “Growth (%)” shows the fluctuations in tax revenue through various property market cycles. Some of the financial years reported show stamp duty revenues have been severely impacted, which undoubtedly would cause significant budgetary concerns.

Table 1: Stamp Duty revenue fluctuations (source: State Revenue Office)

	Revenue ($m)	Growth (%)
1996-97	$1,152.9	
1997-98	$981.0	-14.9
1998-99	$1,006.2	2.6
1999-00	$1,293.7	28.6
2000-01	$1,284.0	-0.7
2001-02	$1,885.2	46.8
2002-03	$2,115.7	12.2
2003-04	$2,445.6	15.6
2004-05	$2,337.2	-4.4
2005-06	$2,671.2	14.3
2006-07	$2,961.4	10.9
2007-08	$3,705.6	25.1
2008-09	$2,801.0	-24.4
2009-10	$3,603.9	28.7
2010-11	$3,909.9	8.5
2011-12	$3,307.0	-15.4
2012-13	$3,276.1	-0.9
2013-14	$4,167.5	27.2
2014-15	$4,938.3	18.5
2015-16	$5,838.8	18.2
2016-17	$6,133.7	5.1
2017-18	$6,932.7	13.0
2018-19	$6,008.7	-13.3
2019-20	$6,142.6	2.2
2020-21	$6,424.5	4.6
2021-22	$10,361.1	61.3

(c) Efficiency of resource allocation;

Stamp duties are an inefficient tax because they are narrow based. Meaning they are infrequent and target a small segment of society, thereby moving monies away from consumption-based taxes. Additionally, they distort the market by adding a significant burden to market participants. Participants may avoid market transactions by renovating, not moving, or not entering the property market. Such options are available to second and subsequent homeowners who may hold onto housing that would otherwise benefit first-home buyers. Adding stamp duty to the purchase price makes it more difficult for people to enter the market and break out of the rental cycle. Right sizing of property is an important factor in addressing the housing shortage. If older Victorians had an efficient way to downsize without using their retirement savings towards a payment that provides no return, it could make more stock available for younger families – creating a more efficient market.

Further, as many older Victorians are residing on traditionally larger parcels of land, enabling more tax efficient downsizing opportunities would potentially release more land for in-fill subdivision, thus helping alleviate the current Victorian housing crisis.

Another little-known housing fact is that liquidity has fallen while stamp duties as a proportion of median house prices and average earning has risen. Liquidity is defined as the proportion of houses that are on the market as a proportion of housing stock. SQM Research (2021) found in 2012, 3.2% of Melbourne's detached housing stock was available for sale. In 2021, this proportion fell to 1.5%. When considering all housing stock, liquidity fell from 3.4% in 2012 to 2.1% in 2021. This has a direct impact on house prices because of supply and demand influences. Over the period 2011-2021, stamp duty as a proportion of median house price rose from 3.2% to 4.2%. As a proportion of annual average earning in Melbourne, stamp duty currently sits at 48.9%. This is up from around 30% some nine years ago. The impact of stamp duty on households at a time of financial vulnerability is obvious.

Currently independent data suggests only 18.5% of properties for sale in Melbourne fall under the $600,000 threshold for stamp duty exemption. Additionally, the current median house price in Melbourne is $975,000, this is $275,000 above the threshold for stamp duty exemption. The prevailing stamp duty thresholds are not in line with market reality. A broad-based tax framework has the potential to address issues inherent in the current system.

Numerous academic papers have found a link between the existence of stamp duty and the reduction of property turnover. The extent that the removal of stamp duty would have on property markets is subject to modelling but that it will have a positive impact is considered to be established.

Environmental context

When place of employment or education for homeowners changes significantly, stamp duty is an impediment to relocation. As a consequence, greater pressure may well be placed on Victorian transport infrastructure and systems at a cost to government and the environment. Longer commutes place strain on individuals, their families and potentially on the health system.

Homeowners ready to down-size from properties on large blocks are reluctant to do so due to the stamp duty implications. Land suitable for redevelopment is locked up, hindering population growth in areas that may have well established public transport and related infrastructure.

(d) Effects on housing supply and development;

Typically, housing supply comes from the release of new land for residential subdivision and in-fill development (dividing of larger allotments within the existing urban environment). The recently introduced Windfall tax will have an influence on these developments with the suggestion that the tax will be passed onto end users. The debate regarding this is not addressed in this submission. However, it should be noted that land transfer tax is calculated upon the contract, which is likely to include the windfall tax, thus further adding to the cost of housing provision. The removal of transfer tax would help in reducing the cost to the end user, making land more affordable.

New South Wales treasury report (2022 p3) evaluating property tax and home ownership noted that replacing land transfer duty with a broad-based tax would enhance home ownership rates. The key points being made to support this were:

- Replacing transfer duty with a broad-based tax, in the NSW case, annual land tax. Such a broad-based tax is likely to increase the frequency of dwelling sales through reduced upfront buying costs and lower savings required.
- That tax rates be structured in favour of owner-occupiers, to encourage purchases. This would further assist first-home buyers.

(e) Overall tax efficiency.

Tax is necessary. Efficient tax that is balanced across society and is predictable, enables responsible planning by governments to meet the needs of the society it serves. It is well established in economic literature that stamp duty is one of the most inefficient taxes with an estimated welfare cost of 35 cents lost for every dollar raised (HIA 2011). This loss, referred to as welfare loss, refers to the decrease in social and economic well-being caused by imposition of the transfer of purchasing power from the taxpayer to the taxing authority.

The Henry review (2009 p48) notes: "*Stamp duties are a highly inefficient tax on land, while land tax could provide an alternative and more stable source of revenue for the States*." This view is held by numerous economists. REIV members attest to numerous instances of clients being concerned of the impact of transfer tax on their ambitions.

2. Examining potential alternatives to land transfer duty, assessing models from interstate and international jurisdictions, noting the pros and cons of various proposed or implemented solutions; and

The REIV advocates for a review of alternatives by a wide range of experts. The options may include a broad-based GST, or other efficient taxation form as determined by those who are expert in the field. There is extensive literature highlighting the inefficiencies of transfer tax and impacts on markets and households and the need for reform is clear. REIV understands that the question to be addressed is “How”.

Key concerns in transitioning from land transfer tax to more efficient forms of tax are generally considered a major hurdle for governments due to the immediate impact upon budget revenues. However, efficient tax that is balanced across society and is predictable, enables responsible planning by governments to meet the needs of the society it serves. Therefore, alternative tax arrangements must equate over the transition period, to provide governments with approximately equivalent levels of revenue. Economic modelling is clear in that annualised land tax or a GST amendment, which would only need to be minor, would achieve this. The issue, therefore, is a discussion about and modelling of alternative models and their impact on Victorians.

As the committee would be aware, the Australian Capital Territory has entered a 20-year transition term for the removal of stamp duty to an ongoing land tax arrangement. This was done to provide equity to those who had recently purchased and avoid a double “tax hit”. Such a system has the potential to create initial uncertainty and concern among homebuyers and would require the Victorian government to provide clarity of purpose and intent of the process and impact upon buyers. This model is not recommended by the REIV.

NSW has introduced a reduced form of the ACT approach with first-home buyers being offered the option of stamp duty or ongoing land tax. If the land tax option is selected, then the subject property remains permanently locked into land tax. Future buyers will not be able to select transfer duty. This approach is very likely to extend beyond the 20-year option of the ACT.

Internationally, land tax is typically based upon unimproved value. There appears to be consensus that taxing improved property disincentivises development, further compounding housing shortages. The Grattan Institute (2019) proposed a broad-based tax calculated against the unimproved land value of all property types, including owner-occupied residential property, should replace transfer tax. The pros and cons of such a tax are:

Pros

- Reduced market distortion
- Will not impact land use because the unimproved value will remain the same irrespective of any improvements.

- Enables collection through council rates. The system is in place for evaluation of unimproved value, thus no further infrastructure is required.
- Properties that are currently exempted from council rates could remain so if land tax is collected through councils.
- More stable and predictable tax revenue

Cons

- Potential to impact negatively on asset-rich, cash-poor households such as retirees and those on the federal government social security payments who own their own home.
- Councils are likely to request financial support to isolate tax revenue destined for state government and deal with public inquiries/complaints as numbers of annual objections to assessed values may increase.
- Transition is likely to attract negative publicity and exposes the potential for unjustified and/or false claims of societal impact.
- Without appropriate measures, recent homebuyers will be required to pay double tax. That is stamp duty and then ongoing broad-based tax.

The period of transition from transfer tax to broad-based tax is important. The longer the transition period, the more likely it will remain confusing to members of the public and it is possible subsequent governments will alter/reverse transition arrangements. Thus, a short transition period is desirable. This period could be based upon average "hold period" of houses (the average duration of time a household retains a house after purchase before reselling it for whatever reason). For example, some sources suggest the average period households remain in a property is approximately 11 years. On this basis, an 11-year transition rate could be reasonably argued.

Another possible replacement of lost tax revenue caused by the removal of transfer tax is to increase the current GST levy. Some sources suggest an increase as little as 0.5% may address many of the nation's housing needs.

Summary

The REIV advocates:

- A broad-based tax that is equitably distributed throughout society;
- If a broad-based land tax option is to be considered, then it be calculated on the unimproved value;
- Transition time to a new system should be minimised to avoid potential market confusion.

3. Any other related matters

The following is a summary of the issues regarding stamp duty that have been frequently raised in publications. Stamp duty is:

- An inefficient tax,
- Levied at a time when buyers are most financially stretched,
- Inhibits house market movement, thereby reducing the availability of suitable and needed houses to home buyers. This is because of older people avoiding downsizing as it is too expensive to move,
- Creates house price issues through affecting supply,
- Further creating inequality throughout the spectrum of society,
- Affects job mobility due to moving costs,
- Is seen as difficult to change because it is a change from a transaction based to recurrent tax.

These points are discussed in detail throughout the publications and meticulous reproduction of such narratives here would serve little purpose. However, to assist with the understanding of the rationale behind these important considerations, Table 1 provides a concise critique of the main points raised.

Table 2: Issues raised in previous publications.

Stated issue	**Rationale**
An inefficient tax,	Stamp duties are an inefficient tax because they are narrow based. meaning they are infrequent and target a small segment of society, thereby moving monies away from consumption-based taxes. Additionally, they distort the market by adding a significant burden to market participants. Participants may avoid market transactions by renovating, not moving, or not entering the property market. Such options are available to potential second and subsequent homebuyers who may hold onto housing that would otherwise benefit first-home buyers.
Levied at a time when buyers are most financially stretched,	The net effect of taxing at the point of purchase is that buyers consider the “entire” cost of acquisition. This has a negative effect on house prices and causes further financial vulnerability for the buyer. Removal of stamp duty is likely to attract further investment into housing.

Inhibiting house market movement, thereby reducing the availability of suitable and needed houses to home buyers. This is because of older people "sitting" on their large houses as it is too expensive to move creating a mismatch of housing,	Modelling has shown stamp duty reduces mobility. Existing homeowners are discouraged to transact and typically contrast the option of renovation to the cost of moving. In doing so, when renovation is chosen, housing supply to buyer categories is further limited. This in turn can prevent the efficient up-sizing or down-sizing of housing across the market.
Creating house price issues through affecting supply,	Inelastic markets are ones where the supply and demand of goods and services are not significantly affected by price changes. Tax structures should aim to ensure minimal impact on markets. Stamp duty has been shown to significantly impact property prices and therefore is seen as a hindrance to market activity.
Further creating inequality throughout the spectrum of society,	The burden of transfer stamp duty is not equally shared across housing markets. Stamp duty, as a proportion of wages has risen. In 2012, Stamp duty as a proportion of the average earnings was 30.5%. In 2021, this rose to 48.9%. This further exacerbates the buying burden and availability of housing.
Affecting job mobility due to moving costs,	Stamp duty increases the cost of moving. This can reduce labour mobility as people may choose to remain in place in favour of further job opportunities due to the costs associated with relocation, of which stamp duty is a significant component. This has a negative effect on productivity within the economy.
Probably avoiding because transitioning from transaction-based tax to recurrent tax is considered difficult.	Literature has acknowledged the difficulties in transitioning from a transaction based to a broad-based taxation framework. However, it is generally agreed that this should not deter governments from making such a move as the long-term benefits notably outweigh the ephemeral concerns.

References

Coates B, and Nolan J. *NSW should swap stamp duties for a broad-based property tax.* Grattan Institute; 2019, Available from: <https://grattan.edu.au/wp-content/uploads/2019/12/NSW-productivity-Commission-Tax-submission-final-standalone.pdf>

Henry K, Harmer J, Piggott J, Ridout H, Smith G. *Australia's future tax system: report to the treasurer.* Canberra: Commonwealth of Australia; 2009 Dec Available from: http://www.taxreview.treasury.gov.au/content/downloads/final_report_part_1/00_AFTS_final_report_consolidated.pdf.

HIA (2011), *Tax Forum,* Housing Industry Association Submission to the Tax Forum, <https://treasury.gov.au/sites/default/files/2019-03/Housing-Industry-Association-1.pdf>

June 2021: TTRP 21-08
Treasury Technical Research Paper Series: The economic costs of transfer duty: a literature review. <https://www.treasury.nsw.gov.au/sites/default/files/2021-06/the_economic_costs_of_transfer_duty_a_literature_review.pdf>

SQM Research (2021), *Stamp Duty: The Relationship to Australian Housing Affordability and Supply,* SQM Research prepared for the Real Estate Institute of Australia, <https://sqmresearch.com.au/Stamp_Duty_2021.pdf>

Mawby N, (2022), *Melbourne first-home buyers running out of options for government help.* published in REA Group
<https://www.realestate.com.au/news/melbourne-firsthome-buyers-running-out-of-options-for-government-help/>