

To Senate Standing Committees on Economics
Affordable Housing Inquiry 2013
Name and address: withheld

Dear Sir/Madam,

Thank you for accepting this submission to the Senate Inquiry into Affordable Housing.

Introduction

An Inquiry into affordable housing is really an inquiry into affordable land.

A fairly priced market in housing and land will only exist if it is protected by a regime of inter-governmental agency checks and balances. These balances limit opportunistic and self-interested manipulations by special interest groups.

Had recommendations of previous housing affordability Inquiries been adopted, it is likely this issue would not be the subject of this Inquiry today. It can be argued that a lack of political will to enact policy revisions is holding back reform.

So, why have most recommendations from past Inquiries not been actioned?
Is the reason for inaction based on petty self-interest, a desire to protect one's asset base? Understandable - but if so, is this straying into the area of conflict of interest?

High land cost is not only a hurdle to those starting out in life wanting to buy a home but imposes drag on the wider economy. The high cost of land is one the main factors for the decline in vitality of the manufacturing segment of the national economy.

The current distortion in the price of land has multiple causes.

Much as squeezing a balloon simply causes deformation but no loss of volume, attempting to address this multi-dimensional affordability problem in a piecemeal manner will prove ineffective. To slowly deflate land cost, and make sure it does not inflate again, requires that all facets of the problem be tackled simultaneously.

To bring the cost of land to an affordable level therefore requires a whole of government approach - Federal, State and Municipal.

This is the 3rd Inquiry in 10 years to directly look at housing affordability. After reviewing the work of earlier Inquiries and other literature, it is difficult to believe this matter is being taken seriously. The reasons for political reluctance in not addressing inequities within the system need to be explored. Calls for a Royal Commission into the Real Estate Industry as a whole are premature. I believe a Senate Inquiry into government policies, as they relate to land supply, demand and pricing is in order.

The previous two Inquiries related to affordable housing issues are:

1. *First Home Ownership* Report, Productivity Commission Inquiry, 2004
2. *A Good House is hard to find* Report, Senate Select Committee on Housing Affordability in Australia, 2008

Previous Inquiries provided thorough analysis and sound recommendations. I again trust the Inquiry panel to make intelligent recommendations to address this problem.

Summary:

- Government policies are negatively impacting on land prices - the current tax regime facilitates property speculation, land supply policies do not match demand, lax lending standards are only casually supervised, a Claytons policy of rapid population growth is not being matched by infrastructure and services – all of these policies need to be revised;
- Government needs to articulate a Population Policy;
- There is an annual cost to government in terms of: tax exemptions for home owners (\$36B) & generous tax losses allowed property 'investors' (\$7B); collateral damage to business with higher start-up and running costs;
- There seems two possible ways to improve land supply - either fully privatise land supply or use forced land acquisitions against select land-banking entities;
- Land value tax can replace existing income & consumption taxes such as Stamp Duty – a recommendation of the Henry Taxreview, an Inquiry subject in itself;
- Vacant land and speculative hoarding can be addressed with higher taxes;
- Tax system facilitates speculation and needs revision – poorly targeted negative gearing and Capital Gains Discount allowances, misuse of speculative Interest-only Loans and highly leveraged Equity Loans for existing property;
- Assistance to first home buyers is inflationary;
- Self Managed Super Funds (SMSF) - SMSF loans for residential property are not full recourse; possible danger to government with taxpayer bail-out of lenders;
- RE industry is in need of greater accountability - what is the role of lobbyist, time to ban the nonsense of vendor bids, reduce excessively high sales commission down to 1%, sales data to be made public as is the case of share prices, proof of Australian citizenship or visa status needs to be shown at sales;
- Allowing Temporary or Student visa holders to buy existing dwellings needs to be explained - how exactly does such a sell-off help housing affordability;
- Senate Inquiry into government policies, as they relate to land supply, demand and pricing is in order. Such an Inquiry should include a focus on the effect of Real Estate Industry lobbying on policy formulation.

Land price inflation and the impact of government policies

The high cost of housing in Australia is well documented, with all major cities and some provincial ones regularly appearing on global lists of most unaffordable cities.

As noted in the Executive Summary of *A Good House is hard to find* Report, "the average house price in the capital cities is now equivalent to over seven years of average earnings; up from three in the 1950s to the early 1980s."

The Institute of Public Affairs (IPA) in a paper titled *How land supply restrictions have locked young people out of the housing market* noted that, "Adjusted for inflation, the price of houses in Australia has more than doubled (trebled in Sydney and Perth) over

the past 30 years. . . costs were shown to be derived from state governments and local authorities acting to restrict the availability of land for housing.”

According to Senator Bob Day in his 2013 paper *Home Truths Revisited*, “For more than 60 years the average Australian family was able to buy its first home on one wage. The median house price was around three times the median income. Young couples got into the housing market relatively easily and worked up from there.”

In addition to the relative cost increases and supply restrictions above, land plot sizes are now less than half that of 30 years ago making value anomalies even greater.

This evidenced land price inflation can arguably be traced back to policy areas over which all levels of government have authority, for example:

- tax policies - facilitate and reward property speculation;
- land supply policies – supply is not matched to population growth demand and is inequitable in comparison with earlier arrangements;
- lending standards – relaxed over time, almost casual oversight by Australian Prudential Regulation Authority (APRA); APRA inexplicably sees no inflationary effects from over-use of Interest-only Loans, Equity Loans and high LVRs;
- population growth policy – a Clayton’s policy, run on an ad-hoc basis, marginal planning in terms of appropriate infrastructure & services required;
- FIRB policy facilitates the sell-off of residential real estate to Temporary Resident and foreign Student visas holders. It is time the relevant Minister explains to a Senate panel exactly how opening the market in existing homes to this group of buyers helps housing affordability.

Population Policy

It was noted in ‘*An Australian Population Policy – Research Paper 17*’ that Australia's population policy, rather than being articulated, “ is implicit in its immigration program, but it is a policy by stealth, a policy without consensus, and a highly erratic policy, as exemplified by the wild swings in immigration targets over time. This is not a satisfactory situation.”

For a government to allow this important matter to simply drift along with ad-hoc forward planning in a policy vacuum is incomprehensible. Population growth needs to be managed as it cuts across many government programs, including those dealing with immigration, family and social welfare, education, health, employment, regional development and urban planning, etc. It seems that both major parties believe in, or have been sold on, the idea of ‘Big Australia’ by lobbyists. The notion of an unplanned for, underfunded ‘Big Australia’ needs the reality check of incisive Senate questioning.

Australia needs a Population Policy.

The cost to taxpayers, loss of revenue; collateral damage to business

As noted in a 2013 report Grattan Institute, *Renovating Housing Policy*, “home owners profit from government outlays worth about \$36 billion a year. This is mainly the result of exemptions for the family home from land and capital gains taxes and the

eligibility test for the aged pension. Negative gearing rules, and the capital gains discount introduced in 1999, provides residential property investors with nearly \$7 billion a year. . . Private renters, by contrast, receive very little support through the tax and welfare system, even though they make up nearly one in four households.”

Businesses become collateral damage with capacity constraints being caused by high land valuations. Start-up costs for new businesses and the running costs for existing ones are higher than would otherwise be the case in a properly functioning market.

Improve land supply - either privatise land supply or force land acquisitions

Senator Bob Day, in his paper *'Home Truths Revisited'*, notes that “Since its inception in 1973, the South Australian State Government's land agency has seen land prices rise from \$15,000 per block (in current dollars) to \$160,000 per block, more than a tenfold increase. By comparison, the cost of building a 135 square metre house increased from \$97,000 in current dollars to just \$102,000 over the same period, virtually no increase at all. . . - a ten-fold increase for a commodity (land) controlled by government (with a so-called "price containment" policy), compared with virtually no increase at all for a commodity (the house) controlled by the private sector (with no price containment policy).”

One way to restore housing affordability, in the Senator's words, “lies in governments stepping aside from the land management role and allowing the natural forces of supply and demand to return to the market. . . home buyers should not have to pay for their infrastructure “before” they use it but should be allowed to pay for it “as” they use it as was the case in previous generations.”

The current front-loading of infrastructure costs for land release could be replaced by a comprehensive land value tax structure, one of the recommendations of the 2010 Henry Taxreview. Further investigation of a Land Value Tax could be considered a recommendation for this Inquiry and would make the subject of an Inquiry in itself.

Alternately, the Australian government could use more forcefully a German style compulsory acquisition land policy, applying it to land-banking entities. The German government has a system of “compulsory acquisition” (*Basic Law (Constitution) of the Federal Republic of Germany, Article 14 (3)*). As noted in Article 14(3), “Property entails obligations. Its use shall also serve the public good.”

The policy could target land-bankers deemed to be causing artificially high demand and excessive prices by withholding or drip-feeding supply. Land acquired could be used to fill land quotas that planners designate for urban expansion each year. Land sitting idle for more than say five years could be the subject of such resumption.

Vacant land

Underutilisation of land creates the artificial appearance of a shortage in property.

Earthsharing, in its 2009 paper '*I want to live here*', investigated speculative land hoarding in Melbourne. It calculated that up to 1 in every 15 Melbourne properties are vacant. Melbourne would not be the only capital city where this is happening.

If there were a genuine market in land, then local government rates or state land taxes would be set at a rate to make the owners of vacant or underused land either use the land or else sell the land.

The Australian Bureau of Statistics (ABS) could be asked to gather Genuine Vacancy Rate statistics so as to reveal the degree of speculative land hoarding.

Tax system facilitates speculation

The current tax system has effectively turned shelter into a speculative commodity.

Tax regulations seem to be designed to increase the trading temperature of the market. The elements of tax policy that seem to exacerbate land prices include:

- allowing negative gearing to be claimed on existing dwellings;
- generous Capital Gains Tax discount;
- allowing speculative Interest-only Loans and highly leveraged Equity Loans to be used for purchase of existing homes;
- access to high Loan to Valuation Ratios across the board

Negative gearing, supposedly designed to promote new construction, attracts only one dollar of every twenty dollars in investment loans. In other words, the other 95 percent of negatively geared investment loans are used to buy existing dwellings. This does little for construction activity, offers investors a tax advantage to outbid other buyers at sales, and creates more systemic debt into the bargain. Allowing negative gearing to be claimed for purchase of existing dwellings is inflationary in effect.

Any change to the treatment of negative gearing would need to also apply to shares. For example, only new shares bought at Initial Public Offering issue would be eligible.

Assistance to first home buyers

Economist Saul Eslake recently had this to say about *First Home Buyer Grants*: "It's hard to think of any government policy that has been pursued for so long, in the face of such incontrovertible evidence that it doesn't work, than the policy of giving cash to first home buyers in the belief that doing so will promote home ownership."

The observed effect of such grants is that they push up the price of homes as soon as such a grant is announced. Any subsequent increase in grants is matched by an even greater upward movement in home prices. The use of First Home Buyer Grants, as an adjunct of housing affordability, has proven a failure.

Self Managed Super Funds (SMSF)

From an Australian Financial Review article recently (Morgan Stanley chief warns SMSFs 'sowing seeds of next finance wreck'): "the vigour with which investors are borrowing money in their self-managed super funds to buy property" was "sowing the

seeds of a future economic wreck. . . we have a tax system and culture that drives property investment in a way that can lead to its own strong risks. . . I think the single biggest economic wreck – and one that will occur in this country in the next five to 10 years – will be in the SMSF space.”

One of the main dangers in allowing SMSFs to enter the residential property market is that the loans used by SMSFs are not full recourse. If a downturn in property values does occur, then it is possible that government, read taxpayers, will be required to bailout or subsidize losses incurred. SMSFs are supposed to be used as a nest-egg for retirement, not as a leveraged vehicle to further facilitate gambling in real estate.

One solution to limit lending dangers caused by over-zealous SMSF borrowing is for government policy to mandate loans as full recourse and on low LVRs, say 50 percent.

RE industry needs to be more accountable

- Do political donations inadvertently nurture a conflict of interest mentality?
- What is the point of ‘Vendor bids’ – does the vendor really want to buy their own property? Former ACCC Chairman, Graeme Samuel, once noted there is little difference between vendor bidding and dummy bidding, and that vendors have no more intention of buying their own properties, than “the tree or the gnome in the garden.”
- Adjusted for inflation, housing debt repayments have more than doubled compared to a decade ago, is it time to mandate the halving of RE sales commissions to a maximum of 1 percent, rather than current rate of 2 percent?
- Just as the sale price of shares is listed publicly, the price of properties sold needs to be public knowledge as an aid to market transparency. Agents could submit to a government Agency this information the day of sale and again subsequent to settlement. This data should be easy to access by the public, eg. on State of sale and Federal government websites.
- Proof of Australian citizenship or visa status to be lodged at all sales.

List of Recommendations:

1. Government draft a Population Policy so as to properly manage resource and administrative issues which includes housing and urban development;
2. Allow negative gearing claims for new construction only, apply grandfathering provisions to negative gearing for existing dwellings;
3. CGT discount, as recommended by AFTS, move to "more neutral personal income tax treatment of private residential rental investment . . . through a 40 per cent discount on all net residential rental income and losses, and capital gains";
4. Land value tax to replace Stamp Duty, income and consumption taxes;
5. Increase land taxes on vacant land or vacant property held by absentee landlords for more than say 2 years;
6. Removal of First Home Buyers assistance;
7. ABS publish data related to land price inflation as part of the CPI;
8. ABS gather Genuine Vacancy Rate statistics so as to reveal degree of speculative land hoarding in major cities;
9. APRA reports to the Senate on the inflationary impact of Interest-only Loans, Equity Loans and high LVRs on land values;
10. Commission a study into land-banking, urban planning and the role of Government in facilitating affordable land releases;
11. Commission a comparative study into the benefits of private industry assuming control of land releases versus a German style system of meeting demand via "compulsory acquisition" from land-banking entities;
12. Legislate that SMSFs only use full recourse loan arrangements on low LVR;
13. Ban the use of Vendor bids at property auctions;
14. Mandate that property sales commission be set at maximum of 1 percent;
15. RE agents update a government website designed to capture property sale price data and this data is made publically available, as are share prices;
16. Proof of Australian citizenship or visa status to be lodged at all sales;
17. FIRB publishes data on all sales to foreign buyers of residential real estate;
18. Appropriate government Minister to appear before the Senate and explain how allowing Temporary residents & foreign Student visa holders to purchase existing residential real estate improves housing affordability;
19. Politicians submit to the public record the subject of talks they have with property lobbyists, registered and unregistered;
20. Senate Inquiry into government policies, as they relate to land supply, demand and pricing is in order. Such an Inquiry should include a focus on the effect of Real Estate Industry lobbying on policy formulation.

Thank you for this opportunity to make a submission on Housing Affordability. I hope you can enjoy the exercise of juggling the pros and cons of the many arguments and recommendations you receive from all submissions.

Resources

An Australian Population Policy *Research Paper 17 1996-97*

http://www.aph.gov.au/About_Parliament/Parliamentary_Departments/Parliamentary_Library/pubs/rp/RP9697/97rp17

2004 Productivity Commission Inquiry Report titled 'First Home Ownership'

2008 Senate Select Committee on Housing Affordability in Australia

2009 Earthsharing study 'I want to live here'

<http://www.earthsharing.org.au/2009/11/25/i-want-to-live-here-report-2009/>

2010 'Australia's Future Tax System' (AFTS) or Henry Taxreview

2010 Dr. T.Dwyer 'Land value taxation solving the efficient tax problem'

<http://www.prosper.org.au/2009/05/21/land-value-taxation-solving-the-efficient-tax-problem/#>

2013 Prosper Australia paper: 'Land Bubble, Tax Bubble' <http://www.prosper.org.au/>

2013 Senator Family First Bob Day, 'Home Truths Revisited'

<http://www.familyfirst.org.au/files/Home-Truths-Revisited-May-2013.pdf>

2013 Grattan Institute, *Renovating Housing Policy*

<http://grattan.edu.au/publications/reports/post/renovating-housing-policy/>

2013 Saul Eslake '50 years of housing failure'

<http://www.prosper.org.au/2013/09/03/saul-eslake-50-years-of-housing-failure/>

2013 Australian Financial Review: Morgan Stanley chief warns SMSFs 'sowing seeds of next finance wreck'

http://www.afr.com/p/business/financial_services/morgan_stanley_chief_warns_smsfs_AFjp2spVpG51XM2rtYdr5K