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**REAL ESTATE INSTITUTE OF AUSTRALIA  
COMMONWEALTH GOVERNMENT  
PRE BUDGET SUBMISSION 2012/2013**

**PURPOSE**

In the context of the preparation of the 2012-2013 Budget the Real Estate Institute of Australia (REIA) seeks the Commonwealth Government's consideration of the following:

- Retention of current arrangements for negative gearing of property investments
- No Capital Gains Taxes on the family home
- No increase in Capital Gains Tax on property investments
- Removal of stamp duty on property transactions
- Increase the amount of the First Home Owners Grant
- Allowing first home buyers access to their superannuation for the purchase of a home
- Monitor HAF and NRAS to observe its effects on housing supply and to conduct a review which considers additional measures to bridge the demand - supply imbalance.
- Ensure that the National Housing Supply publishes its *State of Supply Report* in a timely manner.
- Appointment of a National Small Business Commissioner

**BACKGROUND**

The REIA is the peak national association for the real estate profession in Australia.

The REIA's members are the State and Territory Real Estate Institutes, through which around 80% of real estate agencies are collectively represented. The real estate industry employs approximately 80,000 people. The REIA represents an important element of the broader property and construction sector which together makes a significant contribution to Australia's social climate and economic development. Property contributes \$300 billion annually in economic activity and played an integral role in the Government's response to the global financial crisis.

Importantly, REIA represents an integral element of the small business sector. According to the ABS statistics, 73% of real estate agency businesses employ

fewer than 10 employees (over 50% of this portion employed fewer than 5 employees). Only 0.6% of businesses employ 50 or more persons.

## **CONTEXT OF SUBMISSION**

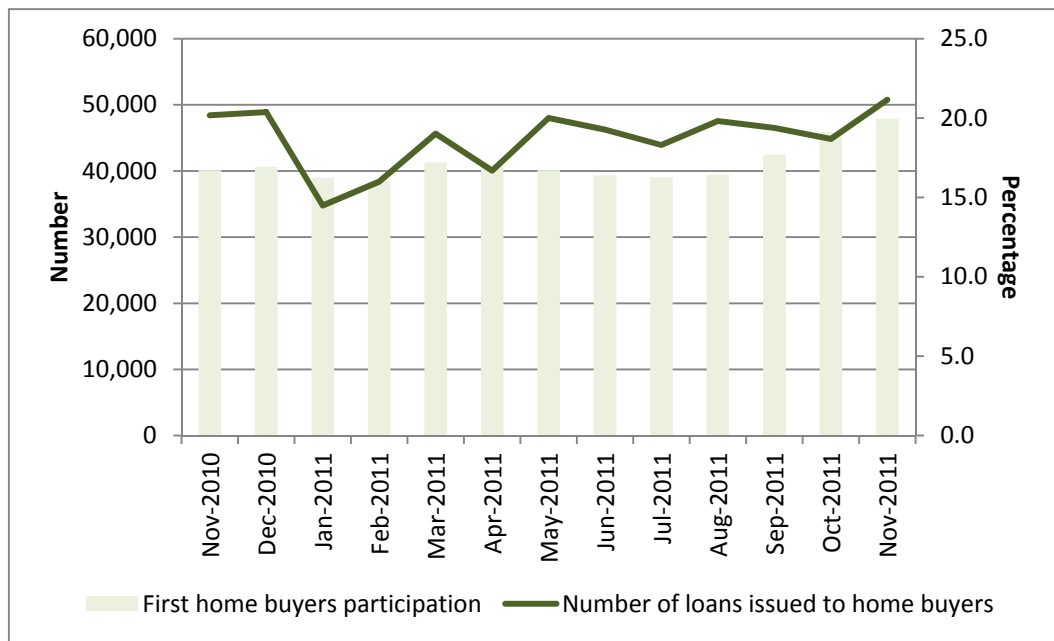
Global economic growth has moderated over 2011 compared to the previous year. Economic instability in the Euro-Zone countries together with slower growth in Asia and a continued sluggish recovery of the US economy contributed to this. The sovereign credit and banking problems in Europe led to a worsening of financial conditions in the region; slowing economic activity in Europe which has been affecting trade with Asia over the past twelve months. Over the second half of 2011, the economies of the US and much of Asia showed some improvement compared to the beginning of the year. The US labour market strengthened with some growth in private-sector employment, retail sales increased over the past six months with consumer confidence showing a slight improvement. All expectations are that over 2012 the global economy will remain relatively weak and patchy. This will have repercussions on Australia's economic aggregates.

Australia's economy continued to perform better than other advanced economies during 2011. Relatively low and steady unemployment, moderate inflation, strong public finances, investment in the mining sector and growing public investments have contributed to Australia's economic growth, boosting national income and demand. Despite this, the instability in the global economy was the key reason for softening credit growth and declining asset prices together with households being more cautious with their spending.

At the end of 2011, the official cash rate was lowered by a total of 50 percentage points over two months. Instability in the Eurozone and slowing economic growth in China were amongst the main reasons for the interest rate cuts.

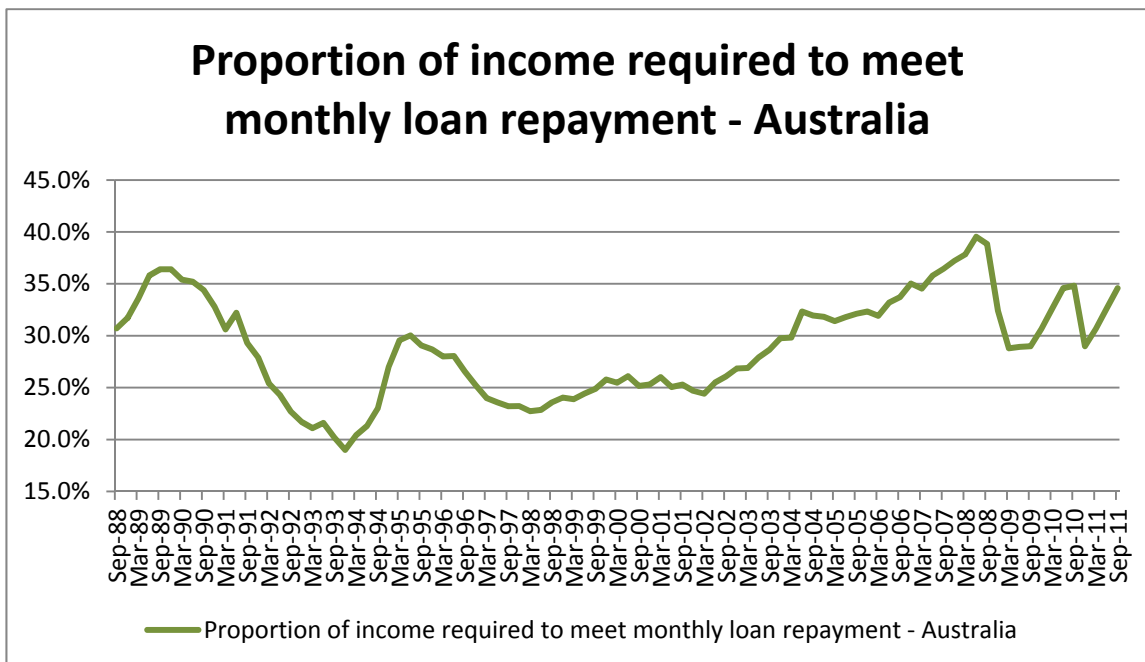
Conditions across industries varied noticeably with the mining sector showing strong growth while activity in the construction industry continued to decline as the stimulus-related public building activity ran down and household demand, including first homebuyers, was subdued. Higher interest rates and constraints on availability of investment capital exacerbated the already acute housing supply imbalance. Higher borrowing costs also slowed down the number of housing loan commitments, adding to deteriorating housing affordability and almost halving the proportion of first home buyers from the levels in mid 2009.

The graph below shows the number of loans issued to home buyers and the proportion of first home buyers in housing finance commitments from November 2010 to November 2011. During this period, the number of home loans issued to home buyers increased 4.9 per cent while the participation of first home buyers increased from 16.7 per cent to 20 per cent.



Source: Australian Bureau of Statistics (ABS)

The REIA Deposit Power/Housing Affordability reports have recorded two slight improvements in housing affordability during 2011. There was no evidence of a pattern of ongoing improvement with decreases in the proportion of family income to meet monthly loan repayments evident over the March and the September quarters. In the September 2011 quarter the proportion of income required to meet loan repayments was recorded at 33.6%, the lowest level since March 2010. This means that the average Australian household is spending about \$509 on weekly loan repayments, which is \$206 per month more than they were spending in March 2010.



Source: Real Estate Institute of Australia (REIA) Deposit Power Housing Affordability report

Over the last year, the average loan size decreased 0.9 per cent, while monthly loan repayments grew 1.9 per cent.

The November and December 2011 interest rate cuts will help housing affordability but will not be sufficient of its own to address the matters of housing supply and housing affordability in Australia.

The REIA seeks Government consideration of nine specific matters as part of the preparation of the Federal Budget 2012/2013. These are aimed at contributing to Australia's continuing economic development, addressing the supply of rental housing, improving affordability, ensuring adequate access to housing finance and improving the operating environment for small business.

## **RETENTION OF CURRENT ARRANGEMENTS FOR NEGATIVE GEARING OF PROPERTY INVESTMENTS**

### *Proposal*

- Negative gearing in its current form for the purpose of property investment is complementary to the goals of the Housing Affordability Fund (HAF) in addressing the supply of rental accommodation.
- The Henry Review proposed the replacement of current negative gearing arrangements with the introduction of a 40 per cent discount for income from rental properties. This means that deductions are also discounted by 40 percent. The argument stated by the review is that the current structure of tax income from savings creates distortions, causing misallocation of savings in particular in the rental property market and leads to investors taking on excessive debt. The Henry Tax Review considers the introduction of a broad 40 percent discount for income from rental properties would mitigate those distortions.
- According to taxation statistics, in 2008-09 the total number of rental property schedules was 2,366,580; 76% of the total number of rental property schedules paid a total amount of \$18,904 million interests on loan which represents 60% of the total rental property expenses and an average interest expense of \$10,474 per rental property schedule. The average loss across all the schedules, not just negative geared property is \$2,766.

**Taxation Statistics 2008-2009**

|                                       |     |                |
|---------------------------------------|-----|----------------|
| <b>Rental property Schedules</b>      | No. | 2,366,580      |
| <b>Rental Income</b>                  | No. | 2,307,625      |
|                                       | \$  | 24,958,503,273 |
| <b>Other rental Income</b>            | No. | 342,940        |
|                                       | \$  | 186,796,194    |
| <b>Interest on loan</b>               | No. | 1,804,760      |
|                                       | \$  | 18,903,832,707 |
| <b>Total rental property expenses</b> | \$  | 31,649,209,057 |
| <b>Net rental income</b>              | No. | 2,351,000      |
|                                       | \$  | -              |
|                                       | \$  | 6,503,905,489  |

- The table below quantifies the impact of the Henry Review recommendation for rental properties. We see that for an investor with an annual income of \$80,000 (some sources suggest that taxpayers who earn this annual income own 80% of all loss-making properties), and using the average loss of \$2,766 from the taxation statistics 2008-09, we see that the average property investor would pay an additional \$332 in tax. This represents a rent increase of around \$7 per week or 2 percent of the median house rent for three bedroom houses. The impact on many investors and their properties will be greater than this. In an already tight rental market – with an average vacancy rate of just 2.5 percent ranging from 1.4 per cent in Sydney to 3.1 per cent in Adelaide and Darwin in September 2011 – the impact on renters would be dramatic.

**With Negative Gearing**

|                                   |          |
|-----------------------------------|----------|
| Personal Income                   | \$80,000 |
| Average loss on net rental income | \$2,766  |
| Taxable income                    | \$77,234 |
| Taxes                             | \$16,720 |

**With 40% discount on savings**

|                                   |          |
|-----------------------------------|----------|
| Personal Income                   | \$80,000 |
| Average loss on net rental income | \$2,766  |
| Taxable income                    | \$78,340 |
| Taxes                             | \$17,052 |

- ***The REIA proposes that negative gearing be retained in its current form for the purpose of property investment.***

## NO CAPITAL GAINS TAX ON THE FAMILY HOME

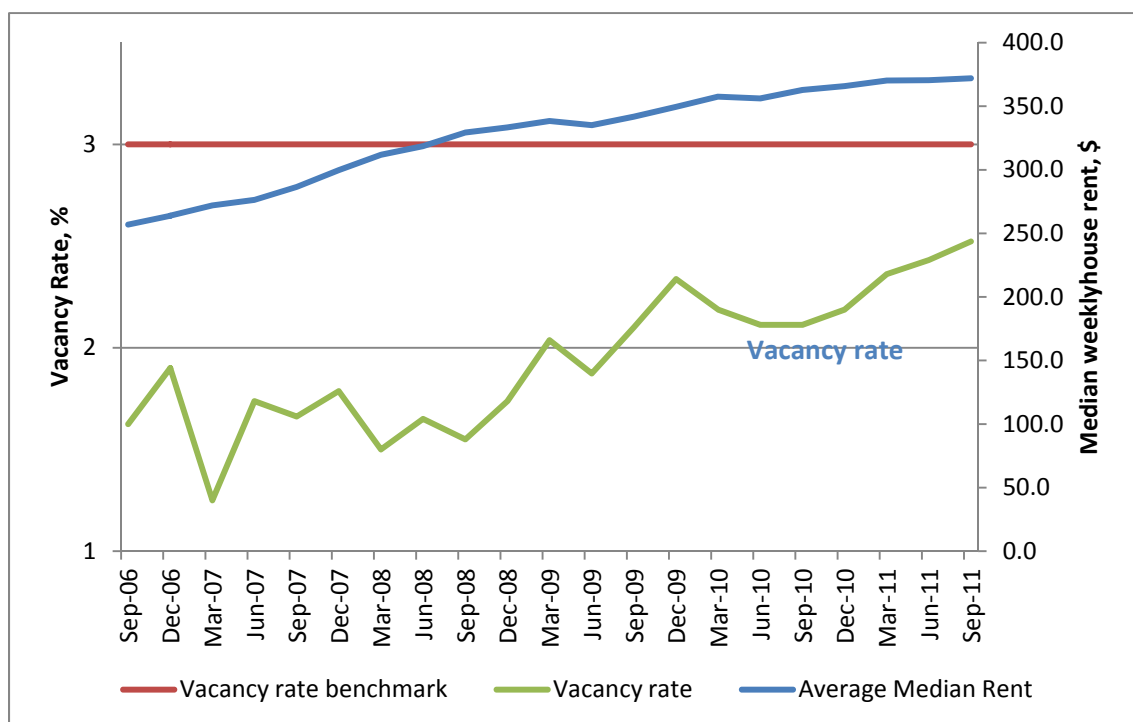
### *Proposal*

- Some submissions to the Henry Review have argued that the current structure of property taxes is inequitable and brings about overinvestment in the family home. Many have proposed the introduction of a capital gain tax on properties above a certain value - \$1 million is a popular proposed trigger point.
- The Henry Review proposed owner-occupied housing is tax-exempted or close to exempt in practice. This is because taxing long-term gains on owner occupied housing, could create a bias against this type of savings penalising those taxpayers who choose to defer consumption by saving for a house.
- The cost of administering an annual CGT payment on family homes also needs to be considered. A way of valuing subject property would be required. A general movement in prices would not be sufficient or equitable. Houses are not a homogeneous product. There are many differences in the attributes of houses and their condition and maintenance. It is these differences that determine why one property is worth more than another even when they are next door to each other. Not only are there differences in the characteristics determining the base line valuation but improvements to the property such as renovated kitchens, extensions and landscaping need to be reviewed on an annual basis if an accurate assessment is to occur. An appeal mechanism will also need to be in place to allow house owners across Australia to dispute Government valuations.
- ***The REIA proposes that a capital gains tax is not imposed on the family home.***

## NO INCREASE IN CAPITAL GAINS TAX ON PROPERTY INVESTMENTS

### *Proposal*

- Again, many submissions to the Henry Review called for the doubling of CGT on rental properties.
- The Henry Review proposed a 40 percent discount for income from capital gains of rental properties, eliminating the current CGT discounts on rental properties held by twelve months or more and thereby increasing the amount of tax paid by real estate investors.
- The Henry Review proposal would have major consequences on the supply of rental housing in a market that already has tight vacancy ratios. Over the period 2006-2011, the vacancy rate in Australia has remained below the 3 per cent benchmark and was 2.5 per cent in September 2011. During the same period, the average real median rent increased by 44.8 per cent.



Source: REIA

- Any proposal that increases the tax paid on capital gains on property, such as in the Henry Review, if implemented, would discourage investors from allocating financial resources to the property market, exacerbating the already low levels of vacant rental properties and consequently pushing rents up further.
- The impacts on rents could be similar to the situation in 1985 when the Hawke Government denied many investors tax deductibility of interest payments. With a market response that led to an undersupply of rental property and escalating rents before the decision was reversed less than 24 months later. The REIA believes that any increase in capital gains tax arrangements for rental property, would lead to a similar response to that in 1985.
- ***The REIA proposes that capital gains tax on property investments is not increased.***

## ABOLITION OF STAMP DUTY ON PROPERTY TRANSACTIONS

### *Proposal*

- The Henry Review identified stamp duties as a most inefficient tax. Whilst stamp duties are a state tax and are thus not determined by the Federal Government states will not act unilaterally on the matter unless leadership is

shown by the Federal Government. At the October 2011 Tax Forum, according to the Treasurer, the state tax reform discussion were probably the most passionate discussion at the forum with even the states acknowledging that their own state taxes harm labour mobility and housing affordability.

- Stamp duties represent additional costs to property transactions, thereby discouraging turnover of housing and distorting choices between renting and buying, and between moving house and renovating. Individuals who move more frequently would pay more taxes than those who move less. Others, who would have to buy or sell if they changed jobs, could be deterred by these costs thus reducing labour mobility. These distortions lead to a sub optimal outcomes, reduce investment in the property market and impede labour mobility.
- An Australian National University research paper by Andrew Leigh, “how do stamp duties affect the housing market”, shows that increases in stamp duties lower turnover in the short and medium run. Specifically, a 10 per cent increase in stamp duty diminished housing turnover by between 2 and 5 per cent.
- Similarly a OECD report, “Going for Growth in 2011”, also notes that lower transaction costs such as stamp duties encourages mobility.
- From the fiscal revenue perspective, stamp duties are a major source of revenue for states. Revenue from conveyance stamp duties is however highly volatile, unreliable and unpredictable.
- According to the Henry Review “stamp duties on conveyances are inconsistent with the needs of a modern tax system. While a significant source of state tax revenue, they are volatile and highly inefficient and should be replaced with a more efficient means of raising revenue”.
- The Henry Review recommended that a land tax was an efficient means of replacing the revenue forgone from abolishing state stamp duties. In reality this is not the case. In practice it is likely that a significant proportion of the economic incidence of the tax is passed forward to consumers or backwards to investors adding distortions and reducing the efficiency of the tax and detracting from the claimed simplicity, equity and sustainability of the tax.
- An outcome of the Tax Forum was that the Council of Australian Federation will work with the NSW Treasurer, Mike Baird, and the Queensland Treasurer, Andrew Fraser, to develop a state tax reform plan, for further discussion with the Commonwealth. The Council will develop the plan; for discussion amongst state, territory and Commonwealth treasurers who will then take it to COAG for agreement and implementation with the first iteration by the end of 2012, including a clear timetable for harmonisation and additional steps beyond that. The Treasurer noted that the state tax reform plan needs to be feasible; practical and it must also be genuine reform. The

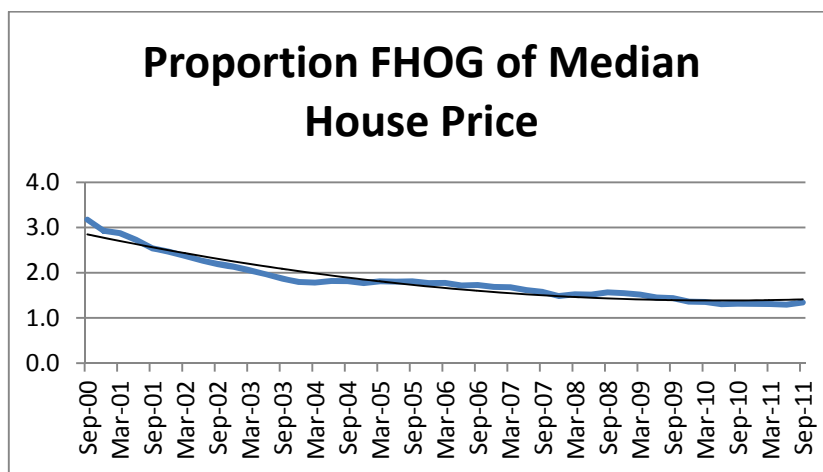
Commonwealth Government is urged to ensure that momentum is not lost in this process.

- ***The REIA proposes conveyance stamp duties be abolished and replaced by an efficient source of revenue for states and territories.***

## THE FIRST HOME OWNERS GRANT

### *Proposal*

- One of the most important housing policy instruments in assisting first home buyers with housing affordability is the First Home Owners Grant (FHOG), which was introduced in July 2000.
- The REIA urges Government to not only retain the grant but to review the amount currently provided as the relative size of the grant has declined markedly in relation to house prices. When the FHOG was introduced in July 2000, the Australian quarterly weighted average median house price was \$220,443. The Australian weighted average median house prices in the most recent quarter for which data is available, September 2011, was \$521,238.
- The graph below shows the contribution of the grant towards the purchase price has more than halved from 3.2% to 1.3% over the period. The proportion of FHOG in median house prices exhibits a downward trend since the introduction of the grant. Except in those states/territories which have stamp duty concessions for first home buyers, when stamp duties are taken into account the decline is even more marked.



Source: REIA

- Coincidentally with the introduction of the Boost in October 2008 the FHOG, for an established dwelling, had in essence retained parity with the time it was introduced.
- ***The REIA proposes that the FHOG be set at \$15,000 for all housing, new and established, and that it be indexed to median house price movements annually.***

## **ALLOW FIRST HOME BUYERS ACCESS TO THEIR SUPERANNUATION FOR THE PURCHASE OF A HOME**

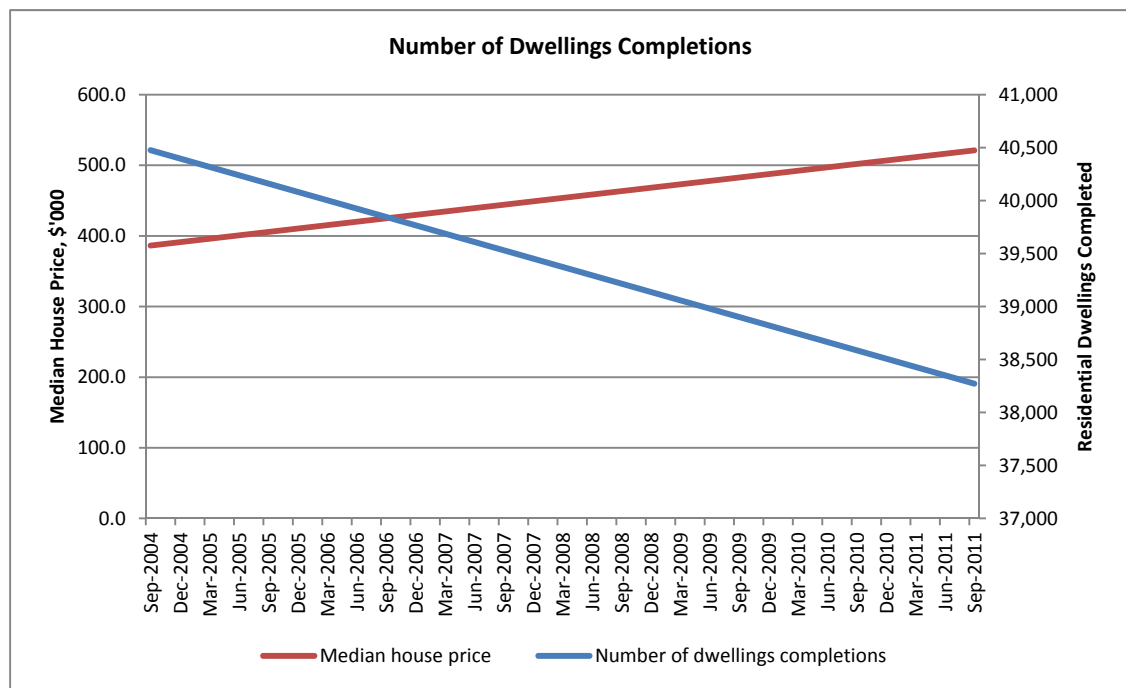
### *Proposal*

- Notwithstanding the response by first home buyers to the Boost, the REIA is concerned that the overall level of homeownership in Australia has not shown significant improvements since 1995 and that first home buyers find it increasingly difficult to enter the housing market. Although the Boost has helped the participation of first home buyers in the market, it was a short term measure and did not provide first home buyers long term support.
- The REIA notes that the Government has made some changes to the First Home Saver Accounts aimed at encouraging new participants to open such accounts. Whilst the REIA welcomes and supports the changes it believes that more should be done to assist first home buyers save for a deposit.
- As part of a package of measures to address the affordability problem, the REIA proposes that the Commonwealth Government should establish a scheme which would encourage young Australians to contribute to voluntary superannuation by allowing access to these resources for the purposes of raising a deposit for a first home.
- The scheme would be an adjunct to the First Home Savers Account but would allow flexibility for the saver to decide whether all or part of the voluntary superannuation payments was needed to augment the home purchase.
- The integrity of compulsory superannuation would be maintained by limiting the scheme to the voluntary superannuation contributions of first home buyers.
- ***The REIA proposes that first home buyers have access to their voluntary superannuation contributions for the purchase of a home.***

## MONITOR HAF AND NRAS

### Proposal

- One of the factors that contributes to increases in house prices is the under supply of housing. Supply has been unable to keep pace with demand due to constraints on land availability, lengthy planning delays and associated costs of approvals, zoning policies, skill shortages and lower yields stemming from the increased cost of entering the property investment market.
- The graph below shows the trends of median house prices and the number of new residential dwelling completions over the period Sep04-Sep11. There is an inverse relationship between median house and the number of dwellings completed: the upward trend in median house prices is associated with a downward trend in the number of dwelling completions.



Sources: ABS, REIA

- In July 2008, the Federal Government established the Housing Affordability Fund (HAF) to address housing supply problems, particularly the holding costs incurred by developers as a result of long planning and approval waiting times and infrastructure costs. It also targets infill and greenfield developments.
- The REIA is acutely aware that housing affordability is a major issue to be addressed and is supportive of the Federal Government's housing supply strategy including the National Rental Affordability Scheme (NRAS) and the Housing Affordability Fund.

- According to a recently released the third National Housing Supply Council *State of Supply* report the gap between the supply and demand for housing will increase over the next years, which will put further pressure on house prices.

| Year ended 30 June | Cumulative Demand - Supply Gap |
|--------------------|--------------------------------|
| 2010               | 186,800                        |
| 2011               | 214,700                        |
| 2012               | 243,700                        |
| 2013               | 272,800                        |
| 2014               | 301,100                        |
| 2015               | 328,800                        |
| 2025               | 556,900                        |
| 2030               | 640,200                        |

Source: National Housing Supply Council, 3<sup>rd</sup> State of Supply report

- REIA considers it is important to not only monitor the impact of the National Rental Affordability Scheme and the Housing Affordability Fund on housing supply to gauge whether its objectives are being met but to also conduct a review which considers additional measures to bridge the demand-supply imbalance.
- ***The REIA proposes that Federal Government's HAF and NRAS programs be monitored to observe its effects on housing supply and to conduct a review which considers additional measures to bridge the demand - supply imbalance.***

## TIMELY RELEASE OF NATIONAL HOUSING SUPPLY COUNCIL'S STATE OF HOUSING SUPPLY

### *Proposal*

- The National Housing Supply Council was established in 2008 to monitor housing demand, supply and affordability in Australia and to identify gaps between housing supply and demand. It reports through its *State of Supply Report*.
- With housing affordability recognised as a policy priority it is imperative that the Council reports in a timely manner. The document provides valuable information not only to Government policy makers but also to industry.
- The Council's annual reporting has however been less than timely on this important matter.

- ***The REIA proposes that Federal Government ensure that the National Housing Supply Council's State of Supply Report is published in a regular and timely manner.***

## **APPOINTMENT OF A NATIONAL SMALL BUSINESS COMMISSIONER**

### *Proposal*

- The Australian Government has recognised the important role that small business plays in the economy and that impediments to its operation need to be removed to achieve its potential and to be integral for further economic development. A resilient and confident small business sector is vital for sustained long term growth.
- During 2011 the then Minister for Small Business, Senator Nick Sherry, announced a review of services to small businesses and sought comments on a range of proposals including a national Small Business Commissioner.
- Some of the state governments have also recognised the need for a small business by making such appointments. During 2011 a small business commissioner was appointed in NSW, Western Australia and Victoria. South Australia has approved the creation of a Commissioner's position.
- A small business commissioner at the national level would complement the role of the state commissioners and facilitate not only the development of small business but assist in reducing some unnecessary costs.
- ***The REIA proposes that Federal Government appoints a national Small Business Commissioner.***

## **CONCLUDING COMMENT**

- The REIA welcomes the opportunity to present the Government with proposals for the 2012/2013 Federal Budget which are aimed at contributing to Australia's continuing strong economic development, addressing the supply of rental housing and improving housing affordability. These are aimed at contributing to Australia's continuing economic development, addressing the supply of rental housing, improving affordability, ensuring adequate access to housing finance and improving the operating environment for small business.

- **The REIA proposes that**
  - ***Negative gearing be retained in its current form for the purpose of property investment.***
  - ***A capital gains tax is not imposed on the family home.***
  - ***Capital gains tax on property investments is not increased.***
  - ***Conveyance stamp duties be abolished and replaced by an efficient source of revenue for states and territories.***
  - ***The FHOG be set at \$15,000 for all housing, new and established, and that it be indexed to median house price movements annually.***
  - ***First home buyers have access to their voluntary superannuation contributions for the purchase of a home.***
  - ***The Federal Government's HAF and NRAS programs be monitored to observe its effects on housing supply and to conduct a review which considers additional measures to bridge the demand - supply imbalance.***
  - ***The REIA proposes that Federal Government ensure that the National Housing Supply Council's State of Supply Report is published in a regular and timely manner.***
  - ***The REIA proposes that Federal Government appoints a national Small Business Commissioner.***

**PREPARED BY**  
Real Estate Institute of Australia

January 2012