SUBMISSION TO THE PRODUCTIVITY COMMISSION INQUIRY INTO FIRST HOME OWNERSHIP

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Executive Summary

1. The housing affordability problem, particularly amongst first-home buyers, is at the forefront of political, economic and social domestic concerns in Australia. A case study on NSW, presented in this submission, provides an appropriate considering some of the questions pertinent to the Productivity Commission's inquiry into the issue.

2. An inflationary housing market has seen residential property prices rise nearly fivefold in Sydney and nearly threefold in the rest of NSW over a seventeen period between 1986-2003. This inflationary process is driven by the dynamics of the housing market, and derives ultimately from the failure to develop a coherent policy on land.

3. Average wages have not increased in line with inflation in land and housing. Consequently, housing affordability has declined sharply: a typical house Sydney cost just under 4 years of average earnings in 1986, while in 2003 it costs over 12 years' worth of earnings. Low interest rates in recent years have masked the long term trend towards deteriorating housing affordability.

4. Redress of this long-term problem requires radical changes to public policy. Selective measures to assist first home buyers are inappropriate and ineffective. It is much better to tackle the general problem of housing affordability.

5. Taxes on property transfers have, not surprisingly, been politically targeted as a culprit for the housing affordability crisis. They have generated surging revenues in an inflationary land/housing market. There are significant problems arising from stamp duties as a barrier to mobility. However, closer analysis shows that only a very small proportion of

the problem of housing affordability is due to stamp duties – amounting to about 2% of the deterioration in housing affordability in Sydney and 1.4% in the rest of NSW over the last 17 years.

6. Stamp duty has become a fundamentally important source of State revenue and could not be reduced unless an alternative revenue source were found. That alternative could be land tax. Although less in the political spotlight, land taxation and its interaction with the housing market could hold an important key to resolving the housing affordability crisis.

7. Land tax revenue have grown more slowly than property-related stamp duty revenues. By lifting the exemption currently enjoyed by owner occupied properties (other than those paying the 'premium property' rate), much more revenue would be generated than that currently raised by stamp duties. A revenue-neutral tax reform would require a lower land tax rate than the current rate of 1.7%.

8. Uniform land taxation could make a major contribution to housing affordability by 'creaming off' part of any potential capital gain, and thereby reducing the attractiveness of land as a form of investment. Consequently it would help stem the damaging inflationary and cyclical effects associated with speculation in the housing market.

9. Implementing reform that emphasises the extension of uniform land taxation would require careful consideration, particularly in terms Federal/State fiscal relations. The relationship of land tax to local government finance is also relevant to formulating an appropriate model for land taxation.

10. It is only by addressing these issues of tax reform that the pressures causing a crisis of affordability for many aspiring first home buyers can be resolved.

11. Measures to increase the supply of public housing could also contribute substantially to resolving the problems, but a detailed analysis of the housing rental sector, public and private, is not included in this submission.

**Note: This submission has been compiled with the research assistance of Jennifer English*

Introduction

Housing affordability, particularly in the major cities, is currently a central political, economic and social concern in Australia. The Federal government's establishment of an inquiry by the Productivity Commission into how first-home buyers are affected provides an opportunity to raise a number of questions. What is the nature of the problem of housing affordability? What has been driving rising residential housing prices? Are there other reasons to be concerned about the role of property-related taxes such as stamp duty? If so, what other taxes might produce equivalent revenue without causing comparable problems? For example, would the extension of an annual land tax to include owner-occupied properties have less damaging socio-economic effects? To what extent would such reforms reduce the pressures of inflation in land/housing markets and thereby benefit aspiring first-home buyers?

This submission explores these issues with reference to the situation in the State of New South Wales. It is acknowledged that the Productivity Commission Inquiry must examine nationwide trends. However, it is submitted that the NSW situation provides a very significant case study. It is in Sydney that residential property prices have reached the highest levels, so the focus on that city draws attention to the most stressed situation; but some attention is also paid to non-metropolitan NSW data in order to illustrate the broader regional situation. A seventeen year period from 1986 to 2003 is taken as the basis for the study. The historical patterns leading to the current situation are thereby revealed.

The analysis proceeds by (i) examining house price trends; (ii) identifying the intensity and nature of the 'housing affordability' problem; (iii) examining the trends in stamp duty, its impact on housing affordability, and the dependence of State government finances on stamp duty; (iv) examining the requirements for payment of land taxes and the trends in land taxes as a source of State revenue; and (v) considering the possibilities for restructuring of State government finances in order to achieve better housing affordability outcomes, and thereby reduce the economic obstacle currently facing aspiring first home buyers.

Housing Prices

Table 1 shows what has happened to housing prices in Sydney and Other NSW over the period 1986-2003. In broad outline, property prices have risen nearly fivefold in the

metropolitan area and nearly threefold in the rest of the State. In the last two years (2001-03) there has been a particularly marked inflationary surge, surpassed in relative terms only by the surge in Sydney (but not elsewhere in the State) during the housing boom of 1988 when median house prices rose in one year by about 67%. In the year 2002-03 the price rises averaged 29% in Sydney and 39% in Other NSW, the latter from a lower base, of course. In absolute terms the Sydney/other NSW price relativities have continued to widen.

Table 1: Median Priced Houses: Sydney and Other NSW, 1986 - 2003

Year	Median Priced House in Sydney ($)	Median Priced House in Other NSW ($)
1986	87,000	71,000
1987	90,000	70,000
1988	150,000	77,200
1989	182,000	93,700
1990	187,000	105,100
1991	186,000	114,500
1992	183,000	119,800
1993	185,000	120,200
1994	205,000	125,400
1995	220,000	133,800
1996	245,000	137,600
1997	281,500	145,700
1998	325,000	156,700
1999	355,000	164,200
2000	410,000	179,900
2001	405,000	176,400
2002	485,000	201,300
2003	625,000	279,300

Source: Housing Industry Australia/Commonwealth Bank (figures taken in the second quarter of each year)

To understand this inflationary process requires an understanding of the dynamics of the housing market. Four points stand out. One is that the demand for housing as a commodity is driven by exchange values, not just by use values. Of course, housing does have use value – the value of shelter, security and amenity provided to its occupants. However, housing wealth is also a store of value and a source of capital gains. It is favoured in this respect by its tax treatment, particularly (i) the exemption of owner-occupied housing (other than a tiny proportion of very highly valued properties) from land tax, (ii) the exemption of owner occupied housing from capital gains tax, and (iii) the negative gearing provisions that effectively provide a subsidy to owners of investment properties.

Second, the demand for housing responds to changes in the broader investment environment. This imports a cyclical tendency, causing periodic inflationary booms in housing prices. There is switching of investable funds between share markets and housing markets, for example, such that surges of housing demand tend to follow share market declines, as in 1987-89 and 2001-02. These surges of demand tend to impart a 'ratchet effect' into the pattern of housing prices, periods of rapid inflation alternating with periods of relative stability but without significant periods of deflation to offset the long-term upward tendency.

Third, housing therefore becomes a focal point for speculative processes which further fuel inflation. The 'herd' behaviour of investors in speculative markets is well known – rising prices cause increases in demand, contrary to simple 'textbook' economic theory, because they are seen as signals of expected future price rises. The resulting increases in demand then bring about those further price rises: in effect, the expectations become self-fulfilling. First-home buyers are not normally drivers of this process, but they become minor players to the extent that they bring forward their purchases (sometimes encouraged to do so by the availability of a first-home subsidy) in expectation of future price rises.

Fourth, it is the price of land rather than the housing itself that is the inflationary driver. Over the last decade, the price of constructing houses has drifted upwards roughly in line with general national inflationary levels in the 2-4% per annum range for the Consumer Price Index (CPI), plus a 10% step-up when the Goods and Services Tax (GST) was introduced. So, in round terms, one might have expected an increase in housing prices of about 50%, excluding land values, over the decade. In other words a new medium priced house in Sydney valued at $185,000 in 1993 could have been expected to rise in price to about $277,500 by 2003. In practice, its value (as shown in Table 1) rose to $625,000. So only about 21% of the total price rise was due to the house itself, the other 79% being the result of rising land prices. The corresponding proportion for Other NSW were 38% and 62%. What this means is that no general solution to the problem of housing affordability for first-home buyers is possible without tackling 'the land question'. This is reflected in the analysis later in this submission of the possible effects of broadening the land tax revenue base.

Housing Affordability

How do these trends in housing prices affect housing affordability? And what else has been changing housing affordability over time, particularly as it impacts on prospective first-home buyers? Addressing these questions is necessary before exploring how the problem may be tackled. For this purpose it is useful to identify two types of quantitative measure:

- the index of housing affordability, calculated regularly by the Housing Industry Association in conjunction with the Commonwealth Bank;
- the ratio of median house prices to annual average earnings.

The former index is defined as 'the ratio of average household income to the ('qualifying') income required to meet payments on a typical dwelling (as expressed as an index). In calculating qualifying income, a deposit of 20 per cent with repayments equal to 30 per cent of income is assumed, using a conventional 25 year loan. An increase in the index represents an improvement in affordability' (HIA/CBA, *Housing Report*, February 1991, p4). In other words, this measure of affordability assumes that an average priced house is bought with funds borrowed from a bank to cover 80% of the purchase price. The index responds primarily to three variables: average house prices, average incomes and housing interest rates.

Table 2 below presents the relevant HIA/CBA data. It shows housing affordability in Sydney falling in the 1987-89 period when both house prices and interest rates were rising sharply. The index then rose in the 1990's as interest rates fell and house price inflation was more modest. A fall in affordability in the mid 1990s was reversed by more rapidly rising house prices after 1997, outweighing the effects on affordability of low interest rates. By 2003 Sydney's affordability index was at its lowest level for the whole seventeen year period. The situation in NSW outside Sydney, according to this index, reflects a broadly similar cyclical pattern, but at a generally higher level of affordability because of lower average house prices. A marked decrease in affordability in 2002-03 still leaves the affordability index for Other NSW roughly similar to where it had been seventeen years earlier.

Table 2: The HIA/CBA Housing Affordability Index:
Sydney and Other NSW, 1986 - 2003

Year	Sydney	Other NSW
1986	128.6	128.0
1987	127.9	132.9
1988	97.4	148.9
1989	74.3	114.8
1990	79.6	111.2
1991	90.9	116.4
1992	116.9	141.1
1993	126.8	154.8
1994	124.6	162.4
1995	105.7	137.6
1996	106.1	148.4
1997	123.1	187.5
1998	111.6	181.1
1999	105.9	178.3
2000	87.3	153.6
2001	103.3	185.5
2002	89.9	170.6
2003	73.9	126.0

Source: Housing Industry Australia/Commonwealth Bank (figures taken in the second quarter of each year)

Table 3 shows the relevant data for the alternative index of housing affordability, based on data on median housing prices (shown in Table 1) and on average annual earnings. A much more dramatic picture emerges here. Whereas it took just under 4 years of average annual earnings to buy a median priced house in Sydney in 1986, for example, it would take over 12 years for someone purchasing in 2003. This represents a significant worsening of the situation facing first-home buyers in particular. Even in Other NSW where house prices have not climbed so rapidly overall, this index of affordability has worsened considerably – from three and a quarter years to five and a half years of average earnings to buy a medium priced house.

It must be borne in mind that the time taken to buy a house in practice is usually much longer than indicated by this average earnings/house price ratio. To infer that the data in Table 3 shows the number of years in which a typical house purchaser could actually pay off a house implicitly assumes that: (a) all that person's earnings are allocated to house purchase (i.e. no eating, clothing, house rental or other consumption expenditures in the meanwhile), and (b) there are no interest payments associated with house purchase. Relaxing these two unrealistic

assumptions could normally be expected to lengthen the relevant time period by a factor of three or even more. For many individuals and families aspiring to first-home ownership, the relevant time period is infinity, ie. they can never afford to buy a house in their lifetime.

It is little wonder in these circumstances that the proportion of first-home buyers in total home buyers has recently dropped to a record historically low level. ABS figures show that in September 2003 first-home buyers accounted for a mere 13.3 per cent of all new loans for owner occupied homes.

Table 3: How many years of average full time earnings taken to buy an average house, 1986 - 2003

Year	Average Yearly Earning (NSW) ($)	Number of years of wages it takes to buy a median priced house (Sydney)	Number of years of wages it takes to buy a median priced house (Other NSW)
1986	22,006.40	3.95	3.23
1987	23,072.40	3.90	3.03
1988	24,876.80	6.03	3.10
1989	27,201.20	6.69	3.44
1990	29,010.80	6.45	3.62
1991	30,305.60	6.14	3.78
1992	31,356.00	5.84	3.82
1993	31,933.20	5.79	3.76
1994	33,451.60	6.13	3.75
1995	35,521.20	6.19	3.77
1996	37,003.20	6.62	3.72
1997	38,012.00	7.41	3.83
1998	39,504.40	8.23	3.97
1999	41,293.20	8.60	3.98
2000	43,326.40	9.46	4.15
2001	46,170.80	8.77	3.82
2002	47,829.60	10.14	4.21
2003	50,648.00	12.34	5.51

Source: Calculated from ABS Statistics and Table 2

The ratio of house prices to average annual earnings (as shown in Table 3) exhibits some cyclical features. However, unlike the HIA/CBA index, these cyclical features are minor by comparison to the long-term secular trend towards a greater problem of housing affordability. This measure more starkly reveals the nature of the long-term problem. In the HIA/CBA index the long-run tendency towards more unaffordable housing is masked by the low interest rates that have prevailed in recent years. A climb in interest rates (such as is now occurring) is unlikely to cause falling prices – as noted earlier, house price patterns tend to operate with a

'ratchet effect' – so this could be expected to further depress the HIA/CBA affordability index. The underlying secular trend is towards declining housing affordability, as shown in the average earnings/house price ratio. As Table 3 shows, the root of the problem is long-run tendency for the rate of house price inflation to outstrip growth in average earnings. As with any such asset inflation process, it impacts most severely on new entrants, ie. on those who do not have existing assets to trade-up for more valuable property. The generalised housing affordability problem is thereby manifest a particular crisis for first-home buyers.

The situation on facing aspiring first-home buyers is quite conservatively depicted by this analysis, because of growing inequalities in the distribution of income. There is abundant evidence of increased income disparities in Australia over the last decade. Increased disparities in earnings mean that the calculations in Table 3 based on average earnings tend to understate the impediments to home-purchase. If aspiring first-home purchasers, on average, have lower incomes than the mean for the whole population, the severity of the problem of access to home ownership is even greater than represented here.

Stamp Duties in an Inflationary Housing Market

Do stamp duties compound the housing affordability problem? At first sight they seem to do so, because they are an additional cost incurred when buying a home. Indeed, the revenues raised by this 'tax' have risen dramatically as a result of inflation in real estate markets. By the same token, State governments have become increasingly reliant on revenue from stamp duty and hence reluctant to scale back on the rate of stamp duty unless some comparable revenue source replaces it. This issue requires careful analysis.

Historically, stamp duty was intended to be a fee to cover the cost of stamping and filing documents that transferred an interest in property. Today as the stamp duty[1] payable on a median priced house in Sydney soars above $23,000, it no longer makes sense to understand stamp duty as a simple 'filing fee'. Nonetheless, it continues to be the instrument of transfer of property that is subject to the duty, not the property itself. The duty payable is based on the value of the property (including improvements) or the consideration paid (including GST), whichever is greater. Thus it is the current market value of the property which forms the basis on which stamp duty is calculated; and such duty is payable whether or not the transfer was

for monetary consideration. The duty must be paid by the purchaser (or transferee) within three months from the date of exchange of contracts.

As Table 4 below shows, stamp duty is a progressive tax because as property values increase so too does the rate of stamp duty applicable. So the transfer of a residential property valued at $200,000 in addition to the flat base rate incurs a duty of $3.50 for every $100 exceeding $80,000, while a transfer of a property valued at $400,000 in addition to the flat base rate incurs a duty of $4.50 for every $100 exceeding $300,000. The rates of stamp duty shown in Table 4 were introduced in 1986 and have not since been modified despite fundamental change in the residential property market.

Table 4: Rates of Stamp Duty, NSW, 1986 - 2003

Dutiable value of the property	Rate of Duty
$0 - $14,000	$1.25 for every $100 or part of the dutiable value
$14,001 - $30,000	$175 plus $1.50 for every $100 or part, by which the dutiable value exceeds $14,000
$30,001 - $80,000	$415 plus $1.75 for every $100 or part, by which the dutiable value exceeds $30,000
$80,001 - $300,000	$1,290 plus $3.50 for every $100 or part, by which the dutiable value exceeds $80,000
$300,001 - $1Million	$8,990 plus $4.50 for every $100 or part, by which the dutiable value exceeds $300,000
Over $1Million	$40,490 plus $5.50 for every $100 or part, by which the dutiable value exceeds $1,000,000

Source: Office of State Revenue, NSW Treasury

How have these stamp duty requirements interacted with residential property price inflation? Not surprisingly, given the lack of any 'indexation' in the scales for stamp duty payments, the relentless land/housing inflationary process (shown in Table 1) has impacted dramatically on

[1] All subsequent references to 'stamp duty' refer to stamp duty on land transfer unless otherwise indicated.

the absolute levels of stamp duty payable on the purchase of residential properties everywhere. Table 5 shows the patterns for Sydney, taking three price categories for illustrative purposes: the median priced house; half the median (a relatively cheap home unit in an unfashionable suburb, for example); and double the median (a substantially larger than average house, for example, or an average house in a particularly sought-after location).

Table 5: Stamp Duty Payable on Three Housing Price Categories: Sydney, 1986 - 2003

Year	Stamp Duty on ½ Median Priced House ($)	Stamp Duty on Median Priced House ($)	Stamp Duty on 2 x Median Priced House ($)
1986	651.25	1,535.00	4,580.00
1987	677.50	1,640.00	4,790.00
1988	1,202.50	3,740.00	8,990.00
1989	1,675.00	4,860.00	11,870.00
1990	1,762.50	5,035.00	12,320.00
1991	1,745.00	5,000.00	12,230.00
1992	1,692.50	4,895.00	11,960.00
1993	1,727.50	4,965.00	12,140.00
1994	2,077.50	5,665.00	13,940.00
1995	2,340.00	6,190.00	15,290.00
1996	2,777.50	7,065.00	17,540.00
1997	3,418.00	8,342.50	20,825.00
1998	4,177.50	10,115.00	24,740.00
1999	4,702.50	11,465.00	27,440.00
2000	5,665.00	13,940.00	32,390.00
2001	5,577.50	13,715.00	31,940.00
2002	6,977.50	17,315.00	39,140.00
2003	9,552.50	23,615.00	54,240.00

Source: Calculated from data in Tables 3 and 4

These illustrative calculations set out in Table 5 show that the stamp duty payable on the transfer of a median priced house has increased over fifteenfold over the period of seventeen years. During the same period stamp duty payable on a property valued at half the median price has increased over fourteenfold, and on a property value at double the median price stamp duty has also risen almost twelvefold. While stamp duty payable on property transactions has generally been on a constant year-by-year incline, data from 2002 and 2003 shows a significant steepening. During this last year stamp duty payable on a median priced property jumped $6,300 while stamp duty payable on a property of twice that value jumped by over $15,000.

This is by no means the full picture. Houses in Sydney now frequently trade at over $2 million and, in attractive harbourside locations, for example, sometimes beyond $20 million. In 2002 Sydney's top 200 real estate sales ranged from $4.5 million for a Wahroonga home to $28.5 million for a house in Point Piper. The stamp duty on a $4.5 million home is $232,990 and on a $28.5 million home it soars to $1,552,990. A second or even third home could be bought outright with the amount of stamp duty payable on these homes! The dramatic house price inflation by the seaside and harbourside has put prices out of reach for many buyers who have sought to purchase homes in the gentrifying suburbs of the inner-west instead, pushing prices up to the million dollar mark in even in previously unfashionable suburbs such as Summer Hill and Ashfield. In early 2002 there were over 30 suburbs in Sydney with average homes valued at $1million-plus (as reported in the *Sydney Morning Herald*, April 27 2002). With the continued inflation in the housing market, this number can be expected to increase, accompanied by further escalation in revenues derived from stamp duty on such properties.

The situation is less dramatic in non-metropolitan NSW, given the lower average property prices, but there too the situation has changed significantly over the study period. As Table 6 shows, stamp duty payable on median priced houses outside Sydney has increased sevenfold over the period 1986-2003. During the same period stamp duty payable on a property valued at half the median price and double the median price has increased around sixfold. As in Sydney, stamp duty payable on property transactions in non-metropolitan NSW has generally been rising continuously. The data in Table 6 shows a similarly noteworthy increase in duty payable between 2002-03: stamp duty on a median price house jumped over $2,700 during that period, and by over $7,000 for a double median priced house.

Table 6: Stamp Duty Payable on Three Housing Price Categories: Other NSW, 1986 –2003

Year	Stamp Duty on ½ Median Priced House ($)	Stamp Duty on Median Priced House ($)	Stamp Duty on 2 x Median Priced House ($)
1986	511.25	1,132.50	3,460.00
1987	502.50	1,115.00	3,390.00
1988	565.50	1,241.00	3,894.00
1989	710.75	1,769.50	5,049.00
1990	810.50	2,168.50	5,847.00
1991	892.75	2,497.50	6,505.00
1992	938.25	2,683.00	6,876.00
1993	941.75	2,697.00	6,904.00
1994	987.25	2,879.00	7,268.00
1995	1,060.75	3,173.00	7,856.00
1996	1,094.00	3,306.00	8,122.00
1997	1,165.75	3,589.50	8,689.00
1998	1,262.00	3,974.50	9,593.00
1999	1,363.50	4,237.00	10,268.00
2000	1,640.00	4,786.50	11,681.00
2001	1,577.00	4,664.00	11,366.00
2002	2,014.50	5,535.50	13,607.00
2003	3,379.50	8,265.50	20,627.00

Source: Calculated from data in Tables 3 and 4

These increased stamp duty payments have generated substantial socio-economic concerns. To the extent that stamp duty adds to the total cost of acquiring housing it poses a particular problem for first-home buyers. Saving up enough for a deposit is hard enough as it is in an inflationary property market. It is especially so for people who are renting their current residence and confronting the inflation in rents that generally accompanies inflation in house prices. Stamp duty adds to the total loan required, which makes it yet more difficult for first-home buyers to generate the deposit required by banks. This is because they usually have no prior security that would enable them to more easily borrow for such a purpose.

Along with a number of other States, the NSW State government recognises this distinctive burden placed on first-home buyers; and over the years it has devised a number of different schemes to address such problems. The current scheme, known as First Home Plus, provides concessions and exemptions to first-home buyers/builders in NSW. In the metropolitan area, first-home buyers are exempt from duty on homes costing up to $200,000. Concessions on duty are then on a sliding scale for property valued between $200,000 and $300,000. The

duty payable is calculated as 8.99% of the value less $17,980. There are no concessions on homes valued over $300,000. In non-metropolitan areas first-home buyers are exempt from duty on homes valued up to $175,000. Concessions are then similarly on a sliding scale for property valued between $175,000 and $250,000. The duty payable is calculated at 9.65% of the value less $16,885. There are no concessions on homes valued over $250,000. Exemption and concession provisions also apply to blocks of vacant land in metropolitan and non-metropolitan areas upon which first home buyers may wish to build their homes.

Qualification for the concessions and exemptions under this scheme are not means-tested. However, the reality, at least in Sydney, is that there is no need for means-testing because very few people would be in a position to qualify for such exemptions or concessions anyway. Even a transaction valued at half the median house price, at around $360,000, would simply not fall within the parameters of the scheme. While First Home Plus may be more effective in other regions of NSW, it does little to address the chronic crisis in the capital city. Additionally, because most housing transactions in metropolitan areas are not covered by First Home Plus, the benefits of the grant given to first-home buyers/builders under the Commonwealth First Home Owner Grant Scheme is negated. Under that scheme one applicant per transaction is given a non-means tested $7,000 grant towards the purchase of their first property. Unlike First Home Plus, the grant is flat rate and awarded regardless of the price of the property.

While the Commonwealth First Home Owner Grant Scheme was introduced to help countervail the extra financial burden GST created in respect of housing costs (and to offset a looming recession in the construction industry), rising levels of stamp duty have undermined its effectiveness. The fundamental flaws in the Commonwealth scheme have become more evident in the process. To the extent that the first-home buyers subsidy adds to effective housing demand it adds to the inflationary pressures which, together with stamp duties, limits its ability to help low and middle income earners into home ownership. There are inherent equity concerns too, as a significant number of the Federal governments' subsidy payments to first home buyers have gone to purchasers of homes costing over one million dollars. One investigation (reported in *Progress*, November-December 2003:6) found that there were 543 such cases between July 2000 and September 2003. In four particular cases identified by the Office of State Revenue, the houses were valued at over $5million. Clearly, the scheme and its adverse interaction with stamp duty and the problem of housing affordability demands

reconsideration. In the judgment of this researcher, first-home owner subsidies are an inappropriate means of seeking to deal with a more generalised problem of housing affordability.

The effect of stamp duties on spatial mobility also deserves consideration. Any such charge on property transactions (along with other fixed costs such as legal fees) can be expected to act as a disincentive to movement. While people seeking to buy their first home get some relief from stamp duty under First Home Plus, there are presumably many other people who might consider a change of location, perhaps because of a new job or because of retirement, but who are put off by the extra cost of making the change. If so, therein may lie significant social costs. If people stay in inconveniently located housing, they may have to undertake long-distance commuting, which impacts adversely on transport and environmental conditions as well as being costly in itself. Of course, people may want to stay in inconveniently located housing for all sorts of personal reasons, but it is presumably better if they don't feel 'locked in' because of the tax system.

What proportion of the housing affordability problem is due to stamp duties? Contrary to some recent political rhetoric, it is evidently a very small proportion. Although stamp duty payments in aggregate have risen dramatically over the years, the tax is a relatively small part of the housing affordability problem as a whole. As Table 7 below shows, stamp duty as a percentage of median priced houses has grown from 1.7% to 3.77% over the last seventeen years in Sydney, and risen from 1.6% to 2.960% in Other NSW. So, in round terms, the contribution of stamp duty inflation to the greater housing affordability problem has been about 2% of the total in the metropolitan area and under 1.4% on average of the total in non-metropolitan areas. These comparatively low figures tend to suggest the crux of the housing affordability crisis lies elsewhere.

It is also pertinent to note that the preceding calculations are a 'maximum estimate' for two reasons. First, they relate to median priced homes. Since first-home buyers usually enter the market for cheaper than median priced houses, and stamp duty is on a sliding scale, stamp duty as a proportion of purchase price would generally be lower for first-home buyers (even before taking into account government subsidies). Second, to the extent that stamp duties raise the total price which must be paid by the purchaser, they could be expected to reduce demand and thereby lower the prevailing market prices, other things being equal. In other

words, the earlier reasoning about first-home buyers' subsidies tending to increase demand works in reverse here – stamp duty, by tending to reduce demand, may have a mildly moderating effect on market prices. There is no reliable method of estimating the magnitude of these effects.

Table 7: Stamp Duty as a Percentage of Median House Prices 1986 - 2003

Year	Stamp Duty as a % of Median Priced House (Sydney)	Stamp Duty as % of Median Priced House (Other NSW)
1986	1.76	1.60
1987	1.82	1.59
1988	2.49	1.61
1989	2.67	1.89
1990	2.69	2.06
1991	2.69	2.18
1992	2.67	2.24
1993	2.68	2.24
1994	2.76	2.30
1995	2.81	2.37
1996	2.88	2.40
1997	2.96	2.46
1998	3.11	2.54
1999	3.23	2.58
2000	3.40	2.66
2001	3.39	2.64
2002	3.57	2.75
2003	3.77	2.96

Source: Calculated from data in Tables 4, 5, and 6

The main problem needed to be confronted by those who would wish stamp duty on home purchases to be lowered is the dependency of State governments on that revenue source. In NSW for example, over the last seventeen years, stamp duty has significantly increased in relative importance as a component of government revenues. Table 8 shows the revenue generated by stamp duty in each year from 1986 to 2003. The revenue generated by stamp duty is recognised by the NSW Treasury as falling into a number of distinct categories. For our purposes the key categories of stamp duty are Contracts and Conveyances and First Home Purchase Scheme. Contracts and Conveyances (CC) is the category that refers to stamp duty paid on the transfer of land. Stamp duty payable under the First Home Purchase Scheme (FHPS) is distinguished from CC as a separate source of stamp duty because in earlier times a

system of deferred payment existed and NSW Treasury Budget Papers categorised such payments separately. In more recent years however, the stamp duty referred to under Contracts and Conveyances includes payments made under the First Home Purchase Scheme.

It is interesting to observe changes in the relative importance of stamp duty derived from land-related transactions as a percentage of total stamp duty. Table 8 distinguishes between the revenue generated by stamp duty as a whole and the revenue generated by stamp duty under the categories of Contracts and Conveyances and First Home Purchase Scheme. Although the Budget Papers distinguish CC and FHPS from one another, for our purposes it makes sense to understand them jointly. As set out below, the final column of the table seeks to show what percentage these land-related stamp duties (CC+FHPS) comprise of the State's total stamp duty receipts. In 1986 land-related stamp duty constituted just over 40% of total stamp duty revenues; seventeen years later they constitute almost 70% of such revenues. There has been some notable fluctuations over the two decade span, particularly in the period 1987-1989 when the housing boom caused a jump from 41% to 60%. However, rates generally remained in the 40 percentile bracket until 2001-02 when there was a clear break in this trend. Land-related stamp duties as a percentage of total stamp duties rose a further 20% in this one year alone. This increase outstrips that of the late 1980s property boom and constitutes a dramatic 'ratcheting-up' of the role of land-related stamp duty in total stamp duty.

Table 8: Stamp Duty Revenue, NSW, 1986 - 2003

Year	Contracts and Conveyances (CC) $M	First Home Purchase Scheme (FHPS) $M	CC + FHPS $M	Total Stamp Duty Receipts $M	(CC +FHPS) as a % of Total Stamp Duty Receipts
1986-87	520.673	21.422	542.095	1,328.052	40.8
1987-88	1,020.900	23.000	1,043.900	1,981.100	52.7
1988-89	1,496.200	24.600	1,520.800	2,516.600	60.4
1989-90	970.909	25.058	995.967	2,043.290	48.7
1990-91	737.180	31.980	769.160	1,871.613	41.1
1991-92	827.918	43.137	871.055	2,033.758	42.8
1992-93	844.530	37.460	881.990	2,150.384	41.0
1993-94	1,169.109	37.431	1,206.540	2,653.250	45.5
1994-95	1,091.658	30.842	1,122.500	2,624.183	42.8
1995-96	1,105.000	26.000	1,131.000	2,611.400	43.3
1996-97	1,450.000	22.000	1,472.000	3,108.200	47.4
1997-98	1,800.000	20.500	1,820.500	3,679.500	49.5
1998-99	1,800.000	24.000	1,824.000	3,922.000	46.5
1999-00	2,249.000	Included in CC	2,249.000	4,512.000	49.8
2000-01	2,075.000	Included in CC	2,075.000	4,476.000	46.4
2001-02	3,050.000	Included in CC	3,050.000	4,557.000	66.9
2002-03	3,550.000	Included in CC	3,550.000	5,095.000	69.7

Note: CC: Contracts and Conveyances
FHPS: First Home Purchase Scheme

Source: Budget Papers, NSW Treasury

A fuller appreciation of the significance of these trends requires that they be considered relative to the total revenues generated by the NSW government. Table 9 below shows different measures of the relative importance of the stamp duty revenues in relation to aggregate State revenues. Over the seventeen year time span, a number of modifications have been made to the layout of the NSW Budget Papers and the titles given to certain categories of revenue. For this reason it has been difficult to devise headings completely consistent with those used in the Budget Papers themselves in certain years. Table 9 seeks to present the data in as consistent a form as is possible in order to identify changes in the patterns of revenue over the years.

The second column in Table 9, 'Total Current Receipts', refers to the total amount of recurrent revenue received by the State each year, excluding that which is derived from capital receipts. The fourth column shows what percentage total stamp duty comprises of

such revenue, and the fifth column narrows the scope to show what percentage of current revenue is made up by land-related stamp duty. In order to better understand the relationship between land-related stamp duty and State revenues, it is also necessary to deduct from current receipts figures the grants made by the Commonwealth government to the State. In this way it is possible to determine the role of stamp duty and land-related stamp duty in the sphere of 'self-generated' State revenue. The third column displays the levels of State 'self-generated' income over the time series. Subsequently the sixth column of Table 9 sets out what percentage of 'self generated' State revenue is derived from stamp duty as a whole, and the seventh column once again narrows the focus down to looking at what percentage is derived from land-related stamp duty.

As shown in Table 9, land-related stamp duty (CC+FHPS) revenue has increased over the seventeen year time span, both as a proportion of total current receipts and 'self generated' revenues. It has jumped from comprising 5% of total current receipts and 9% of 'self-generated' receipts in 1986, to 11.4% and 22.3% respectively in 2003. This increase has not been steady year-by-year. As with trends shown in preceding tables, most distinguishable is the housing boom in 1987/88 which caused a notable peak stamp duty as a proportion of State revenue. During those two years, land-related stamp duty's relative importance almost doubled, up from 9% to almost 18% of the State's 'self-generated' revenue. During those years this change was mirrored by the share of land-related stamp duty in total current revenue, this proportion jumping from 5% to 11%. These figures declined after the 1989 peak, with land-related stamp duty typically comprising between 8% and 13% of 'self generated' State revenue and between 5% and 8% of total State revenue during the 1990s. However, recent years have once again seen these figures climb noticeably. In 2001 the relative importance of land-related stamp duty in NSW's 'self-generated' revenue rose from 13.7% to over 20%; and the figure rose even higher in 2002 to a record 22.3%. In total revenue terms, land-related stamp duties in 2002 comprised 11.4%.

Table 9: Stamp Duty as a Share of NSW Government Revenue, 1986 – 2003

Year	Total Current Receipts $M	Total Current Receipts Less Commonwealth (CTH) Grants $M	Total Stamp Duty Receipts as a % of Total Current Receipts	(CC +FHPS) as a % of Total Current Receipts	Total Stamp Duty Receipts as a % of Total Current Receipts Less CTH Grants	(CC +FHPS) as a % of Total Current Receipts Less CTH Grants
1986-87	10,853.133	5,995.882	12.2	5.0	22.1	9.0
1987-88	12,146.900	6,942.800	16.3	8.6	28.5	15.0
1988-89	13,880.600	8,585.100	18.1	11.0	29.3	17.7
1989-90	14,592.024	9,178.434	14.0	6.8	22.3	10.9
1990-91	15,358.404	9,708.334	12.2	5.0	19.3	7.9
1991-92	15,707.506	9,895.023	12.9	5.5	20.6	8.8
1992-93	16,516.873	10,607.408	13.0	5.3	20.3	8.3
1993-94	18,022.000	11,561.000	14.7	6.7	23.0	10.4
1994-95	19,073.000	12,110.000	13.8	5.9	21.7	9.3
1995-96	20,503.000	13,064.000	12.7	5.5	20.0	8.7
1996-97	21,543.000	14,170.000	14.4	6.8	21.9	10.4
1997-98	23,350.000	15,667.000	15.8	7.8	23.5	11.6
1998-99	24,982.000	16,083.000	15.7	7.3	24.4	11.3
1999-00	26,575.000	17,077.000	17.0	8.5	26.4	13.2
2000-01	28,126.000	15,154.000	15.9	7.4	29.5	13.7
2001-02	30,102.000	15,171.000	15.1	10.1	30.0	20.1
2002-03	31,140.000	15,904.000	16.4	11.4	32.0	22.3

Note: CC: Contracts and Conveyances
FHPS: First Home Purchase Scheme
CTH Grants: Commonwealth Grants

Source: Budget Papers, NSW Treasury

Land Tax: a More Fruitful Policy Approach

Alongside stamp duties on property transactions are other State taxes affected by inflationary processes, most obviously land tax. Land tax has been less 'in the political spotlight' than has stamp duty. However, it is equally pertinent to ask how it interacts with the problem of housing affordability and the situation facing prospective first-home buyers.

Land tax is an annual tax on the ownership of land. It is of long standing in NSW. The tax payable is calculated from the unimproved value of the land itself, meaning that buildings on the land or other improvements are not taken in account when the land is valued. The value of land is ascertained by the Office of State Revenue on the basis of annual evaluations made

by the Valuer-General. Land values are determined as at 1 July preceding each land tax year and land tax liability is incurred on the 1 January of the relevant tax year.

Land tax does not apply to all land owners in NSW, because there are numerous exceptions including land owned by non-profit religious societies, charitable or educational institutions. The most important exemption is that which applies to land used for owner-occupied residential purposes. At present, land tax does not apply to principal places of residence where the 2003 value of the land falls below $1.68 million. Originally this exemption applied across the board to all owner-occupied properties where the land did not exceed 2,100 squared metres. From the tax year of 1998 owner-occupied land became subject to land tax if its value exceeded $1 million; and the 2,100 metre rule was abolished. Had the State government kept the threshold at $1 million an increasing number of properties would have become taxable as inflationary processes continued. This would have significantly broadened the land tax base over time. However, the State government, responding to the fierce political pressure mounted by those in high land value areas like Sydney's Eastern Suburbs and North Shore, decided on indexation of the threshold to the rate of inflation. In six years the threshold has risen by 68%. Such indexation acknowledges the politically sensitive relationship between an inflationary property market and State revenue, and contrasts sharply with the rates of stamp duty left untouched since their introduction in 1986. However, being politically astute is not necessarily being economically rational. It is timely to assess how these land taxation arrangements are operating in practice.

Table 10 shows the rates at which land tax must be paid on non-exempt properties in NSW. During the period immediately preceding the first year shown in this table, land tax rates had been on a sliding scale similar in form to that of current stamp duty rates. It had been a progressive tax in that the rate of taxation was higher on more valuable land. In 1986 a system of flat rate land taxation was introduced – at a rate of 2% of the value of land above the requisite threshold, which was then set at $94,000. Land tax has remained a flat rate tax ever since.

As Table 10 shows, for almost a decade from 1990 the threshold remained steady at $160,000 while the rate of taxation until 1996 also remained constant at a rate of 1.5%. With the threshold still steady at $160,000, the rate was increased to 1.65% in 1997, and rose again in 1998 to 1.85%. Although housing prices and land values are distinct concepts, it seems

reasonable to posit that rising house prices (as shown in Table 1) reflect similar inflationary trends in land values. While the value of a plot of land is not directly affected by the house built on it, the market price of a house *is* greatly determined by the value of the land upon which it stands. Consequently during this steadily inflationary 1990-98 period increasing numbers of properties became subject to land taxation. These would typically have comprised either 'investment' properties or 'weekenders'. By definition, land in the form of owner-occupied properties remained exempt, so the inflationary processes did not render any more of these properties liable to land tax.

Then in 1998-99 the arrangements changed in two partially self-cancelling ways. The introduction of the premium owner-occupied property threshold made more properties liable to tax. But the general land value threshold (on investment properties) was raised. Since 1999 thresholds on both investment and premium owner-occupied properties have been rising continuously each year. In 2003 the threshold for premium properties rose by $266,000, that being a 19% increase on the previous year's threshold and the most significant increase since the introduction of the premium property tax.

Table 10: Rates of Land Taxation, NSW, 1986-2003

Year	Land Value Threshold on Investment Property $	Land Value Threshold on Premium Property $	Land Tax Rate*
1986	94,000	N/A	2%
1987	94,000	N/A	2%
1988	125,000	N/A	2%
1989	135,000	N/A	2%
1990	160,000	N/A	1.50%
1991	160,000	N/A	1.50%
1992	160,000	N/A	1.50%
1993	160,000	N/A	1.50%
1994	160,000	N/A	1.50%
1995	160,000	N/A	1.50%
1996	160,000	N/A	1.50%
1997	160,000	N/A	1.65%
1998	160,000	1,000,000	1.85%
1999	176,000	1,116,000	1.85%
2000	192,000	1,234,000	1.70%
2001	205,000	1,319,000	1.70%
2002	220,000	1,414,000	1.70%
2003	261,000	1,680,000	1.70%

Note: 'Investment property' includes 'weekenders' and all other properties other than the single property for each household which is a tax-exempt residence.

***** An additional flat rate $100 charge applies per property

Source: Office of State Revenue, NSW Treasury

How have these changes in land tax arrangements and rates affected the potency of the tax as a revenue source? As with the preceding analysis of stamp duty, it is pertinent to consider the role of land tax in NSW State government revenue. Table 11 shows the relevant magnitudes and trends for the period 1986-2003. The table is similar to Table 9 in that it seeks to show the relative importance of land tax in respect of both the State government's total current receipts and its 'self-generated' revenue ('Total Current Receipts Less Commonwealth Grants').

Compared to the rising relative importance of stamp duty over the seventeen year time period, revenue derived from land tax as a proportion of both total current receipts and ' self-generated' revenue has risen only moderately. The total volume of tax receipts, as shown in the second column of Table 11, has climbed from about $345 million in 1986-87 to $1,134 million in 2002-3. However, expressed as a proportion of State revenues, the growth has been

slow. In 1986 land tax formed 3.2% of total current receipts and 5.8% of 'self generated' revenue. Seventeen yeas later the figures are 3.6% and 7.1% respectively. The period of stable rates and thresholds from 1990–98 was one in which the potency of the tax as a revenue source was quite weak, accounting typically for only about 3% of the State's total current receipts and 4-5% of its 'self-generated' revenue. The years since then have seen a modest increase in these shares. However, unlike stamp duty, the land and property price boom of the last few years has not caused the share of land tax in State revenue to surpass the peak established in the wake of the 1988-89 land and housing boom.

Table 11: Land Tax Revenue, NSW, 1986 – 2003

Year	Land Tax ($M)	Total Current Receipts ($M)	Total Current Receipts Less Commonwealth Grants ($M)	Land tax as a % of Total Current Receipts	Land Tax as a % of Total Current Receipts Less Commonwealth Grants
1986-87	345.577	10,853.133	5,995.882	3.2	5.8
1987-88	413.300	12,146.900	6,942.800	3.4	6.0
1988-89	497.300	13,880.600	8,585.100	3.6	5.8
1989-90	627.389	14,592.024	9,178.434	4.3	6.8
1990-91	789.580	15,358.404	9,708.334	5.1	8.1
1991-92	825.913	15,707.506	9,895.023	5.3	8.3
1992-93	549.334	16,516.873	10,607.408	3.3	5.2
1993-94	519.229	18,022.000	11,561.000	2.9	4.5
1994-95	509.718	19,073.000	12,110.000	2.7	4.2
1995-96	580.000	20,503.000	13,064.000	2.8	4.4
1996-97	625.000	21,543.000	14,170.000	2.9	4.4
1997-98	839.321	23,350.000	15,667.000	3.6	5.4
1998-99	961.000	24,982.000	16,083.000	3.8	6.0
1999-00	889.000	26,575.000	17,077.000	3.3	5.2
2000-01	919.000	28,126.000	15,154.000	3.3	6.1
2001-02	999.000	30,102.000	15,171.000	3.3	6.6
2002-03	1,134.000	31,140.000	15,904.000	3.6	7.1

Source: Budget Papers, NSW Treasury

The ratio of land-related stamp duty revenue to land tax receipts was a little over 3:2 twenty years ago, and it is now well over 3:1 ($3.6 billion compared with $1.1 billion). A strong case can be made for reversing this trend in relative shares, i.e. for shifting to a greater emphasis on land as a means of increasing housing affordability.

Land tax has significant advantages as a revenue source, compared with stamp duty. As an annual tax to be paid, rather than an impost on buying and selling property, it has no equivalent disincentive effect on mobility. Indeed, it may even work in the opposite direction, encouraging mobility among 'asset rich, income poor' people seeking to reduce their land tax commitments by moving to lower-valued property. More importantly from the housing affordability perspective, land tax tends to reduce property price inflation. Because it 'creams off' part of any potential capital gain, it reduces the attractiveness of land as a speculative investment. Other things being equal, that reduced speculative demand can be expected to produce more land/housing price stability.

A uniform land tax on all property at a progressive rate would also be a fairer source of regular revenue. Unlike stamp duty, it would not discriminate between movers and non-movers. As a regular annual payment it would not have the 'lumpy' characteristic of stamp duty and would not impact at times of particular financial stress (like when moving house). It would result in a more rational use of our residential and transportation resources because, unlike stamp duty on property transfer, it is not a disincentive to spatial mobility. People's locational choices could be expected to factor in the ongoing land tax obligations associated with living in particular cities and regions.

Narrowing these concerns to matters of 'fiscal arithmetic', it is interesting to ask how would existing land tax provisions have to change to produce comparable revenue to the existing stamp duties. If, for example, the rates of stamp duty were cut back so that their share of the total 'self-generated' State revenues were halved (from the 2002-03 NSW figure of 22% to 11%) that would mean a fall in revenue of $1,775 million (in 2002-03 figures). What changes to land-tax arrangements and rates could generate an equivalent revenue, ie. create a revenue-neutral outcome? The most direct measure to produce that outcome would be to remove the exemption of all owner-occupied property from land tax.

It is not difficult to establish a 'ballpark' figure of what the land tax rate would need to be if the owner-occupier exemption were removed and an additional revenue of $1,775 million were sought. For example, 2001 Census data indicates that in 2001 the number of potentially taxable private dwellings stood at 1,413,033 in Sydney and 871,359 in Other NSW.[2] If the

[2] For the purposes of this calculation, apartments/units houses and semi detached/town houses are counted equally.

land those dwellings stand upon is valued at half the current median house price of those regions (i.e. $312,000 in Sydney and $140,000 in other NSW) that would give a total value of previously exempt (because of being owner occupied) land that would then be taxable valued at $562,856 million (i.e. $440,866 million in Sydney and $121,990 million in Other NSW).

Some of these lands would continue to be tax-exempt because their value falls below the $261,000 threshold. Not many in Sydney would have a value lower than this threshold, given the prevailing metropolitan land values, but perhaps half of those in the rest of the State would do so. A reasonable estimate would be that a third of the total land value would be tax-exempt because it is in small tracts with values below the taxable threshold. So, in round terms, the estimated total taxable land value would be $375,237 million (ie. two thirds of the total $562,856 million land value). To produce a land tax revenue of $1,775 million annually would require that this property be taxed at 0.47% (ie. 47 cents per $100 property value). This is between a quarter and a third of the land tax rate on non-exempt property, now standing at 1.7%. A more conservative estimate of what land tax rate would be needed to generate the $1,775 million, based on the assumption that *half* of all land tax value would be exempt (because of the threshold), indicates a necessary land tax rate of 0.63%. This is still only just over a third of the current rate. Put differently, were the current 1.7% land tax rate to be maintained and extended to two thirds of owner-occupied properties in NSW, the revenue would be much more than sufficient to eliminate stamp duty altogether. On the basis of the assumptions set out here, it would generate annual revenue in the order of $6,379 million compared with the current land-related stamp duty of $3,550 million in NSW.

Judging whether this policy change is desirable would entail an array of broader political and social as well as economic judgments. A case for stamp duty in its original sense as a ‘filing fee’ can easily be made. Moreover, the preceding calculations are only meant to be indicative of the broad magnitudes of revenues involved in the hypothetical tax changes. However, what this simple ‘fiscal arithmetic’ reveals is that quite low rates of land taxation can be potent revenue-raisers. That is pertinent to the politics as well as the economics of tax reform. Low rates of annual land tax may not generate the overwhelming political opprobrium that has previously caused the major political parties to shy away from embracing any tax reform that can be interpreted as ‘a tax on the average family home’. In the broader sweep of electoral judgments, the key issues are what form the overall reform package takes and how it is presented.

It is also pertinent to consider how any such reform of stamp duty and land tax arrangements might fit into the overall structures of Federal-State financial relations. Stamp duty and land tax are State government taxes. They differ fundamentally in this respect from the major taxes, like income tax and company tax, that go to the Federal government. The States have relied on the Federal government passing some of those revenues on to help them meet their major expenditure commitments on health, education, roads and so on. That is the principal feature of the long-standing 'vertical imbalance' in Federal-State financial relationships: the Federal government raises most of the taxes but the State governments do much of the spending. Not surprisingly, the States have been eager to exploit whatever revenue-raising sources are available to them, such as stamp duties, land tax, payroll tax and gambling tax. As noted earlier in this submission, the effect of property price inflation, without indexation of the rates of stamp duty, has been particularly important for State government finances. A reconsideration of these issues of public finance is timely because the Federal government is now passing on the revenues from the GST directly to the States, so it would be opportune to consider what supplementary revenue sources are necessary and desirable.

The relationship to local government finance is also relevant. The principal 'self-generated' revenue source of local government is also based on land values. This is the revenue from local council rates, the levels of which depend on the unimproved capital value of each individual property. According to the NSW Department of Local Government, these local government rates generated an annual total of approximately $ 1,515 million in NSW in 2001-02 (comprising $1,347 million from residential property and $167 million in farmland rates). A policy change that replaced these local government rates with an apportionment to local governments from a uniform land tax could be an economically efficient, and electorally palatable, reform. More generally, the potential volume of regular land tax revenues opens up an array of possibilities for financing the provision of infrastructure and social services. In this way tax reform designed primarily to deal with the problem of housing affordability, particularly for first-home buyers, can be linked to broader concerns about policies to promote social justice and more balanced urban and regional development.

These reforms, emphasising the extension of land taxation, are more potent than policies such as first-home buyer subsidies which do not tackle the roots of the crisis of housing

affordability. The Productivity Commission is urged to pay particular attention to these matters in its deliberations about policy responses to the first-home ownership crisis.

Conclusion

The problem facing many first-home buyers reflects a more general problem of housing affordability. This submission does not claim to provide a comprehensive analysis of its origins. However, the inference is that a key driver is the focus on housing and land as sources of capital gains rather than residential use-values. The current structure of taxation encourages this, and revenue patterns are shaped by its consequences. Rapid inflation in residential property prices has driven major increases in stamp duty payments, for example. It has been a significantly less powerful driver of revenues from land tax. As a result, the balance between stamp duties and land taxes as revenue-raisers has changed markedly. There is a case for reversing this trend on the grounds that annual land taxes have less adverse consequences for housing prices and spatial mobility.

A switch to higher rates of land taxation seems likely to be the most effective general means of taking the 'heat' out of the inflationary processes affecting housing affordability and disadvantaging prospective first-home buyers. The effects of the different forms of land-based taxation on spatial mobility, the distribution of income and wealth, and patterns of urban and regional development warrant further consideration and analysis. Although this submission focuses on the situation in NSW, the arguments and analyses have a broader national significance. Indeed, addressing the problem of housing affordability through the extension of land tax would work satisfactorily only if it were a nationally uniform arrangement. To the extent that the NSW experience described in this submission is reflected in inflationary real estate pressures in other States too, there are grounds for thinking that the patterns and processes discussed here have more general resonance.

It is hoped that the Productivity Commission will give serious attention to the matters raised in this submission, alongside other important considerations such as how to increase the supply of public housing (identified in a previous Productivity Commission report as an effective means of providing affordable housing).