

# TRANSCRIPT

## LEGISLATIVE COUNCIL ECONOMY AND INFRASTRUCTURE COMMITTEE

### **Inquiry into Land Transfer Duty Fees**

Melbourne – Thursday 11 May 2023

#### **MEMBERS**

Georgie Purcell – Chair

David Davis – Deputy Chair

John Berger

Katherine Copsy

Jacinta Ermacora

David Limbrick

Bev McArthur

Tom McIntosh

Evan Mulholland

#### **PARTICIPATING MEMBERS**

Nicholas McGowan

**WITNESS**

Mr Brendan Coates, Economic Policy Program Director, Grattan Institute.

**The CHAIR:** I declare open the Legislative Council Economy and Infrastructure Committee's public hearing for the Inquiry into Land Transfer Duty Fees. Please ensure that mobile phones have been switched to silent and that background noise is minimised.

I would like to begin this hearing by respectfully acknowledging the Aboriginal peoples, the traditional custodians of the various lands we are gathered on today, and pay my respects to their ancestors, elders and families. I particularly welcome any elders or community members who are here today to impart their knowledge of this issue to the committee or who are watching the broadcast of these proceedings. I also welcome any members of the public watching via the live broadcast.

To begin, we will just go around the room and introduce committee members to the witness, starting with Ms Copsey.

**Katherine COPSEY:** Katherine Copsey, MP for Southern Metro.

**Evan MULHOLLAND:** Evan Mulholland, MP for Northern Metropolitan.

**Tom McINTOSH:** Tom McIntosh, Member for Eastern Victoria.

**John BERGER:** John Berger, MP for Southern Metro.

**The CHAIR:** Georgie Purcell, MP for Northern Victoria.

**David LIMBRICK:** David Limbrick, South-East Metro.

**Bev McARTHUR:** Bev McArthur, Western Victoria Region.

**The CHAIR:** Great, thank you.

All evidence taken is protected by parliamentary privilege as provided by the *Constitution Act 1975* and further subject to the provisions of the Legislative Council's standing orders; therefore, the information you provide during the hearing is protected by law. You are protected against any action for what you say during this hearing, but if you go elsewhere and repeat the same things, those comments may not be protected by this privilege. Any deliberately false evidence or misleading of the committee may be considered a contempt of Parliament.

All evidence is being recorded. You will be provided with a proof version of the transcript following the hearing. Transcripts will ultimately be made public and posted on the committee's website.

For the Hansard record, can you please state your name and the organisation you are appearing on behalf of.

**Brendan COATES:** Thank you, Chair. My name is Brendan Coates, and I am Economic Policy Program Director at the Grattan Institute.

**The CHAIR:** Great. Thanks, Mr Coates. We welcome your opening comments now but ask they be kept to a maximum of 10 to 15 minutes to ensure we have plenty of time for discussion and questions.

**Brendan COATES:** Thank you, Chair. My opening statement will actually be relatively short. I have not intended to make it anything lengthy. I would prefer to take questions from the committee. I would like to start by saying that we really welcome the inquiry, and we are very grateful for the opportunity to give evidence here today. Stamp duty is one of Australia's most costly taxes. It is a substantial share of the Victorian government's budget revenue, but it is very costly because it generates big distortions in how people behave that affect their lives and then ultimately affect their wellbeing. So whether that be people choosing not to downsize in a situation where they probably should, to get a house that better suits their needs or to upsize their home in order to support a growing family, and it leads to a misallocation of the housing stock as well. It leads to people buying larger homes when they first buy a home on the basis they do not want to upgrade later in the future.

And while home ownership is not the only form of housing tenure that can exist in Victoria, it is still the most common form and preferred form of tenure for most Victorians. So if you are making it difficult for people to make those choices, then they will not. They will choose to stay in their existing home, or they will choose to buy a larger home.

I would also point out that stamp duty is also really unfair. It is a tax that tends to hit younger people much more, so we are in a situation where people will buy a home, they will pay a whopping great amount of stamp duty, they may upgrade in future, and with house prices having risen the way that they have, they are paying much more to upgrade than they were in the past. That is leading to a situation where you have got a larger share of the tax take coming from younger Victorians. Whereas, you know, once you have bought your home – now I have bought mine, I am not intending to move hopefully for at least another 30 to 40 years so I will not be contributing anymore to the tax system via property taxes for an extended period of time. I think that is particularly problematic when we face very large costs to deal with issues like health care, aged care and other expenditures for which the state is responsible.

Stamp duties also act as a tax on divorce. Some of the work we have done more recently shows that a lot of people move, that a lot of people sell their home and have to buy again, for reasons other than those that are planned. You have situations of illness. You have situations of separation. And what we have seen in some work we have done recently is, if you are a member of a couple, you lose your house as part of a settlement, which is often what happens because we have to separate the assets that come from the household when there is a divorce. If you are a woman, less than half of women buy again within a decade. So it is one of those things, those hurdles, that is not just contributing to making it harder to buy a home in the first place but also making it harder for people to get back into the property market if, due to life circumstances, they find themselves having to sell the home that they are otherwise in.

The challenge, though, is that we have to raise the revenue that will pay to keep schools open and hospitals running, and that is not an easy thing to do. We would observe that the big challenge when it comes to stamp duty is that, one, we have been unable to work out what tax is going to replace it, because you will need to raise the revenue in some form or another. There is no way that we can simply abolish stamp duty and just carry on business as usual. Secondly, we have found it really hard to manage the transition. So Grattan's position is that we should replace stamp duty with a broad-based property tax based on a council rates base. That is one of the most efficient taxes that the Victorian state government has access to, as other states do around Australia, and the model we should be looking to adopt in the transition is something a little bit like what the ACT has done, where they are part way through a transition away from stamp duty towards property tax. They have set a 20-year deadline in order to achieve that transition. We think it could be done in something closer to 10 years, particularly if there was some sort of credit made available for people that have recently purchased a home, paid stamp duty and do not want to buy again.

That to us is a much better model than the model that has been trialled very briefly in New South Wales, which allows people to opt in. Now the opt-in model has benefits. It means that anyone who has purchased a home recently or even a long time ago is exempted from the change. That neutralises a lot of the political pain that comes from the change. The consequence, though, is you end up with two problems. One is if you have an opt-in model, you replace a tax that is paid up-front to the Victorian state government of \$40,000 or \$50,000 a year on a median-priced home with a tax that may be of equivalent value but paid out over 20 years, so there is a big financing gap. Secondly, and just as importantly, you end up with what economists call adverse selection. So if I buy my first home, as I did in 2016, and I think I am only going to live there for a few years, I will choose to pay the land tax because the net present value of what I will pay over the life of owning that property will be much less than I paid, as it turns out, in stamp duty. Now I have bought the larger home that I expect to be in for a long time, I would choose the stamp duty. So you have the situation where, even in the long run, the revenue you raise from replacing stamp duty with property tax is lower structurally than what you had at the beginning, and that is a big problem. The New South Wales government estimated it was about 20 per cent lower when they did their work.

So if we are interested in replacing stamp duty with land tax, the number one thing we need to agree on is that there is going to be something to replace it. And the number two thing we need to agree on is what is a way in which we can replace it that simultaneously allows the government to continue to pay for the services it offers Victorians. At the same time it deals with the political challenges of asset rich, income poor households, which you can do just by allowing people to deal with any payment they make, any liability that arises from the

property tax to debit that against the value of their home until it is eventually sold – no-one has to move. But also to deal with situations like people who have recently purchased a home a gradual transition, like what the ACT has done, combined with some sort of credit, if it is available, if it is affordable, for people who recently purchased a home, would probably be the way that we would recommend proceeding with that reform. Happy to stop there.

**The CHAIR:** Thank you – very succinct. We will go around the room now with questions from members – around 5 minutes each – and then around again if time permits, starting with Ms Copsey.

**Katherine COPSEY:** Thank you. That was a great segue into my question, actually, which is: can you explain in Grattan's view how credit can be used to make sure that a transition does not disadvantage people who have recently paid stamp duty?

**Brendan COATES:** Thank you, Katherine. The first point I would make is that there is a debate in the literature about where the economic incidence of stamp duty falls today. Does it fall on the purchaser, who is the person who legally has to pay the stamp duty, or does it fall on the vendor, as in the person who is selling the home, who actually gets less for the property because the person who is buying it has to pay stamp duty? My read of the literature is most of the cost of those stamp duty payments – the economic incidence – actually falls on the vendor, as in they receive less for the home than they would if the purchaser did not have to pay stamp duty. So if you think about the economics of that, that would suggest that the vendor is already paying it and the purchaser is in fact not. But there is some evidence that suggests that part of it potentially is borne by the purchaser as well. So a credit is a way of both on the pure economics but also the politics managing that transition. If you have recently purchased a home – you have paid 50 grand on stamp duty for the median-priced home in Melbourne – then that is a lot of money. You might be aggrieved if you start to pay a land tax. So a way that could work would just be a simple credit that lasts a couple of years. It could start at a higher level then basically be phased out over somewhere between three and five years on the property tax that would apply on the property. If you have a gradual transition where the stamp duty is coming down over 10 years and the land tax is going up over 10 years, to the point where it fully replaces the value of the stamp duty revenue to the state, you could have a situation where you basically exempt them for potentially five years from the point of purchase. So if they bought three years ago and the reform comes in, they might be exempt for the first two years. So there are different models that you could do.

The answer to that question, Katherine, ultimately comes down to what the revenue hit is and therefore how much revenue the state government has to give up in the process of that transition, because obviously the more generous the credit, then the larger the revenue hole you are creating that you are not going to get back. Now, there is an economic pay-off to that. There is potentially a budgetary pay-off for the state government as well, because you get a larger economy. But that is ultimately going to be the result of some pretty detailed modelling by a government, or by this committee, in order to make clear exactly how you balance those pieces of the puzzle.

**The CHAIR:** Thanks. Ms Copsey, do you have another question?

**Katherine COPSEY:** Yes. I am also interested to hear how a deferred tax could be used to enable people that have valuable land – so asset rich, income poor – in the event of a transition. What is Grattan's view on that?

**Brendan COATES:** Thanks, Ms Copsey. What we would envisage is what applies often today when it comes to council rates and is also available via the federal government's home equity release scheme. If you are in a situation where you are unable to pay your council rates – I believe this is the case in Victoria; it is certainly the case in some other jurisdictions, certainly in the ACT – you are able to defer the value of any property tax liability that arises in a year. So let us say you own a property that is worth \$1 million and there is a tax of \$2000. That tax can be deferred. It can basically accrue as a debt accumulating against the value of the property, with interest of course. And then, over the course of 20, 30 years, even, you will find that the value of that debt becomes much smaller than the value of the property, and at the end of the day the property can be sold. Typically, that occurs when someone either goes into aged care or they pass away, and the debt can be discharged. So that is how we would see it working today.

The federal government also has the home equity release scheme, which is an alternative way or means that people can use to basically borrow against the value of the home in order to, in that situation, boost their retirement income, given they have got a large asset that they are not actually utilising in retirement.

**The CHAIR:** Thanks, Ms Copsey. Mr Mulholland.

**Evan MULHOLLAND:** Thank you. Thanks for coming in and for your submission. I thought your submission was very valid, particularly on women's economic security and it being a barrier to that, especially in the case of divorce. I just wanted to ask you: in terms of stamp duty, but more so supply, do you think stamp duty and restrictions on supply are having an impact more broadly on family formation? Victoria has got, I think, the lowest rate of family formation in the country at 1.48 children per woman. Do you think that supply constraint and stamp duty is slowing that here?

**Brendan COATES:** Certainly, Mr Mulholland. I would say housing affordability and the cost of housing itself are clearly affecting the rates of household formation. Now, that can be in the form of people choosing to have more children. It can be in the form of people choosing to stay living at home or in the form of people choosing to stay in share houses. Certainly I think it is no coincidence that the household headship ratio, so the share of younger people in Victoria that are living as the head of the household – as defined by the ABS, they are the prime breadwinner in a particular household – is lower in Victoria and in Melbourne than it is in most other states, and that correlates pretty strongly with housing costs. Now, restrictions on supply arising from land use planning rules are certainly a big driver of high housing costs in Victoria – you know, we see that in the premium for well-located land close to the city centre – and the costs of those supply restrictions have ratcheted up in recent years. Now, of course land use planning rules have a role to play. You do not want to put an abattoir next to a school, but it does appear to –

**Bev McArthur** interjected.

**Brendan COATES:** Well, that is another –

**The CHAIR:** I agree with the first statement, Bev.

**Brendan COATES:** You know, what we are talking about here is we are talking about land uses that affect the neighbours, and there are a variety of them, as the committee's comments make clear. But the cost of those land use planning restrictions is that you see fewer people living close to jobs and living close to amenities, and we certainly see that in Victoria. There is a really strong correlation where we see more objections, certainly at VCAT and at the council level for properties, in past work that Grattan has done, which link pretty closely with the socio-economic status of the area. So we see less housing being built than arguably should be built in the east and the south, and we probably see – I would not say more housing than what we need, because we need more housing, but certainly the pattern of urban development is favoured more in the west than the north.

**Evan MULHOLLAND:** Just on the supply thing, I understand your view on stamp duty, and they are all very big, hard reforms. But in terms of the micro level and in terms of supply, particularly where it gets held up with local government and some of the things we were talking about there, do you think more can be done to incentivise local government to approve planning approvals where they are slowed down? I guess we are seeing a generational shift where lots of young people are describing themselves as yimbys – as in, 'Yes, in my backyard' – countering some of that old narrative. What do you think of that, and how do you think government can incentivise approvals and disincentivise the holding up of approvals and so many VCAT applications?

**Brendan COATES:** Thank you. I was at the launch of YIMBY Melbourne a couple of weeks ago, and it was a very exciting thing to see happening. I am really excited to see what that group can produce. When it comes to restrictions on housing construction, there is a set of rules that are set at the state government level – the zones – and that is a state government responsibility ultimately. So that is one place and probably the biggest place that you would hope to see change, because the zoning rules actually do the most to determine what can be built. On top of that, though, we then see the way particular councils operate, and you see essentially more councils opposing particular developments and things often going to VCAT. There are a lot of costs and delays. Sometimes they end up being approved; sometimes they do not. So in the case of the second, in particular, there is a role the state government can play to incentivise councils to actually allow more housing to be built. The best way to probably do that would be to pay the councils or to reward the councils for set

targets for housing supply. If they meet those targets or if they exceed them, then there can be some financial benefit on offer. That financial benefit could come from a broader tax on the upzoning of rezoned land. That could then be used to meet community needs for infrastructure and other demands in the local community.

There are good reasons why some people in communities do not like to see more housing being built. It affects the quality of life in their street. On occasion I think that that is often overblown, but it is a real thing. So if the concern is 'I'm going to have a lot more medium-density housing in my area' and the benefit is 'I get six new parks around the corner', then that is the sort of political sentiment we should be looking to achieve.

**Evan MULHOLLAND:** Excellent. Cool.

**The CHAIR:** Thanks, Mr Mulholland. Mr McIntosh?

**Tom McINTOSH:** Thanks for presenting. Just given the conversation around a replacement of the tax or a transition or anything along those lines, there are some voices that put forward different alternatives and one is for less tax. I represent Eastern Victoria, so there is demand for services to ensure that our regional and rural Victorians have adequate road services and all that sort of stuff. Do you see any risks to potential changes in the tax system here in Victoria with the implications that could have, not just for regional and rural Victorians but also our suburban new suburbs where we need that infrastructure invested in by the state government to support community and people?

**Brendan COATES:** Thank you for the question. So if the concern is we need to have sufficient revenue to provide the services that we need, including services in regional Victoria and the kind of infrastructure provision that is needed as we grow the city, then the best way in which we can achieve that is to make sure that any tax that replaces stamp duty is of the same size as the existing stamp duty regime so that we are generating at least the same amount of revenue as what we were previously. I think it is well documented that Victoria has got a few challenges when it comes to the state budget. We are in a world, as we have seen in New South Wales – New South Wales has run intergenerational reports that show state budgets are going to be put under more strain in future, not less. So you probably want a tax that is going to grow with the costs of providing those government services. And taxing land, taxing what are often unearned rents that are arising from, you know, investments in the community, in infrastructure, in schools and in health care, that accrue to the land – the property value – of the owner, that the owner has done nothing to generate is just about the best way we can do that going around. And certainly if you solve that problem at the state level where there is enough revenue, then we can be in a position where we can reassure regional Victorians and others that there will be the services there that they expect and need.

**Tom McINTOSH:** Yes. The presenter of the last submission talked about equity within the system. So the suggested low rate broad-based property levy is not suggesting less revenue but suggesting that it is more broadly collected, is it?

**Brendan COATES:** As in that it encompasses agricultural land in particular?

**Tom McINTOSH:** No, just from your suggestion, because the words 'low rate' are in there, but that is accumulated across many to get the equivalent. So you are not advocating for abolishing or reducing revenue or anything like that.

**Brendan COATES:** No. The one thing I would add, though, that does go to this question is that stamp duty is a progressive tax – as in we charge higher rates of stamp duty on more expensive properties than we do on less expensive properties. That leads to a concern that if you replace a tax that is progressive with respect to property value with one that is flat, which is what our first best principles approach would suggest, you are going to increase inequality. It is worth keeping in mind that the evidence we have is that properties that are more expensive are turned over less often. So if you are thinking about the tax liability that attaches to a particular property – the net present value of that over, say, 100 years – it is not clear to me that replacing a stamp duty that is progressive in nature, with a higher tax rate on a \$2 million property than a \$500,000 property, with a flat-rate tax applying to all land would actually lead to different outcomes than what we see currently. But if that was a concern, the costs of imposing a progressive land tax or property tax, where the ad valorem tax rises in line with the property value, that is certainly something that could be considered. That is what the ACT has done. The economic costs of that kind of progressive rate and ad valorem rate per

property are very low or appear very low based on some work that was done by KPMG a few years ago, so that is another way in which we would address the concerns. I am not sure if that goes to your question or not.

**Tom McINTOSH:** I think that is adequate, thank you. I am mindful of time.

**The CHAIR:** Thanks, Mr McIntosh. Mr Berger.

**John BERGER:** Thank you, Chair. Thank you for your appearance and presentation today. I am interested to hear a little bit more about the adverse selection and a bit more detail around that.

**Brendan COATES:** Certainly, Mr Berger. So, let us say we went down the New South Wales model, noting that the New South Wales model may not last very long with the new government in power. If we went down the New South Wales model, it involved people having a choice of being able to pay stamp duty or land tax, and that would be how you would manage the transition. The value of that is that no-one is being levied a tax that they have not chosen to pay through an action that they have made, that is, purchasing a new property. The issue is that if you want to at the aggregate replace stamp duty with land tax you work out what is your land tax rate that you would need across the state that would replace the revenues that you previously got out of your stamp duty. Now, if you then give that option to people, they have got information about how long they expect to stay in the property that the government does not have. So if you apply the same tax rate – maybe it is 0.2 per cent of the property value – across the whole state, then if someone only expects to stay in the property for five years and they buy a million-dollar home, at the moment they would have to pay \$50,000-ish in stamp duty. They would instead, if they know they are only going to stay there for five years, only pay \$10,000, so they would choose land tax and the government would be short \$40,000.

**John BERGER:** Is that adverse or calculated?

**Brendan COATES:** Well, the economic term is adverse selection, but it is clearly calculated. It is an adverse outcome because if the response from the government was to say, 'Okay, well, we need to increase the value of the tax to account for the fact that there is adverse selection' – people will make that choice – then you further weight the choice in favour of the stamp duty over the land tax. Let us say we are going to raise 20 per cent less revenue if we did this and people choose the thing that is best for them. Then if you say, 'Well, let's make the land tax 20 per cent higher than what we would otherwise need in order to replace the stamp duty,' then even more people will choose to pay the land tax over the stamp duty.

**John BERGER:** But nonetheless, it is a choice.

**Brendan COATES:** It is absolutely a choice, but the consequence for government – the economic term is adverse selection; it is not suggesting any morality or immorality in the choice, it is just the economic term that is used to describe that behaviour.

**John BERGER:** Thank you.

**The CHAIR:** Thanks, Mr Berger. Mr Davis.

**David DAVIS:** Thank you for your thoughtful submission. We are in a position – and I pick up your points on New South Wales and Canberra – that in 2014 the current Premier went to the election, and on the night before he promised he would not introduce new taxes. In 2018 we had a series of similar promises by him and the Treasurer, and yet there are 44 new taxes introduced since the change of government in 2014, so I come at this from a position of mistrust. If we moved to a position where we brought in a land tax of this type, the risk to me – and I will ask you a very clear question at the end – is that we will get stuck with both, and that is effectively where it feels like it is heading in Canberra at the moment. Can you guarantee that if we moved in this way that we would not end up with both? Effectively higher tax –

**Brendan COATES:** The contention there is that the outcome in the ACT is that there are higher tax rates and tax collections than otherwise would have been the case in the counterfactual world where that never happened.

**David DAVIS:** I think that is the received view, widely.

**Brendan COATES:** I think that is the received view. I am not sure how strongly it is backed by the evidence. I would be happy to take on notice going and looking back at that, because it is not something that we have done recently. I do have recollections that the change was pretty close to revenue neutral, but setting that –

**David DAVIS:** This is my point. I think that was the intention, but I think that is not what people think has happened.

**Brendan COATES:** No, and –

**David DAVIS:** Even aside from Canberra – and I think this is a live case study – the risk here in Victoria if next year, say, or later this year, we went to a land tax system, what is to stop the state government breaching promises to get rid of the stamp duty and we all end up with both?

**Brendan COATES:** I think the reason many people think in the ACT, or the claim is made, that they are paying higher taxes is because house prices have gone up a lot further – the value of the property tax base is much higher. That is potentially a different question to: is this regime charging them higher taxes than they would have if the old regime had been in place with the same increase in property prices that we have seen? But just setting that aside for one moment, I think it is pretty unlikely that you would end up in a world where you collect substantially more revenue out of a land tax than a stamp duty for the very reason why we have not actually made this change previously, which is that land taxes are highly salient. People see it on their bill every year, their council rates. Stamp duty is something you pay once and then you often forget about for 20 years. For example, there is evidence in the US that states that collect their land tax through repayments on mortgages, basically through the banks, have higher rates of land tax than states that do not because that salience of the annual bill is the thing that ends up restraining the amount of money that you collect. No-one talks about the fact they paid stamp duty 20 years ago, but plenty of people complain today that they got their land tax bill last month. So can I guarantee it? No, I cannot, because I am not the Premier, but –

**David DAVIS:** But a fiscally challenged government, as I think you indicate Victoria now is, might be tempted to have both or a version of both.

**Brendan COATES:** If I was sitting in the shoes of Tim Pallas as the Treasurer and I was seeking to raise the revenue take, I would not look at this and think, ‘This is a great place to raise the revenue take’, because of the political costs that I have just outlined. If I was the Treasurer sitting in those shoes, I would be looking at other revenue measures in order to get there.

**David DAVIS:** Thank you.

**The CHAIR:** Thanks, Mr Davis. You touched before on stamp duty being a divorce tax. Could you tell us a little bit more about the research you did into that? And with your comments about 50 per cent of women not buying a home within 10 years, would you go as far as to say that it is impacting women sort of more adversely in that circumstance?

**Brendan COATES:** Yes, I would. Thank you, Chair. The work was done using the HILDA dataset – this is the household, income and labour dynamics survey; I may have bungled that.

**The CHAIR:** We would not know anyway.

**Brendan COATES:** Well, the record will show, clearly. That tracks people longitudinally over time, so what we do is we can see how people’s life circumstances change over time. What we see is that we can measure in that survey when do people separate, were they home owners beforehand, did they lose their home as part of that experience, and then what share of them bought again within, say, a five- or 10-year period. What we find is that of women who separate from their partner and lose their home, 34 per cent, so a third, buy again within five years and only 44 per cent do within 10 years. For men the numbers are 42 per cent of separating men buy again within five years and 55 per cent buy again within 10 years. And the reason why stamp duty is such a problem for that is that if you buy a home for, say, \$1 million as a couple, then a couple of years later you separate, you have to sell the home to liquidate the home to be able to share the equity that you have in that home between the two of you. The reason that is such a problem for older women in particular is because when you are 45 or 50, you may only have 15 years left in the workforce. You will find it very hard to be able to purchase a home and pay off the loan, including the stamp duty, by the time you are retiring. So the effect that



stamp duty has is, compared to someone who never separates, that person has had to pay another whack of \$50,000 in stamp duty that they otherwise never would have had to pay. If they bought a new home when stamp duty was gone, they would still have to pay the land tax, but they would have had to pay the land tax in their existing home if they had never divorced in the first place. We think this is a big concern, because we know that – I do not have the stats in front of me – a large number of women who find themselves renting at retirement end up in poverty. We know that half of all retirees who are renting are living below the poverty line today.

**The CHAIR:** Yes, the largest growing cohort of people experiencing homelessness. In the circumstance where women are affected by this, have you explored any options about, I guess, concessions or exemptions that do not currently exist to assist women in that circumstance? Obviously you do not have the power to implement them, but recommendations that have been put forward.

**Brendan COATES:** We have not gone down the path of recommending concessions to stamp duty in that situation. Where we have gone in the past is Grattan has proposed that a shared equity scheme is probably the easier way to deal with that situation. We proposed one at the federal level. The Victorian government does have one as well. So we think that is probably the better pathway in the first instance. If you have a concession for older women to avoid paying stamp duty but you do not fund it from anything, then obviously that is a hit to the bottom line.

**The CHAIR:** Yes. Great, thank you. Mr Limbrick.

**David LIMBRICK:** Thank you, Chair, and thank you, Mr Coates, for your submission. I was particularly interested in the analysis. There is actually a really good chart, figure 2.3, which shows I believe, and maybe you can clarify this for me – this looks like evidence of misallocation of housing stock, and it seems to be suggesting that a renter is more likely to choose the right size house because they have less spare bedrooms. Am I reading that correctly?

**Brendan COATES:** That is right. I am just pulling that one up. So when we look at figure 2.3 in the submission, you certainly see – this is households needing extra bedrooms or with spare rooms. If I recall correctly, because this has come from a previous report, I believe this is with reference to the Canadian occupancy standard, which is a standard that says how many bedrooms you need based on the size of the household. But what it clearly shows, irrespective of what precise measure we have used here, is that certainly those without a mortgage, often older people, have many more bedrooms. So it points to the fact that people do not downsize when they arguably could – noting that stamp duty is not the only reason that people do not downsize – but it leads to a misallocation of the housing stock. When you think about right now at a time when we lack housing relative to demand, anything we can do to improve the allocation of the housing stock would be a huge step forward.

**David LIMBRICK:** Yes. You briefly mentioned there that there are other factors. We have all discussed the idea of, you know, the empty nester having misallocated housing because they do not want to downsize and pay the stamp duty. The Department of Treasury and Finance – we brought that up with them in the last hearing, and their response was that they did not believe that stamp duty was the biggest driver in that particular scenario. They said a larger driver was the way the assets test and pensions work. So I suppose what I am getting at is we may see potentially some reallocation of that group, but there are still going to be other frictions apart from stamp duty. Is that the case?

**Brendan COATES:** Yes. And even broader than that, you know, a lot of the barriers to downsizing are not financial at all. It is people, you know, being either unable to find a –

**David LIMBRICK:** They love their house.

**Brendan COATES:** Yes, they love their house, they love the garden, they have the memories, or they are unable to find a property that is suitable in the neighbourhood for them to move into, which goes to questions around restrictions on what can be built. And then, yes, within the financial domain stamp duty is one of several of these impediments to downsizing. I actually think the bigger issue with the misallocation of the housing stock is arguably, potentially – we have not done the work on this – on the way in. That is actually a big one as well. People choose a larger home when they may not have kids for five or six years, seven years, basically because they are worried about having to pay stamp duty a second time when they upgrade.

**David LIMBRICK:** Right. So they are planning for the future and taking that into account. That is a really good point. And in your recommendation for switching to a broader base, you are effectively saying that we should just model it on the council rates, that is what I am seeing here. And you put in an estimate here of \$5 for every \$1000 of land value – so 0.5 per cent. Am I reading that correctly? It seems like a pretty small increase overall. Is it?

**Brendan COATES:** Well, yes.

**David LIMBRICK:** That would cover the current stamp duty gap.

**Brendan COATES:** That would. So, you know, I always am cautious when I start trying to multiply by too many zeros, but, you know, if you are talking about a home that is worth \$1 million where the land is worth half that, which is often the case for residential property, then you are talking about an annual levy of \$2500.

**David LIMBRICK:** How do we think that that would actually be raised? At the moment councils charge that, but would the state government simply replicate that system, or are we proposing that the council would raise it and pass it on? How would that actually work, do you think?

**Brendan COATES:** We would do it in the same way as we do the fire services levy here in Victoria.

**David LIMBRICK:** Yes. Okay.

**Brendan COATES:** You could think of this as an expanded version of the fire services levy to replace stamp duty.

**David LIMBRICK:** I will pass it on to Mrs McArthur.

**The CHAIR:** Thanks, Mr Limbrick. Mrs McArthur.

**Bev McARTHUR:** Well, I am glad you raised the fire services levy. I am also interested in whether you subscribe to taxes on taxes. The GST is applied to the fire services levy and it is applied to stamp duty. Would you propose that GST be applied to the property tax?

**Brendan COATES:** That is a good question. You may be testing my knowledge of how the fire services levy precisely works here in Victoria, because it is applied to the value of the property.

**David DAVIS:** I am not sure it does now. It used to, I think, Beverley. I do not think it does now.

**Brendan COATES:** The fire services levy is a tax on the value of the property, right? The property itself – the value of the property – is not liable for GST, so I do not believe that that is true.

**Bev McARTHUR:** Well, it must have been changed, because you used to pay tax on the fire services levy – GST – after you had paid it.

**Brendan COATES:** That would probably have been at the time when the fire services levy was applied to insurance.

**David DAVIS:** Correct.

**Brendan COATES:** Right. Thank you. So now we are in a world where the levy is applied to the value of property, which is GST exempt because there is no transaction. If I have to sit in my home every year, then I am not making a transaction that is liable for GST or anything else. So, no, this would not be liable for GST because it is a tax on the value of the land, not a tax on any transaction that might take place.

**Bev McARTHUR:** How would it apply to rural properties and businesses?

**Brendan COATES:** You could apply it in line with the existing council rates base, right?

**Bev McARTHUR:** As an independent public policy advice institute, how often do you suggest that governments should actually abolish taxes and not replace them, or reduce taxes? I am mindful of somebody who once said, 'I'd be very happy to pay more tax if I could be assured the government was spending it

wisely.’ Where do you stand in that situation – in actually encouraging governments to reduce their level of taxation?

**Brendan COATES:** We tend to focus more on improving the efficiency of the tax mix. The reason we do that is because that is where we think the biggest gains are, whether that is reducing taxes on insurance duties or whether it is reducing taxes by stamp duty. Grattan has a budget policy program which assesses the fiscal sustainability of state and federal governments. It would be our observation that in a world where you have got an ageing population, we have difficult choices to make. We can either reduce the services and spending that is available via things like the health system, which tends to be more efficiently delivered by a universal public insurer, or we can raise the revenues we think that we will need to meet the fact that those costs are shifting onto the state’s books because that is what people want to consume – more health care. So we have tended to be of a view that if we are thinking about solving state or federal government budget issues, it is probably going to be a mixture of spending cuts and tax rises, and we tend to support both.

**Bev McARTHUR:** Okay. I am just interested also in your assumption that in a stamp duty situation people decide how long potentially they are going to stay in a property. How valid is that really, because it does not take into account the fact that, as you have mentioned, there can be divorces, there can be domestic violence situations, there can be deaths and so on. Is it practical to suggest that people make a decision about property based on how long they are expecting to be there? Things change dramatically suddenly.

**Brendan COATES:** Certainly there are many reasons that things can change. Those things for the individual person can often appear random, but at the population-wide level you do know that some portion of people are going to have to shift. What we tend to find, though, is that: if you think about people in your own life that are buying a home, if they buy a two-bedroom apartment as a 26-year-old, are they intending to have a family with two children in that apartment or not? There are certainly enough people out there who choose to make that one step onto the property ladder and then upgrade. Many people go on what you might call a property journey where they start on one property and then go to the next one. There are enough of them for it to materially affect the revenue that you would raise with the opt-in model. It is sufficiently prevalent. Even though life is full of chances and strange events, there are certainly enough people for whom people will make a calculation, particularly if it is like: ‘I’m choosing an apartment so I’m probably not going to be able to live in with two kids.’ Then you know that place has got a shelf life of five or six years, if that is what your plans in life probably are, noting that that can change too.

**The CHAIR:** Thanks, Mrs McArthur. We have got 15 minutes left, so we will go around again, but try and keep it brief. Ms Copsey.

**Katherine COPSEY:** I just have one further question, actually. Mr Coates, you have already touched on this in your answer to Mr Berger’s question earlier, but I just want to drill down a little on the New South Wales model and the impact of that model of a choice between paying stamp duty now or land tax later over a longer period. Can you outline with a bit more substance the impact that can have on a state budget?

**Brendan COATES:** That is a great question, Ms Copsey. So when it comes to the New South Wales experience, it is worth pointing out that there was a difference between what was originally proposed and then what the government in fact legislated. I think it is pretty clear, looking from the outside as an observer, that the objective was to put forward an opt-in model, then to be very clear, as Premier Perrottet was at the time, that this model would not be able to be implemented by New South Wales alone and that it would need federal support. That federal support was not forthcoming, and they ended up with something much less ambitious that they had legislated before the last election. So the question was – just remind me again, Ms Copsey. I am sorry.

**Katherine COPSEY:** It is the choice model, the opt-in of paying stamp duty now or land tax over a longer period of time – what the impact of that model is, or can be, on a state budget.

**Brendan COATES:** If you think of, say, the Victorian budget, I think it raises \$8.9 billion or \$8.5 billion from stamp duty in a given year at the moment, at least according to the budget papers. So you have got \$8.5 billion of state revenue. If you allowed everyone the choice of choosing stamp duty over land tax – so the 4 or 5 per cent of properties that are turned over each year, because that is what that revenue is raised from – then what you would see happen is the government giving up \$8-plus billion in revenue and getting some smaller amount of money in year one, because it would get a land tax. Now, that land tax would then be

repeated each year, so over time you would lose \$8 billion and then you would gradually see more of that revenue rise. Now, that period can take a long period of time; I cannot recall the particular modelling done by New South Wales Treasury on that proposal, but it was a sizable share of revenue for quite a long period of time. Then you would see some sort of evening off, some equilibrium level, where not everyone would choose the land tax over the stamp duty. So the people who expect to hold their property – noting the uncertainties that the committee has raised – for longer than, say, 15 years or so would ultimately still choose to pay the stamp duty, right. But then because of this issue of adverse selection, where people at each point when they are making a property purchase choose to do what they think, in their expectation at the time they make the decision, is going to be most financially beneficial to them, you end up – I believe the revenues were 20 per cent below. So in the New South Wales context, when they did the model, if you applied that to Victoria, that is a long-term budget hole of about \$1.6 billion – probably more like \$2 billion given that stamp duty revenues are likely to continue rising in the long term as property values rise.

**The CHAIR:** Thanks, Ms Copsey. I do not think we have any –

**Evan MULHOLLAND:** Just a quick one.

**The CHAIR:** Yes, Mr Mulholland.

**Evan MULHOLLAND:** Sorry. I asked this of a previous panel, so I will ask you: just in regard to supply and effect on supply of housing policy proposals, there is a policy that has been floating around the media of a rental freeze. Do you have a view on what that would do to housing supply and development and the effect that policy would have on the housing market?

**Brendan COATES:** No worries. So the idea of a rental freeze, what the impact would be, and I note that when we talk about what I commonly refer to as rent controls, there are different levels. So the ACT, for example, has a policy that the rent cannot rise I think more than a couple of percentage points above the rental CPI for that state, for that jurisdiction, whereas if you have a pure rent freeze where rents cannot rise at all, the effects – it is a scale.

So what would be the effect? Well, the main effect would be a transfer from the landlords to the existing renters where rents would otherwise continue rising, most likely, particularly in a supply constrained environment. That would see those renters benefit. They would get lower rents, particularly in the short term. In the short term, if you froze rents in a world where rents are rising by 10 per cent a year, the concern that we would have is that at the moment the reason we have such high rents or rising rents is partly migration but also partly because a lot of us have spread out. We have decided to move out of share houses, to move out of the family home, to get a home with more bedrooms or home offices. We would say that probably two-thirds of the impact of the rental crisis at the moment is actually from the latter of those – it is the choices of Australians since the pandemic – and that about one-third is arising from the rapid return of migration post the pandemic. So if you have a situation where people are not exposed to the cost of scarce housing, fewer people will move back in with their parents and fewer people will move back home or into share houses, and the net effect will be there will be fewer homes for people that have to find a place. The concern is that you end up in a world where homelessness is higher because people cannot find a home and as a result of that they end up living in caravans or in tents, particularly, for example, in situations where there is domestic violence and they have to leave.

What does it do to long term supply? Well, the impact on supply itself from this does not appear to be particularly large when we have looked at it because the main constraint on supply in a lot of the literature is the land use planning rules that we discussed earlier. Changes in rental controls around how fast rents can rise do not have a huge bearing on that. What they do do is affect the incentive of the landlord to maintain the existing properties, so you see the quality of the housing stock fall.

**David DAVIS:** You end up with slums.

**Brendan COATES:** You end up with poorer quality housing than you otherwise would. There are two ways in which we add to housing supply: we add new dwellings, or we fix up or add some improvement to a home that is already owned. So we do not think the impact on supply would be that large, but you would then get a big issue where you have insiders and outsiders. Those that have a rental property that is a rent-controlled apartment, for example – this is widespread in places like New York – do very well, but no-one else can get into the area, so you end up with a two-tier rental market. I think that is something we should really try to avoid.

**The CHAIR:** Thanks, Mr Mulholland. Mr Davis, do you have anything? No. Mr Limbrick.

**David LIMBRICK:** Thank you. I wanted to touch on something that was discussed earlier today. Stamp duty revenue is a function of not just the house price and the rate but also of transactions. It was also suggested earlier today that lowering the stamp duty rate would incentivise more transactions to take place, that we could actually be on the wrong side of the Laffer Curve and that maybe lowering the rate might be able to be done potentially without lowering revenue. Do you think that is even a possibility, or do we have modelling to know that that is the case?

**Brendan COATES:** Look, it is an interesting question. I think my initial reaction is to be a bit sceptical because most Laffer Curves tend not to exist the way that we would like them to in real life. That is my experience. But you would need modelling that basically determines the rate of household turnover, and we have not actually done modelling on that. I am not sure if the Reserve Bank has in fact done modelling that tries to causally derive, using econometrics, what in fact drives household turnover.

**David LIMBRICK:** Yes, but it is a reasonable thing to suggest that a lower stamp duty rate would incentivise some transfers to happen that would not otherwise happen on the margins – that seems like a reasonable thing.

**Brendan COATES:** Yes, so at the margin you would see more transfers happen. The question is: does that lead to more or less revenue? My instinct is that it probably leads to less revenue, but it is not something that we have looked closely at. Look, if we end up with a world where we reduce the rate of stamp duty, that is better than leaving it where it is. We would probably prefer a situation where we go all the way, because the land tax is the most efficient tax that we have. There are big economic gains from shifting to that from stamp duty. If you in fact see many more transactions occurring in a world where stamp duty falls, what that would tell me is that stamp duty is actually a bigger impost on people's choices than what we actually thought it was.

**David LIMBRICK:** Right. Thank you.

**The CHAIR:** Thanks, Mr Limbrick. Mrs McArthur.

**Bev McARTHUR:** I am very interested to go back to this issue of applying a land tax to rural property and the farming community. So what modelling have you done on the extra costs added to agricultural production if you tax rural properties? Currently in many local government areas the greatest proportion of rates are paid by farmers and rural properties, so not only are they stung in that department, paying a higher rate on the dollar than households in those communities and significantly higher than in urban and metropolitan communities, but now with your proposal there would be an added tax. How much is that going to affect the cost of production?

**Brendan COATES:** Well, economic theory would tell us that if you have a tax on land, then the effect of that is basically a reduction in the value of that land, right? So the value of those properties would fall. It does not tend to lead to a change in the markets for goods and services because those markets are unchanged as a result of the levying of the tax. Yes, let us say if you are a farmer or a baker or a dentist and you own your premises – or a home owner – obviously you are paying more. There is a transfer that is occurring from those that currently pay stamp duty, which tend to be younger, to a community that currently do not who would have to pay something, and that is defrayed across, you know, everyone who owns property. So there is that transfer that occurs, but we would not expect there to be a change in the price of agricultural produce and therefore food in the supermarkets as a result of the change.

**Bev McARTHUR:** How could you possibly come to that conclusion? If you add an extra tax on the cost of production in agriculture and you are saying –

**David DAVIS:** It is an input cost, isn't it?

**Bev McARTHUR:** Absolutely an input cost. How could you possibly come to the conclusion that it would not add to the cost of the end product?

**Brendan COATES:** Well, those markets have not changed. The price which the farmer can charge for the product with the supermarket or anyone else has not changed.

**David DAVIS:** But it is the export side of it. So if you are a farmer and you are exporting your produce, you are going into a market there where your cost base has now gone up. That is surely going to have an effect on your competitiveness overseas.

**Brendan COATES:** The farmer is seeking to maximise the yield on the farm. The land tax does not change that calculation. The net effect on the farmer is that they have an additional cash flow outlay. So it makes the farmer worse off than they would have been otherwise, noting that obviously farmers have to pay stamp duty when they purchase properties as well.

**Bev McARTHUR:** Yes, but they do not change their properties very often. You might have a farmer that has been in the property for 50 years. You are suggesting that they now pay an annual tax. That is a new cost to production.

**Brendan COATES:** But I do not see how it changes the production decisions of the farmer themselves. Their net wealth will be lower, just as anyone's would be if they were paying stamp duty, as I outlined the transfer before, but it is not changing the production choices I can imagine them making.

**Bev McARTHUR:** They would have to add the cost of that extra input onto their produce, onto the end product.

**Brendan COATES:** Well, I think that depends on has the market changed for the product that they are ultimately selling. So at the moment if we assume that market is competitive –

**Bev McARTHUR:** Or else they reduce their amount of income.

**Brendan COATES:** Yes.

**Bev McARTHUR:** So that is what you are really suggesting, that the farming community would actually have their income reduced as a result of a property tax levied annually.

**Brendan COATES:** The first-round effect of the tax, of replacing stamp duty with land tax – I will point out that we have not done detailed work on the impact on the agricultural sector based on the rate of transfer or turnover of properties, of replacing with a property tax. The first-round effect of replacing stamp duty with land tax would be that those farmers would have a larger cash flow outlay because of the tax. You know, that is the design. Keep in mind that there is a second-round impact of the tax, which is a larger domestic economy. We estimate that the GSP in Victoria could I think be up to \$4 billion or \$5 billion a year higher. So there is a second-round effect that Victorians are wealthier as a result, and the agricultural community would share in that because Victorians would have more money to spend to pay for goods and services, including agricultural produce, and they may in fact buy more.

**The CHAIR:** Thanks, Mrs McArthur.

**Bev McARTHUR:** Totally unacceptable.

**The CHAIR:** That is time. Thank you very much for your contribution today, Mr Coates – it is very much appreciated you coming along – and for your submission as well.

**Witness withdrew.**