Issues from the Henry report on Australia's future tax system for housing policy

A report prepared by National Shelter

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The views in this report may not reflect those of all member organisations of National Shelter.

Contents

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This report was prepared by Craig Johnston at Shelter NSW and was then circulated via the Shelter NSW website to illicit feedback prior to final editing for National Shelter. His version was further revised by Tegan Richardson (Queensland Shelter), Adrian Pisarski (Queensland Shelter), and Mary Perkins (Shelter NSW).

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Introduction

The Henry review of taxation was a review of aspects of Australia's taxation and transfer system conducted over 2008 and 2009 and culminating in a report dated December 2009. Overseen by a panel of experts and resourced by the Commonwealth Treasury, it was chaired by the secretary of Treasury, Ken Henry.[1] Branded as a 'root and branch' review, it was given a broad brief to consider structural changes, not just tinkering. This openness was, however, qualified by a couple of restrictions in its terms of reference. These were that it could not consider or propose increasing the rate or broadening the base of the goods and services tax (GST), nor removing the preservation of tax-free superannuation payments for people aged 60 and over.[2]

When the Government released the report 4 months after its completion, it was accompanied by the government's response in the form of a tax plan that reflected the government's priorities at the time. The tax plan did not include measures to address the tax treatment of housing.

The report was being considered by many commentators to be the basis of long term taxation reform over a 40 year time-span rather than something for immediate reform. In this context many of the housing sections were not seen as high priority. This scenario was changed by the election outcome and the subsequent negotiations regarding the formation of government which included a Tax Forum where all elements of the Henry review are to be discussed.

This report considers the Henry review and the tax plan in that context.

The review report was presented in 2 parts:

- an overview (part 1)
- a 'detailed analysis' (part 2) in 2 volumes

As well, there was:

- a consultation paper (in full and summary versions)
- a background paper (*Architecture of Australia's tax and transfer systems*)
- a consultation paper and a report (*The retirement income system: report on strategic issues*) on retirement income

While the main focus of the review was on taxation, it also gave considerable attention to the uses to which revenue from taxation was applied, specifically, where the money was directed to individuals or households rather than to general purposes of government such as defence or environmental protection. It is these payments from tax revenue to individuals that it calls 'transfers', and the system of taxation, transfers and their interaction is the 'tax–transfer' system.[3] This is represented schematically at Attachment 1: Schema of the tax–transfer system, on page 16. This memo deals only with those taxes and transfers that relate to housing: see Attachment 2: Major taxes and transfers relating to housing, on page 17, and Attachment 3: Henry's housing- and land-related recommendations, on page 18.

Taxation

In a criticism of the Government's response to the Henry review reports, the *Australian Financial Review* commented:[4]

> Treasurer Wayne Swan has rule out almost 30 changes to the tax system proposed by Ken Henry, his top bureaucrat, because they run counter to the government's "values" and

"economics".
Presumably, those values include the redistribution of wealth from renters to home owners, and those economics involve slashing the number of new entrepreneurs.
For these are likely consequences of the government's failure to pick up recommendations that would temper demand for housing, augment its supply, and keep home and business ownership within reach of most Australians.

The particularly complicating aspect of the tax treatment of housing comes from a dwelling having two economic aspects: it provides a housing service and thus is a consumption good, and it is an asset and thus is an investment good. The value of the housing services can be measured by the opportunity cost of its use, namely how much income it would bring you if you rented it to someone (else). The value of the asset will depend on the real increase (or decrease) in value at the time you sell it to someone else.[5]

Either of those two aspects of the good, the consumption (housing service) aspect and the investment (asset) aspect, can be taxed – or not taxed – by governments. Which aspects are taxed, and how taxation is effected (including what taxation revenue is foregone), will impact on the consumption and investment choices of homeowners. Those choices will, in turn, impact on the rental market, where there is a separation between the consumption (housing service used by a tenant) of and investment (asset owned by an investor) in the dwelling.

In Angus Freeman's study of 12 OECD countries he found that this dichotomy between the consumption and investment aspects of a dwelling was a key factor in the nature of taxation systems. The tendency observed was that, where owner-occupied housing is treated as a consumption good, the government does not deem, or impute, a rental income to the taxpayer and tax her on that income, does not allow the taxpayer to claim mortgage and non-mortgage costs of the dwelling from their income tax assessment, and exempts income from the sale of the dwelling from capital gains tax.[6] In this way an owner-occupied dwelling will get tax advantages over other classes of asset.

Where the tendency is to treat a dwelling as an investment good, on the other hand, governments will tax the imputed rent they calculate on the dwelling, allow the taxpayer to claim deductions for mortgage interest and other costs, and fully tax realised capital gains when the owner sells the dwelling.[7] In this way an owner-occupied dwelling will get no tax advantages over other classes of asset.

Where the owner of the dwelling (the investor) is not also the consumer of the housing service (the resident), the government will tax the dwelling as an investment good. The government taxes the income got from rents, allows deductions for expenditures associated with earning the income, and taxes realised capital gains.[8] In countries where owner-occupied housing is treated as a consumption good not an investment good, private rental will have a comparative disadvantage (since it is an investment good and taxed accordingly). The tax system favors one tenure (owner-occupation) over another (rental). Tenure patterns are clearly associated with the taxation system and the concessions (subsidies) embedded in it.

Table 1: Outcomes from the relative tax treatments of owner-occupation and private rental

Country	Tax treatment of		Extent of favor to owner-occupation from relative tax treatment	Expected relative expenditure on private rental from relative tax treatment
	Owner-occupation	Private renting		
USA	C+	I	most favor	highest
Britain	C+	I	most favor	highest
Ireland	C+	I	most favor	highest
Canada	C	I	more favor	higher
Australia	C	I	more favor	higher
France	C+	I CGexempt	more favor	higher
Finland	C+	I CGexempt	more favor	higher
Germany	C	I CGexempt	some favor	lower

Netherland	I CGexempt	I CGexempt	some favor	lower
Spain	I CGexempt	I CGexempt	little or no favor	lowest
Japan	I	I	little or no favor	lowest
Sweden	I	I	little or no favor	lowest

Notes: C+ = consumption good with mortgage tax relief, C = consumption good,
I CGexempt = investment good with capital gain tax exemption, I = investment good
Source: Angus Freeman, 'A cross national study of tenure patterns, housing costs and taxation and subsidy patterns', *Scandinavian Housing and Planning Research*, 1997, p.168, table 4.

In the group of countries surveyed by Freeman, Australia is one where owner-occupation is treated as a consumption good, and private rental treated as an investment good, for tax purposes. See Table 1. The way that owner-occupation and rental housing are taxed favors owner-occupation over rental (column 4).

Income tax

The Henry review proposed that governments' revenue-raising should be concentrated on 4 broad-based taxes, covering personal income, business income, economic rents, and private consumption.

While Henry proposed that most personal income be taxed, he allowed for some exceptions. The critical two items were superannuation and owner-occupied housing, these being the main forms of 'lifetime savings' for most Australians.[9] Three factors mitigating against the notion of taxing an imputed rent on owner-occupied housing were: the absence of such an approach since the earlier part of last century; general practice in the OECD countries; and likely public opposition of a force that would bring down any government that dared to introduce it. ('Given there is little community acceptance for applying income tax to the family home, any attempt to subject it to taxation is unlikely to be sustainable.'[10]) Just as it did not propose taxation of imputed rent for owner-occupied housing, the review also did not propose extension of the capital gains tax to owner-occupied housing through its proposal for taxation of income from all savings sources (above a 40% threshold).[11] (National Shelter has called for the removal of the exemption from capital gains tax of higher priced owner-occupied housing above a set threshold, e.g. $2 million.)[12]

It did not take an approach of *tenure neutrality*. Henry did raise suggestions that it thought would make housing supply more responsive to demand by reducing the impact of taxes on dwelling prices. These were the removal of conveyancing stamp duties[13], levying land tax on all land based on its value (not using the use of land and the size of holdings to determine land-tax liability)[14], and changing the taxation of investment properties.[15] However, it was keen to affirm that it did *not* think that the tax system was the main place to address unaffordability in Australia's housing, because other factors had a bigger impact, namely interest rates and land release policies.[16]

> The tax system is unlikely to be an effective instrument to move housing prices toward a particular desired level and the tax system is not the appropriate tool for addressing the impact of other policies on housing affordability.

Taxing rental income

There are a number of features about the way income from rental properties is treated that the review thought distorts the rental property market. One is the 50% discount on capital gains tax that is given on disposal of assets. The review proposed the ending of this tax advantage, as part of a wider proposal to introduce a consistent, uniform, approach to taxing income from non-wage sources. This proposal is for all income from bank deposits, bonds, rental properties, and capital gains and for certain interest expenses to get a 40% tax discount. In this way no one investment choice would be favored over another.

The other feature is the ability of a taxpayer to claim losses on borrowings to invest (i.e. when investment is negatively geared), which leads investors to take on too much debt. Australian households hold about $700 billion of assets in the form of rental properties. Around 70% of them do not make any money on the properties: they have been going into more debt to finance purchase of the properties.[17] The review report considered that tenants benefited from the current arrangements in the form of lower rents, since gearing does not encourage higher rents (favoring long-term capital gain over short-term rent revenue). Currently, investors with no or low levels of gearing form the minority of the market, so the current tax advantages available to highly geared investment can operate as a subsidy to renters by placing downward pressure on rents.[18] That is, the current negative gearing arrangements help to keep rents lower than they would be otherwise.

But the review considered the tax advantage to investors (and the consequential indirect subsidies to tenants) as neither transparent nor well-targeted to improve affordability for low-income renters. It also considered that the rental market would better suit tenants if more providers were in it for the revenue streams rather than for capital gains: this opinion was based on research findings that negatively-geared investors were around half as likely to hold their property after five years as investors who were not negatively geared[19]; the review report's assessment was that tenants would have greater security of tenure from landlords who were less likely to sell the dwelling (i.e. who were not negatively-geared).

The effect of the review's proposal for a 40% tax discount on all savings income (replacing all current arrangements) on the rental market would be to discourage investors who are interested in the benefits from negative gearing and who churn properties in that market, and encourage investors who are more interested in long-term revenue (as mentioned above).[20] That is, in a (smaller) private rental market there would be more stability and a focus on rent revenue streams. Another likely effect, associated and consequential to this, would be a preference by investors for rental housing with 'high rental yields'[21] – which presumably might involve higher rents.

The review was concerned that introduction of a 40% tax discount on savings, replacing other favorable tax treatments, could have short-term impacts on supply of private rental housing as this investment class lost its advantages, leading to investor flight. For this reason it proposed the change only take place in the area of residential rental income 'following reforms to the supply of housing and to housing assistance.'[22] These latter reforms are those relating to social housing and rental assistance (see below: page 10). What seems to be behind the qualification ('following reforms to…') is an expectation that reforms in housing assistance would cushion renters from market shocks associated with the withdrawal of investment from rental housing. The review presents its housing assistance reforms as a more effective and equitable means of subsidising low-income renters since they would be targeted[23] – unlike the benefits to tenants from living in negatively-geared dwellings that might have lower rents, since there is no guarantee that only low-income renters live in such dwellings.

Box 1 compares the main impacts on negatively-geared rental properties of the review's proposal for a general 40% tax discount on savings, with tax changes introduced in 1985 (and reversed in 1987).

Box 1: Changes to tax treatment of negative gearing – those of 1985, and as recommended by Henry

The effect of applying the recommended savings income discount to net rental income would be that a negatively geared investor would still be able to offset net rental losses against other income, including labour income. While the extent of the offset would be reduced, negatively geared investors would continue to access ongoing deductions that they might value for cash flow reasons.

Under the savings income discount, there would also be a generally better outcome for rental property investors that finance out of equity. The more neutral treatment would reduce the crowding out of other potential investors in rental housing by those undertaking negative gearing, and improve the long-term stability of the housing market.

Accordingly, this is quite a different approach to that adopted in 1985 (and reversed in 1987). In 1985 the tax benefits of negative gearing became restricted through the introduction of quarantining measures for excess deductions. As such, negatively geared investors could not access the entire net rental loss in the income year it was incurred, rather, excess interest in any year was carried forward and offset against future rental income or any gains taxable under capital gains tax from the sale of such investments.

Source: Australia's Future Tax System Review Panel, *Australia's future tax system: report to the Treasurer, Part two – Detailed analysis*, 2009, vol.2, p.419, box E4-1.

Land tax and conveyancing stamp duty

The review report's positions on land tax and conveyancing stamp duty – both being state, not Commonwealth, taxes[24] – are unsurprising since there is a consensus among economics advice agencies that land tax is a good thing and conveyancing stamp duty is a bad thing.[25] Indeed this view seems broadly shared by economists.[26]

Conveyancing stamp duties (sometimes called purchaser transfer duty in New South Wales) are seen to have negative effects on the allocation of a society's housing stock because they impose efficiency costs, in discouraging people from moving.[27]

The review report recommended these be phased out, and the revenue loss for the phasing-out be offset by increased revenue from land tax. The review expects that reductions on conveyancing stamp duty would lead to higher property prices.[28]

(Interestingly, this position is at odds with the housing developer lobby, who argue that conveyancing duty adds to the cost of development and is a contributing factor to housing unaffordability.) For this reason (and the loss of revenue to governments from the elimination of this tax), Henry links phasing out of the tax with reforms to land taxation – reforms which would involve *increases* in land tax which in turn would lead to *lower* land prices.[29]

Taxing the value of land is seen as efficient because the tax does not affect how the land is used or how much is used, and indeed, it *reduces* the sale-price of the land.[30] In doing so, the tax equalizes the after-tax return from land with the return from other investments; this means that land tax does not distort investment decisions.[31]

However, in practice, with current land tax arrangements, where some land is included in the land tax base and other land is not, land can shift in and out of the tax base depending on who owns it. So the review considered it was unlikely that land tax was being fully reflected in lower land prices for residential property. Those who bear the part of the tax that is not reflected in lower land prices are investors, through lower returns from their land ownership, or renters, through higher rent. Renters are particularly affected in the long run, as landowners adjust rents to get a better return on their investment.[32]

The review recommended increased use of tax on unimproved land values.[33] However it suggested land tax be reformed so that its base was broader (that is, it captured more landowners, indeed all of them, with no exemptions), and in this way removed distortions on investment decisions, as well as generating more revenue.

The notion of broadening the base of land tax is controversial because that notion means that the land sitting underneath owner-occupied dwellings would be taxable (on the unimproved value of the land). In New South Wales, for example, land on which there is a principal place of residence is exempt, as is land used for farms. The exemption of land occupied by owner-occupied housing removes around 60% of land by value, and around 75% of residential land, from the tax base.[34] The review nevertheless recommended that there be a low threshold under which the rate of tax would be zero, and this threshold be set so that there would be no tax liability on most agricultural and other low-value land.[35] Since capturing all owner-occupiers with land valued above the threshold would likely create a tax liability for some landowners who were 'asset rich but income poor', Henry proposed mechanisms for deferral of actual payment of the (accumulated) tax liability until the owner moved (i.e. sold the dwelling/land), noting that South Australia had a mechanism for deferral of payment of local government rates (property taxes).[36]

The other application of land tax that Henry recommended be changed is the practice of taxing larger land holdings at a higher tax rate (in all jurisdictions where there is land tax, except the ACT[37]): he said this discourages land-based investment by institutional investors, such as in rental housing where it discourages large investments.[38] He suggested this method of taxing land could be one of the factors underpinning the dominance of the provision of rental housing by small investors.[39] He recommended that taxing on aggregate holdings be ended, and that the tax be charged at a flat rate on the unimproved value of the land irrespective of the total value, or, alternatively, it could be charged using stepped rates based on the value of the property per square meter, starting with a zero rate on low-value land.[40]

Nontax measures and housing supply

Henry made it clear that he did not think the tax system was the critical factor in determining housing affordability; rather, the key influences were interest rates and the supply of dwellings. He made a number of recommendations about taxation that would remove distortions in investment decisions and have flow-on effects for supply or affordability (as mentioned above). He also considered some matters that affect supply of new dwellings, that are located in the environmental planning and development assessment systems regulated by state governments but administered by local governments:

- land-use planning and zoning, building regulations, and development assessment
- charges for local infrastructure

On land-use planning and zoning, building regulations, and development assessment, Henry shares the policy consensus of politicians, public servants, and the developer industry that these systems need to work better in the cause of property development.[41] The current policy climate is one where the environmental protections, quality controls and mechanisms for citizen participation offered by those systems are under relentless attack by the property development industry, often couched in terms of the costs of various mechanisms which could be passed on by developers to consumers and thus adversely affecting housing affordability. Henry points to various environmental or social purposes of those regulatory systems, and notes: 'Housing affordability needs to be considered against the other policy objectives that motivate these regulations.'[42]

On the various 'user pays' type charges that are applied to help finance local infrastructure associated with developments[43], Henry refers to submissions made to the review by people concerned that infrastructure charges impact negatively on housing affordability: these submissions had proposed that there be lower infrastructure charges (lower than the cost of provision) to improve housing affordability. The review noted this would involve ratepayers providing a subsidy to the new housing. The report commented: 'Subsidised infrastructure is a high-cost way to lower house prices because it encourages the delivery of infrastructure to areas where it is of relatively low value. Further, developers have less incentive to build housing that uses infrastructure efficiently (for example, by building more high-density housing).'[44] It agreed with an assessment made by the Productivity Commission in 2004, in that agency's review of access to homeownership, that in situations where supply of land is restricted, developer charges are borne by the original land holder by reducing the above-normal return (economic rent) they would otherwise receive when selling their land, and so the charges are unlikely to affect housing affordability substantially.[45] See Attachment 4: Who pays infrastructure charges?,on page 23.

However, where infrastructure charges are implemented poorly or are designed to operate as taxes, they can discourage housing supply and contribute to higher house prices.[46] He rejects any use of such charges as a tax on the profits of development, and suggests they should be set to reflect the cost of infrastructure.[47]

Transfers

The review's discussion of the transfer system focused on a need to:

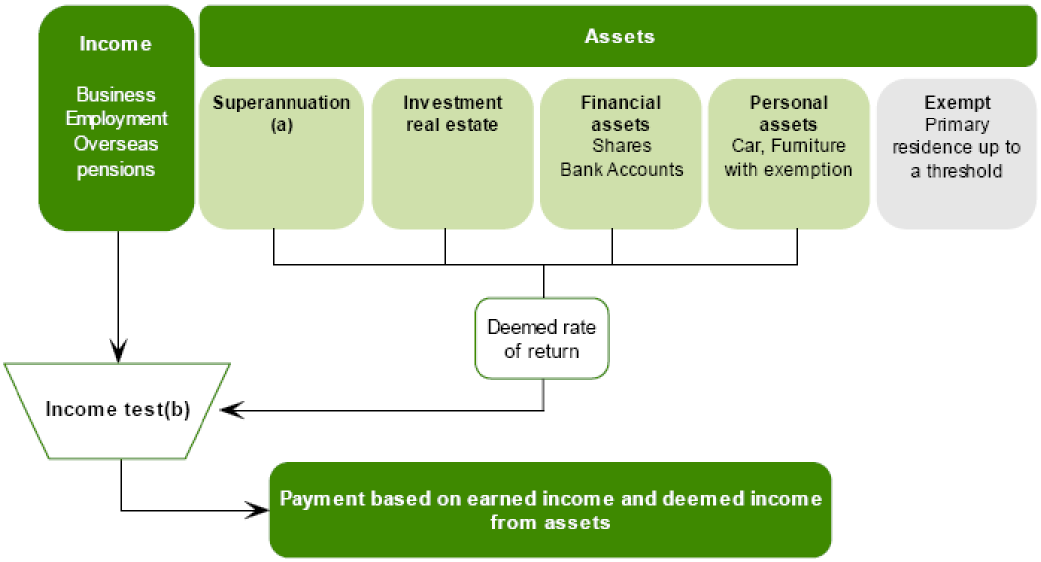
- capture all income (including deemed income from assets) into income-assessment for purposes of income-support payments, on a tenure-neutral basis – so that homeowners and renters are treated equally; and
- to direct (target) assistance to people most in need.

A core underpinning principle to its analysis is that of *capability*, in the sense that individuals should be able to realize their potential, and the role of an income-support system should therefore be to remove or alleviate barriers (such as poverty) and to do so in way that does not introduce new barriers (e.g. work disincentives).[48]

Income-support payments

The core notion around means-testing for eligibility for (income support) transfer payments is to capture income from all sources, including from assets, and in the case of assets, to deem an income stream from them. The same income ceiling for eligibility for the income-support payment would apply to all on a tenure-neutral basis (i.e. for both homeowners and nonhomeowners). The assets test would be abolished. See Figure 1.

Figure 1: A comprehensive means-test base for assessing eligibility for income support



Notes: (a) Deeming on account-based superannuation assets would apply from age-pension age; special arrangements would apply to income streams where deeming is difficult; superannuation assets would not be deemed for people under age-pension age unless they are being drawn down. (b) Free areas and withdrawal rates would apply to determine the amount of income-support payment.
Source: Australia's Future Tax System Review Panel, *Australia's future tax system: report to the Treasurer, Part two – Detailed analysis*, 2009, vol.2, p.541, chart F2-3.

However, there would be a concession to homeowners in the calculation of the deemed income for this purpose from their principal place of residence, in that its value would be exempt up to a certain, high, point, and only that part of the dwelling value over such threshold would be deemed to generate income. The principal place of residence for owner-occupiers is currently exempt from the asset test (although there is a higher asset-free area for nonhomeowners). The review thought that this exemption shelters very high levels of wealth.[49] It thought there should there should still be an exemption for an owner-occupied dwelling, where the primary role is to provide shelter and other support, but there was a dwelling value (threshold) beyond which the dwelling could be treated as an asset with an expectation of generating a return on the investment in it.[50] Dwellings valued higher than this threshold – which would be a high threshold – should be treated under the test, but only for the difference between the threshold figure and the value of the dwelling.[51] The value of that difference would be used to deem an income for mean-testing. It did not indicate a recommended cap, but gave an example: a cap of $1.2 million (that is, assessing age pensioners' owner-occupied dwellings where those dwellings are worth more than $1.2 million) would mean that about 100,000 age pensioners' homes would be partially assessed under the mean test. That is, there are some 100,000 age pensioners whose owner-occupied dwellings are worth more than $1.2 million: setting that amount as the cap for an owner-occupied dwelling under the pension asset test would mean that those pensioners would be deemed to get an income from their dwelling on the amount that is the difference between $1.2 million and its actual value ($1.21 million, $12 million, or whatever, etc.).[52] Note that Henry did not actually indicate a recommended value as a threshold.

The review thought that the housing costs associated with children are better met via the family payments system, through the calculations in determining per-child family payments, rather than having an extra housing payment for children's housing costs.[53] This would require that rent assistance for parent renters (who get higher maximum rates of rent assistance than singles and couples without children) be sufficient to ensure that child payments are not required to cross-subsidize those parent renters' renting costs.

The review recognized that some older people who are owner-occupiers might access the equity in their dwelling to generate income, through reverse mortgages or selling a proportion of the dwelling to a finance institution.[54] It commented that the taxation and social security means-test treatment of these products is 'already generous and should not be made more so.'[55]

Private renters

The main transfer to private renters (also available to tenants of community housing providers and of state-owned and managed Aboriginal housing) is rent assistance delivered through Centrelink.[56] The review made eight key comments.[57]

The purpose of rent assistance should be to ensure that adults with limited means can afford to live in an adequate standard of rental housing. Therefore eligibility for the payment should be based on a person's means (assessed under the income-support system means-tests) and their rental costs. Rent assistance is thus best paid as part of the income-support system.[58]

As an income-support payment, eligibility for rent assistance should be assessed through that system, rather than through eligibility for a social security payment with another purpose, such as family assistance. He considered that recipients of family assistance (a payment made to assist with the costs of children) should not be eligible for rent assistance on that basis. Eligibility for rent assistance should no longer be attached to receipt of more than the base rate of family tax benefit Part A – that is, it should not be available to working households who are not eligible for income support (i.e. to recipients of Family Tax Benefit part A who get more than the base rate of that benefit).[59] This change would give clear functions to both payments, with rent assistance contributing to the income support for adults and family assistance providing for the direct costs of children.[60] Removing family assistance recipients from eligibility would also enable a proposed increase in the maximum rate of rent assistance (see next paragraph) to be better targeted. While the delinking of eligibility for family tax benefit with rent assistance would deprive some families of rent assistance, the increase in the maximum rate of rent assistance would increase the income level at which people who have high rent costs can access rent assistance, meaning more families would be eligible for rent assistance on the basis of their income.[61]

Following his position on the *discrete roles of rent assistance and family payment*, Henry recommended rent assistance not be paid at higher rates for recipients with children (compared with the rates for recipients with no children), as currently – where the payment is increased according to the number of children in the household. His position is that the payment to deal with the costs of (extra) children, including housing costs, is the family payment.

The review considered that the current maximum levels of payment are too low, cutting out below a level that would ensure access to an adequate standard of housing in private rental markets.[62] He recommended it be increased so that assistance is sufficient to support access to an adequate level of housing in private rental markets. It recommended the upper rent cap be set with reference to rents of 1 and 2 bedroom dwellings in the 25th percentile of rents across capital cities.[63] The review discussed the possibility of upward movements in rents in private rental housing consequent to higher rent assistance payments. But it considered any such rent increases would not be significant and, more fundamentally, it considered them to be an essential way in which markets work that would assist in encouraging the supply of rental housing.[64]

He recommended the minimum rent thresholds (for eligibility for the payment) be set as a proportion of a recipient's base rate of income-support payment, e.g. 20%, rather than as a flat rate, as at present. This is because the current practice means recipients of allowances pay a greater proportion of their base payment in rent before rent assistance starts than pensioners do (allowances being lower than pensions): the change would result in more consistent recognition of rent costs for income-support recipients and be consistent with targeting assistance towards those with high housing costs.[65] This recommendation mirrored a recommendation from a 2009 review of pensions by the secretary of the Department of Families, Housing, Community Services and Indigenous Affairs, Dr. Jeff Harmer (who was also a member of the Australia's Future Tax System Review Panel), for a lifting of the minimum rent threshold for eligibility for the payment.[66] See Box 2.

The review considered that the current indexation of the payment, linked to movements in the Consumer Price Index, means that assistance is not well-targeted over time, exposing private renters to the risk of rent fluctuations. Over the three years to 2009 average rents grew at an annual rate of 10% whereas the maximum rate of rent assistance increased 3.7% a year in this period.[67] He recommended rent assistance be indexed to reflect the growth in rents in private rental markets, which could be measured by an index of rents paid by income-support recipients.[68] This recommendation mirrored a recommendation from the Harmer pensions review of 2009, for indexation of rent assistance to an index that indicated charges in rents.[69] See Box 2.

Box 2: The Harmer report on rent assistance

The Harmer report:

- recognised that pensioners in the private rental market were paying high rents.
- identified Centrelink's rent assistance payment as having 'a very specific role in the income support system since it is conditionally linked to a particular expenditure of a minority of pensioners'
- acknowledged the rent assistance payment as 'a particularly important determinant of living standards for pensioners who pay private rent'.
- identified a decline in the value of the payment of around $9.00 to $10.00 a week since 2000, as a result of price increases in the rental market, a decline associated with the payment being indexed according to CPI not by changes in actual rents.
- concluded that the payment had 'become less effectively targeted' as a result of the way in which it has been indexed.
- identified the value of the rent assistance threshold (the minimum amount of private rent paid before rent assistance is available) as having fallen as a proportion of the base rate of pension; for example, it was 20.6% of the single pension rate in September 1997 but 17.4% in September 2008.
- concluded that the lower value of the rent assistance threshold resulted in some rent assistance being provided to pensioners who pay 'relatively modest levels' of rent, and in the maximum rate of rent assistance being paid to pensioners paying both very high and medium rents.
- identified this 'fiscal drag' effect of the decline of the threshold as having been exacerbated by rents having risen at a higher rate than the CPI.
- suggested the payment be indexed according to 'a separate index that more appropriately reflects changes in the costs of private rent', for example, according to the actual rents paid by social security recipients.
- suggested the threshold rent for payment be increased (an action that would cause some pensioner renters to lose their rent assistance payment), the money-saving from which would allow for the amount paid to recipients paying high rents to be increased.

Source: Dr. Jeff Harmer, *Pension Review report*, Department of Families, Housing, Community Services and Indigenous Affairs, Canberra, 2009.

Henry considered a notion that rent assistance should vary geographically, that is, be paid at higher or lower rates depending on where in Australia the recipient lives, but he did not support it (for either rent assistance or its proposed high housing-needs payment for renters).[70] The reasons were various. Some were related to dynamics in high-rent markets that could offer countervailing or partially-compensatory benefits to recipients, e.g. access to better services or lower costs of travel in areas where the high rents are locationally-based. Some were logistical, e.g. rent boundaries would be hard to set because there can be as much variation in rents within a major city as there is between the average rent in that city and the average rent in a regional (country) area. Some were jurisdictional, e.g. while the Commonwealth had a responsibility to assist people with high rents on a national basis, regional rents that significantly vary from national averages were likely to do so for reasons beyond the control of the national government, and could be due to state government policies that affect rental housing costs in particular regions.[71]

He also recommended rent assistance be extended to public housing tenants, and as the flip-side to this, public housing tenants would generally pay rents that reflect market rates, so that the subsidy to private renters and public housing tenants is equitable.[72]

Public housing tenants

The key point Henry made about transfers to public housing tenants was that the level of support was not equitable compared with the lower support given to private renters through rent assistance. Removal of this difference is the rationale behind two recommendations (which complement each other):[73]

- extension of eligibility for rent assistance to public housing tenants
- charging actual rents paid in public housing according to the market rent[74]

Extension of rent assistance to public housing tenants is something that has been advocated by some, but not all, National Shelter affiliates.[75]

The recommendation that public housing tenants (indeed, social housing tenants generally) be charged rent at market rates is not something that has been advocated by most nongovernment welfare organizations. While formally most state and territory housing authorities and mainstream community housing organizations *set* the rent on a dwelling at market rates, the actual rent *charged* to the tenant tends to be done on a nonmarket basis, typically by charging a rent as a proportion of their income, e.g. 25% or 30%, capped at the market rent, or, alternatively, as a proportion of the market rent (a submarket rent), e.g. 75% or 80%.[76]

Henry argues against the predominant model, income-based rent-charging, as inequitable and as having undesirable effects. On the inequity, he notes that the average level of rent subsidies in public housing is around $220 a fortnight compared with average assistance of around $90 a fortnight for rent assistance recipients.[77] On the effects, he considers the model to be a barrier to workforce participation, noting that an estimated 110,000 public housing tenants have high effective marginal tax rates that would discourage work-entry.[78] Another undesirable effect would be that, since tenants with the same income pay the same rent regardless of the size, location, condition or general amenity of the house they occupy, they have an incentive to maximise their 'in-kind subsidy' — that is, they stay in larger and better houses than they would normally occupy if they had to pay directly for their housing.[79]

The charging of rents on a nonmarket basis to 'price in' housing affordability is the key, indeed decisive, feature of social housing that distinguishes it from other housing services, whether provided by government agencies, community housing providers, or private landlords. That's what makes it *affordable housing*.[80] Affordable housing is a specific supply-side response to housing unaffordability, complementing tenant-directed subsidies such as rent assistance, housing benefits, vouchers, etc. If social housing (specifically here, public housing) is not provided with rents charged on a nonmarket basis, this raises some fundamental questions about why there needs to be government provision of this product for tenants without high/special housing needs or for tenants whose difficulties with the private market are solely based on unaffordability (housing stress).

Public housing

Henry's approach is for social housing to be primarily financed from tenants' rents, with affordability for and the costs of any high housing-needs (see next section) achieved through the income-support system. The Commonwealth government, as funder of rent assistance and of a proposed high housing-needs payment, would become the main funder of housing assistance to households.

He anticipates that these changes would 'encourage the formation of a more dynamic social housing market that would reduce reliance on the current system of block grants'[81] – such as currently through the National Affordable Housing Agreement. He does not recommend the Commonwealth, or the states, stop providing funds to build new social housing dwellings, but rather, they should ‘retain’ this option.[82] Clearly, affordable housing would not be the dominant component of the future system.

Henry’s recommended move to a new model is based on assumptions:[83]

- The current system provides poor incentives to both recipients and providers of public housing.
- The current system might not be sustainable. He notes declining levels of Commonwealth grants to the states over the years. He also criticizes the result of Commonwealth provision of grants through block funding based on the population in each state, rather than the quantity or quality of the dwellings provided. ‘This funding mechanism provides an incentive for States to transfer management of public housing to community providers. The tenants transferred to community housing become eligible for Rent Assistance and, with fewer tenants, the effective per-dwelling funding in the public housing stock increases.’[84]

The Henry model is similar to, but not exactly the same, as an idea that has been in circulation for some decades, namely that the Commonwealth should take primary responsibility for assisting housing affordability by providing income support to households, and the states should provide affordable housing in the form of social housing. This model was recommended by the Industry Commission in 1993.[85] The Council of Australian Governments (COAG) subsequently endorsed a proposal for ‘(a) the Commonwealth accepting responsibility for housing subsidies and affordability, and (b) the states and territories … taking responsibility for the management and delivery of public housing services’, at its meeting of April 1995.[86] In June 1996 the COAG noted a paper that proposed that the Commonwealth extend eligibility for rent assistance to public housing tenants, which would be payable at higher level and specifically at a level that would enable state housing authorities to charge market rents; the Commonwealth discontinue capital grants to the states; and existing funding requirements and restrictions on the states be removed.[87] The proposal was to have been discussed at a COAG meeting in November 1996, but housing assistance did not appear on an agenda of a COAG meeting for another 10 years, at the COAG meeting of 20 December 2007, and the approach then taken was one that asserted the primacy of Commonwealth initiatives within the existing framework of responsibilities rather than a rearrangement of roles.[88]

Special payment for renters with high housing-needs

The review proposed the establishment of a new transfer payment for renters who had high housing-needs. This payment would be similar to rent assistance in as much as it helped very-low income renters with housing costs, but would be different in that it would not be addressing affordability as such but, rather, other characteristics of the housing services being consumed by the tenant that a standard housing service would not ordinarily meet and that involves higher costs.[89]

It seems that the consumers who would be eligible for this payment would not be tenants with high welfare needs, but, rather, high housing-needs – though these circumstances might overlap. The review considered that addressing the needs of ‘people with high needs’ is a role for social housing, and it gives examples of such high needs as a lack of access to adequate housing in the private market because of factors like discrimination, lack of suitable dwellings, or excessive premiums for risk – factors that would adversely affect people with mental or physical disabilities or substance-abuse problems.[90] It is thus clear that the review’s concern, despite the omission of the qualifier ‘high *housing* needs’ on page 596, is with low income and socially-disadvantaged ‘people with high housing needs’ who need some extra assistance to deal with financial stress in private rental housing.[91] On page 605, it gives some examples of high housing-needs, namely being homeless or having health at risk from a current dwelling.[92]

The level of assistance would be based on the high-housing-need category to which a recipient belongs, such as having a disability or being homeless. The payment would reflect the potential housing costs for a provider in servicing high housing-needs customers, such as modifications to housing or the greater need for maintenance and repairs. The high housing-needs payment would depend on the assessed needs of an individual recipient.[93] It would be ‘scalable’.

The high housing-needs payment would not be paid direct to the tenant but would be directed to a landlord of the tenant’s choice. It would be ‘portable’. (This arrangement it is similar to the 3 private rental subsidy schemes in New South Wales.[94]) The concept for the payment is not a recurrent subsidy to housing providers to meet their costs, nor is it a direct payment to consumers in the way rent assistance is; rather, it is a hybrid form, in which the payment is for the tenant but the payment goes to the provider so as long as they are providing the service to that tenant (at the tenant's discretion).[95] The review said the payment should focus initially on social housing tenants (public housing and community housing), but once it was established, the government should explore the scope for extending it to private providers.[96]

The high housing-needs payment is not intended to replace funding that housing providers can also receive for delivering other support services to their tenants.[97]

The review saw the combination of rent assistance and a new high housing-needs payment as resulting in the Commonwealth government becoming the main funding provider for housing assistance. Henry's model is a user-directed funding model for the provision of social housing, one that aims to be neutral between the public rental and private rental tenures, and one that claims to encourage more responsive provision of social housing.[98]

The review appears to be focusing here not on the *welfare* (non-income-related 'support') needs of social housing tenants which they share with other people with like capabilities in other housing tenures (such as meals-on-wheels services for people with disabilities and frail older people – this is my example), but on needs based on *specific interactions with the mainstream housing market*. This would be where there is a systemic mismatch between the capabilities of the person (e.g. their mental or physical disability, or substance-abuse) and access to dwellings (e.g. discrimination, lack of suitable dwellings, excessive premiums for risk).

It is these scenarios that present a public policy case for government funding of dwellings and providers (social housing).

We might deduce that in Henry's model, social housing does *not have a role of poverty alleviation*, which is effected through the income-support system generally, or of *housing affordability*, which is effected through rent assistance (and other measures outside the transfer system like interest rate policy, land supply, etc).

Low-income mortgagors

The review did not give great consideration of direct payments to low-income homepurchasers. Henry did note however that owner-occupiers were in receipt of a number of benefits in the taxation and income-support systems which result in a greater level of assistance than private renters would receive through rent assistance[99]

Judith Yates points out that home owners already receive an annual subsidy of more than $8000, concessions to investors (most of whom are also home-owners) receive over $4000 in benefits, while tax expenditure directed towards renters equate to just over $1000 per rental household per year[100].

The benefits discussed in the review included the exclusion of owner-occupied dwellings from the means-test for income support (a situation which the review did not contest, in fundamentals: see page 9, above), and their equity in their dwelling not being taxed.

The review recognized that some homeowners would be in housing stress or have cash-flow problems, but considered they had options that were not available to renters, such as repayment deferral or restructuring options through their banks, or through accessing equity in their homes.

It did not recommend extending rent assistance to them, and did not recommend development of simple assistance arrangements 'at this time'.[101]

Responses of the Commonwealth government and Opposition

As part of its response to Henry — branded as 'A tax plan for our future: simpler, fairer, stronger' — the Rudd Government promised to introduce a tax discount of 50% of interest income up to a maximum of $1,000, for interest from savings deposits held with a bank, credit union or building society, as well as interest on bonds, debentures, and annuity products.[102] This is a watered-down version of Henry's recommendation 14, which recommended a 40% tax discount on a wider range of income sources and with no ceiling. The discount is to be funded by a proposed tax on profits ('rents') from the mining of coal and iron ore ('minerals resources rent tax').[103]

The Government reported that it will not introduce the following Henry recommendations on housing and housing-related matters:[104]

- Include the family home in means-tests (see Rec 88c)
- Introduce land tax on the family home – this is a state tax and thus an issue for the states (see Rec 52 & 53)
- Restrict eligibility to rent assistance for families (see Rec 103)
- Reduce the CGT discount, apply a discount to negative gearing deductions, or change grandfathering arrangements for CGT (see Rec 14 & 17c)
- Introduce a bequests tax (see Rec 25)
- Ask the states to charge market rents to public housing recipients (see Rec 106)

This leaves open consideration of recommendations 14 (part), 15, 69, 70, 102, 103 (part), 104 (though this would make no sense, from a 'Henry' perspective, without implementing recommendation 106), and 105.

Box 3 indicates the full list of recommendations of the Henry report (and some that the Government considered to be potential misinterpretations of the recommendations) that the Government will *not* implement 'at any stage'. In addition, the Government says it will 'never' increase the rate or broaden the base of the GST or remove tax-free superannuation payments for people over 60.

Box 3: The Government's 'no' list to Henry

The Government has indicated it will not introduce the following Henry recommendations:

- Include the family home in means-tests (see Rec 88c)
- Introduce land tax on the family home – this is a state tax and thus an issue for the states (see Rec 52 & 53)
- Require parents to work when their youngest child turns 4 (see Rec 85)
- Limit payments to single income-families (see Rec 92 & 93)
- Restrict eligibility to rent assistance for families (see Rec 103)
- Do any changes to the tax system that harm the not-for-profit sector, including removing the benefit of tax concessions, raising the gift deductibility threshold or changing income tax arrangements for clubs (see Rec 9e, 13, 41, 43 & 44)
- Reduce overall remuneration to the members of our defence forces (see Rec 6d, 8c & 9e)
- Reduce the CGT discount, apply a discount to negative gearing deductions, or change grandfathering arrangements for CGT (see Rec 14 & 17c)
- Remove the Medicare levy (see part of Rec 5)
- Reduce indexation of the age pension (see Rec 84)
- Remove the benefits of dividend imputation (see Rec 37)
- Think of limiting pensioner and low income concessions for utilities, transport and other essential services (see Rec 107)
- Introduce a bequests tax (see Rec 25)
- Align preservation age with pension age (see recommendation in AFTS Retirement income strategic issues paper)
- Offer a government annuity product (see Rec 22)
- Ask the States to charge market rents to public housing recipients (see Rec 106)
- Abolish the Luxury car tax (see Rec 80)
- Index fuel tax to CPI (see Rec 65)
- Change alcohol tax in the middle of a wine glut and where there is an industry restructure underway (see Rec 71)

Source: Prime Minister, Treasurer, 'Stronger, fairer, simpler: a tax plan for our future', media release, 2 May 2010, p.4.

Following the re-election of the Gillard government, the Government announced it would convene a tax summit in June 2011 which will revisit the Henry review.[105]

During the 2010 federal election campaign, the Liberal-National Opposition commented that the Henry review was 'an important body of work that should make a significant contribution to the public policy debate'.[106] They criticized the Government for treating the review 'with contempt'. They promised to release all the costings, modeling and other data underlying the review recommendations within 30 days of coming to office. They also promised to undertake 'a proper public consultation and review process on taxation' (which they considered the review not to have been[107]) and to develop a green paper and then a white paper on taxation. They would then take their tax reform agenda (developed through this process) to the voters at the next federal election.

The Coalition promised that it would *not* introduce the following Henry Tax Review recommendations on housing and housing-related matters:[108]

- Introduce a bequests tax (R25)
- Include the family home in means-tests (R88(c))
- Introduce land taxes on the family home (R52 & 53)
- Restrict eligibility to rent assistance for families (R103)
- Reduce the CGT discount, apply a discount to negative gearing deductions, or change grandfathering arrangements for CGT (R14 & 17c)
- Ask the states to charge market rents to public housing recipients (R106)

This leaves open consideration of recommendations 14 (part), 15, 51, 52, 69, 70, 102, 103 (part), 104 (though this would make no sense, from a 'Henry' perspective, without implementing recommendation 106), and 105.

Box 4 indicates the full list of recommendations of the Henry report that the Coalition has rejected.[109] In addition, the Coalition said it would not increase the rate of GST or broaden the GST base.

Box 4: The Opposition's 'no' list to Henry

The Coalition parties have indicated they would not introduce the following Henry recommendations:

- New taxes on business activity (R26)
- Scrapping the private health insurance rebate (R7(b))
- Means-testing the Child Care Rebate (R100)
- Reduce indexation of the age pension (R84)
- New taxes and charges on small businesses and sole operators (R10)
- Remove structural and concessional offsets such as the Low Income Tax Offset without appropriate compensation (R5)
- Introduce a bequests tax (R25)
- Remove the Medicare levy (part of R5)
- Remove tax concessions, raising the gift deductibility threshold or changing income tax arrangements for clubs (R9e, 13, 41, 43 & 44)
- Taxes on Australians driving to work (recommendations 61-68)
- Include the family home in means-tests (R88(c))
- Introduce land taxes on the family home (R52 & 53)
- Require parents to work when their youngest child turns four (Rec 85)
- Disadvantage families relative to separated couples (R91(b))
- Limit payments to single-income families (R92 & 93)
- Restrict eligibility to rent assistance for families (R103)
- Reduce overall remuneration to members of the defence forces (R6d, 8c & 9e)
- Reduce the CGT discount, apply a discount to negative gearing deductions, or change grandfathering arrangements for CGT (R14 & 17c)
- Remove dividend imputation (R37)
- Change pensioner and low income concessions for utilities, transport and other essential services (R107)
- Offer a government annuity product (R22)
- Ask the States to charge market rents to public housing recipients (R106)

○ Abolish the Luxury car tax (R80) ○ Change alcohol tax (R71) ○ Align preservation age with pension age

Source: Liberal Party of Australia, 'The Coalition's real action plan for lower, fairer and simpler taxes', 2010, pp.5-6.

The Opposition's election housing policy had a proposal for state governments to issue vouchers to renters and homeowners to assist those consumers in meeting the costs of housing services. The homeowner could use the value of the voucher to repay mortgage; a renter would use it towards paying their rent, the balance of which they would pay themselves. The vouchers would be paid for by state governments, by diverting money from existing public housing system to the new program (i.e. it would replace public housing). This description is how it was presented in that policy document:[110]

> The Coalition will encourage each State and Territory to establish an affordable housing voucher scheme for eligible people to access housing support services. Housing support vouchers could be used in any registered accommodation or to meet mortgage payments where the eligible person owns or is purchasing their own home. The vouchers would be registered in the name of the recipient and entitle the holder to accommodation support to the value established in the relevant schedule. Under the Coalition's Voucher scheme all existing tenants in State and community housing would be issued with an appropriate voucher to reflect their eligibility criteria. Voucher holders would be responsible for meeting the balance, if any, of rental/payment required by the landlord or mortgagee of the registered dwelling. Owners of registered accommodation would be permitted to charge up to the level of rental prescribed under the terms of the voucher.

There was extensive debate in the late 1980s and early 1990s about giving subsidies direct to consumers, in the form of housing allowances or vouchers, versus giving subsidies to landlords, in the form of grants to state housing authorities. This was largely settled by an Industry Commission report of 1993, which did not recommend scuttling the public housing system, but rather, retaining public housing to meet long-term needs *and* using of rental allowances (and headleasing from the private sector) to meet short-term needs. It commented, in short: 'A mix of approaches is desirable in order to respond flexibly to the varying needs of people'.[111] Since then, the two approaches, rent assistance to (most) tenants and subsidies to social housing providers, have been used to assist low-income renters (with no direct grants to homepurchasers to meet ongoing mortgage costs[112]).

Post Election and conclusion

In the aftermath of the federal election tax reform was revisited. The Independent members determining who would form government insisted that all matters from the Henry review be open for consideration.

The implications for this are that nothing can now be considered ruled in or out, but open to consideration. This will require National Shelter to convene a special meeting to consider the implications of this report and to develop specific policy considerations which are forwarded to all parties.

Henry's review is indeed a far reaching document and contains fundamental shifts in the way housing and land, renting and owning are treated by the taxation and transfer systems. The adoption or otherwise of Henry's recommendations will reshape the housing landscape.

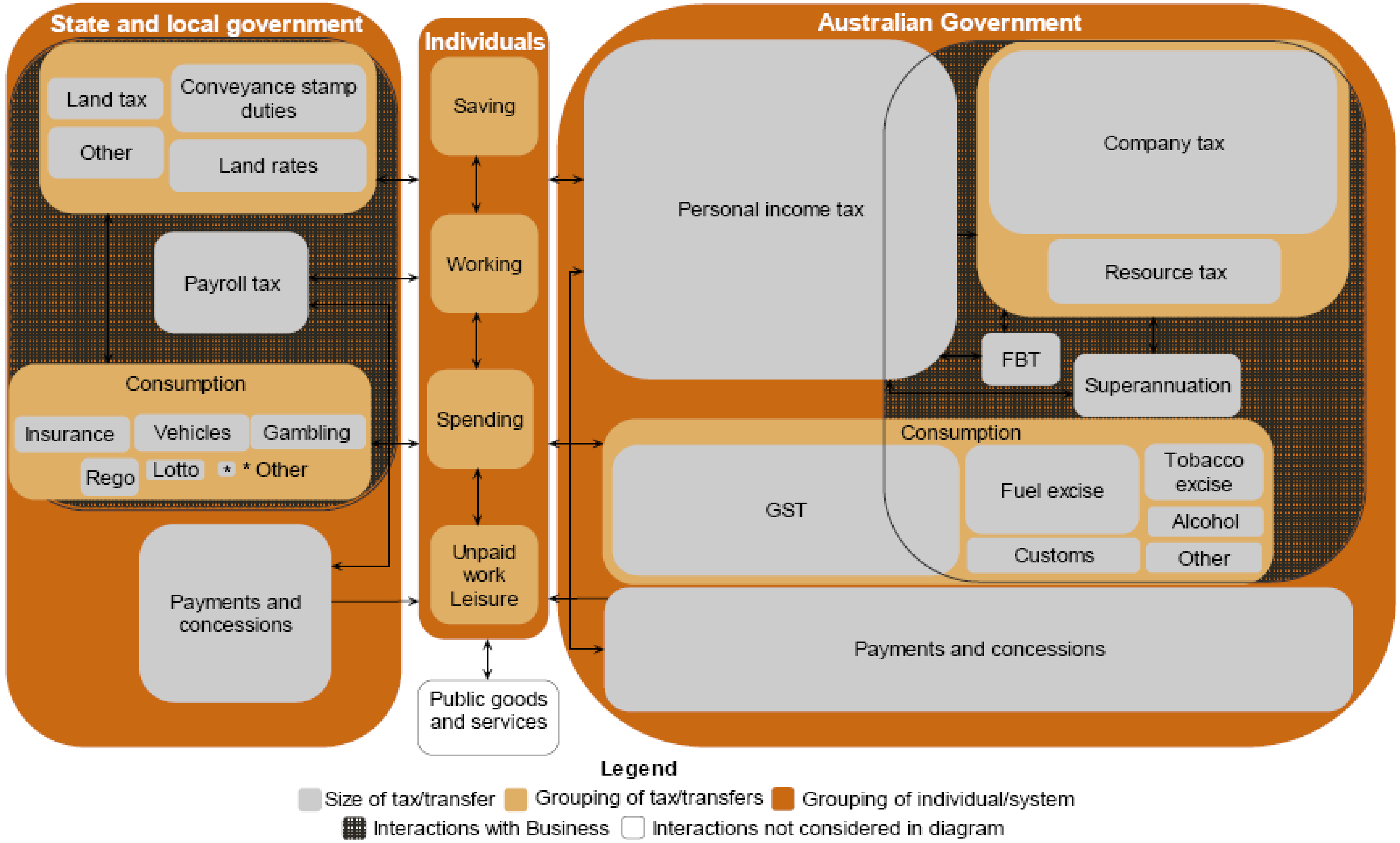
How we tax housing or compensate through our transfer system will determine if and when we may deal with the under supply of housing, particularly affordable rental housing, and how fairly our systems are considered internationally and by future generations.

Recommendations

- That National Shelter broadly distribute this report among members and stakeholders and illicit views about the tax treatment of housing and transfers.

- That National Shelter develop a specific set of recommendations following a meeting convened for that purpose.
- That National Shelter writes to the Federal Ministers and bureaucracies concerned with final recommendations by the end of March 2011.

Attachment 1: Schema of the tax–transfer system



Source: Australia's Future Tax System Review Panel, *Australia's future tax system: consultation paper*, 2009, p.40, chart 2.1.

Attachment 2: Major taxes and transfers relating to housing

	Owner-occupied	Private landlord	Private renter	Public tenant
Taxes				
Income tax (Australian Government)	Exempt.	Taxable. 50 per cent discount on capital gain. Costs deductible.	n/a	n/a
Stamp duty (All States)	Taxable at progressive rates based on property value (some first home buyers exempt).	Taxable at progressive rates based on property value.	n/a	n/a
Land tax (All States except Northern Territory)	Exempt.	Taxable based on land values. Deductible from income tax. Thresholds exclude many small-scale holdings.	n/a	n/a
Rates (local governments)	Taxable, based on land values. Some exemptions.	Taxable based on land values.	n/a	n/a
Transfers				
Income support assets tests (Australian Government)	House value not counted toward total assets. Home-owning couple subject to maximum rate threshold of $243,500.	Property value counted toward total assets.	Non-home-owning couple subject to maximum rate threshold of $368,000.	Non-home-owning couple subject to maximum rate threshold of s $368,000.
Rent Assistance (Australian Government)	n/a	n/a	Eligibility determined by access to other payments. Payment rate determined by rent (capped) and family circumstances.	Not eligible.
First Home Saver Accounts (Australian Government)	Savings of first home buyers receive Government contributions and preferred tax rates.	Existing property owners ineligible.	Savings of first home buyers receive Government contributions and preferred tax rates.	Savings of first home buyers receive Government contributions and preferred tax rates.
First Home Owners Grant (Australian and state governments, administered by States)	Until 30 June 2009, $14,000 grant for first home purchased — $21,000 if a newly constructed home. To revert to $7,000 from 1 July 2009.	Not eligible.	n/a	n/a
Public housing (Australian and State governments)	n/a	n/a	n/a	Eligibility determined by income and other criteria indicating disadvantage. Recipients pay a rent, usually around 25 per cent of their income.
National Rental Affordability Scheme (Australian and State governments)	n/a	Eligible institutional investors receive $8,000 per dwelling rented to eligible tenants.	Low to moderate income renters access a home at rent 20 per cent below market rates.	n/a
Home purchase assistance (State governments)	Includes direct lending, deposit and mortgage subsidies. Generally means-tested by income.	n/a	n/a	n/a
Private rental assistance (State governments)	n/a	n/a	Payments to help meet ongoing, bond or other rental costs. Generally means-tested by income.	n/a

Source: Australia's Future Tax System Review Panel, *Australia's future tax system: consultation paper*, 2009, p.204, table 11.1.

Attachment 3: Henry's housing- and land-related recommendations

14. Provide a 40 per cent savings income discount to individuals for non-business related: (a) net interest income; (b) net residential rental income (including related interest expenses); (c) capital gains (and losses); and (d) interest expenses related to listed shares held by individuals as non-business investments …

15. When the 40 per cent savings income discount is introduced a smooth transition should be provided to minimise any disruption that may arise. The transition to a savings income discount for net residential rental income should only be adopted following reforms to the supply of housing (Part Two Section E4 Housing affordability) and reforms to housing assistance (Section F5 Housing assistance).

25. While no recommendation is made on the possible introduction of a tax on bequests, the Government should promote further study and community discussion of the options.

51. Ideally, there would be no role for any stamp duties, including conveyancing stamp duties, in a modern Australian tax system. Recognising the revenue needs of the States, the removal of stamp duty should be achieved through a switch to more efficient taxes, such as those levied on broad consumption or land bases. Increasing land tax at the same time as reducing stamp duty has the additional benefit of some offsetting impacts on asset prices.

52. Given the efficiency benefits of a broad land tax, it should be levied on as broad a base as possible. In order to tax more valuable land at higher rates, consideration should be given to levying land tax using an increasing marginal rate schedule, with the lowest rate being zero, with thresholds determined by the per-square-meter value.

53. In the long run, the land tax base should be broadened to eventually include all land. If this occurs, low-value land, such as most agricultural land, would not face a land tax liability where its value per square metre is below the lowest rate threshold.

69. COAG should place priority on a review of institutional arrangements (including administration) to ensure zoning and planning do not unnecessarily inhibit housing supply and housing affordability.

70. COAG should review infrastructure charges (sometimes called developer charges) to ensure they appropriately price infrastructure provided in housing developments. In particular, the review should establish practical means to ensure that these changes are set appropriately to reflect the avoidable costs of development, necessary steps to improve the transparency of charging and any consequential reductions in regulations.

88. The current income and asset tests for income support payments should be replaced with a comprehensive means test based on a combined measure of employment income, business income and deemed income on assets. The comprehensive means test would: ... (c) continue the means test exemption for owner-occupied housing up to a high indexed threshold …

102. The maximum rate of Rent Assistance should be increased to assist renters to afford an adequate standard of dwelling. To ensure that Rent Assistance can be maintained at an adequate level over time, the rent maximum should be indexed by movements in national rents, which could be measured by an index of rents paid by income support recipients.

103. To better target an increase in the maximum rate, Rent Assistance should be part of the income support system, with eligibility based on rent paid and the income support means test, rather than on eligibility for another payment (for example, Family Assistance).

104. Mechanisms should be developed to extend Rent Assistance equitably to public housing tenants along with removing income-linked rent setting in public housing.

105. A high-need housing payment should be paid to social housing providers for their tenants who have high or special housing needs or who may face discrimination in the private market. This payment should be funded by the Australian government. The Commonwealth and the States should retain the option of providing capital for social housing construction.

106. Income-linked rents should be phased out in social housing, with providers charging their tenants rents linked to the market rate, with existing rent-setting for current tenants phased out using grandfathering or other transitional arrangements. However, continued use of income-limited rents is appropriate in some circumstances, such as in remote Indigenous communities.

120. States should allow local governments a substantial degree of autonomy to set the tax rate applicable to property within their municipality.

121. Over time, State land tax and local government rates should be more integrated. This could involve: (a) moving to a joint billing arrangement so that taxpayers receive a single assessment, but are able to identify the separate State and local component; and (b) using the same valuation method to calculate the base for local government rates and land tax (with this method being consistent across the State).

Attachment 4: Who pays infrastructure charges?

Who bears the burden of developer charges depends on the relative elasticity of the demand and supply of land (Neutze 1997). Following Wood et al. (forthcoming), Chart E4-6 illustrates the impact of infrastructure charges on the price and allocation of land, depending on whether land for housing is freely available or restricted.

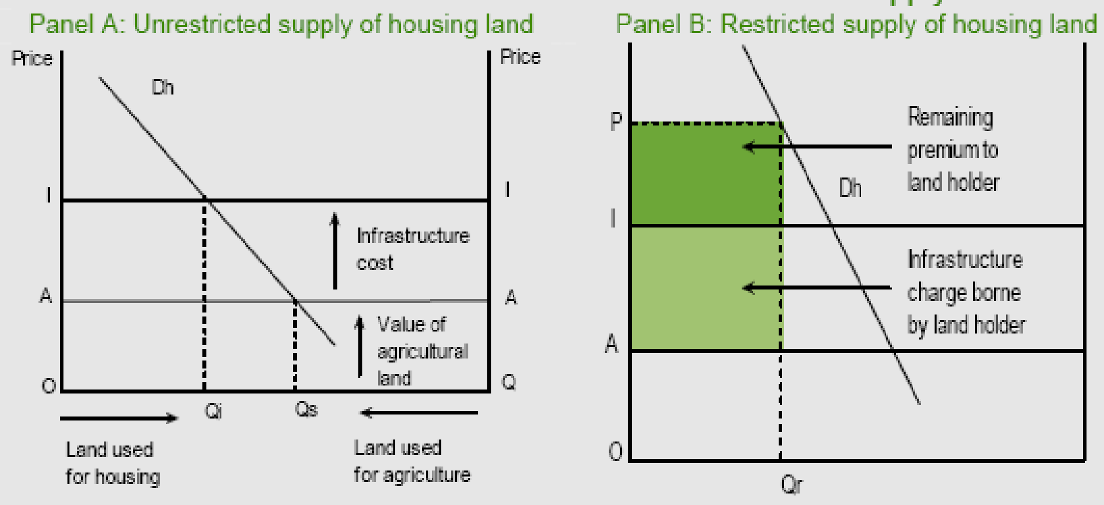
The amount of total land (OQ) is divided between demand for housing land (Dh) and agriculture, which is valued at a fixed price (OA). To make land useable for housing, infrastructure worth AI must be added to the land.

If there are no restrictions on the use of land for housing at the fringe of a city and infrastructure is provided free, Qs land is used for housing (Panel A). With infrastructure for new housing effectively subsidised, the price of land for housing is equal to the value of agriculture (OA). Where there is a charge imposed for the infrastructure, the amount of land used for housing will fall to Qi. The cost of land used for housing at the fringe increases to OI, so that it equals the cost of agriculture plus the value of infrastructure. In this example, subsidised infrastructure can reduce the cost of housing because additional land can be acquired and converted to residential use at a price OA. However, this is not a good outcome from the viewpoint of efficient resource allocation: if the full social cost of housing is reflected in appropriate infrastructure charges demand for housing is Qi.

In contrast, if the supply of land available at the fringe is limited to the amount Qr due to zoning or planning restrictions (as in Panel B), free infrastructure has no impact on housing supply. The restriction in land supply means that prices at the fringe (OP) are higher than the value a marginal agricultural user would be willing to pay. Landholders receive an 'economic rent' (AP) when developing their land for housing. The price is determined by the demand for land in relation to the constrained supply. An infrastructure charge (IA) levied on land holders who are developing their land for housing reduces the size of this rent (from AP to IP), without affecting the price of housing. Only if the infrastructure charge exceeded AP would it raise house prices.

This is a stylistic comparison of two extreme cases, where land for housing is either fully elastic or fully inelastic. The real situation is likely to fall somewhere between these two extremes. That said, the value of agricultural land at the fringe of cities generally exceeds its opportunity cost in agricultural production, reflecting restrictions on the supply of land for housing.

Chart E4–6: Incidence of infrastructure and land supply



Source: Australia's Future Tax System Review Panel, *Australia's future tax system: report to the Treasurer, Part two – Detailed analysis*, 2009, vol.2, pp.427-428, box E4-3.

Notes

[1] This paper refers to the author of the reports as ‘Henry’, for convenience; occasional variations in writing style and some repetitiveness indicate multiple authorship.
[2] This refers to the nontaxation of superannuation benefits paid from a taxed source, either as a lump sum or pension, to people aged 60 and over, effective from 1 July 2007. See Australian Taxation Office, ‘Simplified superannuation – final decisions’, 5 September 2006, online at <http://simplersuper.treasury.gov.au/documents/decision/html/final_decision_full.asp>.
[3] Not to be confused with a ‘tax transfer’, which is where a jurisdiction transfers responsibility for a particular tax to another jurisdiction, or a ‘transfer tax’, which is which a tax applies to the transfer of an asset from one party to another (e.g. conveyancing stamp duty).
[4] ‘Feeble tax response weakens affordability’, *Weekend Australian Financial Review*, 8-9 May 2010, Commentary, p.62. The editorialist makes the point about business ownership by pointing to the fact that two-thirds of loans to small businesses are secured by a house; in this way, reduced access to homeownership reduces the chances of a business getting credit, this inhibiting entrepreneurship.
[5] Richard Disney, ‘Australia: issues in the tax treatment of pensions and housing’, paper presented to ‘Australia’s future tax system’ conference, University of Melbourne, 18-19 June 2009, p.24.
[6] Angus Freeman, ‘A cross national study of tenure patterns, housing costs and taxation and subsidy patterns’, *Scandinavian Housing and Planning Research*, vol.14, 1997, p.167.
[7] Freeman, p.167. Imputed rent is the estimated rent that an owner-occupied dwelling would attract if it was rented out at market rates. Since most owners live in their own dwellings and do not rent it out and so do not get a rental income from the dwelling they live in, taxation of owner-occupied dwellings would involve deeming the rent they would get if they did rent it and then taxing the owner on the rental income they don’t actually get.
[8] Freeman, pp.167-168.
[9] Australia’s Future Tax System Review Panel, *Australia’s future tax system: report to the Treasurer, Part one – Overview* (K Henry, chairperson), Treasury, Barton ACT, 2009, p.32; Part 2, p.12. (From the next reference to this part, just ‘*Overview*’.)
[10] Australia’s Future Tax System Review Panel, *Australia’s future tax system: report to the Treasurer, Part two – Detailed analysis*, vol.1 of 2 (K Henry, chairperson), Treasury, Barton ACT, 2009, p.13. (From the next reference to this volume, just ‘*Detailed analysis*, vol.1’.)
[11] See next section.
[12] National Shelter, ‘“Housing Australia affordably”: National Shelter policy platform’, 2009, p.14.
[13] Australia’s Future Tax System Review Panel, *Australia’s future tax system: report to the Treasurer, Part two – Detailed analysis*, vol.2 of 2 (K Henry, chairperson), Treasury, Barton ACT, 2009, pp.415-416. (From the next reference to this volume, just ‘*Detailed analysis*, vol.2’.)
[14] *Detailed analysis*, vol.2, p.416.
[15] *Detailed analysis*, vol.2, p.417-420.
[16] *Detailed analysis*, vol.2, p.421.
[17] *Detailed analysis*, vol.1, p.69. Negative gearing arrangements do not apply to rental properties only. Henry notes: ‘The same results apply for other types of geared investments that yield capital gains; in particular shares, where margin lending arrangements are used to negatively gear share investments.’ (p.69)
[18] *Detailed analysis*, vol.2, p.419.
[19] The research referred to is Gavin Wood and Rachel Ong, *Factors shaping the decision to become a landlord and retain rental investments*, Australian Housing and Urban Research Institute, Melbourne, 2010.
[20] That is, the review expects the removal of the tax advantages to negatively-geared investments, such as rental housing, will lead to disinvestment (less rental housing).
[21] *Detailed analysis*, vol.2, p.418.
[22] *Overview*, p.34.
[23] *Detailed analysis*, vol.2, p.420.

[24] The review's brief was not confined to Commonwealth taxes: it also considered the main taxes imposed by state/territory governments.
[25] Owen Gabbitas and Damien Eldridge, *Directions for state tax reform*, Productivity Commission, Belconnen ACT, 1998, pp.155-170; Productivity Commission, *First home ownership*, Melbourne, 2004, pp.96-105; Independent Pricing and Regulatory Tribunal of NSW, *Review of state taxation: report to the Treasurer*, Sydney, 2008, pp.59-60,119-122; Government of Tasmania, 'State tax review: discussion paper', Department of Treasury and Finance, Hobart, 2010, pp.33-41. The same observations have been made by a major report on the British tax system recently released by the Institute for Fiscal Studies (London): see James Mirrlees, Stuart Adam, Tim Besley, Richard Blundell, Stephen Bond, Robert Chote, Malcolm Gammie, Paul Johnson, Gareth Myles and James Poterba, *Tax by design*, 2010, ch.16, pp.4-5,37-39 (online at <http://www.ifs.org.uk/mirrleesreview/design/ch16.pdf>).
[26] See, for example, Frank Stilwell and Jennifer English, 'Housing affordability, stamp duty and land tax', School of Economics and Political Science Working Paper, no. ECOP2004-2, University of Sydney, Sydney, 2004.
[27] *Overview*, pp.48-49.
[28] *Detailed analysis*, vol.1, p.264.
[29] *Detailed analysis*, vol.1, p.264.
[30] D*etailed analysis*, vol.1, p.247; note the word 'reduce' is not a mistake: the review does not say that land tax increases the price of land. It argues that a tax on land value does not increase the value of land, but that land would merely have a lower after-tax rental return, i.e. what is lower is their economic rent, being the return to the landowner above that needed to keep the land in its current use: see *Detailed analysis*, vol.1, p.249. Since buyers of land know they will be subject to land tax, their demands falls commensurately (i.e. they will buy land at a lower price): see *Detailed analysis*, vol.1, p.249.
[31] *Detailed analysis*, vol.1, p.248.
[32] *Detailed analysis*, vol.1, p.261.
[33] *Detailed analysis*, vol.1, p.151.
[34] *Detailed analysis*, vol.1, pp.260-261; these data are Australia-wide
[35] *Overview*, p.48.
[36] *Detailed analysis*, vol.1, p.266.
[37] There is no land tax in the Northern Territory.
[38] *Detailed analysis*, vol.1, p.261.
[39] *Detailed analysis*, vol.1, p.261-262.
[40] *Detailed analysis*, vol.1, p.264.
[41] *Detailed analysis*, vol.2, pp.420-423.
[42] *Detailed analysis*, vol.2, p.422.
[43] *Detailed analysis*, vol.2, pp.423-429.
[44] *Detailed analysis*, vol.2, p.426.
[45] *Detailed analysis*, vol.2, p.426. The Productivity Commission's report was *First home ownership*, Melbourne, 2004, and its discussion is on pages 163-165.
[46] *Detailed analysis*, vol.2, p.426. Developer charges for local economic and social infrastructure are not a tax in as much as they are a fee for provision of particular services related to the development itself. Developer charges for affordable housing (of the 'inclusionary zoning' type) are a tax in that the payer does not get a specific benefit from their payment; they are distributive.
[47] *Detailed analysis*, vol.2, p.424.
[48] The 'capability' approach is drawn from the Indian economist (and Nobel prize winner) Amartya Sen.
[49] *Detailed analysis*, vol.2, p.549. See Australia's Future Tax System Review Panel, *Australia's future tax system: the retirement income system – report on strategic issues* (K Henry, chairperson), Barton ACT, May 2009, p.44; the sentence in the final report is the same as in this earlier report; no data were given to amplify the statement.
[50] *Detailed analysis*, vol.2, p.550.
[51] *Detailed analysis*, vol.2, p.540.

[52] *Detailed analysis*, vol.2, p.550.
[53] *Detailed analysis*, vol.2, p.571.
[54] *Detailed analysis*, vol.1, p.120. See also Catherine Bridge, Toni Adams, Peter Phibbs, Mark Mathews and Hal Kendig, *Reverse mortgages and older people: growth factors and implications for retirement decisions*, final report no.146, Australian Housing and Urban Research Institute, Melbourne, 2010.
[55] *Detailed analysis*, vol.1, p.120.
[56] Note that some 5-10% of rent assistance recipients are in not living in the private rental market but, rather, in various forms of social housing (community housing, Aboriginal housing, retirement village, nursing home).
[57] *Detailed analysis*, vol.2, p.595.
[58] *Detailed analysis*, vol.2, p.612.
[59] *Detailed analysis*, vol.2, p.612.
The income limits ($ pa) above which only the base rate of family tax benefit part A may be paid are indicated in the following table:

No. children 0-12 years	No. children 13-15 years			
	Nil	One	Two	Three
Nil		65,609	86,104	106,599
One	59,331	79,826	100,321	120,815
Two	73,548	94,043	114,537	135,032
Three	87,765	108,259	128,754	149,249

The figures are those for 1 July to 19 September 2010.
[60] *Detailed analysis*, vol.2, p.612. Henry's comments on the role of family payment in meeting the costs of children, including housing costs, are indicated on page 7 of this paper.
[61] *Detailed analysis*, vol.2, p.612.
[62] *Detailed analysis*, vol.2, p.595.
[63] *Detailed analysis*, vol.2, p.610.
[64] *Detailed analysis*, vol.2, p.611. His argument here is predicated on his proposal for market-based rent-charging in public housing (see page 9 of this paper).
[65] *Detailed analysis*, vol.2, p.612.
[66] Jeff Harmer, *Pension Review report*, Department of Families Community Services and Indigenous Affairs, Canberra, February 2009, pp.93-94.
Rent assistance is not paid to pensioners only: it is also paid to people with dependent children who get more than the base rate of Family Tax Benefit, people who have care of a child between 14% and 35% of the time and are not eligible for Family Tax Benefit but meet other Family Tax Benefit requirements, and people who receive an allowance or benefit (but don't have dependent children) and are over 25 years, or have a partner, or are under 25 and living permanently or indefinitely apart from their parents or guardians.
The rates and rent thresholds as at 20 September 2010 are indicated in the following table:

Household arrangement	Maximum amount of rent assistance ($ a fortnight)	Rent threshold ($ a fortnight)	Rent ceiling ($ a fortnight)
Single	115.20	102.40	256.00
Sharer (each)	76.80	102.40	204.80
Couple (combined)	108.60	166.80	311.60

Higher amounts are available for families with children. The sharer rate does not apply to the Disability Higher amounts are available for families with children. The sharer rate does not apply to the Disability Support Pension or Carer Payment.
The table indicates that a social security recipient is eligible for rent assistance if their fortnightly rent is over the rent threshold (e.g. $102.40 a fortnight for a single person). For each $1 they pay in rent over this threshold they get 75¢ rent assistance. Once their rent reaches the rent ceiling (e.g. $262 for a single person) they do not get any extra rent assistance, i.e. they get the same amount of rent assistance if paying $256 a fortnight as paying $257 or $357 a fortnight. The maximum amount of rent assistance they can get is $115.20 a fortnight; they would get this if their rent is at the rent ceiling.
[67] *Detailed analysis*, vol.2, p.603.

[68] Rents for properties in the National Rental Affordability Scheme (NRAS) are already indexed to movements in market rents rather than CPI.
[69] Harmer, p.75.
[70] *Detailed analysis*, vol.2, p.614.
[71] *Detailed analysis*, vol.2, p.614.
[72] *Detailed analysis*, vol.2, p.491.
[73] *Detailed analysis*, vol.2, p.595, 612.
[74] Henry's recommendation 106 involves the phasing out of existing rent-charging for current tenants using grandfathering or other transitional arrangements, and continued use of income-limited rents in some circumstances, such as in remote Indigenous communities.
[75] See Shelter NSW, 'The supply and allocation of social housing in New South Wales: submission to the Public Bodies Review Committee, Legislative Assembly, Parliament of New South Wales', February 2006, pp.15-17. National Shelter has not called for rent assistance to be paid to public housing tenants, but rather, for the Government to carry out a 'comprehensive review' in the 'medium term' of rent assistance, including examining the following options: extending eligibility to public housing tenants, either via direct payment to the tenant or via a 'per tenant' subsidy to state/territory housing authorities (National Shelter, p.15).
[76] Craig Johnston, *Supply of social housing*, Shelter Brief no. 41, Shelter NSW, Sydney, November 2009, pp.22-25.
[77] *Detailed analysis*, vol.2, p.604.
[78] *Detailed analysis*, vol.2, p.606.
[79] *Detailed analysis*, vol.2, p.607. However, he does note that many public housing tenants have little choice about the particular dwelling they occupy.
[80] In this paper, 'affordable housing' refers to *dwellings* provided to consumers on the basis that the consumer's recurrent costs in living in the dwelling, whether mortgage repayments or rent, are low enough for them to be avoid housing stress. The term is tenure-neutral. It is not the same as 'housing affordability' or 'affordability of housing', which refer to the degree of *lack of stress* a consumer has in meeting their ongoing housing costs. Conversely, 'housing unaffordability' refers to the degree of stress or crisis a consumer has in meeting their ongoing housing costs.
[81] *Overview*, p.66.
[82] *Detailed analysis*, vol.2, p.491.
[83] *Detailed analysis*, vol.2, p.607.
[84] *Detailed analysis*, vol.2, p.608.
[85] Industry Commission, *Public housing*, vol.1, *Report*, Belconnen ACT, 1993, p.105.
[86] Council of Australian Governments, 'Communiqué: attachment A – long-term housing assistance reform', 14 June 2006.
[87] See <http://www.coag.gov.au/coag_meeting_outcomes/1996-06-14/>.
[88] The COAG meeting of 20 December 2007 identified seven areas for its 2008 work agenda, one of which was housing. In that area it identified 5 'Commonwealth/state implementation plans' to be delivered to the March 2008 COAG meeting: a $500 million Housing Affordability Fund with the goal of streamlining development approval processes and reducing infrastructure charges and developer costs; a National Rental Affordability Scheme, conditional on financial support from the states and territories; building 600 new dwellings for homeless people, requiring a matching investment and the release of suitable land from the states and territories; an audit of Commonwealth, state and territory land for possible release for housing development (excluding operating Defence bases); and state and territory participation in the work of the Commonwealth's National Housing Supply Research Council. It indicated that work to be done after March would comprise consideration of a new National Housing Affordability Agreement to replace the Commonwealth State Housing Agreement when it expired in June 2008, and development of specific objectives for Indigenous Australians and for social inclusion. See <http://www.coag.gov.au/coag_meeting_outcomes/2007-12-20/>.
[89] This payment would not be an alternative to rent assistance but, rather, another payment for a different purpose.
[90] *Detailed analysis*, vol.2, p.596.
[91] *Detailed analysis*, vol.2, p.598.

[92] *Detailed analysis*, vol.2, p.605.
[93] *Detailed analysis*, vol.2, p.613.
[94] Housing NSW, 'Housing pathways: private rental subsidy – fact sheet', July 2010, p.2.
[95] *Detailed analysis*, vol.2, p.597.
[96] *Detailed analysis*, vol.2, p.614.
[97] *Detailed analysis*, vol.2, p.613.
[98] *Detailed analysis*, vol.2, p.615.
[99] *Detailed analysis*, vol.2, p.608.
[100] Dr. Judith Yates. *Tax expenditures and Housing.,* Australian Housing and Urban Research Institute, September 2009.
[101] *Detailed analysis*, vol.2, p.613.
[102] Australian Government, 'Improving incentives for savings', factsheet, n.d. (2010), <http://www.futuretax.gov.au/documents/attachments/Fact_Sheet_Helping_Australians_Save.pdf>, viewed 31 August 2010. This was originally to have come into effect for the 2011-12 financial year but on September 7 the Government announced a 1-year deferral and it will now start in July 2012 (John Kehoe, 'Modest relief ahead of summit', *Australian Financial Review*, 8 September 2010, p.51).
[103] This proposed tax is a successor to a tax, a Resource Super Profits Tax, that was announced by the Government on May 2 in response to the Henry review's report, which recommended a uniform resource rent tax on nonrenewable resource (oil, gas, and minerals) projects (recommendation 45).
[104] Liberal Party of Australia, 'The Coalition's real action plan for lower, fairer and simpler taxes', Barton ACT, 2010, pp.5-6.
[105] Fleur Anderson, John Kehoe and Sue Mitchell, 'Second shot at tax reform', *Australian Financial Review*, 8 September 2010, pp.1,51.
[106] Liberal Party, pp.4-5.
[107] 'Unlike Labor's Henry Review process, our process will involve full public debate and consultation on the future of the Australian taxation system.' (Liberal Party, p.5)
[108] Liberal Party, pp.5-6.
[109] The Coalition has rejected 25 recommendations to Labor's 19.
[110] Liberal Party of Australia, 'The Coalition's plan for real action on housing', Barton ACT, 2010, p.6, online at <http://www.liberal.org.au/~/media/Files/Policies%20and%20Media/Community/Housing%20Policy.ashx>, viewed 24 August 2010. See also Jacob Saulwick, 'Coalition plan for rental vouchers', *Sydney Morning Herald*, 27 August 2010, p.4, which helps to make more sense of the proposal.
[111] Industry Commission, p.66.
[112] Direct assistance to homepurchasers consists of small subsidies to assist market entry (First Home Owner Grant, First Home Save Accounts, and First Home Owner Boost) or to ward off mortgage default, not ordinary, ongoing mortgage repayments.