From:	Richard Clark
To:	Housing
Subject:	Housing Affordability
Date:	Saturday, 29 June 2019 5:03:09 PM

Attention: The Secretary, Select Committee on Housing Affordability, Parliament House

re: House of Assembly Select Committee on Housing Affordability

Please see below a written submission with respect to 1 (k) in the Terms of Reference and, if not deemed acceptable and/or applicable under 1 (k), I respectfully submit it under 1 (l) in the Terms of Reference ‘any other matters incidental thereto’.

Submitted by:

Richard Clark
[redacted]

1 (k) calls for ‘successful strategies in other jurisdictions that could be effective in improving affordability in Tasmania’. Relying on something tried and tested excludes innovative strategies (at a point in time when fresh approaches need to be considered) and I doubt it was the intention of the committee to discount the possibility that a novel scheme could be devised, so I write in good faith with a new proposal to improve housing affordability. Alternatively, please accept this submission under 1 (l) of the Terms of Reference.

The strategy involves a repositioning of house ownership in the community to home ownership. It is designed to dampen the sentiment that houses are an investment opportunity for the purpose of profit and instead promote that home ownership is an essential human need. While other investment vehicles are available to investors (retail property, property trusts, shares, derivatives, superannuation etc), residential homes ought, as far as possible, to be owned by the occupant. We would not sanction an individual buying up all of the food stock in a supermarket, restricting its availability and on-selling it at an inflated price, yet we currently encourage just that through supporting the purchasing of houses as investments rather than applying countervailing mechanisms to support both owner-occupancy and the dampening of inflation in the residential housing market (of particular concern in Tasmania).

Saving an owner around 20% of the fortnightly repayments, the proposal involves a scheme to reduce the cost of servicing the interest component of a mortgage by funding the loan through the Commonwealth Government, who have the capacity to borrow cheaply through issuing government bonds at an interest rate well below bank lending rates. The interest rate applied to the loan would be set at the Federal Government’s 10-year bond rate plus a small percentage to cover administration. The government would issue new 10-year bonds as and when required to raise the capital for each property funded under the scheme. Importantly, the scheme would be cost-neutral for the Federal Government. To qualify for scheme, the new homeowner would need to be the owner/occupier and, critically, allow a covenant to be placed on the title that restricts the future sale of the property in three important ways: first, the property could only be re-sold at arms-length via a blind process administered either by the State or Federal Government (similar to a tender process); second, any second or subsequent purchaser must be an owner/occupier (and would qualify to enter the scheme if they required a loan); third, the price of the property would be capped at the original purchase price plus CPI (and plus the independently assessed value of any home extensions/improvements, not including maintenance).

Persons entering the scheme ultimately forgo capital gains on the property (in real terms) in lieu of the discounted interest rate on their mortgage. It could be regarded that they are getting their capital gain upfront insofar as the reduced interest repayments under the scheme are an immediate untaxed cash benefit.

The scheme does not provide assistance for would-be property investors. Persons in the scheme who wish or need to relocate (permanently or temporarily) cannot access the scheme a second time on another property unless they have divested themselves of the original property. Should they wish to retain their original property and let it out, they can do so, however its value as an investment property is limited since there are no capital gains to be realised (adjusted for inflation). Should they decide to retain the property, they could continue to receive the discounted interest rate (in lieu of the covenant eliminating capital gains when they do eventually sell) or, optionally, they could refinance using a commercial lender which would enable them to claim the loan interest on tax as an investor. However, if they do re-finance, the covenant would still apply and they would never be able to realise a capital gain in real terms from the disposal of the property. Re-financing would open the way for them to purchase a subsequent property as an owner/occupier under the scheme, as would disposal of the original property, but a person cannot own two properties concurrently under the scheme.

To encourage participation (and home ownership), the State government would waive stamp duty on the purchase of the house under the scheme, further increasing housing affordability.

Scenario

A couple with two children on one income of $80,000 wish to purchase a home for $500,000 (around the median house price in Hobart in 2019). The property is independently valued and assessed as worth $480,000. The Federal Government, under the scheme, would lend up to 85% (for example) of the assessed value of the property. ($480,000 x 0.85 = $408,000) The couple then need to have a deposit of $92,000 (+ costs, including conveyancing and independent valuation). Note that provided the independently assessed value and purchase price are within +/- 10%, the purchase price would be the amount used for the purposes of determining the CPI adjusted maximum value of the property if re-sold.

The couple enter into a loan agreement (mortgage) with the Federal Government. The Federal Government charges the 10-year bond rate (the rate at which it can borrow the money, currently 1.39% on 17 June 2019) plus 0.5% to cover costs associated with administration of the scheme.

The couple would therefore initially pay $408,000 x 0.0189 = $7711 interest pa, comprised of

$408,000 x 0.0139 = $ 5,671 interest plus $408,000 x 0.005 = $ 2,040 administration. As principal payments are made (paying down the mortgage), the government rebuys the exchange traded bonds to the value of the principal repaid, shrinking their exposure as a lender. At the end of the first 10-year period, the government simply issues another 10-year bond to cover the outstanding balance of the mortgage. The new interest repayment rate would be reset to reflect any change in the 10-year bond rate.

This makes the purchase of a house far more affordable compared with a bank loan at, say, 3.59% interest on a mortgage currently offered by UBank (rate as at 19 June 2019). For comparison:

Government loan: $408,000 at 1.89% over 30 years, principal and interest = $685 per fortnight

UBank loan: $408,000 at 3.59% over 30 years, principal and interest = $855 per fortnight

The saving is around $170 per fortnight or $4,420 pa. Importantly, the cost of paying the mortgage under this scheme has reduced their fortnightly mortgage repayments by almost 20%, making housing far more affordable.

Over the life of a 30-year principal & interest loan, the couple saves around $132,000 in interest and around $14,000 in stamp duty (excl. first homebuyer concessions). The price that the property could be sold for after 30 years, assuming a 2% CPI, is $739,000 ($331,000 more than the original price, but the 'same price' adjusted for inflation).

Critically for the integrity of the scheme: in 30 years, the home is still affordable for the next purchaser.

The proposed strategy makes use of the Federal Government's capacity to raise capital at substantial discount. Additional measures such as the covenant and methods of sale are included to both prevent large rises in the value of houses purchased under the scheme. This would also serve to reduce inflation in the wider housing market, serving to dampen all rises in house prices above the rate of inflation, since it would be increasingly difficult to sell a house in a street for 30% above the notional value of four or five houses in the same neighbourhood that are under the scheme and which could become available for tender at any time. Because the scheme reduces the potential for capital gains in the housing market as a whole (as an increased proportion of housing stock only rises in value in line with the CPI), investors would become less likely to outbid or pay over the market price for fear of being caught with an asset that is unlikely to appreciate over time, which would level the playing field for would-be owner-occupiers.

Obviously, the State government does not collect or regulate Federal taxation, consequently the proposed strategy will necessarily involve a partnership with the Federal Government. This could be rolled out as a Tasmanian pilot scheme designed to improve housing affordability that could eventually be extended nationally.

Thankyou for your consideration. Please feel free to contact me should you wish to discuss any of the details or methods by which the scheme could be made to work (for example, the sale of properties under the scheme at arm's length).

Regards

Richard Clark