BUSTING MYTHS ABOUT NEGATIVE GEARING

NEGATIVE GEARING AT A GLANCE

What is it? Negative gearing allows investors to deduct losses made on rental properties from their other income, thereby reducing their overall annual tax liability. In addition the discounted tax rate for capital gains means that an investor pays tax on only 50 per cent of any capital gains that are realised when an investment property is sold.

How much does it cost? It's estimated between 1995- 2012, negative gearing cost taxpayers an inflation-adjusted $33.5 billion (2012 dollars). The Australia Institute put the combined cost of negative gearing and capital gains discounts at $7.7 billion a year[i].

In June 2015, the Parliamentary Budget Office (PBO) estimated the proposal to remove negative gearing with grandfathering would raise **$2.939 billion over the next four years.** They **c**alculated this would be expected to increase revenue by around $42.48 billion over the next ten years, to 2024-25, as negatively geared properties were progressively released onto the market and the concession was unwound over the course of a decade. **That's the equivalent of a cheque for $1781.43 for every Australian citizen[ii].**

According to the Reserve Bank of Australia head of financial stability, the build-up of investors out-competing homeowners leaves young Australians disenfranchised and locked out of the housing market.[iii] Worse still, a report by Moody's estimated **negative gearing is increasing house prices by 9% - or about $*44,000 - nationwide.*** *According to the same report, at its 2008 peak, negative gearing added 15% to valuations. Even the current 9% support is a substantial subsidy to Australia's existing property investors[iv].*

For the same amount we currently spend on negative gearing and capital gains discounts via revenue foregone each year, the government could:

- Build a brand new home for every single homeless Australian currently sleeping rough,
- Take more than 20,000 desperate families off the social housing waiting list and build each of them a brand new home *each year*,
- Convert more than 5000 new rental homes in currently empty buildings through the Greens 'Convert to Rent' program and fund another 20,000 brand new rental homes under the NRAS scheme per year, and
- Still have over $2 billion left over for schools, hospitals and public transport.[v]

MYTH 1: REMOVING NEGATIVE GEARING WILL BE TOO UNPOPULAR

FACT: If it's a numbers game, the number of people that would benefit from scrapping negative gearing *far outweigh* the number of people who currently benefit from it.

It's often said that any changes to negative gearing would be politically risky due to the large number of voters invested in the scheme. The most recent figures put the total number of Australian taxpayers with net rental property losses at 1.292 million[vi].

However, there are almost 4.8 million Australians renting privately[vii]. Many would be first home buyers trying to save for their first deposit and forced to compete with more affluent investors. This means there's **more than four times as many private renters as there are negatively geared property investors**.

A report released in April 2015 also shows that up to 1.5 million Australians are living in entrenched, long-term poverty[viii]. Removing negative gearing for future purchases would free up almost $3b over the next four years, and $42 billion over the next ten to spend on affordable housing supply which would be one of the strongest steps we could take to alleviate poverty and inequity in Australia.

Who supports reform?

FOR	AGAINST
David Murray, head of government's financial system inquiry, former head Commonwealth Bank	The Property Council of Australia
Australian Council of Social Services (ACOSS)	Real Estate Institute of Australia
Combined Pensioners and Superannuants Association	Housing Institute of Australia
GetUp!	Master Builders Australia
The Australia Institute	
Aged and Community Services Australia	
National Shelter	
Equality Rights Alliance	
Salvation Army	
Anglicare Australia	
Homelessness Australia	
Brotherhood of St Laurence	
Tenants Unions NSW and Victoria	
The Grattan Institute	
AHURI	
OECD	
IMF	
Senior economists including Saul Eslake	
Prosper Australia	
Australian Workers Union	
Aussie Home Loans founder John Symond	
Baptist Care Australia	
YWCA	

The major political parties could also be said to be opposed to reform out of self-interest, given 95% of federal MPs also own investment properties, with the top ten controlling 95 properties[ix].

MYTH 2: WHEN THEY ABOLISHED NEGATIVE GEARING RENTS WENT UP

FACT: Despite the Treasurer and other coalition MPs saying we'd see a "surge in rents" if negative gearing was removed, this has overwhelmingly been proven to be false.

In 1985 the Hawke government quarantined 'losses' generated through property investment against the income from the same assets. It's often referred to as an action that led to an increase in rents and an investor 'strike'. In fact national investment in rental property increased over that period by 42% (in terms of the total value of loans), and rents only rose in two already overheated and undersupplied cities: Perth and Sydney. Beyond these cities, rents remained flat.

PHOTO: Treasurer Joe Hockey says scrapping negative gearing pushed up rents in the 1980s. (AAP: Tracey Nearmy)

ABC FactCheck investigated whether abolishing negative gearing pushed up rents in May 2015.

The verdict:

"While the rent increases in two cities did coincide with the temporary removal of negative gearing tax deductions, it is unlikely that change had a substantial impact on rents in any major capital city in Australia. Mr Hockey's claim doesn't stack up."[x]

Many other reports point to the same finding, and all centre around three key points:

Firstly the evidence shows overwhelmingly NG does little to boost housing supply, with investors piling into established homes rather than new construction. This drives up prices.

Secondly they argue, even if investors sold their properties in revolt, the homes would be sold to renters – reducing the demand for rental properties and making no net difference to the balance of rental properties and therefore rents unchanged.

Finally, the rental data from the time period of 1985-1987 shows beyond reasonable doubt that rents did not jump nationally after negative gearing was temporarily removed. In fact there was flat of falling rent across Melbourne, Brisbane, Adelaide, Hobart, and Canberra.

Even if removing negative gearing led to the number of new investors declining and some investors selling off their properties, those properties would likely be purchased by first home buyers who themselves are renting, therefore freeing up a rental property for someone else, helping offset the very sharp decline in home ownership rates among those under 45[xi].

When economists modelled the impacts of the changes proposed in the Henry Tax Review on rental property investment and rent prices, they found *that modest reform would increase investment in rental housing and reduce rents by an average of $300 a year,* and they concluded "a flight of investors from private rental housing seems unlikely".[xii] This is even more important since we are seeing record levels of investors in the property market, all competing with first home buyers and families wanting to upsize or downsize*:* between 2000 and 2013, lending for investment housing has risen by 230% compared with 165% for owner occupied housing[xiii].

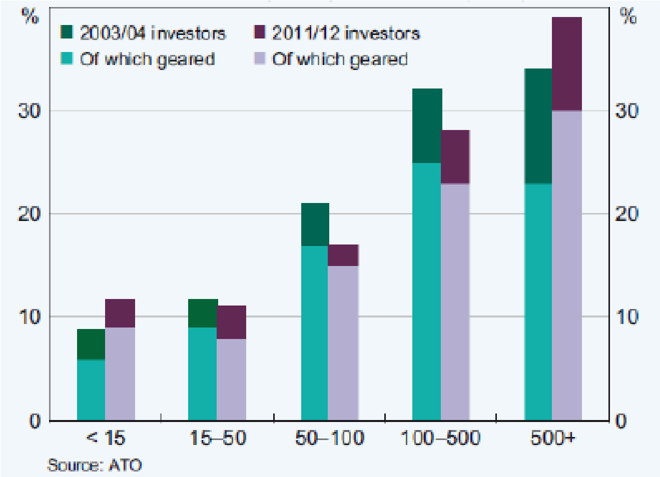
MYTH 3: REMOVING NEGATIVE GEARING WILL HURT 'MUM AND DAD' INVESTORS THE MOST

FACT: Supporters of negative gearing tend to use deceptive figures like *taxable income,* which is the income figure *after* other deductions are applied. This figure also ignores other income held in private trusts. This means the figures for middle income households that negative gearing advocates use actuallyhave much higher incomes before deductions are subtracted.

The more appropriate measure to use is *total income.* When we look at the number of taxpayers using total income **the proportion of low to moderate income earners who are negatively geared is actually very low:** only 12% of people earning a total income of $50,000-$100,000 (478,595 out of 3.9 million Australians) are claiming a net property loss.[xiv]

When the Reserve Bank compared investment in rental properties at different levels of total income they found over half of individual taxpayers with negatively geared rental housing investments are in the top 10% of personal taxpayers, 30% earned over $500,000, and 60% of negatively geared rental property investors came from the top 20% of households by disposable income[xv]. (Figure 1)

Figure 1: Property Investors by total income (RBA 2014 cited in ACOSS 2015).



Source: RBA (2014) "Financial stability review, September 2014. Box C: Households' investment property exposures, evidence from tax and survey data."

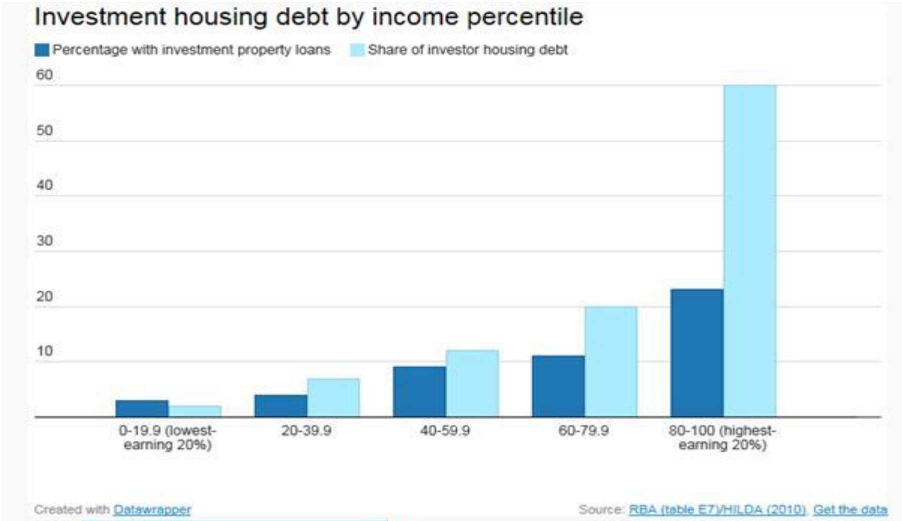
Research looking at the number of investors by income is also useful and shows low income earners have vastly lower rates of property investment: households in the top 20% of income distribution have 60% per cent of all investor housing debt while the bottom 40 per cent account for less than 10 per cent. This shows only a very small minority of those on lower incomes would be affected by a decision to scrap negative gearing[xvi] (Figure 2).

The overwhelming majority of independent analysts argue the claims by Treasurer Hockey that "most people who access negative gearing are middle-income Australians" and that those claims are untrue. Saul Eslake, chief economist for Bank of America Merrill Lynch, goes so far as to call the latter assertion a "lie".

The great majority of negative gearers are not, as Hockey claims, the mums and dads of middle Australia. Analysis from The Australia Institute showed:

- The top 10 per cent of income earners receive 55 per cent of the benefits of negative gearing and capital gains discounts; and
- households in the lower half of the income range receive only about 20 per cent of the benefits of negative gearing and slightly more than 7 per cent of the capital gains benefits

Figure 2: Property Investors by income distribution (Source: RBA/HILDA data in Michael Janda 2014)[xvii]



MYTH 4: LOW TO MEDIUM INCOME EARNERS USE NEGATIVE GEARING THE MOST

FACT: Negative gearing benefits the rich the most

Parliamentary Library research using the most recent figures available from the ATO shows that if negative gearing was removed, 93% of people earning $50,000 or less would be unaffected, along with nearly 90% of people earning a total income of $50,001 to $80,000[xviii]. This is because only 7% of taxpayers earning below $50,000 and only 11% of taxpayers earning between $50,000-$80,000 have net rental property losses.

The percentage of taxpayers in each income bracket with net rental property losses (eg using negative gearing) are highest for those with the highest incomes and those with 'zero' incomes, meaning self-funded retirees with property investments:

- Over half of individual taxpayers with negatively geared rental housing investments are in the top 10%, with 30% earning over $500,000[xix].

- The number of people using negative gearing is almost four times higher for those with incomes of $150,000 than for those with a total income of $50,000 or less.

MYTH 5: NEGATIVE GEARING IS NEEDED TO KEEP RENTALS AFFORDABLE

FACT: There's no evidence that landlords pass on any of the benefits of the concessions they receive to renters through lower rents or long term, stable housing. In fact in the last decade, rents tripled across Australia and homelessness increased as a direct consequence.

Australia's private rental market is one of the most expensive in the world, and offers less secure and more costly housing conditions than most OECD countries[xx]. Research shows investors are driven to realise their investment rather than provide a long term public service, and 'churn' properties in and out of the market, which impacts terribly on tenants. Research shows 25% of tenancies are terminated in the first year due to a sale[xxi], and negatively geared investors are twice as likely to sell within 12 months[xxii]. The massive undersupply of affordable rental dwellings in Australia (estimated to be more than 500,000 dwellings), combined with a tight rental market and low vacancy rates, high competition and the time constraints renters face when finding a home puts all the bargaining power in landlords' hands.

The Greens "Rental Health Check" in 2013 surveyed 278 renters across Australia and strongly verified the unfair impacts of the investment market:

- 65% had been forced to leave their rental through no fault of their own, with 22% having to move more than once in the past 5 years – the most common reason being that the house was sold
- 50% had been renting for more than 10 years, but most had been in their current house for less than two years,
- 75% had their rent increased in the past 2 years – with 14% by more than $50 per week, 61% did not consider their rent affordable, and 67% are in rental stress, with 47% paying 30%-50% of their income in rent, and
- 68% would like to be able to enter into a long term leas of at least 2-5 years, currently unavailable in the largely unregulated rental market,

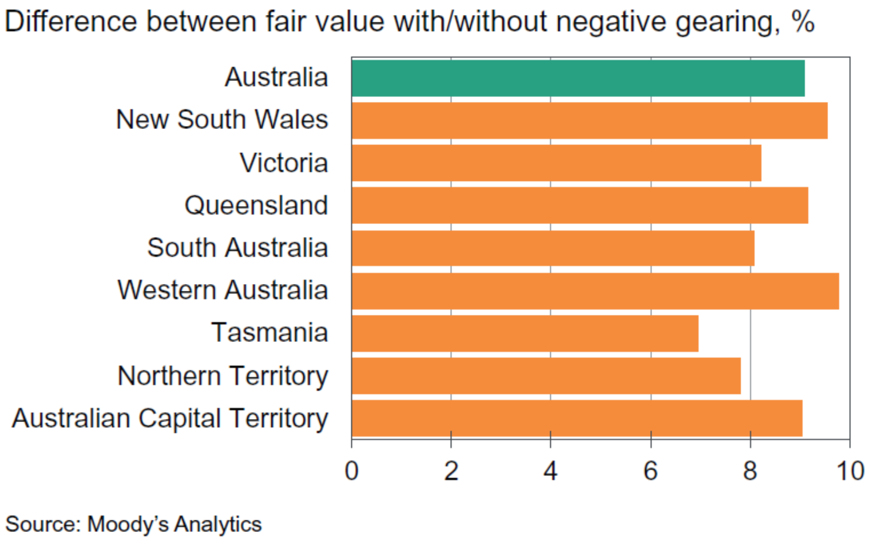
(You can complete the Rental Health Check at http://greens.org.au/rental-health-check)

As described earlier, when economists modelled the impacts of modest changes proposed in the Henry Tax Review on negative gearing and capital gains discounts they found reform would increase investment in rental housing and reduce rents by an average of $300 a year.[xxiii]

Moody's Analytics estimate negative gearing increases house prices by 9% - or about $44,000; and added 15% at its 2008 peak[xxiv] (Figure 3). In turn this only drives up rent prices – since nothing prevents landlords from pegging rent to the current 'market rate'.

The argument negative gearing keeps rents low is completely absurd: renters know the opposite is true.

Figure 3: How much does Negative Gearing add to housing prices?
(Source: Moody's Analytics July 2014 'Australian Housing Update: *Not Overvalued, Yet'*)



When we look at rent increases since 2000 – 2015 we see:

- The average Australian rent has at least doubled in every city since 2000; in Perth and Darwin rents have tripled or almost tripled (highlighted, below)[xxv]. Note also these figures are based on the average capital city prices, and are much worse for inner and middle ring areas.

- The so called recent “cooling” of rental prices of between 1-10% recently in Perth, Darwin and Canberra are coming off record year on year increases of 87 – 214% since 2000[xxvi].
- Meanwhile returns on residential property investment over the past 10 years have been significant: Investors have seen a record average return across Australian cities of 9.13% for houses, and 9.85% for apartments[xxvii].

The tables below show increases in rents since 2000, these are conservative figures using city averages which do not represent the rental stress and prices in middle and inner suburbs.

Quarterly median rents 3 bed house since 2000

HOUSES	SYD	MEL	BRI	ADE	PER	HOB	DAR	CAN	AUS
2000 median rent	230	190	185	165	164	150	230	200	198.2
2015 median rent	**450**	**350**	**370**	**330**	**450**	**330**	**600**	**420**	
difference ($ rise)	200	160	180	165	316	180	420	270	199.2
percentage increase	87	84.2	97.3	100	192.7	120	182.6	135	100.5
times increase	**1.9**	**1.8**	**2.0**	**2.0**	**2.9**	**2.2**	**2.8**	**2.4**	**2.0**

Quarterly median rents 2 bed apartment since 2000

UNITS	SYD	MEL	BRI	ADE	PER	HOB	DAR	CAN	AUS
2000 median rent	**250**	**170**	**150**	**130**	**137**	**125**	**190**	**175**	**187.3**
2015 median rent	**500**	**374**	**370**	**280**	**430**	**280**	**520**	**380**	**391.75**
difference ($ rise)	250	204	220	150	293	155	330	205	204.45
percentage increase	100	120	147	115	214	124	174	117	109
times increase	**2.0**	**2.2**	**2.5**	**2.2**	**3.1**	**2.2**	**2.7**	**2.2**	**2.1**

Source: REIA publishes two reports quarterly which include these figures; the first of these is the *Market Facts* (the latest was released in September 2014). These are reported on a capital city basis, rather than state-wide.

MYTH 6: NEGATIVE GEARING INCREASES RENTAL SUPPLY

FACT: There is no evidence that negative gearing increases supply of new homes or rental housing. In June 2013 only 5 per cent of housing investment loans went toward construction of new dwellings[xxviii].

Many arguing for reform suggests negative gearing only apply to new dwellings. This would likely skew the profile of investment toward properties most likely to yield higher capital gains at the upper end of the market. The rental property investment boom in the early 2000s that coincided with the introduction of Capital Gains Tax concessions drove new construction in inner city areas and exclusive holiday apartments which are of small benefit to low and moderate income earners desperate to find affordable accommodation close to work or suburban hubs.

After two decades, negative gearing has proven itself to be a failed and costly policy. Rents in Australia have almost tripled in the last 15 years, and demand has not kept up with supply: we currently have gap of more than 500,000 affordable rental properties. In June 2015 the Reserve Bank provided a compelling argument to scrap negative gearing, with its head of financial stability saying the impact of government policies and individual (investor) decisions over many years has given us comparatively low-density cities that create large price premiums for the most convenient districts in those cities, and when prices rise beyond what people can afford it’s not always feasible or attractive for potential homebuyers to move to cheaper areas[xxix].

All evidence shows negative gearing is only reinforcing a system which is the exact *opposite* of what’s needed: it reinforces the bias in favour of small speculative investors with one or two properties, when more investment by larger institutions such as super funds is what’s needed to stabilise the rental market and give tenants more secure, longer term tenure[xxx].

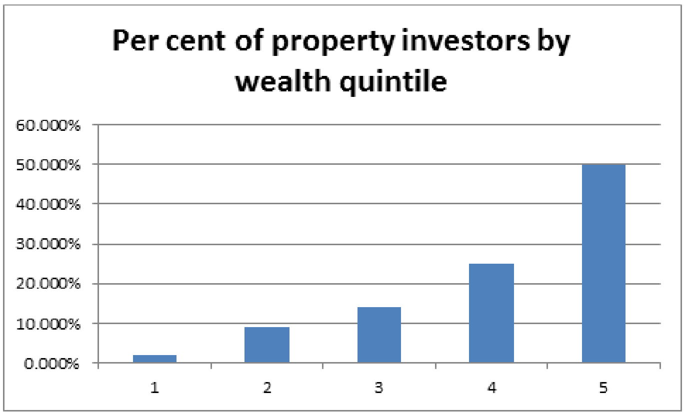
MYTH 7: NEGATIVE GEARING DOESN'T DISTORT THE TAX SYSTEM / "IS NOT A SUBSIDY"

FACT: It's a tax avoidance and wealth creation subsidy.

Negative gearing is one of Australia's largest tax expenditures, and it's also one of our most inequitable. Not only is used to a greater extent by people in higher income brackets but the 'losses' claimed (and therefore deductions from income tax) are also greater as their income increases[xxxi].

The truth is, the larger the income, the higher the benefit. (Figure 3)

Figure 3: Percentage of property investors by wealth



(Source: Parliamentary Library using ABS 2011-12 Household and wealth distribution)

People with total higher incomes are also more likely to borrow more and therefore claim higher amounts of interest on mortgage repayments than those on lower incomes.

Taxpayers are not only subsidising property investors to acquire more assets, but are also paying them to minimise or avoid paying tax. The subsidy has been described as "upside down and back to front"[xxxii] - providing greater benefits to people on higher incomes than to those on lower incomes, and greater subsidy to people who have established themselves in home ownership than those who are struggling at the beginning of the home purchase process.

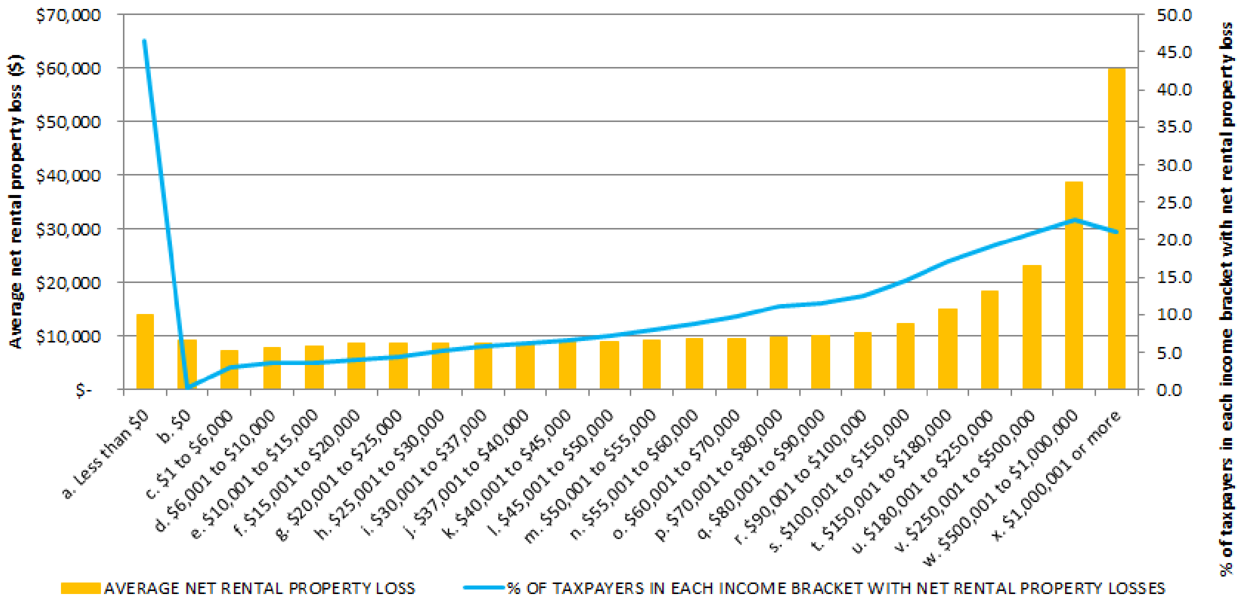
Figures provided by the Parliamentary Library show both the proportion of individuals using negative gearing *and* the average net rental property loss is greater the higher the income (Figure 4).

On average, residential property investors using negative gearing and capital gains discounts are receiving a benefit of about $4500 per year, but this rises to $9200 for households in the highest income quintile[xxxiii].

The benefits of negative gearing are strongly skewed in favour of higher income households. ABS data on the distribution of property investors between wealth quintiles (Figure A) shows the large majority of households owning investment properties are in the two highest quintiles.

Parliamentary Library research shows 1930 millionaires collectively claimed rental property losses of $115m – a tax deduction worth almost $60,000 each.

Figure 4 – Average net rental property loss by proportion of income
(Source: Parliamentary Library using ATO Taxation statistics 2011-12)



Source: ATO Taxation Statistics 2011-12. Note that 'Other' taxable incomes have been excluded.

The biggest winners from negative gearing were the nation's highest income earners. Almost 60,000 people with incomes of more than $180,000 a year lost a combined $1.4 billion on properties – translating to an average deduction in their taxable income of $24,000 for each taxpayer.[xxxiv]

The Henry Tax Review also found that two thirds of capital gains are received by the top 10% of taxpayers.

[i] The Australia Institute, 28 April 2015 Top Gears: How negative gearing and the capital gains tax discount benefit the top 10 per cent and drive up house prices
[ii] The Australian population was 23.846 million according to the ABS population clock at 8 June 2015 http://www.abs.gov.au/ausstats/abs%40.nsf/94713ad445ff1425ca25682000192af2/1647509ef7e25faaca2568a900154b63?OpenDocument
[iii] Reserve Bank of Australia Reserve head of financial stability Luci Ellis quoted in Business Insider Australia (2015) 'The Budget Office revealed Australia would be $42.5 billion better off by scrapping negative gearing'. Oliver Chang 7 June 2015 at www.businessinsider.com.au
[iv] Moody's Analytics July 2014 'Australian Housing Update: *Not Overvalued, Yet.*
[v] *Calculations:*
A home for the homeless: 6800 Australians in primary homelessness x $200,000/dwelling = $1.36billion pa;
Take 20,000 families of the waiting list each year: 10,000 x $200,000/dwelling = $4billion pa;
Create 5000 *Convert to Rent* conversions @$21,000 each = $105mpa
Provide 20,000 NRAS rentals per year: ~$10,000 full subsidy per year x 20,000 homes = $200m pa.
Total: $5.265 billion
Total The Australia Institute estimate we spend on Negative Gearing and CGT discounts: $7.7b
[vi] Australian Taxation Office Taxation Statistics 2012-13 Individuals –Detailed Tables Table 1 (Net rental property loss)
[vii] 2.29. million households renting minus ~450,000 social housing tenants = 1.84m private renters x 2.6 average household size = 4.785m individuals. Source: Most recent ABS census figures for 2011 -12 – Community Profiles Table B32

[viii] Committee for Economic Development (CEDA) (2015) *Addressing entrenched disadvantage* at http://www.ceda.com.au/research-and-policy/policy-priorities/disadvantage
[ix] Lindsay David, Paul Egan and Philip Soos. The Propertied Federal Political Class. 5 August 2014 at http://blog.australiaboomtobust.com/2014/08/propertied-federal-political-class/
[x] ABC Fact check: Did abolishing negative gearing push up rents? Updated 6 May 2015 http://www.abc.net.au/news/2015-05-06/hockey-negative-gearing/6431100
[xi] Grattan Institute director John Daley, on Q&A, cited by Peter Martin in the SMH, March 17 2015
[xii] Wood, Ong and McMurray (2011) The impacts of the Henry Review recommendations on the private rental market – savings income discount and rent assistance AHURI Final Report No 75.
[xiii] ACOSS (2015) 'Tax concessions key driver of housing price inflation' Media release 2 June 2015 at http://www.acoss.org.au/media/release/tax_concessions_key_driver_of_housing_price_inflation
[xiv] Note *Taxable income* or loss is total income or loss, less total deductions, less tax losses from earlier income years. Australian Taxation Office Taxation Statistics 2012-13 Individuals –Detailed Tables Table 9 (Net rent loss – no.) provided by the Parliamentary Library
[xv] RBA 2014 Financial stability review, September 2014 Box C: Households investment property exposures, evidence from tax and survey data, cited in ACOSS (2015) 'Fuel on the fire: negative gearing, capital gains tax and housing affordability' report. At http://www.acoss.org.au/images/uploads/Fuel_on_the_fire.pdf
[xvi] RBA/HILDA data cited in 'The myth of 'mum and dad' property investors', Michael Janda ABC The Drum, 24 Sept 2014 at http://www.abc.net.au/news/2014-09-24/janda-the-myth-of-mum-and-dad-negative-gearers/5766724
[xvii] RBA (table E7)/HILDA (2010) cited in Michael Janda 'The myth of mum and dad property investors' 24 Sept 2014 in the Drum - http://www.abc.net.au/news/2014-09-24/janda-the-myth-of-mum-and-dad-negative-gearers/5766724
[xviii] Parliamentary Library using ATO Taxation Statistics for 2012-13 data (latest available data).
[xix] ACOSS (2015) 'Fuel on the fire: negative gearing, capital gains tax and housing affordability' report. At http://www.acoss.org.au/images/uploads/Fuel_on_the_fire.pdf
[xx] Wulff, Reynolds, Dharmalingham, Hulse and Yates (2011) cited in Lawson (2012) Housing supply bonds and attracting institutional investment. *Around the House* no 91. Shelter NSW. December 2012. p9-12
[xxi] Wood and Ong (2010) Factors shaping the design to become a landlord and retain rental investments. Final Report 142. AHURI. Melbourne , cited in Lawson, Milligan and Yates (2012)
[xxii] Wood and Ong (2010) cited in ACOSS 2015
[xxiii] Wood, Ong and McMurray (2011) The impacts of the Henry Review recommendations on the private rental market – savings income discount and rent assistance AHURI Final Report No 75.
[xxiv] Moody's Analytics July 2014 'Australian Housing Update: *Not Overvalued, Yet.*
[xxv] Source: REIA publishes two reports quarterly which include these figures; the first of these is the *Market Facts* (the latest was released in September 2014). These are reported on a capital city basis, rather than state-wide.
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[xxvii] Source: REIA publishes two reports quarterly which include these figures; the first of these is the *Market Facts* (the latest was released in September 2014). These are reported on a capital city basis, rather than state-wide.
[xxviii] ABS (2013) *Lending Finance,* Canberra. Encompasses lending for housing investment, not for purchase by owner-occupiers, cited in Grattan (2013). See also ABS figures for lending finance used in the Grattan Institute 'Renovating Housing Policy (2013 page 25) report, at http://grattan.edu.au/report/renovating-housing-policy/ . They stated "But in June 2013, only 5 per cent of the money loaned for investment in housing went toward constructing new dwellings". See also McKell Institute 'Switching Gears - Reforming negative gearing to solve our housing affordability crisis' report released June 2015 http://mckellinstitute.org.au/wp-content/uploads/pdf/McKell_Negative-Gearing_A4_WEB.pdf
[xxix] Reserve Bank of Australia Reserve head of financial stability Luci Ellis quoted in Business Insider Australia (2015) 'The Budget Office revealed Australia would be $42.5 billion better off by scrapping negative gearing'. Oliver Chang 7 June 2015 at www.businessinsider.com.au
[xxx] ACOSS (2015) 'Fuel on the fire: negative gearing, capital gains tax and housing affordability' report. At http://www.acoss.org.au/images/uploads/Fuel_on_the_fire.pdf
[xxxi] Parliamentary Library briefing, 5 December 2014 drawing on ABS's 2011-12 *Household and wealth distribution*
[xxxii] Prof. Rick Krever Tax Watch, Monash University in www.shelter.org.au/archive/rpt0911policyplatform-final.pdf
[xxxiii] The Grattan institute using ABS 2013 data (2013) Renovating Housing Policy calculated tax concessions for residential property investors (including capital gains discounts) costs about $6.8 billion a year. Grattan Institute 2013.Older data by Yates (2010) used by ACOSS (2015) show in 2005-06 households in the top quintile were receiving an average benefit $3796 per year from negative gearing (with an additional $1562 from the capital gains discount on investment property) – worth about $103 per week, compared with $416/year or about $8 per week for those in the lowest quintile.
[xxxiv] 'Negative gearing tax system 'just crazy' Shane Wright 1 May 2013 The West Australian Page 6