Reduce tax on residential mobility

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Reduce tax on residential mobility

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How can Europe increase structural growth? This column argues that labour market flexibili a major barrier to labour movement is rigidity in the housing market, abolishing transfer ta residential property could result in gains of up to 0.4% of GDP.

The first EU council president Herman Van Rompuy has recently announced plans for a fol Lisbon Agenda. The next European summit will be focused on how to increase structu growth in Europe. Increasing labour market flexibility should be at the top of the agenda.

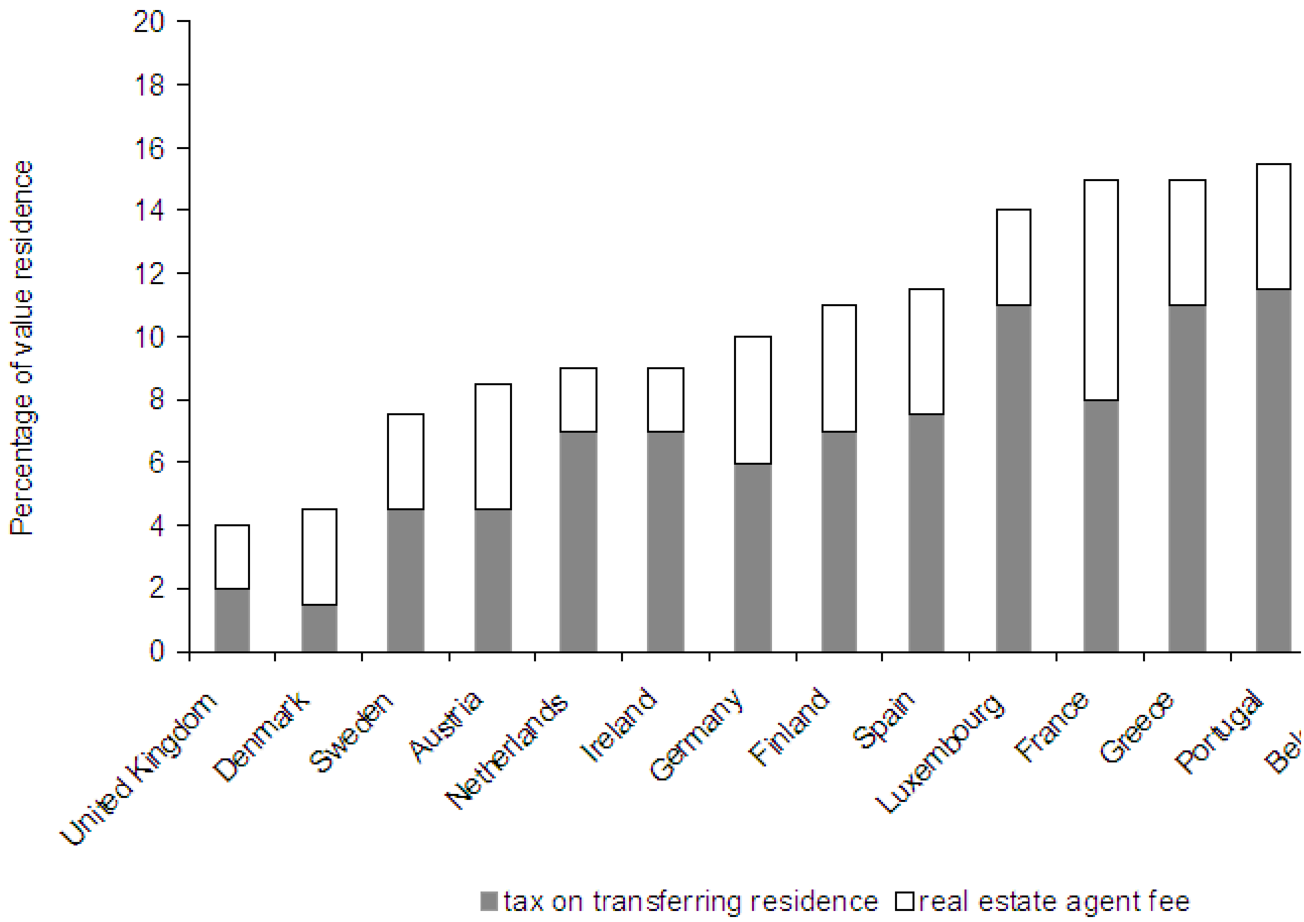
A new and challenging idea proposed by Andrew Oswald (1999) suggests that a lack of r labour market may arise from rigidities in the housing market. Oswald proposes that hc may be a hindrance to smoothly operating labour markets and may increase unempl transaction costs may limit residential mobility and reduce the willingness of homeowners offers outside their own region.

Following from this idea, we argue that an abolishment of transfer taxes on residences ir with a reduction in the general subsidy of owned residences, would increase residential n welfare and increase labour market flexibility.

Transfer taxes are substantial

Transfer taxes are a major part of the transaction costs of residential mobility. Figure transaction costs of moving residence are quite substantial for homeowners in mc Remarkably, governments impose additional burdens in the form of transfer taxes, on top high transaction costs due to costs and commissions. These taxes range from 0.6% in Der in Greece and Portugal, and even 12.5% in Belgium. Rather than promoting mobility expect, governments thus directly add to rigidity in the housing market and cause subst losses.

Figure 1. Transaction costs in the housing market in Europe



Source: Belot and Ederveen (2005)

Welfare gains of abolishing transfer taxes

Simply abolishing these transfer taxes would result in welfare gains. Table 1 provides a ro for the welfare gains of abolishing transfer taxes by calculating the deadweight loss associ transfer tax (Van Ewijk et al. (2007).

The deadweight loss can be expressed as ½ *ε t*, where *t* stands for the tax rate and elasticity of the tax base for the tax rate. A reasonable approximation for ε is eight as rep Ommeren and Van Leuvensteijn (2005). Table 1 reports for each European country a ran effects that follow from the observed tax rate and the size of the tax base as percentage range reflects differences in interpretation as to whether the notary costs and commissio interpreted as a real social cost or as an indirect tax due to regulation.

Table 1. Welfare gains from the abolishment of transfer taxes on residential property in 20

Countries	Welfare effect in billions of euros (2006)	Welfare effect as percenta
Austria	0.08-0.30	0.03-0.11%
Belgium	1.27-2.40	0.40-0.76%
Denmark	0.00-0.03	0.00-0.02%
Finland	0.02-0.11	0.01-0.06%
France	1.44-7.41	0.08-0.41%

Germany	0.40-1.88	0.02-0.08%
Greece	1.60-3.19	0.75-1.49%
Ireland	0.60-1.21	0.35-0.69%
Italy	3.75-14.04	0.25-0.95%
Luxembourg	0.03-0.11	0.09-0.33%
Netherlands	0.71-1.42	0.13-0.27%
Portugal	1.20-2.52	0.77-1.62%
Spain	3.24-9.17	0.33-0.94%
Sweden	0.02-0.16	0.01-0.05%
Switzerland	0.07-0.32	0.02-0.10%
UK	0.09-0.62	0.00-0.03%
Total	14.52-41.70	0.13-0.38%

Source: Van Ewijk and Van Leuvensteijn (2009)

We estimate that abolishment of transfer taxes on residential property would result in an (somewhere between 0.15% and 0.40% of GDP in the 16 European countries presente above. Welfare gains would be especially large in absolute terms in France, Italy and Sp countries, transaction costs are relatively high compared to the average. In Italy, the max loss is relatively high because the overall transaction costs on the housing market in Italy 19% (see Figure 1).

Increase labour market flexibility

In addition to these welfare effects, these measures would improve labour market flexi microeconomic perspective, the housing status of an individual agent can interfere at diffe labour market dynamics. Transaction costs associated with distant moves typically hamper The way in which transaction costs influence unemployment is more complex though. Une the steady state depends on the inflow into, and outflow out of unemployment. Transact affect both inflow and outflow rates. At a first sight, one might expect that transaction cost inflow into unemployment while reducing the outflow – in which case unempl unambiguously in the steady state. This is in line with Oswald's finding of a positive associa the fraction of homeownership and aggregate unemployment.

Fiscal prudence: Reduce subsidies to homeowners

If governments combined a reduction in transfer taxes with a reduction in subsidies for hor then fiscal prudence in the long run would become a key element of this fiscal measure. T transfer tax is paid instantly when the home is bought while the subsidy is a flow of mont to the homeowner thereafter. This means that the fiscal stimulus of the reform will gradually over the years. In fact, homeowners do not have to pay the transfer taxes demand additional finance from banks that are currently reluctant to provide mortga exceed the value of the home due to falling house prices. This measure could the confidence in the housing market. If governments abolish taxes and remove subsidies th be good for governments and people alike.

In many European countries, promoting homeownership is an official objective of gover usually supported by favourable tax regimes. A traditional argument for promoting hom that homeownership creates positive externalities (i.e. homeowners take more care for the neighbourhood). Although these externalities are found to exist, their size is probably warrant policy interventions (Glaeser and Shapiro 2002). In the end, the arguments promoting homeownership are weak.

There is therefore a general tendency to reduce the (implicit) subsidisation of homeowner subsidy is still considerable in many countries (Hendershott and White, 2000).

Conclusion

Governments have the option to kill at least two birds with one stone. Abolishing transfe stimulate the economy in the short run and improve the flexibility of the economy structur transfer taxes provides additional labour market flexibility, because it enables homeown jobs outside their own region reducing the inflow in unemployment and increasing Combined with a reduction in subsidies in the housing market, this measure would also res fiscal policy in the long run.

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