Reduce tax on residential mobility

van Ewijk, C.; van Leuvensteijn, M.

Published in:
VOX : Research-based Policy Analysis and Commentary from leading Economists

Citation for published version (APA):

General rights
It is not permitted to download or to forward/distribute the text or part of it without the consent of the author(s) and/or copyright holder(s), other than for strictly personal, individual use, unless the work is under an open content license (like Creative Commons).

Disclaimer/Complaints regulations
If you believe that digital publication of certain material infringes any of your rights or (privacy) interests, please let the Library know, stating your reasons. In case of a legitimate complaint, the Library will make the material inaccessible and/or remove it from the website. Please Ask the Library: https://uba.uva.nl/en/contact, or a letter to: Library of the University of Amsterdam, Secretariat, Singel 425, 1012 WP Amsterdam, The Netherlands. You will be contacted as soon as possible.

UvA-DARE is a service provided by the library of the University of Amsterdam (http://dare.uva.nl)
How can Europe increase structural growth? This column argues that labour market flexibility a major barrier to labour movement is rigidity in the housing market, abolishing transfer taxes on 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 follow-up Lisbon Agenda. The next European summit will be focused on how to increase structural 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 labour market may arise from rigidities in the housing market. Oswald proposes that high transaction costs may limit residential mobility and reduce the willingness of homeowners to offer outside their own region.

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

Transfer taxes are substantial

Transfer taxes are a major part of the transaction costs of residential mobility. Figure 1. Transaction costs in the housing market in Europe

Remarkably, governments impose additional burdens in the form of transfer taxes, on top of high transaction costs due to costs and commissions. These taxes range from 0.6% in Denmark and 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 substantial losses.
Welfare gains of abolishing transfer taxes

Simply abolishing these transfer taxes would result in welfare gains. Table 1 provides a ranking for the welfare gains of abolishing transfer taxes by calculating the deadweight loss associated with the tax rate and the elasticity of the tax base for the tax rate. A reasonable approximation for the elasticity of the tax base is eight as suggested by Ommeren and Van Leuvensteijn (2005). Table 1 reports for each European country a range of welfare effects that follow from the observed tax rate and the size of the tax base as percentage of the value of residential property.

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

<table>
<thead>
<tr>
<th>Countries</th>
<th>Welfare effect in billions of euros (2006)</th>
<th>Welfare effect as percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Austria</td>
<td>0.08-0.30</td>
<td>0.03-0.11%</td>
</tr>
<tr>
<td>Belgium</td>
<td>1.27-2.40</td>
<td>0.40-0.76%</td>
</tr>
<tr>
<td>Denmark</td>
<td>0.00-0.03</td>
<td>0.00-0.02%</td>
</tr>
<tr>
<td>Finland</td>
<td>0.02-0.11</td>
<td>0.01-0.06%</td>
</tr>
<tr>
<td>France</td>
<td>1.44-7.41</td>
<td>0.08-0.41%</td>
</tr>
</tbody>
</table>
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 increase somewhere between 0.15% and 0.40% of GDP in the 16 European countries presented above. Welfare gains would be especially large in absolute terms in France, Italy and Spain countries, transaction costs are relatively high compared to the average. In Italy, the maximum loss is relatively high because the overall transaction costs on the housing market in Italy are 19% (see Figure 1).

Increase labour market flexibility

In addition to these welfare effects, these measures would improve labour market flexibility microeconomic perspective, the housing status of an individual agent can interfere at different stages of labour market dynamics. Transaction costs associated with distant moves typically hamper the mobility of labour. The way in which transaction costs influence unemployment is more complex though. Unevenly across the steady state depends on the inflow into, and outflow out of unemployment. Transaction costs 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 unemployment unambiguously in the steady state. This is in line with Oswald’s finding of a positive association between 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 homeowners, then fiscal prudence in the long run would become a key element of this fiscal measure. The transfer tax is paid instantly when the home is bought while the subsidy is a flow of money 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 on the purchase of a home due to falling house prices. This measure could then improve confidence in the housing market. If governments abolish taxes and remove subsidies, it would be good for governments and people alike.
In many European countries, promoting homeownership is an official objective of government supported by favourable tax regimes. A traditional argument for promoting homeownership is 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 too small to 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 transfer taxes stimulate the economy in the short run and improve the flexibility of the economy structure. Transfer taxes provides additional labour market flexibility, because it enables homeowners to look for 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 reduce fiscal policy in the long run.

**References**


*This article may be reproduced with appropriate attribution. See Copyright (below).*

**Topics**: Europe's nations and regions, Labour markets

**Tags**: 