Executive Summary

Housing plays a central role in our lives. Access to shelter is a basic human need and a key determinant of individual welfare. Access to well-located, quality housing shapes people's social lives as well as their access to health care, education, job opportunities and recreational activities. Housing also affects well-being on a daily basis as the home is the centre of family life and increasingly of professional life, with the widespread adoption of teleworking during the COVID-19 pandemic. In OECD countries, housing is on average the single-largest expenditure item across all income groups and has accounted for an ever-larger share of total household expenditure in recent years.

Housing also constitutes households' largest lifetime investment and the majority of their wealth, though its significance varies across countries. Housing is a key vehicle for wealth accumulation and is a particularly important asset for middle-class households. In OECD countries, owner-occupied housing accounts on average for 50% of total household wealth across all households and for more than 60% of middle-class wealth. However, the importance of housing varies widely across countries. For instance, homeownership rates range from 44% (Germany) to 93% (Lithuania), while housing wealth (including both owner-occupied and secondary housing) accounts for at least 80% of total household wealth in Chile, Latvia, Lithuania, and Greece, but less than 40% in the United States and New Zealand.

While more equally distributed than financial assets, housing wealth remains concentrated among high-income, high-wealth and older households. High-wealth households, and to a lesser extent high-income households, own a disproportionately large share of owner-occupied housing wealth and own the majority of secondary housing wealth. High-income households also hold a disproportionate share of housing debt, although lower-income households with mortgages generally face higher relative debt burdens. Homeownership and housing wealth are also strongly associated with age, with older households holding more housing wealth and representing a far greater proportion of homeowners.

Recent decades have seen unprecedented growth in house prices, making housing market access increasingly difficult for younger generations. Despite some fluctuations, house prices have seen a strong and continuous growth over the past century, with a rapid acceleration in house price increases in the last 30 years and even sharper growth during the COVID-19 pandemic. House price growth has been uneven across regions, however, with much more significant rises in large metropolitan areas. House price inflation, particularly in urban areas, has been driven by a combination of factors constraining housing supply (e.g. limited space in highly urbanised areas, land use and zoning regulations, rising construction costs) and stimulating demand (e.g. demographic changes, low interest rates, globalisation). Declining housing affordability poses a particular challenge to younger households, with evidence that homeownership rates have been declining for younger cohorts over time, particularly among those with lower income and wealth.

Housing also has wide-ranging environmental impacts. The residential sector has a significant carbon footprint, accounting for around 22% of global final energy consumption and 17% of energy-related CO_2 emissions, with the bulk of the housing sector's energy consumption originating from heating. Housing is also a significant source of fine particulate matter. Housing has wider environmental impacts on land use and biodiversity, for instance through the loss of rural lands and the fragmentation of natural habitats, as well as on transport and water consumption.

Housing taxes are of growing importance given the pressure on governments to raise revenues, improve the functioning of housing markets, and combat inequality. As they emerge from the COVID-19 pandemic, many countries are looking to restore public finances by raising tax revenues while supporting the economic recovery. Many governments are also under increasing pressure to address rising inequality and declining housing affordability, which is more acutely affecting low-income and young households. In addition, in the context of growing international mobility of both capital and people, governments may aim to raise more revenues from less mobile tax bases, in particular real estate. This increased attention on housing taxes reinforces the need to design them effectively and fairly.

Housing taxation already plays an important role in the OECD, with countries levying a wide range of taxes on immovable property. All OECD countries (though not all sub-central governments) levy recurrent taxes on immovable property. Owners of rental properties are taxed on their rental income and, in a minority of countries, owner-occupiers are taxed on imputed rent. Transaction taxes are also commonly levied upon housing purchases and capital gains taxes are levied on the disposal of housing, although many countries exempt capital gains on the sales of main residences. Inheritance and gift taxes may also be levied when immovable property is transferred to heirs.

Nevertheless, the report finds that the way housing taxes are designed often reduces their efficiency, equity and revenue potential. Many countries still levy recurrent property taxes on outdated property values, which significantly reduces their revenue potential (as revenues have not risen in line with property values), their equity (as households whose properties have increased in value may not be paying more tax), as well as their economic efficiency (as property taxes levied on outdated values provide incentives for people to remain in housing that is subject to a lower outdated valuation, even if it no longer suits their needs). Reliance on transaction taxes is high, despite the potential for these taxes to reduce residential, and to some extent, labour mobility. The majority of countries fully exempt capital gains on main residences, and while there may be justification for such an approach, an uncapped exemption provides vastly greater benefits to the wealthiest households and further distorts the allocation of savings in favour of owner-occupied housing. Other forms of tax relief for owner-occupied housing, in particular mortgage interest relief, have been found to be regressive and ineffective at raising homeownership rates. In some countries, features of rental income taxation and inheritance tax rules applying to housing also reduce progressivity and revenue potential. The assessment also shows that, while housing taxes are viewed as harder to avoid and evade than other taxes, tax systems often leave room for such behaviours, reducing the efficiency, fairness and revenues of housing taxes.

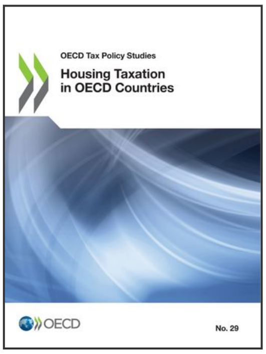
This report also finds that some housing tax policies may help address current housing market challenges, although tax policies may not always be the most effective tools. Tax policies may be used to address specific housing market challenges, such as significantly reducing the carbon footprint of housing, encouraging a more efficient use of land and housing, and boosting the supply of affordable housing. However, tax policies may sometimes be a blunt tool and may even be counterproductive under certain circumstances. In particular, where tax relief is intended to encourage homeownership, it can sometimes contribute to raising house prices and redistributing wealth to current homeowners if housing supply is fixed. Even where tax policies can play a positive role (e.g. vacant home taxes, tax incentives for energy-efficient housing renovations), they may not necessarily be as effective as alternative policy instruments (e.g. regulations) and will generally need to be complemented by other policy measures.

The report identifies a number of reform options that countries could consider to simultaneously enhance the efficiency, equity and revenue potential of housing taxes. The report discusses a wide range of reform options that could help enhance the design, functioning and impact of housing taxes, which includes the following:

- Strengthening the role of recurrent taxes on immovable property, in particular by ensuring that they are levied on regularly updated property values, while lowering housing transaction taxes would increase efficiency in the housing market and improve vertical and horizontal equity.
- Considering capping the capital gains tax exemption on the sale of main residences to ensure that the highest-value gains are taxed would strengthen progressivity and reduce some of the upward pressure on house prices, while continuing to exempt capital gains on the main residence for the majority of households.
- Gradually removing or capping mortgage interest relief for owner-occupied housing would also have positive impacts on progressivity, tax revenues and house price affordability.
- Tax incentives for energy efficient housing renovations could be better targeted to ensure that they reach low-income households. This could contribute to greater emissions reductions and enhance the equity of tax incentive schemes.
- Caution should be exercised when considering tax incentives to encourage homeownership; in most cases, encouraging the supply of housing and promoting the more efficient use of existing housing stock through both tax and non-tax measures is likely to have a greater impact on housing affordability.
- Strengthened reporting requirements, including third-party reporting to the tax authority and international exchanges of information for tax purposes, are also key to ensuring that housing taxes are enforced properly.

Any assessment of housing tax policies should take a holistic view of their interactions with other tax and non-tax policies and with housing market conditions. Interactions between different housing tax policies should be carefully assessed. For instance, residential mobility will be affected directly by both transaction taxes and capital gains taxes, and indirectly by the design of recurrent taxes on immovable property. Reforms aimed at enhancing mobility should therefore consider all three taxes. Carefully assessing interactions between taxes may also help identify cases where, before introducing new tax instruments, countries could consider reforming the design of existing housing taxes. For instance, there may be less need for special taxes to reduce speculation where short-term capital gains are adequately taxed. Similarly, a recurrent tax on immovable property based on regularly updated market values may reduce the need for tax instruments (e.g. infrastructure levies) aimed at capturing property value increases resulting from local public investments. Interactions between tax and non-tax policies are also key. There may be cases where non-tax policies may provide a more effective and equitable alternative to tax measures, especially when the goal is to promote housing affordability. There may also be cases where the success of tax measures depends on other policy settings or housing market conditions.

Housing tax reforms require careful timing and consideration for their impact across different households. Housing tax reforms can have a sizeable impact on house prices, with potentially significant distributional effects as well as wider financial and economic repercussions. A gradual implementation of reforms can help prevent negative macroeconomic shocks while also alleviating the adverse effects of reforms on specific groups of individuals, at least in the short run. Accompanying housing tax reforms with other tax or transfer measures may also help mitigate the impacts of some reforms on more vulnerable people and enhance the public acceptability and political feasibility of policy changes. Governments considering housing tax reforms should also be mindful of the evolution in the macroeconomic environment, in particular changes in interest rates and their potential impact on housing markets and households.



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