30 Apr 2016 The Vancouver Sun J. Geoffrey Howard is a Vancouver lawyer and an advocate for affordable housing.

MARKET ISN'T UNFIXABLE

J. Geoffrey Howard has a few ideas that might solve our affordable housing crisis

We need to ensure more condos reach the long-term rental market rather than being held empty or underused as short-term investments or rented as short-term accommodation to visitors.
— J. Geoffrey Howard

Housing is not only a necessity of life — it is both the single most important driver of our well-being and almost everyone's single largest living expense. Thus, when prices to both buy and rent housing spike far above healthy ratios to local incomes and long-term price trends, governments must step in to moderate prices to protect residents.

JONATHAN HAYWARD/ THE CANADIAN PRESS/ FILES The dramatic rise of real estate prices in the Lower Mainland has caused some observers to fear a 1981-style crash could be in the making.

The current Lower Mainland market is characterized by unprecedented speculative fever that has distorted prices from Squamish to Abbotsford. The extraordinarily high cost of housing, including new rentals, is inflicting hardship on all but the wealthiest buyers. Failure to intervene and reduce prices will only lead to a dramatic price drop that will inflict severe economic pain on everyone from Realtors to builders and developers to homeowners.

Ultimately, the housing bubble is a reflection of the sentiment that Vancouver housing will always go up (or at least never go down) and yield greater returns than other investments. The key is to introduce measures that will change that to an expectation that housing prices will decline significantly to a more affordable level — but still high relative to local incomes — over the near term, while encouraging growth of rental inventory.

PRINCIPAL CAUSES OF THE BUBBLE

Some factors contributing to the real estate bubble are systemic, and either not amenable to short-term adjustment or involve features of life in the Lower Mainland no one wants to change: our high quality of life, our protected parks, security of investment, high immigration rates and a relatively strong job market as examples. While there may be others, the key long-term drivers of the speculative housing bubble that are subject to regulation appear to be the following: Historically ultra-low interest rates: Medium- to long-term mortgage rates of 2.5 to three per cent are the prime enablers of the current price bubble, allowing locals and foreigners alike to carry higher mortgages and thus pay more for houses than more normal rates would permit. However, changing local mortgage rates is not feasible. A large number of wealthy foreign buyers: There is ample evidence that Vancouver is unique in North America as a mid-sized urban area with a very large number of foreign buyers who use substantial wealth acquired elsewhere (and generally only taxed elsewhere, if at all) to buy homes. No land for more detached houses: A shortage of available, desirable land on which to build detached housing is also a factor unique to Vancouver as compared to Canadian cities such as Toronto and Calgary. High construction costs: Vancouver has some of the highest building costs for almost any category of residential building, which is a product of several factors, including high wage and supply costs, but also high municipal charges and costly regulatory compliance costs.

These major long-term factors have been aggravated by these more recent factors: House-hopping renovators: Renovate-to-sell entrepreneurs buy older homes and

either rebuild or renovate them quickly, followed by a period of about a year of sometimes theoretical personal occupation of the house before reselling for a quick profit. They pay no tax on this income by asserting the home was their principal residence. Pre-closing shadow-flipping

(a.k.a. assignments): These are a telltale sign the market is out of control. Because prices are now rising so fast from already astronomical levels, it is economically axiomatic that a fair price for a house agreed one day will be lower than the market value of the same house on closing three or six months later, creating the opportunity to flip houses by assigning contracts to purchase before the closing. Poor regulation of Realtors: Recent newspaper reports have shown a minority of Realtors are more interested in their own gains and are major contributors, both as agents and as buyers and sellers themselves, to the frothy market — yet they receive low penalties even if caught.

WHAT CAN THE GOVERNMENT DO?

There are moves that can be made to better regulate the market. For starters, special taxes on non-tax resident buyers can be introduced alongside a new investment program for non-tax residents. The key to moderating prices is to discourage continued accumulation of and speculation in Vancouver houses by non-tax residents while offering them an alternative that allows them to invest in B.C. and Canada. That alternative could be an immigrant investor fund for building more rental housing.

Governments should bring in a special significant tax, charged on closing, on all purchases of housing in the Lower Mainland by non-tax residents. Using tax resident status to trigger the tax is logical: Those paying their fair share of income and other taxes in Canada on worldwide income and with worldwide asset disclosure as required under existing law will not be penalized, whatever their origins. Enforcement will require purchasers to provide proof they are Canadian taxpayers and swear a declaration they have disclosed income and foreign assets, and paid full Canadian income taxes on worldwide income when purchasing land. To avoid abuse, a minimum declared historic income would be required to be exempt from the surtax. Where the income shown does not support the cost of the house, no exemption will be granted. Corporate buyers and nominees will have to prove that beneficial ownership of the company or property is held by taxpaying residents. No doubt other exemptions would need to be allowed — for example, to cover legitimate gifts between Canadians.

Rather than just deterring overseas buyers from buying in Vancouver with such a tax, a companion initiative could channel the money currently chasing houses to instead create affordable rental housing. Non-tax residents should be encouraged to invest in a new long-term rental housing investor fund that builds rental housing with longterm affordable rents.

The renovate-to-sell flippers should be subject to full taxation on the gains as required by existing law. In addition, the provincial government should bring in a steep flip surtax under the property transfer tax regime locally for any property either resold in less than, say, two years, or a sale where the original contract of sale was assigned from the original buyer (shadow-flipped). For resales within the time limit, owners forced to sell for nonspeculative reasons such as an unexpected transfer could apply for an exemption.

EXPANDING THE RENTAL POOL

For rental housing, condos should be the major source of new rental housing. However, we need to ensure more of them reach the long-term rental market rather than being held empty or underused as short-term investments or rented as short-term accommodation to visitors. The provincial government could consider selectively limiting outright bans on rentals in strata bylaws, at least in new stratas.

Municipal governments could also move to enforce existing land use bylaws to stop owners renting out condos and other rental housing in the short-term rental market — think Airbnb and VRBO.

Although the full scope of the reforms above are significant, none are extraordinary and more than half could be implemented without passing new legislation. Some, such as the flip surtax, will require consultation and careful drafting before being legislated, but even committing to pass them should have a moderating effect on markets. Any additional tax revenue earned by the provincial government from these taxes beyond the cost of administering them could be invested in affordable housing. This ambitious agenda calls on all three levels of government to do their part, with the provincial government taking the lead on several key initiatives. The proposed initiative for immigrant investors entails co-operation from Ottawa since immigration is a federal responsibility. Several of these reforms may need to be reviewed for effectiveness and to ensure they are needed in the medium term if prices correct.

Obviously a small number of non-speculator owners who recently bought at the top of the market may suffer from lower prices if these reforms have the desired effect. That risk always existed and was arguably obvious to any informed buyer in the past two years or so. Introducing these measures strategically and moderating them once the market starts to correct will ensure this group does not face a catastrophic and abrupt market crash as occurred in 1981.

Given the state of the Lower Mainland real estate market, it is urgent to review these options to show market players that governments are committed to addressing the high cost of housing. The costs to the Lower Mainland of either further uncontrolled price inflation or, eventually, a 1981-style crash, are too high to risk.