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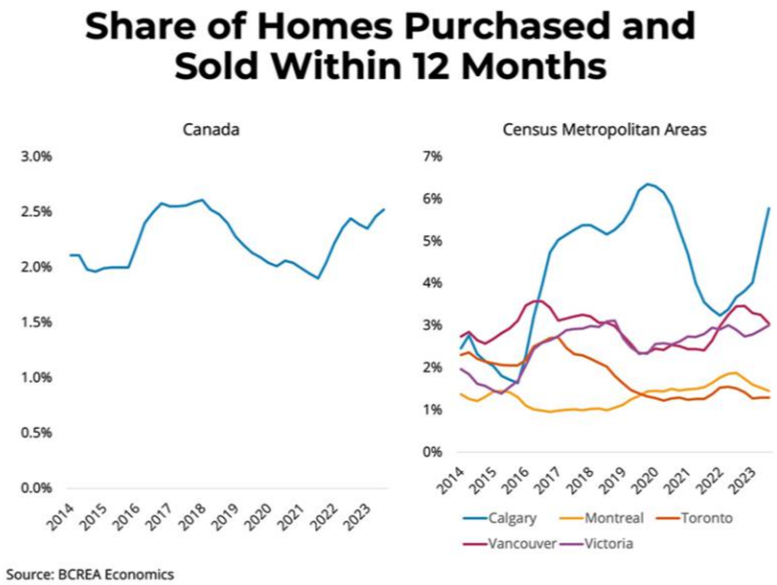
# More Trouble Than It Is Worth – Analyzing the Impacts and Consequences of the Provincial Flipping Tax

## Key Points

- Flipping activity, by any definition, is an insignificant share of overall transactions in BC.
- We estimate that the flipping tax will lower sales in BC by 1.7 per cent, but will have minimal impact on home prices.
- There is a significant risk that the tax will cause potential sellers to delay listing their homes, leading to lower resale housing supply and tighter market conditions.

## Introduction

The BC Government has announced its intention to implement a flipping tax in British Columbia. Specifically, the government is proposing to add an additional tax to the proceeds of the sale on the sale of a home sold within two years of purchasing.




We know that flipping activity can be harmful when markets become overheated, and rapid price appreciation attracts market participants who are purely short-term speculators. It is important to differentiate sellers who are merely trying to profit from short-term market conditions from those who invest their time, labour, and capital to improve the housing stock or provide additional rental units.

In this Market Intelligence, we will look at the potential impact of this policy on the BC housing market and draw out some of its potential consequences.



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## Background

Residential home flipping refers to the act of buying a home and selling it shortly after, to earn a profit. The buyer might speculate that:

Market sentiment will improve, causing an upswing in value.

1) Macroeconomic conditions will improve, such as a decline in interest rates, causing prices to rise.
2) The home will benefit from unexpected announcements, such as a new amenity nearby or a policy change.
3) The home is mispriced or underpriced, allowing the buyer to resell at a higher price.
4) The buyer can undertake short-term renovations and resell at a price that will cover the transaction costs and renovations with profit.

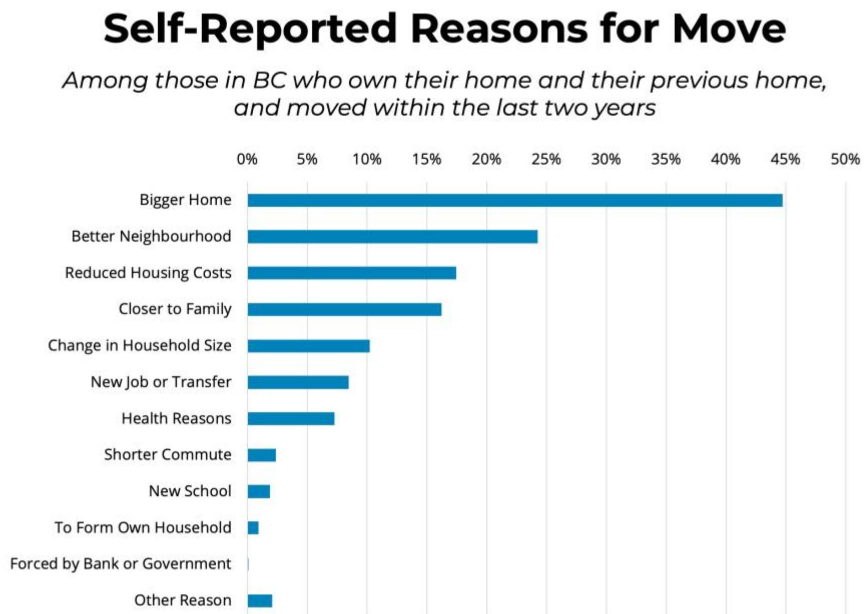
Flipping is controversial in Canada, with critics arguing that flipping contributes to home price inflation, potentially by stoking the “animal spirits” of hot markets. However, the extent to which flippers indeed cause home price appreciation remains theoretically and empirically ambiguous. It is unclear whether flippers cause price appreciation or are merely attracted to markets where price appreciation is highest due to other factors like supply constraints and high population growth. It has been argued that by marketing and effectively staging homes, flippers facilitate the “search process” for long-term buyers. When flippers fix up or renovate properties, they improve the stock of available housing, undertaking considerable risk in the process.

Amid rapidly rising home prices and rents, policymakers have introduced new rules to curb flipping behaviour. In Budget 2022, the federal government introduced new legislation stipulating that the capital gains from “flipped” homes would be treated as full business income starting in 2023, including on principal residences. A sale is deemed to be a “flip” if the sale occurs less than one year after purchase. Before the legislation, sales of homes that were not a person’s principal residence were taxed as ordinary capital gains, meaning that just 50 per cent of the profits were taxable as income. If the sale was of a principal residence, no tax was applied to the capital gain. After the change, profits from sales within one year are treated like normal income, and 100 per cent of the gain is taxed at the individual’s federal and provincial income tax rate. The legislation stipulates that a sale is not deemed a “flip” if there is a death in the family, a new person enters the family, a relationship breaks down, a disability or serious illness arises, the taxpayer or family relocates for work or education, the taxpayer or spouse loses employment, the taxpayer becomes financially insolvent, there is a threat to the safety of the family, or the property is destroyed or expropriated.

But how common is flipping? According to the Bank of Canada, just 2.5 per cent of all sales in Canada were of a home purchased within 12 months as of the latest data. In Vancouver and Victoria, the number is about 3.1 per cent. The BC Government states that, from 2020 to 2022, the proportion of homes that were purchased and sold within two years was approximately 7 per cent, while other estimates are closer to 10 per cent.

But we do not know how many of these sales would have incurred the "flipping tax." It may be that a large proportion of these sales would be classified under one of the exceptions outlined by the legislation, such as relationship breakdowns, deaths, or relocations.

We can get an idea of why those who move from their principal residence shortly after buying by examining the data from the Canadian Housing Survey. We restrict the sample to British Columbians who moved within the last two years and owned their previous place of residence. The stated reasons for moving are displayed below, with responses non-mutually exclusive.




We find that the most common reasons for moving their principal residence were to get a bigger home, a better neighbourhood, to be closer to family, to reduce housing costs, or a change in household size. In about 8 per cent of cases, a new job or transfer was a reason for the move. Changes in household size, new jobs or transfers, health reasons, a new school, or being forced by a bank or government are all reasons that could potentially cause the flipping tax to be exempted. It turns out that 73 per cent of respondents identified at least one of those reasons for their move, indicating that a potentially large proportion of flippers could be exempt from the tax. It is reasonable, therefore, to assume that no more than one in 50 sales are "flips" in BC; whether this is a sufficient proportion to meaningfully push prices upwards is debatable.

High-quality data does not yet exist indicating how successful the federal flipping tax has been in discouraging flipping and weakening prices. It does not appear that we saw a meaningful decline in the small proportion of sales of properties that were purchased within 12 months, and prices have not obviously changed since the introduction of the federal tax. In other jurisdictions where similar rules exist, such as the United States, Australia, New Zealand, and Singapore, the effect of such taxes on prices remains ambiguous; the evidence is mixed and inconclusive, and if an effect exists, it is minor. In Singapore, the sudden reintroduction of a tax on purchases of pre-sale condominiums appeared to decrease sales volume and increase price volatility relative to the resale market, but it did not appear to reduce prices.[1] As British Columbia considers introducing its own flipping tax, it does not have much evidence indicating success in other jurisdictions, within Canada or elsewhere. It is also unclear how the provincial tax will interact with the federal tax, and whether an additional tax is necessary to discourage the practice.

## Details of the Provincial Flipping Tax

The provincial government is proposing to levy a 20 per cent tax on the gain from the sale of a home within a one-year time horizon and a pro-rated tax on sales that occur after one year but within two years. The tax will apply to both properties and assignments of contracts.

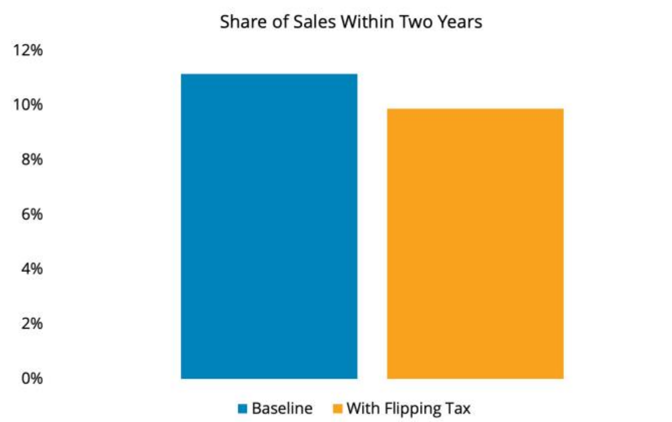
Exemptions will be available for certain life circumstances that might motivate the sale of a property within two years, such as separation or divorce, death, disability or illness, relocation for work, involuntary job loss, change in household membership, personal safety, or insolvency. Exemptions will also be provided for those who add to supply by building rental units or engaging in construction and real estate development.

Most "flipping" activity is already covered by a federal capital gains tax on the sale of an investment property and the federal anti-flipping tax, which levies a tax on the sale of a primary residence if held for less than one year. This tax is **in addition** to any federal or provincial income taxes incurred from the sale of the property.

## Estimated Market Impact of the Proposed Flipping Tax

We have estimated the impact of the provincial flipping tax using BCREA's Real Estate Policy Analysis Model (REPAM). REPAM includes three types of homebuyers: people buying a home to be a principal residence, long-term investors sensitive to borrowing costs and price expectations, and short-term investors who are primarily concerned with short-term price appreciation.

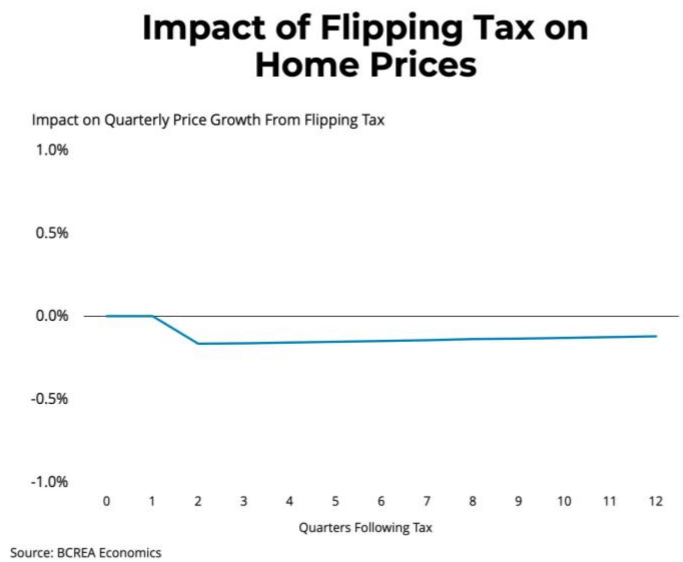
**Impact on Home Sales Within Two Years of Purchase**

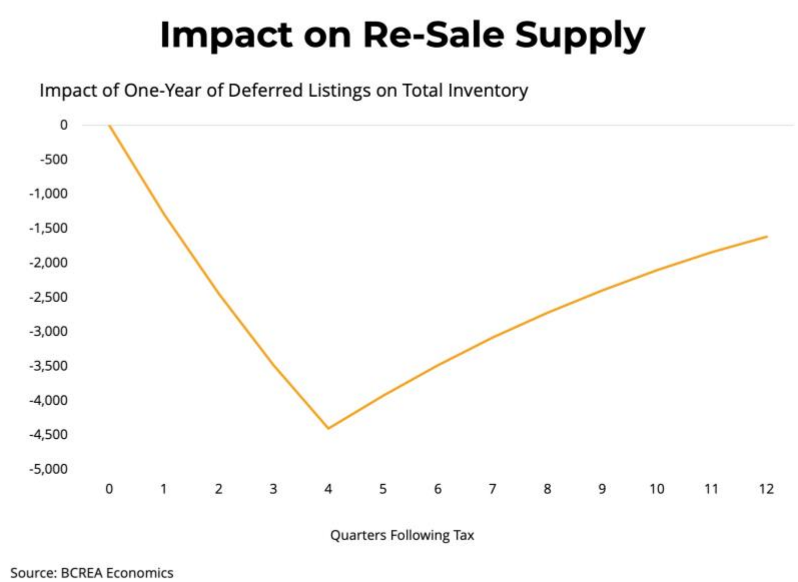



Source: BCREA Economics

[1] Qian, W., Yeung, B., & Fu, Y. (2013, November 7). Stamp duty and informed vs uninformed traders. VoxEU.

To estimate the impact of the tax in our policy simulations, we apply the impact of the provincial flipping tax to the price expectations of investors. That is, short-term flippers may expect a certain rate of return which is then reduced by the amount of the tax. For simplicity, we apply the flipping tax rate of 20 per cent to sales within a one-year time horizon and a 10 per cent tax to sales that occur after one year but before two years. We also assume that 50 per cent of those that sell after one year but before the two-year horizon qualify for exemptions to the tax.



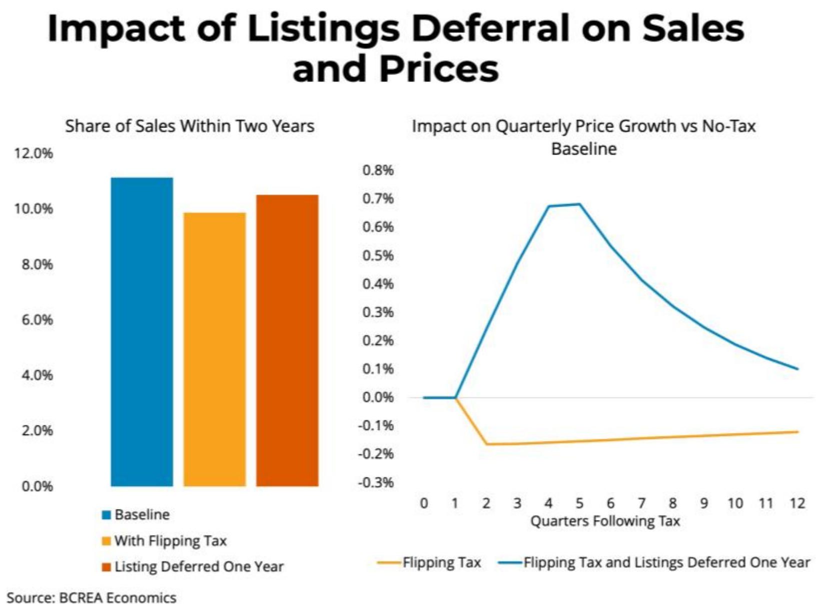

As a result of the flipping tax, we estimate that sales within a two-year horizon would decline from a baseline of about 11 per cent of all sales to 10 per cent. The overall reduction in home sales is about 1.7 per cent over a three-year period. Given the relatively small impact, prices and housing affordability are essentially unchanged with the tax. This is unsurprising, given that short-term flipping is a low share of sales activity.

However, because the government has now implemented a disincentive to sell within a two-year horizon of purchasing, some potential sellers will be prompted to delay listing. The flipping tax could also reduce liquidity in the pre-sale housing market and therefore impair financing for new housing projects and negatively impact housing supply in the long run.

We, therefore, need to account for the general equilibrium impact on the market from a change in resale supply that is driven by the flipping tax. We assume that some portion of potential sellers delay listing for a one-year period[2] to avoid the tax before listing their home. As a result, after the tax implementation, new listings drop before returning to their baseline.

[2] This is a simplification. In reality some sellers will delay longer and some for shorter periods.

While temporary, this drop in new listings causes a permanent drop in the total inventory of active listings compared to our no-tax baseline.




Accounting for these supply-side effects, the decline in active listings prompts markets to tighten which results in higher price growth and price expectations. As a result, some of the dampening effects of the tax are offset as more investors are attracted to the market by rising prices. This causes a slight increase in the share of sales within two years, though still below the no-tax baseline. Importantly, depending on how potential sellers react to the tax, home prices could be higher with the flipping tax than with a no-tax baseline, and affordability could deteriorate. In fact, our estimates show that a 5 to 10 percent decline in new listings due to the tax would negate any positive impacts on affordability from the tax.

Finally, although the government's goal of using flipping tax revenues to fund housing investments is laudable, the flipping tax is expected to generate very little net revenue. In its 2024 Budget, the government projects the tax will generate $11 million in its first partial fiscal year and $43 million in its second fiscal year. However, because the policy will negatively impact home sales, the government will net out much less revenue when accounting for lost revenue from property transfer taxes (PTT), as well as the costs of administering the tax and its complex exceptions. We estimate the policy will generate just $21 million in its first full year after accounting for lost PTT revenue, ignoring administrative costs.[3]

[3] Estimate is based on a median PTT paid of $12,000 for all transactions in BC.

## Conclusion

While this policy may help reduce harmful speculation during over-heated markets, defining a flip with a long horizon of up to two years is counter-productive when accounting for the policy's supply-side effects. Depending on how potential sellers react to the tax, it is entirely possible that the prices would be modestly higher with the flipping tax compared to a no-tax baseline.

Ultimately, speculation is a symptom of under-supplied markets. The only way to prevent harmful short-term speculation in the housing market is to ensure housing is abundant, such that markets can absorb inevitable demand shocks without prices accelerating. The types of supply-oriented solutions the government is encouraging through its Homes for People Plan are likely to be much more effective at reducing speculation than yet another tax.