# NSW Young Liberal Movement Submission on the NSW Property Tax Proposal

**March 2021**

**Prepared by members of the NSW Young Liberals**

[redacted]

15 March 2021

**NSW Treasury**

**Re: NSW property tax proposal**

To whom it may concern,

Please find attached a submission prepared by the NSW Young Liberals on the NSW property tax proposal.

As a Movement, we are concerned about rising house prices, locking Australians out of the Australian dream of owning a home. We believe this is an issue which affects the public at large, but which also has a significant impact on young Australians trying to save for their own home.

The NSW government must trash this tax.

Stamp duty is an inefficient, distortionary and unfair tax which locks Australians out of the property market and is an unstable source of tax revenue. We wholeheartedly support the government in its efforts to remove this tax and we call on it to go further. Currently, stamp duty acts as a handbrake on business transactions involving land rich entities and corporate restructuring and fails to provide sufficiently broad exemptions for charities. These shortcomings should be addressed in the property tax reform. To phase out stamp duty more quickly, we advocate for a property tax credit system for properties on which stamp duty has been recently paid.

We would be happy to respond should you have any further questions. If we can be of further assistance [redacted] can be contacted at [redacted]

Sincerely,

[redacted]

# 1 Introduction

[redacted]

Australia's successful recovery from the COVID-19 pandemic-induced recession is contingent on sensible economic reforms that generate wealth and prosperity for all. Owning your own home, a staple that envelops the Australian dream, is the most direct means of creating wealth and prosperity for individuals as the most valuable asset someone will own in their lifetime. However, as a result of dwelling supply issues and low interest rates, this tenet of the Australian dream has become unattainable for many Australians as supply has not adequately kept up with demand, and governments continue to persist in heavy handed planning laws, pushing prices upwards.[1] This disproportionately impacts younger Australians, who are more likely to be in the earlier stages of the life-cycle of saving. As the NSW Young Liberals, we recognise that this is an issue that affects the lives of all aspirational young people, and we want to advocate and have our voices heard on this reform.

Structural and cyclical issues also plague the current scheme that has exacerbated the housing affordability issue. Outlined in the Consultation Paper, the transaction cost often becomes a barrier for individual mobility due to the substantial upfront payment made when a property is purchased. This indirectly influences the allocation of resources in the economy, as the current system offers little incentive to move properties without major financial burden placed on the individual.

Cyclically, the stamp duty revenue base is heavily influenced by prevailing economic conditions and is susceptible to falls in revenue if property prices fall. This can create significant budget shortfalls and jeopardise the provision of essential services, as Stamp Duty makes up a quarter of total tax revenue in NSW- the highest in Australia (Property Council of Australia, 2015).[2] The NSW Young Liberals welcome the proposed change not to base the property tax off its market value, as this will mitigate the influence of property market performance on the tax burden.

The NSW Young Liberals strongly support the substitution of stamp duty for a broad based property tax. In this submission, we suggest areas where further work may be needed on the proposed reform and areas for further form. Specifically, we raise five key considerations:

- **Considerations for phasing out the current antiquated Stamp Duty program**: Looking at providing credits for stamp duty paid to assist in phasing in the reform quickly.
- **Appropriate pricing and land value calculation methods**: A review of the use of unencumbered land, market and square metre valuation methods for the property tax base to ensure fairness and revenue stability.
- **Further legal reforms to non-residential land**: Exploring the effects of the reform on large-scale businesses, trusts, landholding companies and charities.
- **Logistics of the proposed property tax collection**: Consideration of issues relating to debt collection, including suggested reforms for voluntary deferment, and concessions.
- **Hardship schemes**: Discusses the possibility landlords may pass on a portion of the property tax to tenants, and the viability of legal clauses that would prevent this.

[1] Ong, R., Dalton, T., Gurran, N., Phelps, C., Rowley, S. and Wood, G., 2017. Housing supply responsiveness in Australia: distribution, drivers and institutional settings. AHURI Final Report, [online] (281). Available at: <https://www.ahuri.edu.au/__data/assets/pdf_file/0012/13242/AHURI-Final-Report-281-Housing-supply-responsiveness-in-Australia-distribution-drivers-and-institutional-settings.pdf>

[2] Deloitte Access Economics. 2021. The economic impact of stamp duty: Three reform options. [online] Available at: <https://www2.deloitte.com/content/dam/Deloitte/au/Documents/Economics/deloitte-au-economics-impact-stamp-duty-reform-options.pdf>

## 2 Phasing out stamp duty

[redacted]

As outlined above, we are supportive of replacing stamp duty with a broad-based property tax. However, we are conscious of the challenges this transition may present in ensuring those who have recently incurred stamp duty liabilities aren't left worse off for the sake of a long-term beneficial change. We aim to present below a model for this transition that mitigates the short-term effects of this reform while preserving the intended purpose.

The model presented in the NSW Government's initial consultation paper certainly has its merits - most notably, preserving people's ability to plan their financial affairs around this change. However, we argue there is a more efficient way to mitigate the short-term impact of phasing out stamp duty without jeopardising the efficiency and equity benefits the reform is targeting.

A credit-based system in which landowners who have recently incurred a stamp duty liability would be able to minimise their property tax liability allows a more immediate transition while preventing 'double taxation'. In this model a person would be able to claim a credit towards future property tax liabilities calculated as:

> Stamp duty liability incurred less hypothetical property tax liability for the period of the date of payment of stamp duty to the date of the introduction of the property tax regime

It is important to note we do not propose that this model be implemented inversely - that is, if people would have incurred a property tax liability over this period greater than the stamp duty liability they incurred we are not suggesting they be required to pay this difference. They would simply receive a credit of $0. See below examples:[3]

> **Example 1**: John purchases a residential property to occupy on 17 July 2015. John incurred a stamp duty liability of $22,715. The property tax was introduced in FY2021. The unimproved land value of John's property each year during this period was as follows:
>
> FY 2017: $378,000
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> FY 2018: $410,000
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> FY 2019: $439,000
>
> FY 2020: $419,000
>
> For this period John's hypothetical property tax liability using the rate proposed in the NSW Treasury Consultation Paper would have been $6,938.
>
> In this case, John incurred a stamp duty liability $15,777 greater than his hypothetical property tax liability. John would be eligible for a credit of $15,777 towards future property tax liabilities.

> **Example 2**: Rachael purchases a residential property to occupy on 19 July 2008. Rachael incurred a stamp duty liability of $30,275. The property tax was introduced in FY2021. The unimproved land value of Rachael's property each year during this period was as follows:
>
> FY2009: $446,000<br>
> FY2010: $446,000<br>
> FY2011: $513,000<br>
> FY2012: $513,000<br>
> FY2013: $513,000<br>
> FY2014: $575,000<br>
> FY2015: $641,000<br>
> FY2016: $806,000<br>
> FY2017: $898,000

[3] Examples calculated using anonymised figures accessed using the NSW Valuer General Land Values and Property Sales Map. https://portal.spatial.nsw.gov.au/portal/apps/webappviewer/index.html?id=2536c8e4882140eb957e90090cb0ef97.

FY2018: $1,020,000
FY2019: $1,020,000
FY2020: $867,000

For this period Rachael's hypothetical property tax liability using the proposed rate would have been $30,774.

In this case, Rachael incurred a stamp duty liability $499 less than her hypothetical property tax liability. Rachael would be eligible for a credit of $0 towards future property tax liabilities.

## 3 Tax base and valuation issues

[redacted]

### 3.1 What to tax

The method of calculating the value of land is one of the most important considerations in creating an effective property tax model that is capable of producing a stable revenue stream that is able to capture value gained by government investments in the area.

This is best achieved by calculating the value of a property on the basis of its **unimproved land value**.

Utilising the existing Valuer General valuations of unimproved property value, which are also re-assessed on a regular basis and being combined with proposals for new technological solutions to compile data offers an effective path forward to calculating land value.[4] The Valuer General valuations are a common set of data, updated regularly, which will reduce the potential for concerns around how long term valuations are to be made on property.

In the context of strata schemes, as is presently the case for investment properties liable to pay land tax, the land value for each strata lot is calculated on a proportional basis using the unit entitlement for each lot and the aggregate for the strata scheme.[5]

### 3.2 How to tax

The method of calculating the amount of land tax property holders must pay presents both a practical revenue raising question, alongside a substantial political impediment. As stamp duty is currently collected on a progressive basis, attempts to collect land tax on a completely flat basis would present a serious challenge. In addition to this, implementing a marginal rate would also allow public policy considerations, such as encouraging greater investment in affordable housing alongside the more effective capturing of increases in unimproved value for particular areas that may have benefited from investment.

Calculating the marginal rate of land tax payable on the basis of meter squared value offers the best way to calculate what marginal land tax rate the land holder would fall under. The Henry Taxation Review outlined a number of the benefits of this scheme, including that in the long run implementing a marginal rate based on meter squared value of unimproved property value would enable all properties to fall under the land tax scheme. This includes agricultural properties, which could benefit from an extraordinarily low, or even, as was proposed by Dr Henry, a zero marginal rate.[6] It is also important to note that research undertaken by the NSW Business Chamber has indicated that a smaller number of margins is preferable over a large number on the basis of limiting complexity in the calculation of land tax payable.[7]

A marginal rate of land tax payable on the basis of meter squared value of property enables the tax to be levied on a very broad basis. If the NSW Government is to move to a very broad based land tax in the long term, this model of calculating land tax payable offers both a politically viable, and economically rational pathway forward.

[4] NSW Valuer General, 2019-20 Annual Report (Annual Report, 1 October 2020), 58.
[5] NSW Valuer General, Valuing Land In Strata Scheme Fact Sheet, (Fact Sheet, June 2016), 1.
[6] Ken Henry, Australia's Future Tax System (Report, 23 December 2009), 90.
[7] New South Wales Business Chamber, Taking on Tax: Reforming NSW Property Taxes (Report, 1 February 2016) 20.

# 4 Further legal reforms

[redacted]

The Consultation Paper focuses primarily on the phasing out of stamp duty for transfers of residential and commercial land. While this proposal is welcome, the NSW government should go further and abolish or phase out stamp duty in all its forms.

The *Duties Act 1997* imposes transfer duty not merely on transfers of land, but also on transfers of shares in companies, units in unit trusts and partnership interests in partnerships which hold land in NSW, transferable floor space and land use entitlements, statutory licences and gaming machine entitlements and inventory, property, plant and equipment, livestock and ships in NSW transferred as part of transactions involving transfers of other property subject to stamp duty.

These antiquated and heavy handed duties apply a handbrake to business investment in Australia, and particularly in NSW, and prevent the efficient allocation of capital in the economy. Investment in land rich companies suffers from delays of months while sophisticated taxpayers apply for tax rulings from RevenueNSW, jeopardising transactions. Whole transactions are structured around the effects of stamp duty. Corporate reconstructions and reorganisations are required to go through painstaking processes of applying for exemptions from stamp duty. Australian businesses are carved out of the completion of global transactions because of stamp duty structuring issues.

Stamp duty is a blunt and ineffective tax collection mechanism which significantly affects business transactions and investment. A property tax is a far better way to generate tax revenue, without preventing or distorting corporate transactions. The mischief which landholder duty sought to address, namely the avoidance of stamp duty, does not exist in a property tax perspective, as tax revenue is no longer tied to the transfer of property and will be payable regardless of which entity holds it.

Further, in the current stamp duty regime, there are gaps in the concessions given to charitable entities which we assert should be addressed and remedied with the introduction of the property tax. Section 275 of the *Duties Act 1997* limits full exempt charitable and benevolent body status (and the associated concession) to entities for the relief of poverty in Australia, the promotion of education in Australia and the promotion of the interests of Aboriginal people. These limits cut across centuries of common law and equity and prejudice other types of charitable institutions, such as charities for the promotion of religion or churches and charities for the provision of war widows and returned service personnel, charities which would be recognised under Commonwealth charities legislation.

# 5 Concessions and collection

[redacted]

We support the Government's proposal to alleviate the upfront cost of home ownership in New South Wales by abolishing transfer duty. However, if transfer duty is to be replaced with a property tax, significant issues may arise with debt collection, potential deferment, and concessions for young Australians purchasing their first property.

## 5.1 Collection, debt recovery and voluntary deferment

The NSW Government should carefully consider the mechanics of property tax collection to, first, refrain from placing additional strain on individuals who are still recovering from the financial tumult of the COVID-19 pandemic, and second, ensure that those who cannot cover their property tax liability temporarily will not be forced out of their homes.

Currently, collection of land tax in New South Wales for properties that are not principal residences, primary production land, or below the land tax threshold is managed by RevenueNSW. Land tax amounts are recorded in annual assessment notices and are payable by three instalment dates. Late payments generally incur interest, which is charged partially at a premium rate of land tax payable and partially at market rates.[8] Alternatively, individuals experiencing financial distress may opt-in to payment plans that often include interest-adjusted rates. To avoid a buyer incidentally taking on outstanding land tax liability from the seller, RevenueNSW encourages a buyer to apply for a clearance certificate via four service providers if otherwise not provided one by a seller. However, this outstanding tax bill is generally footed by the seller, reflected in their ultimate receipt of a reduced purchase price.

If a broad-based property tax is introduced, the NSW Government should introduce a similar instalment collection model via RevenueNSW. Discounts should be offered to households who pay their property tax obligation in full before the first instalment date. This incentivisation of timely payments is common-sense in that it will work to improve state revenue stability.

The COVID-19 global pandemic has emphasised the critical importance of mitigating liquidity risk for real property investments. Early signals of the Australian mortgage market tumult attributable to the pandemic were captured by ABA data between 14 May and 19 June 2020. At the conclusion of this data reporting, 485,063 Australian mortgages were deferred.[9] New South Wales households made up a substantial portion of these deferments. As at 11 February 2021, a mere 21% of these deferrals endure,[10] demonstrating how often liquidity issues persist for only short periods of time. In the same way, the NSW Young Liberals encourage the Government to explore the introduction of a voluntary property tax deferral mechanism. Like the conclusion reached by Prosper Australia on deferral, we see no compelling reason why this liquidity relief should be fettered by arbitrary eligibly criteria which may unintentionally exclude, for example, low-income owners, people who are cyclically unemployed, or asset-rich but income poor retirees or women escaping domestic violence situations.[11] Alike the conclusion reached by the Grattan Institute, we implore the government to work in consultation with Moody's and S&P Global in considering whether the deferred taxes could be managed by an independent statutory body and securitised, without adversely affecting our state's credit rating.[12] With deferrals, it is also critical to consider issues of proper indexation of interest on deferred property tax liability to prevent, for example, the disincentive to sell which may arise if the present value of this nominal tax liability is deflated the longer sale is delayed because interest is indexed below a homeowner's time value of money.[13]

### 5.2 First homeowner concessions

Our stamp duty system is manifestly out of touch with the economic realities of prospective first homeowners, particularly those seeking to purchase their first property in metropolitan areas of NSW. Even under the First Home Buyer Assistance Scheme operable between 1 August 2020 and 31 July 2021, a new home and an existing home must respectively be valued below $800,000 and $650,000 for a first home buyer to be eligible for a full stamp duty exemption.[14] Similarly, the value of a new and existing home must respectively be below $1 million and $800,000 for a prospective first home buyer to be eligible for some sort of partial stamp duty exemption. By contrast, the median house price of Sydney is expected to surpass $1.3 million over the next three months, in part due to our historically low interest rates.[15]

If our Government would lead in moving to this new property tax system and completely remove this existing, albeit limited, stamp duty concession, it would effectively remove the element of choice regarding whether to opt into the property tax scheme for prospective first home buyers acquiring houses worth, in present value terms, $1 million and $800,000. However, if the houses are valued above this threshold, the prospective buyers will be, ceteris paribus, indifferent to the proposed removal of this concession. To incentivise a shift towards a more modern property tax system, the NSW Young Liberals

[8] https://www.revenue.nsw.gov.au/taxes-duties-levies-royalties/land-tax
[9] https://www.ausbanking.org.au/banking-activity-update/
[10] https://www.abc.net.au/news/2020-10-15/half-of-deferred-australian-home-loans-back-to-payments/12767990
[11] https://www.facs.nsw.gov.au/__data/assets/pdf_file/0011/325478/LongTermAccommodation.pdf
[12] https://grattan.edu.au/wp-content/uploads/2019/12/NSW-productivity-Commission-Tax-submission-final-standalone.pdf
[13] https://www.prosper.org.au/wp-content/uploads/2019/07/Designing-the-Transition_Final_Helm.pdf
[14] https://www.revenue.nsw.gov.au/grants-schemes/first-home-buyer/assistance-scheme
[15] https://www.smh.com.au/business/the-economy/prospect-of-a-six-figure-hike-in-sydney-house-prices-stokes-affordability-worries-20210129-p56xwb.html

recommend concession for first-home owners. We suggest that this should not be tied to market values or be the form of a low-interest government loan, merely creating more debt for first homeowners. Rather, we suggest a cash grant which favourably brings this reform in line with the concurrent first homeowner grant scheme, as suggested by the discussion paper.

## 6 Hardship

[redacted]

The proposed changes to stamp duty are, at their core, reforms aimed at enabling those least able to enter the property market, to do so. The elimination of stamp duty will assist thousands of young families achieve the dream of home ownership, and eliminate an inefficient tax that hampers the occupational and geographic mobility of labour. Property ownership is an investment in one's family and self, and part of the Australian social fabric. It is simultaneously a useful vehicle through which personal equity and intergenerational security can be built, and livelihoods sustained into retirement. The changes to stamp duty will make this possible for more people, more quickly, by removing a major financial barrier to buying a house or apartment.

However, there are legitimate concerns about the possibility that some homeowners may find it difficult to pay an ongoing property tax. Additionally, renters may be concerned that landlords could ultimately pass on a portion of the property tax through increased rents.

To address concerns about the affordability of the property tax, the NSW government should investigate the feasibility and suitability of a hardship scheme for affected households. This could take the form of a deferred payment mechanism as outlined in section 5 above, whereby, for example, families experiencing temporary hardship could request that their payments be temporarily deferred, and paid at a later, specified date. Perhaps interest could be charged on this "debt" to discourage bad actors from simply delaying payment until a more preferable time.

Alternatively, property tax payments could be allowed to accrue over time and paid when the property is sold, rather than on a regular basis. This would enable low-income property owners, such as aged-pensioners, to remain in their home even if they cannot afford to pay an annual tax. This is especially important as asset prices continue to rise faster than incomes. This system would aim to avoid the adverse outcome of low-income property owners being forced to sell their long-term place of residence as they age. However, this could have a negative impact on government revenue in the short-term if too many households opt to delay paying the property tax.

On the concern that landlords could pass on the property tax through increased rents, it should be noted that property owners will pay the property tax rather than stamp duty, not both. Investors typically pay the cost of stamp duty over the course of their mortgage, as it is included in the principal amount of their home loan. Landlords already pass on that cost through higher rents. Removing stamp duty will reduce the initial cost of purchasing an investment property, and, in turn, investor mortgage repayments. It is unlikely that the proposed property tax will present a greater financial burden on investors compared to stamp duty. Thus, we suggest that there is a good argument that the overall cost of renting is unlikely to increase significantly.