CHARTERED ACCOUNTANTS™
AUSTRALIA + NEW ZEALAND

17 August 2021

The Hon. Dominic Perrottet MP
NSW Treasurer
Tax Reform Taskforce
NSW Treasury
52 Martin Place
Sydney NSW 2000

By email: TaxReformTaskforce@treasury.nsw.gov.au

Dear Treasurer

NSW Property Tax Proposal – June 2021 Progress Paper

Chartered Accountants Australia and New Zealand (CA ANZ) welcomes the opportunity to comment upon the Progress Paper for June 2021 regarding the New South Wales (NSW) property tax proposal.

The Progress Paper introduces a property tax surcharge and indexation of property tax rates. These changes increase complexity about determining future property tax liabilities which makes it difficult to advise property market participants. Lack of certainty about future property tax payments is likely to deter property market participants from opting in to the property tax regime and may extend the already long transitional period and affect the revenue cost of this proposal.

The Progress Paper also discusses exemptions, various types of property owners, concerns about impacts on rents and hardship provisions. This is welcomed. Yet key questions about likely property thresholds, the future of landholder duty, which intermediaries can advise, the revenue cost and distributional impact remain unanswered.

Forty-eight percent (48%) of CA ANZ members have not decided whether to support or oppose this proposal. Our members response indicates that a much high level of education and awareness is needed. Member feedback also indicates that much work remains to be done to provide greater detail about the impact of this proposal on both the NSW economy and individuals. Our members have also indicated that further questions about the operation of the proposal need to be addressed.

The details of the proposal's impact

The additional required detail ranges from major policy issues – such as what are the financial and distributional impacts and how will it affect the property market generally – to detailed issues such as how will this affect my property if I opt in.

The financial and distributional modelling of this proposal (including underlying assumptions) needs to be released so that citizens can have a better understanding of how this proposal affects future revenue, productivity and property prices. This modelling needs to be available on a variety of time lines such as:

- short term (0-4 years),
- medium term (5-10 years),

- 20 years (as that is when the tax reform taskforce expects that half of all properties will be in the property tax system)
- 40 years (which is the term of intergenerational report), and
- 50 years (as that is when the tax reform taskforce expects the debt to be repaid).

This type of analysis can assist in understanding the intergenerational impact of this proposal.

Real life examples of how the property tax operates is also required so that people can develop a better understanding of this proposal works. Rather than relying on assumptions about future factors which can be questioned, it would be useful to use historical data. For example, what would have been the property tax payments on a variety of real life properties if the proposed property tax had been applied during the past 10-20 years.

The examples need to include scenarios that encompass:

- land that has been rezoned,
- units and houses that have experienced sharp declines/inclines in value,
- units and houses that have maintained a steady value,
- units and houses in a variety of geographical areas and price points.

Questions posed by our members

Questions regarding the operation of the property tax include:

- Who can provide advice on the State taxes?
- What is the property threshold that prevents a property from opting in to property tax?
- How will the housing price index for the indexation rules be calculated?
- How will the property tax aggregation rules operate?
- What is the concessional rate of property tax for aged care facilities?
- How will the legislation be drafted? Will there be three sets of differing requirements?
- Will outstanding property tax be shown on a credit register or a claim against the property?
- Won't the stamp duty saving just result in increased prices being paid for property?
- Is this the best way to improve housing affordability?
- Why should unit owners contribute less towards funding State services?
- Are there issues around funding this proposal (especially given the large outlays currently being incurred due to COVID support)? Will future generations be left with a large debt?
- Is Gross State Product per capita an accurate reflection of income growth?
- Can capping of property tax be simpler?
- How do the proposed exemptions and reduced rates affect the financial modelling?

Given the number of outstanding policy and implementation gaps, this reform should not be rushed.

Appendix A provides greater detail the areas that need further clarification.

Should you have any queries in relation to this please contact Susan Franks on 0401 997 342 or susan.franks@charteredaccountantsanz.com.

Yours sincerely

Michael Croker
Tax Leader Australia

Appendix A

Who will provide advice?

It is highly likely that people who buy property will turn to accountants for advice as to whether they should opt in to the property tax and the implications of buying a property that is subject to property tax.

The first question that accountants need answered is: "Will accountants be able to provide advice on State taxes?" Currently an accountant's ability to provide advice on State taxes is a grey area.

Accountants that are registered tax agents can advise on Federal taxes, however that does not extend to State taxes and New South Wales legislation states that non-lawyers cannot engage in legal practice. Legal practice encompasses the provision of advice on the operation of state taxes. Legislative changes are required to clarify an accountant's ability to advise on State taxes.

Property tax favors unit owners

Assuming accountants will be able to advise clients about the State tax consequences of acquiring property, they will be asked by their clients to explain the effect of the proposed property tax.

Currently for owner occupiers the answer is that the client will pay a once off fixed amount of stamp duty on the market value of the property. It is easy to give client a market value price range and associated stamp duty cost so that they have a framework in which to make a purchase decision.

In contrast, property tax is an ongoing annual liability that is based on unimproved land value that will regularly change. The type of property bought will greatly influence the amount of property tax payable.

This is best illustrated by an example which uses real data for two properties which are located within a radius of 6-7 kilometres that sold within 7 days of each other for $1.7M. One is a unit and the other a house. The stamp duty payable in relation to each of these properties is $78,067. In contrast, the property tax associated with these properties is very different. The new 3-bedroom unit has an unimproved land value (UIV) of $105,924 and the older 5-bedroom house has a UIV of $720,000. The unit will have an annual property tax of $717 ($400 + [105,952 x 0.3%]) and the house will have an annual property tax of $2,560 ($400 + [720,000 x 0.3%]) – more than 3.5 times that of the unit.

This property tax outcome is a result of deliberate policy decisions to encourage capital investment in property[1]. The Progress Paper recognises in numerous places that the use of unimproved value (UIV) of land results in apartments being taxed more lightly than freestanding residences[2].

[1] Page 34 of the Progress Paper states "the rate structure thus strikes a balance with the **efficiency goal** of encouraging capital investment across all types of property."

[2] Page 43 of the Progress Paper "The reform was identified as being attractive for apartment developers and an important stimulus, as purchasers would be more likely to choose the property tax over stamp duty due to the lower land values per dwelling." Page 25 of the Progress Paper "Shifting from stamp duty to a tax on unimproved land values would mean that some of the tax burden shifts away from capital (the structure(s) on the land). Lower taxation of capital would encourage investment in better quality homes (e.g., more floorspace, more homes in the most favoured locations and better fixtures)."

Tax reform is usually evaluated from perspectives of efficiency, equity and administrative burden. If a purpose of property tax is to raise revenue in an equitable manner to allow the provision of services to households, then favouring the tax treatment of units over freestanding housing to this extent is questionable.

The revenue sustainability of this model is also questionable. It is noted that The Independent Pricing and Regulatory Tribunal of NSW recommended changing the base of local government rates away from unimproved land value due to concerns about the ability of local governments to fund and provide services due to unit owners contributing substantially less than freestanding owners yet requiring similar level of services from local government. The New South Wales Productivity Commission has also noted that the way rates are imposed and capped is a disincentive for councils agreeing to developments and has recommended that the rate peg be reformed to account for population growth. [3]

Explaining future property tax amounts is difficult

“Australian household debt is 119.5 per cent of GDP, double that of Japan and Europe, and 68 per cent higher than the USA. Overall indebtedness to banks is 137 per cent of GDP, compared with 51 per cent for the USA, 113 per cent for Japan and 89 per cent for the Euro Area.”[4]

In the Progress Paper it is recognised that many property market participants are concerned about how the strong performing property market will affect future property tax liabilities. Many are fearful that they will face higher property prices **and** higher property tax liabilities.

The proposed indexation of the property tax rates (both fixed and ad valorem and the premium threshold) along with a promise to legislate provisions to “restrain future governments from changing the tax rates or the indexation methodology”[5] is meant to reassure property participants about this concern.

Of concern, and surprise, to property participants will be the ability for the property tax rate to increase under the proposed indexation method. Most property participants expected an announcement about a cap on the amount of property tax increases not a formula that allows the tax rate to decrease and increase. The Progress Paper states that this is needed “to ensure that State revenue grows in line with the economy and incomes.”[6]

The proposed indexation method is complex. Each component of the property tax rate (fixed, ad valorem and the surcharge threshold) is altered by a different indexation method. Property market participants will need to consider the following issues all of which are difficult to predict and are largely outside the property owner’s control:

- Changes in the land value of the property they own
- Impact of possible rezoning on the land value of the property they own

[3] Recommendation 6.4 of https://www.productivity.nsw.gov.au/sites/default/files/2021-06/Productivity%20Commission%20White%20Paper%202021.pdf

[4] Page 77 of https://www.treasury.nsw.gov.au/sites/default/files/2021-05/2021_igr_ttrp_-_secular_stagnation_the_long-term_real_bond_rate_outlook_and_policy_issues_for_nsw_and_australia.pdf

[5] Page 28 of the Progress Paper.

[6] Page 28 of the Progress Paper.

- Changes in NSW's gross state product per capita,
- Changes in the land value index and
- How changes in GSP per capita and land value index interact with each component of tax rate.

In addition to this there is a need to predict a factor to bring future property tax liabilities back to today's dollars so that a comparison can be made to the known stamp duty liability to enable a decision regarding whether to opt in to property tax. All of this makes predicting future property taxes difficult. Many are likely to feel that this is all too hard and that the certainty of stamp duty is a safer option.

Specific concerns about the proposed indexation methods include:

- Whether growth in gross state product per capita is an appropriate proxy for income growth. This will be important given State and Federal budget predictions of low or negative wage growth[7].
- The use of GSP growth per capita rather than real GSP growth per capita as this will cause the fixed property tax amount to increase due to inflation[8] even though there is no corresponding increase in real income to support the payment of property tax. There can be significant differences between the gross and real GST per capita growth[9].
- Is growth in housing prices based on market value or unimproved value?
- Does rezoning and proximity to newly built infrastructure impact unimproved land value? Will there be mechanisms to smooth its impact?
- Is the growth rate of housing going to depend upon where the property is located? The NSW valuer general currently prepares the growth rates for unimproved land values on a local government area (council) basis given the information is used to calculate rates.
- If housing price growth is unimproved value, will it be the overall increase in unimproved values in NSW or one of four categories currently used by the NSW Valuer General? The overall increase can be very different to the increase per a category (see table below).
- The current NSW Valuer General categories do not match the proposed classification of properties for property tax purposes. Property tax has a commercial category but the NSW Valuer General divides that category into commercial and industrial. The growth rates between commercial and industrial can be very different (see table below that has been constructed from Valuer General reports). Which one will be used for property tax?

---

[7] "Next financial year the cost of living – measured by CPI – is expected to rise faster than wages. For the two years beyond that – real wage growth is forecast to be flat." NSW Treasurer speech, 31 May 2021 at the launch of NSW Productivity Commission White Paper – Rebooting the economy.

[8] This may not affect the ad valorem tax rate as both the numerator and denominator are likely to contain inflation in their growth rates – thus the impact of inflation may be cancelled out (but not completely if inflation is different for housing as opposed to general inflation).

[9] ABS figures for 2015-16 show that GSP growth per capita was 2% but real GSP growth per capita was 1.4% and for 2019/20 were -1.8% and -2.6% respectively.

Year and source	NSW	Residential	Commercial	Industrial	Rural
2020	3.6%	4.0%	-6.6%	5.5%	4.8%
2019	-5.4%	-7.5%	2.0%	7.3%	5.2%
2018	5.9%	4.4%	13.9%	17.5%	14.3%
2017	15.3%	14.1%	12.02%	11.9%	16.52%
2016	11.3%	11.1%	13.6%	10.4%	12.1%
Average	6.1%	5.2%	6.9%	10.5%	10.6%

A simpler method is needed to reassure property market participants that property tax increases will be capped. If a simpler method is not chosen, then many in the community will prefer the certainty of paying a fixed up-front amount of stamp duty rather than risk the uncertainties of a property tax that is reliant on land valuations and indexation of tax rates that are largely out of their control.

Property tax surcharge aggregation provisions need revision

A property tax surcharge was not included in the original consultation. The Progress Paper states "*the property tax surcharge on large landholdings balances investor tax rates in favour of smaller investors. This reflects the greater benefit that large landholders can receive from opting out of land tax*."[10]

The Progress Paper states a **0.3%** property tax surcharge will apply to aggregate landholdings above $1.5 million of unimproved land. This surcharge will not apply to a principal place of residence and farmland. It will apply to residential investors and to commercial properties.

The rules regarding when properties will be aggregated to determine whether the property surcharge threshold has been met will be important. No information has been released as to how this will be achieved.

The current land tax aggregation rules are a hybrid between legal and beneficial ownership. As such, they allow tax planning to occur to avoid the premium land tax rate. If the current land tax aggregation rules are adopted for property tax purposes, then there will be a continuation of such tax planning strategies. Having aggregation rules that are different between property tax and land tax will unnecessarily increase complexity.

***CA ANZ recommends that there be a review of the existing land tax aggregation rules and that there be one set of aggregation rules for both land tax and property tax*.**

Exemptions

CA ANZ's submission to the consultation paper highlighted the uncertainty regarding:

[10] Page 24 of the Progress Paper.

- how existing exemptions in the stamp duty and land tax regimes would be treated, and
- whether the proposed property tax regime would replicate some of these exemptions.

The Progress Paper addresses these concerns and proposes[11] that:

- Existing stamp duty and land tax exemptions will continue to apply for properties that are not subject to the property tax regime. CA ANZ welcomes this announcement.
- If a property owner is exempt from stamp duty and land tax, then that property owner would be exempt from property tax.

  It is expected that the beneficiaries of this proposal will largely be charities. It is questionable whether open ended long-term exemptions are in the community's interest in times of escalating home prices and limited social housing stock. The continuing exemption that not for profits obtain for land used for *commercial* operations should also be examined on competition grounds alone.
- If a property owner would be exempt from stamp duty but not land tax, then property tax would be payable. This is an appropriate outcome.

- If a property owner would be subject to stamp duty but not land tax, then a concessional rate of property tax will be payable.

  Operators of retirement villages, aged care establishments and nursing homes would fall within this category. The NSW tax expenditure statement indicates that the current land tax exemption for retirement villages is estimated to be around $194 million per annum[12]. With an aging population it is expected that this number will grow.

  CA ANZ advocated in its previous submission for a concessional rate of property tax for this group and supports this position. ***CA ANZ calls upon the NSW tax reform taskforce to reveal what the concessional rate of property tax will be.***

Consideration will also have to be given as to how this system of property tax exemption/concessional rates is worded. Having to deal with three pieces of legislation, two of which are intended to become antiquated, will become burdensome.

Farming land

Land used for primary production that is exempt from land tax is estimated to cost the NSW government around $770 million a year[13]. The Progress Paper suggests that it is considering exempting all farm land

[11] Page 39 of the Progress Paper.
[12] Page 2-12 of https://www.budget.nsw.gov.au/sites/default/files/2020-11/Appendices%20A2-BP1%20Budget%202020-21.docx
[13] Page 2-12 of https://www.budget.nsw.gov.au/sites/default/files/2020-11/Appendices%20A2-BP1%20Budget%202020-21.docx

from property tax[14]. Presumably this is instead of farm land having the lowest property tax rate of 0.3% with no fixed component which is the current proposal.

Farmland is usually sold for farming or development. Farming is usually a long-term proposition, and as noted in the Progress Paper will generally result in the payment of stamp duty in preference to a property tax (it is noted that it is unlikely that land that is not already farm land would be acquired for farming purposes). Farmland sold for development and is land banked, may be able to qualify for the lower farm land rate or exemption due to the use of agistment. Care will need to be taken to ensure that the tax system does not reward land banking.

Foreign investors

Currently foreign investors are required to pay an 8% stamp duty surcharge and a 2% land tax surcharge on all residential property in NSW. The Progress Paper states that there will be no change to this and that these amounts will still be payable even if a property that is acquired is subject to property tax. Foreign investors would not be able to opt in a residential property.[15]

It appears that foreign investors may need to calculate the tax payable in relation to a property acquisition under three different tax regimes – stamp duty for the stamp duty surcharge, land tax for the land tax surcharge and potential property tax – each of which have different rates and thresholds.

CA ANZ strongly supports the policy behind the imposition of foreign investor surcharges. However, a simpler administrative answer is required.

Commercial tenants

Commercial tenants and property owners were both concerned about absorbing the cost of a property tax. The Progress Paper proposes that where a landlord has opted into property tax for a property which has an existing commercial tenancy agreement that permits the pass through of state taxes, then the amount of any property tax that can be passed through be limited to the amount of land tax that would have been payable if the property had not been opted into the property tax.[16]

However, this can be overridden by a written agreement between the landlord and tenant. This then raises questions about the relative bargaining power of the landlord and the tenant. Many small businesses may not find the ability to override this limit by written agreement comforting. Greater communication about existing protections for small businesses may be required.

Paying property tax

Discussion of *when* the property tax will be become due and payable has not occurred. The ACT government, which is now approaching the half way point through a 20 year transition from stamp duty to property tax (known as rates) has implemented an approach to prevent large tax debts arising by allowing people to automate payments of rates with their pay cycle – refer here. Consideration should be given to adopting a similar approach in NSW to help people from accumulating property tax debt.

---

[14] Page 40 of the Consultation Paper

[15] Page 41 of the Progress Paper.

[16] Page 48 of the Progress Paper.

Many people will have difficulty paying an annual property tax due to a lack of recurrent income. This can encompass temporary events such as unemployment which require time to pay arrangements, or permanent events such as retirement which require hardship provisions.

The Progress Paper only mentions that time to pay arrangements will be available[17]. Much greater detail about how they will operate is needed, such as how to apply, what interest rate will apply, and whether this debt will be visible to external creditors.

The Progress Paper does discuss proposed hardship provisions and a proposal to legislate to ensure that no-one would be required to sell their home or small business premises (including primary production land) because they cannot afford the proposed property tax."[18]

There is no indication of how small business will be defined. The are a large range of definitions of small business at both a State and Federal level. To reduce red tape and confusion, a widely used tax definition of small business should be used and any thresholds used in the definition (such as turnover) indexed.

It is unknown whether financiers and people who trade with small businesses, will be able to determine if and how much property tax is outstanding on a property that is owned by the person applying for finance or wanting to receive trade credit. This issue needs resolution.

The Progress Paper proposes to charge a **discount** owner-occupier variable mortgage rate to amounts that are deferred. Using an owners-occupier variable mortgage rate appears appropriate for residential owner occupiers but it is unclear why a **discount** owner occupier variable mortgage rate should be used.

The existing Hardship Review Board appears to be the mechanism through which people who are deemed not eligible for the hardship Scheme of where the Hardship scheme has not provided a sufficient outcome can appeal.[19] As it is currently constituted, the Hardship Review Board can only deal with individuals in genuine hardship.[20] It is unclear how small businesses and farming operations that are conducted through a company and/or trust will be able to access the Hardship Review Board to appeal decisions.

It appears that the scope of the Hardship Review Board would need to be expanded to ensure it can deal with a deferral of tax until a property is sold.

Retrospective operation

CA ANZ supports the proposal to allow people to retrospectively opt into the property tax regime. This initiative is essential to reduce the expected instability of the property market as this reform is implemented. It may not however completely eradicate the instability as there will remain some

---

[17] Revenue NSW already has a payment plan policy which can be accessed here. If payment can be made within 3 months, then a minimum of $40 needs to be paid fortnightly by direct debit and a $65 penalty will apply if a payment is missed and the full amount will be become immediately payable. If more than 3 months is needed, then a payment plan is negotiated – the terms of this payment plan is not easily visible. Greater clarity on how these existing provisions operate will be needed if they are to be extended to include property tax.

[18] Page 51 of the Progress Paper.

[19] Page 51 of the Progress Paper.

[20] https://hrb.revenue.nsw.gov.au/what-we-do

uncertainty about the operation of the property tax until it is passed by Parliament – this is recognised in the Progress Paper[21].

It is proposed that people who purchase property between the date of announcement and the commencement of the legislation will have to pay stamp duty but would have six months from the date of commencement to retrospectively opt in to pay property tax. People who do this would then receive a refund of their stamp duty.

Understanding tax legislation and, in this case, making a comparison between three different state taxes is not easy. The implementation stage is likely to involve a relatively small number of advisers working intensely. ***A six-month period to make a retrospective application may need to be extended to at least a year to ensure that adequate resources are available to help people who have purchased property.***

Financial viability of the reform

The Progress Paper is sending mixed messages about the cost of this reform.

On one hand it is saying that large amounts of revenue will be lost for about twenty years[22] but there is no requirement to change the Government's spending and revenue plans[23]. On the other hand, it is also saying that unless the NSW Government receives at least $1 billion more of GST per year the Government's capacity to proceed with this reform will be materially affected[24].

Concerns about the revenue impact have prompted NSW to:

- Propose "that the Commonwealth establish a Productivity Fund, which would reward states that engage in reforms that boost productivity."[25] and
- Engage "through the Council on Federal Financial Relations on measures to ensure that the State is not penalised through the Commonwealth Grant Commission's system of allocating GST revenue."[26]

It is noted that a technical paper for the NSW Intergenerational report warns that "Governments will need to be careful not to give too much weight to current distorted low interest rates… because real rates will

[21] Page 53 of the Progress Paper.
[22] The consultation paper indicated that this proposal will cost at least $2 billion per annum over the next four years. The $11 billion injection of funds into the NSW economy over the next four years is through a reduction in receipt of tax revenue from active property market participants. Given the impact of COVID on the economy and State funds, a question that needs to be considered is whether transferring $11 billion of government revenue to active market participants who are likely to be short term property market players is the best use of government revenue.
[23] Page 53 of the Progress Paper.
[24] Page 53 of the Progress Paper.
[25] Page 53 of the Progress Paper.
[26] Page 53 of the Progress Paper.

rise over time"[27] and that "the gap between potential growth and the real interest rate is very beneficial for containing debt until around 2040."

2040 coincides with the Progress Paper's estimate of when the large revenue shortfall will diminish and presumably the debt associated with this large revenue shortfall will be at its maximum. Details of the financial modelling need to be revealed so that consideration can be given to the intergenerational impact of this reform.

Housing affordability

Much of the commentary regarding this proposed transition has been around improving housing affordability. The Progress Paper states: "While the reduction in home prices would take time to realise, and the actual magnitude would depend on the final policy choices of the government, a reduction in home prices in the order **of 3-4 per cent** could reasonably be expected"[28]

The NSW Innovation and Productivity Council (the Council) reports that productivity has increased with remote working and that post COVID remote working will remain substantially above pre-pandemic levels with the vast majority of workers wanting to work at least 2-3 days a week remotely. A technical research paper for the 2021 NSW Intergenerational Report found that if all employees worked from home one day a week on average (or alternatively half the workforce working from home two days a week) then "the average household in NSW incurs less transport costs (-5 per cent), lives in larger dwellings (+10 per cent) and ***faces lower average housing (-11 per cent) and land costs (-29 per cent)*** than the baseline scenario"[29] And that there would be an improvement in the total State welfare[30].

If housing affordability is the main aim of this reform, then questions need to be asked about whether it is the most cost effective method of achieving it as the technical research paper implies that housing affordability can be greatly increased at a much small cost to the government by encouraging remote working.

[27] Page 72 of https://www.treasury.nsw.gov.au/sites/default/files/2021-05/2021_igr_ttrp_-_secular_stagnation_the_long-term_real_bond_rate_outlook_and_policy_issues_for_nsw_and_australia.pdf

[28] Page 25 of the Progress Paper.

[29] Page 8 of https://www.treasury.nsw.gov.au/sites/default/files/2021-01/2021_igr_ttrp_-_sensitivity_analysis_on_sydneys_urban_structure_and_house_prices_for_the_2021_nsw_intergenerational_report.pdf

[30] Page 13 of https://www.treasury.nsw.gov.au/sites/default/files/2021-01/2021_igr_ttrp_-_sensitivity_analysis_on_sydneys_urban_structure_and_house_prices_for_the_2021_nsw_intergenerational_report.pdf