Urban Taskforce
AUSTRALIA

17 October 2008

AFTS Secretariat
The Treasury
Langton Crescent
PARKES ACT 2600

By e-mail: AFTSubmissions@treasury.gov.au

Dear Sir/Madam

Re: Australia's future tax system

The Urban Taskforce represents Australia's most prominent property developers and equity financiers. We provide a forum for people involved in the development and planning of the urban environment to engage in constructive dialogue with both government and the community.

We appreciate the opportunity to the Federal Government's review of Australia's tax system.

1. The margin scheme

In general terms, the margin scheme is intended to ensure that GST is only levied on the value of land after 1 July 2000. Under the existing margin scheme, GST is calculated on the margin rather than the sale price itself. Normally the margin is the difference between the purchase price paid by the seller and the price paid by the buyer.

In the May 2008 Federal Budget significant changes were announced to the margin scheme provisions in the GST Act. The changes are contained in the *Tax Laws Amendment (2008 Measures No. 5) Bill 2008* which is currently before Parliament. The changes affect the application of the margin scheme where the land being sold was acquired through a GST-free or non-taxable supply. For example, if the land was acquired through the purchase of an operating farm or business.

The Federal Government is apparently concerned that where the margin scheme is applied to land that was purchased through a GST-free or non-taxable supply, the GST calculated under the margin scheme may not capture the increase in the value of the land after 1 July 2000.

To address this concern, the government says the "value added by the registered entity which sold the land" will be factored into the GST subsequently payable under the margin scheme. The amendments will also apply where the margin scheme is applied to the sale of strata titled units built on land acquired through a GST-free or non-taxable supply.

This legislative amendment applies where the land is acquired through any GST-free or non-taxable supply. For example, the new provisions may also apply to unimproved land that is acquired from the Commonwealth or a State through a GST-free supply under section 38-445 of the GST Act.

The result of the changes is an increase in the GST payable on land (or strata titled units) sold under the margin scheme, where the land was acquired through a GST-free or non-taxable supply. This may significantly reduce the benefit of applying the margin scheme.

The changes to the way the margin scheme operates will impact heavily on developers buying land under a GST-free or non-taxable supply. The changes will make these developments more expensive.

This effectively increases the GST for some types of property development at a time that the Federal Government is attempting to boost the activity in this sector. More of the 'product' produced by property developers (improved land) will now be subject to a double taxation scheme. That's because a wider class of improved land will now be subject to both GST and state stamp duty.

Property developers are taxed several times over – like everyone else they pay income tax – and then they also pay stamp duty and GST on the increase in property value that comes from development. That's on top of the numerous state and local infrastructure charges that, in themselves, can add up to $90,000 for every new home.

While other products may have multiple taxes imposed on their production (liquor and tobacco for example) these products are generally perceived as socially harmful. Property development does not fall into the category. In fact, property development is beneficial to the community in both social and economic terms. So much so, that the government has endeavoured to stimulate this sector in its economic revitalisation package released earlier this month.

We submit that either the state stamp duty burden on property development should be done away with, or the margin scheme should be broadened to ensure that the improvement in land values brought about by property development is not taxed twice.

2. State stamp duties

The NSW Government's independent review of state taxation conducted by the Independent Pricing and Regulatory Tribunal had much to say on the subject of stamp duty. We believe the national review of tax arrangements should take note of the findings of the tribunal in this respect, particularly as they have implications beyond just NSW.

The tribunal found that stamp duty on property was "inequitable" and "the worst" of the major state taxes. In fact, the Tribunal said the tax ranked the lowest (least desirable), of all the eight taxes considered.

The Tribunal revealed that bracket creep had, in NSW, increased the burden of stamp duty rates on the sale of a median priced home by 90 per cent in the last 20 years. In 1987 stamp duty accounted for just 1.9 per cent of the median house price, by 2007 the bracket creep forced this tax rate up to 3.6 per cent of the median house price. Stamp duty rates for the typical home have almost doubled in the last 20 years. This has made new housing more expensive than it needs to be."

The Tribunal said that stamp duty on property purchases scores poorly for efficiency because it distorts investment decisions. The Tribunal also found that the tax discourages property development for resale, because it was levied on the improved value of the property.

The Tribunal's report says stamp duty on property purchases may prevent businesses from adjusting to changed market conditions – with a particular impact on new or growing businesses and on the development of new commercial property. The report found that the tax was inequitable - with less affluent taxpayers who move house paying more tax than affluent landowners who do not move as often.

The Tribunal recommended that the NSW Government moves in the "short term" to reduce its reliance on stamp duty on property purchases and make it more equitable by adjusting the tax rates to account for bracket creep.

This represents a long overdue acknowledgement that stamp duties on property purchases are harming the economy. However, the government should not try to fund stamp duty reductions with increases in other State taxes – such as land tax.

The best solution would be to get a better allocation of tax revenue between the Federal and State governments. The Federal Government raises more than 80 per cent of the total tax revenue collected in Australia – which is significantly more than it needs to meet its spending responsibilities. Some of this cash should be used to reduce the states' reliance on property duties.

Thank you for considering our submission. We are happy to provide further information should you require it.

Yours sincerely
Urban Taskforce Australia

Aaron Gadiel
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