IPTI Xtracts
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NSW Build-to-Rent – Treasurer's Guidelines and Planning Law Details Released

Overview

In late July 2020 the New South Wales Government announced it would provide duty and land tax incentives for qualifying "build-to-rent projects". Qualifying projects must meet conditions set out in the Treasurer's Guidelines. Those Guidelines were first published on 12 February 2021.
The incentives include:

- a 50% reduction in the taxable value of the land (reducing the land tax otherwise payable at general rates)
- an exemption from "surcharge land tax" (the foreign investor land tax surcharge on residential property)
- an exemption from "surcharge purchaser duty" (the foreign investor duty surcharge on residential property).

The concessions are offered for a maximum period of 20 years, expiring in 2040. The Chief Commissioner of State Revenue can later claw back the concessions if key conditions are not satisfied for a period of 15 years – see below for further details.

Land Tax Reduction – Eligibility Requirements

The value of the land on which a build-to-rent property has been constructed will be discounted by 50% if:

- a building is situated on the land;
- construction commenced on or after 1 July 2020; and
- the Chief Commissioner is satisfied the building will be used and occupied as a "build-to-rent property" in accordance with the Treasurer's Guidelines.

It will be necessary for the land owner to apply to the Chief Commissioner for the reduction. If the relevant land will only be used and occupied partly for a build-to-rent property, the concession may be available on a pro rata basis – see further below for details.

The Treasurer's Guidelines

The Treasurer's Guidelines set out when a property is being used and occupied for a "build-to-rent property". The following is a summary of the Guidelines.

1. *There must be a "building" on the property*

- This can include a group of building or parts of buildings on the same parcel of land.

Note that the build-to-rent property cannot be subdivided for a period of 15 years.

2. *Planning Requirements*

- All relevant development consent requirements must be complied with as well as any relevant affordable housing policies under the *Environmental Planning and Assessment Act 1979 (NSW)* (Act).
- The new *State Environmental Planning Policy Amendment (Build-to-rent Housing) 2021* was made and came into force under the Act on 12 February 2021. This operates to:

1. Make certain build-to-rent housing 'State significant development' for which the consent authority is a delegate of the Minister for Planning and Public Spaces. This includes build-to-rent housing outside of the City of Sydney where:
   a) the capital investment value is more than AU$100 million for projects in the Greater Sydney Region or more than AU$50 million for all other projects;
   b) the tenanted component is at least 60% of the capital investment value; and
   c) the development is not prohibited under any other environmental planning.
2. Amend *State Environmental Planning Policy (Affordable Rental Housing) 2009* to include a number of specific provisions for build-to-rent housing. These include:
   a) Making build-to-rent property development permitted with development consent on any land on which residential flat buildings are permissible as well as on land zoned B3 Commercial Core, zone B4 Mixed Use and zone B8 Metropolitan Centre;
   b) Restricting the application of the build-to-rent provisions to properties containing at least 50 dwellings for residential lease on the same lot of land;
   c) Restricting the subdivision of build-to-rent properties for a period of 15 years from the date an occupation certificate is issued (other than in zone B3 where the subdivision prohibition continues in perpetuity);
   d) Specifying a number of non-discretionary building standards for build-to-rent housing, including for building height, floor space ratio and parking;
   e) Allowing for the flexible application of the design criteria in the Apartment Design Guide under *State Environmental Planning Policy No 65—Design Quality of Residential Apartment Development,* such as requiring the consent authority to give consideration to the amenities proposed to be provided to tenants though common spaces and shared facilities; and
   f) Requiring that the ground floor of build-to-rent developments located in business zones contain active uses that encourage interaction between the inside of the building and adjoining external public areas (and not residential accommodation or car parking).

3. *Building Requirements*

- The buildings on a parcel of land must contain at least 50 self-contained dwellings used specifically for the purpose of build-to-rent.

- The property must comply with affordable housing policies that may be imposed under the *Environmental Planning and Assessment Act 1979*, including any state environmental planning policies made from time-to-time to promote the development of affordable or social housing.
- The build-to-rent dwellings must be available to the general public without restriction (other than those required for public health and safety, or to promote announced Government policy, or to ensure designated affordable and social housing is used for that purpose).

Note that it is permissible for the build-to-rent dwellings to be spread across multiple buildings on the same parcel of land. Further, if an adjacent land parcel is consolidated with a land parcel that already qualifies as a build-to-rent property, it is not necessary for any additional build-to-rent dwellings on the adjacent land parcel to also meet the 50 dwelling threshold to qualify for the concessions.

4. *Ownership Structure*

- The dwellings and common land comprising the build-to-rent property must be held within a unified ownership structure, which can include a group of entities holding joint ownership. However, it is not permissible for the structure to provide a de facto subdivision or divided ownership of the build-to-rent property.

5. *Management Structure*

- The build-to-rent property must be managed by a single management entity, with on-site access to management for tenants.
- The management function can be outsourced to a third party – it does not need to be undertaken by the landowner.

It is important to note there is an exemption from the above management requirements for specific build-to-rent dwellings that are made available for use as affordable or social housing for a continuous period of 15 years.

6. *Lease Conditions*

- Each tenancy with a build-to-rent dwelling must be subject to a Residential Tenancy Agreement under the *Residential Tenancies Act 2010*. The landlord must comply with all requirements of that Act.
- Tenants must be offered a range of lease terms, including a genuine option to enter a lease for a fixed term of at least three years. However, a landlord will not be in breach of this requirement if a tenant who is made the offer of a fixed three year term opts for a shorter period instead.

7. *Other Factors*

As a "catch-all", the Chief Commissioner may have regard to any other factors that he or she considers relevant in determining whether a property is being used for build-to-rent. It is expected that Revenue NSW will release public guidance on how it will administer these concessions.

Proportionate Reductions in Land Value

If the whole of a parcel of land is used for build-to-rent purposes, the land tax concession should not be reduced. This is notwithstanding the parcel may not be wholly used for build-to-rent dwellings. The Treasurer's Guidelines include examples of where this may be the case, including where part of the property is reasonably used for on-site management accommodation and facilities necessary to operate the build-to-rent business.

However, if a part of a parcel of land is not used for build-to-rent purposes, the value of land tax concession will be reduced. This will be relevant if part of the parcel will be used for retail or other purposes. The reduction may be calculated on a basis the Chief Commissioner considers appropriate. The Guidelines suggest that floor space and area may provide a reasonable basis of apportionment.

Surcharge Land Tax Exemption – Eligibility Requirements

The eligibility requirements for the land tax reduction outlined above act as a "gateway" for the surcharge land tax exemption. The owner must first be entitled to a land value reduction under those provisions before the surcharge land tax exemption can apply.

The exemption applies to land owned as at midnight on 31 December in a year (the "taxing date"), starting with land owned as at midnight on 31 December 2020.

The additional eligibility requirements for the surcharge land tax exemption are that:

- the owner of the land must be an "Australian corporation"; and
- there must be a building that is a build-to-rent property on the land; and
- that building must have been constructed by the owner or a related body corporate.

Note that the building can be constructed either before or after the taxing date (meaning a refund may become retrospectively available).

The exemption will apply for a maximum period of 20 years. It will not apply to land owned as at midnight on 31 December 2040.

Surcharge Land Tax – Exempt Person

The Chief Commissioner may approve a "foreign person" as an "exempt person" for particular land if the Chief Commissioner is satisfied that person is likely to be entitled to a surcharge land tax refund. This allows the exempt person to claim the exemption without having to first pay the surcharge land tax and then seek a refund.

The approval may be subject to conditions.

Surcharge Purchaser Duty – Eligibility Requirements

Once again, the eligibility requirements for the land tax reduction outlined above act as a gateway to the surcharge purchaser duty exemption. The transferee must be eligible for a land value reduction under those provisions before a surcharge purchaser duty exemption can apply.

The additional eligibility requirements are that:

- the owner of the land must be an "Australian corporation"
- the transfer must have been entered into on or after 1 July 2020 (but a transfer made after that date, in conformity with an agreement for sale or transfer entered prior to that date, will qualify).

Surcharge Purchaser Duty – Refunds

If surcharge purchaser duty has already been paid, and the eligibility requirements are satisfied, the owner will be entitled to a refund.

This refund must be applied for:

- within 12 months of the Australian corporation first becoming entitled to a land tax reduction; and
- no later than 10 years after completion of the transfer to the Australian corporation.

The refund may be for the full surcharge purchaser duty amount paid or a lower amount as set out in an order made by the Treasurer.

Surcharge Purchaser Duty – Exempt Transferee

The Chief Commissioner may approve a person as an "exempt transferee" for a particular transfer (or class of transfers) if the Chief Commissioner is satisfied that person is likely to be entitled to a full surcharge purchaser duty refund. An exempt transferee does not need to pay the surcharge purchaser duty and then seek a refund.
The approval may be subject to conditions.

The Claw Backs
As noted at the outset, all of the above exemptions and concessions may potentially be cancelled and clawed back if, within a period of 15 years after the land tax reduction first becomes available, the land is subdivided or the ownership of the land is otherwise divided.
Further, there may be claw backs if approvals were provided on a conditional basis, or undertakings were provided, and those conditions have not been satisfied or the undertakings were breached.
In addition to any tax or duty that may be payable as a result of a claw back, penalties and interest may apply.

What About Land Acquired and Owned by Foreign Trusts?
As explained above, the surcharge land tax and surcharge purchaser duty exemptions require the land to be acquired and owned by an "Australian corporation".
We expect that this requirement can be satisfied where the Australian corporation acquires and holds the land as trustee, but this will need to be confirmed with Revenue NSW.
A similar issue may also arise where the land is held by an Australian corporation as bare trustee (nominee / custodian) for a foreign person. This is a common structure for REITs.
In relation to the surcharge land tax exemption, we note there is the additional requirement that the building be constructed by the Australian company or a related body corporate. This may suggest that the exemption won't be available where land is held by a bare trustee that does not itself (or via a related company) undertake the construction.

To provide certainty, it will be important for Revenue NSW to publicly set out its views on these issues.

Will Landholder Duty and Surcharge Duty Apply?
Surcharge duty may also be payable in addition to landholder duty if a "relevant acquisition" is made in a private landholder that has a residential land holding in New South Wales.
The surcharge purchaser duty exemption is limited to transfers of residential-related property. It does not appear to extend to surcharge duty on a relevant acquisition in a private landholder.
This may be relevant if the investors in an Australian company that owns a qualifying build-to-rent property exit the project by selling their interests in the company. The incoming investors may potentially be liable for both landholder duty and surcharge duty.

K&L Gates' Comments
The release of the Treasurer's Guidelines is welcome. It provides a degree of certainty to those developers and institutional investors who are considering undertaking a new build-to-rent project in New South Wales.

However, the Guidelines do significantly narrow the categories of build-to-rent projects that will qualify for the concessions. Specifically, the requirement for tenants to be offered a Residential Tenancy Agreement likely means that the concessions will not be available for "commercial residential premises" (such as serviced apartments, boarding houses and co-living developments) where residents are more likely to have a licence to occupy their accommodation in form of a rooming agreement.

Similarly, the fact that the dwellings must be offered to the general public (except in limited circumstances, such as for affordable and social housing) likely means that a qualifying build-to-rent project cannot be exclusively targeted at specific classes of residents (such as retirees or students). While these incentives will assist qualifying projects, institutional investors will also need to take into account other tax obstacles for build-to-rent projects, including GST. For foreign investors, the lack of Managed Investment Trust concessions for residential rent may also be a factor.

Given the strict requirements, qualifying projects will need to be approached holistically having regard to the ownership structure, management structure, lease tenure and resident profile, financing requirements, planning requirements and construction issues. For foreign investors, there will be additional considerations in respect of FIRB and cross-border tax.

It is worth noting that the New South Wales Government is separately considering abolishing stamp duty and land tax in favour of a new annual property tax. However, those reforms (if implemented) are unlikely to apply to high value residential development sites for a number of years (to protect Government revenues during the transition period). Accordingly, the build-to-rent incentives set out above are likely to be the only state tax concessions that are available in New South Wales for build-to-rent projects over the next few years (and possibly longer).

On the cusp of a boom': Double-digit house price rise tipped as banks continue rate cuts

Economists for the nation's biggest mortgage lender believe a new housing boom will push home prices in Sydney and Melbourne up by at least 12 per cent over the next two years as banks drive lending rates below 2 per cent.

But tumbling interest rates could leave the Reserve Bank with few options to deal with any future economic downturn, with warnings it may have to print money to finance government spending programs.

At the start of the coronavirus pandemic, economists and housing analysts feared a collapse in home prices that would feed into a downward economic cycle of wealth destruction and subdued consumer spending.

Instead, on the back of record low interest rates and large government support programs including the JobKeeper wage subsidy and the COVID supplement for welfare recipients, prices in all capital cities bar Melbourne have risen over the past 12 months. Regional areas have seen even larger increases.

Commonwealth Bank predicted on Monday prices would continue to lift. It believes Sydney's prices will climb 7.5 per cent this year and 5.8 per cent in 2022 and is tipping Melbourne prices to increase 7 per cent in 2021 and another 5 per cent the following year.

That would take Sydney's median house price towards $1.2 million and Melbourne's beyond $920,000.

Dwelling prices are tipped to climb by 16.6 per cent in Brisbane over the next two years, 17.7 per cent in Perth and 15.5 per cent in Canberra.

CBA’s head of Australian economics, Gareth Aird, said with interest rates below the return on rental properties, the fundamentals for house prices were strong.

“The Australian housing market is on the cusp of a boom. The boom is being driven by record low mortgage rates coupled with a V-shaped recovery in the labour market,” he said.

Lenders continue to cut their fixed mortgage rates, with ANZ on Monday slicing another 0.05 percentage points from many of its products. It is now offering 2.04 per cent on its one-, two- and three-year fixed-rate mortgages on loans with a loan-to-value ratio of up to 80 per cent, the lowest of any of the major banks.

The Reserve Bank of Australia have kept interest rates on hold at an historic low of 0.1 per cent.

Canstar group executive for financial services Steve Mickenbecker said there were now 120 fixed rates below 2 per cent on the Australian mortgage market. The average variable rate is 3.29 per cent.

“Average is no longer good enough when the savings are so huge,” he said.

The RBA has signalled it could keep official interest rates, cut last year to 0.1 per cent as part of its quantitative easing program, at record low levels until at least 2023.

Mr Aird said low interest rates were likely to be the norm, but that could cause problems whenever Australia faced even a slight economic downturn.

Ordinarily, the RBA would cut interest rates to stimulate demand, but with rates already at extremely low levels it might be forced to print money to hand directly to the federal government to spend.

He said Australia was inching towards this “new paradigm”.

“It may still be a long time away, but the bottom line is that the system as we know it will need to be reset and the printing press will be part of that reset,” he said.

Coolabah Capital Investments chief macro strategist Kieran Davies said the RBA might have to continue its quantitative easing program simply because countries around the world were printing money to stimulate their economies.

He said other central banks had engaged in even larger spending programs that in turn put downward pressure on their currencies.

If those central banks continued to buy government debt, the RBA might have no option but to continue its own program of debt purchases to keep the Australian dollar lower than it would otherwise be.

“The actions of other central banks clearly have an impact on the RBA’s policy decisions,” he said.

Stamp duty vs. land tax: which one would cost you more?

The NSW government's plan to abolish stamp duty in favour of a broad-based land tax is a bid to remove one of the major hurdles people face if they want to move homes.

Under the proposed changes, announced as a part of the state budget, home buyers would be given the option of paying an upfront stamp duty on purchase or paying an ongoing land tax.

But even though stamp duty has been in place in some form since 1865, it is still believed to be a highly inefficient form of tax that discourages many people from moving.

An example would be downsizers, who are now at retirement age and living in a large family home and would like to move to a smaller, more manageable property. They are often hamstrung because of the large transaction costs.

With a median house price of more than $1 million in Sydney, stamp duty is around $40,000 on a $1 million purchase.

At this stage, the government proposes that owner-occupiers, investors, and owners of commercial properties would face different levels of land tax, which poses an interesting question for property investors and what it might mean for house prices.

Investors could lose out

Looking at the numbers, on the surface, it appears that investors who buy large family homes could be losers under a land tax.

Based on the initial figures outlined by the government late last year, they would be forced to pay $1500 plus 1% of the land value each year. And based on this information, for metropolitan NSW the average residential land value is around $630,400 and the corresponding owner-occupied property tax would be $2391.

By contrast, an investor would pay $7804 a year for that same property.

Given the high prices and the already low yields in Sydney, it makes the prospect of owning property as an investor far less appealing over the long term.

Typically, if investors are priced out of houses, they look to units, but under the proposed changes there could be little difference.

For apartments, it looks as if the net result might be about the same or slightly better, given the smaller land component.

It seems the government will allow people to opt in if they buy between now and when new changes come through. However, on the surface, it looks as if investors will pay more in the future and once a property has opted into the new scheme it will remain that way going forward.

What you might pay in NSW

PROPERTY TYPE	CURRENTLY LIABLE TO STAMP DUTY?	CURRENTLY LIABLE TO LAND TAX?	POTENTIAL PROPERTY TAX RATE
Commercial property	Yes	Yes	$0 + 2.6% of unimproved land value
Investment residential property	Yes	Yes	$1500 + 1% of unimproved land value
Owner-occupied residential property	Yes	No	$500 + 0.3% of unimproved land value
Primary production land (farmland)	Yes	No	$0 + 0.3% of unimproved land value

Owner-occupiers hit too

Similarly, for owner-occupiers who are looking at a home for the long term, it appears that a land tax would be detrimental compared with paying stamp duty upfront.

House price values may also be impacted if people hold off buying a property in the hope of qualifying for any changes should they come about.

We do, however, expect the government to backdate any changes or offer rebates, so this strategy is not advised.

A number of economists have also predicted that in the short term prices might rise as the money saved on stamp duty could go towards the purchase and drive up demand.

With a longer-term view in mind, however, the belief is that a land tax makes property more efficient, so there could be an increased supply of larger homes. Generally a sought-after commodity, they could fall in value and become more affordable.

The government is taking a voluntary approach to rolling out the scheme, giving homeowners the opportunity to choose between the upfront stamp duty or the land tax.

The opt-in capability of the scheme is appealing, but it is important to remember once a buyer has opted in, future buyers of that property won't be able to opt-out and they will pay land tax instead of stamp duty.

In NSW, on average about 5% of properties change hands each year, so on average each is transferred once every 20 years.

If in the first year all buyers switch to land tax, the government will lose 95% of the money it would have received from stamp duty in that year.

Ray Ellis, CEO of First National Real Estate, expects a two-tier market to emerge. He says the proposal could introduce complications that make some properties less saleable than others.

"If a buyer elects to pay an annual property tax instead of one-off stamp duty, all subsequent purchasers of the property will be forced to pay annual land tax," he says.

"This would have the potential to make properties locked into an annual tax regime less attractive to downsizers and buyers with the capital and intention to stay for the long term."

State of the nation

NSW residents do not currently pay land tax on their principal place of residence, on land used for primary production or on land valued below $755,000.

It is paid on any vacant land, including vacant rural land, land where a house, residential unit or flat has been built, holiday homes, investment properties, company title units, residential, commercial and industrial units, car spaces, commercial properties including factories, shops and warehouses as well as land leased from state or local government. For 2021, land tax is 1.6% above the $755,000 threshold and 2% above the "premium" threshold of $4,616,000.

Stamp duty by state

STATE	STAMP DUTY PAYABLE ON A $500k PURCHASE	TRANSFER FEE
NSW	$17,835	$146.40
ACT	$11,400	$409
NT	$23,928.60	$149
QLD	$8750	$1379
SA	$21,330	$4185.50
TA	$18,247.50	$212.22
VIC	$21,970	$1268
WA	$17,765	$264.70

The Northern Territory is the only state or territory with no land tax. However, for a purchase between $525,001 and $3 million, the stamp duty is 4.95% of the property value.

While the ACT has generous concessions, its land tax rate is 1.12%. It also recently abolished stamp duty for first home buyers and commercial property under $1.5 million.

Tasmania has a maximum land tax rate of 1.5% and if you were to buy a $400,000 home you would be up for $13,997 in stamp duty.

Victoria's land tax is 2.25%. The state government recently announced land tax waivers up to 50% for purchases of property up to $1 million. Currently land tax starts at 1.4% for properties valued at $25,000 or less and rises to 5.5% for those valued at or above $960,000.

In South Australia, the land tax is 2.4%. Stamp duty is based on a sliding scale, ranging up to $21,330 plus $5.50 for every $100 over $500,000.

In Western Australia the land tax is 2.67%. Generally, for a residential property valued between $360,001 and $725,000 the stamp duty is $11,175 plus 4.75% for every dollar over $360,000.

Queensland has Australia's highest general land tax rate at 2.75%. It has a general rate of stamp duty for those purchasing an investment and a concessional rate for those purchasing a home.

The concessional rate is $10,150 plus $4.50 for every $100 or part of $100 over $540,000 for homeowners purchasing a home between the value of $540,001 to $1 million. This is less compared with the general rate of $17,325 plus $4.50 for every $100 or part of $100 over $540,000.

While land tax thresholds are redetermined each year, rising property values have meant that some property owners have been pushed over the threshold without even realising it in years gone by.

With Victoria and NSW changing their stamp duty regulations, the other states could soon follow.

Two-speed approach

The Real Estate Institute of Australia has already called for a co-ordinated approach that could see knock-on benefits to the economy as a whole.

Steve Mickenbecker, group executive of financial services at Canstar, says land tax is less likely to distort householders' choice of property, whereas stamp duty is seen as a barrier to getting onto the property ladder.

Tim McKibbin, chief executive of the Real Estate Institute of NSW, says the reform has the potential to adversely affect the housing market for months, but this won't occur until mid-2021 at the earliest.

The Real Estate Institute of Western Australia recommends a two-stream revenue collection approach. The president, Damian Collins, says this would allow buyers to decide whether to pay the stamp duty upfront or whether to opt in for an annual fee for the duration of ownership. A reduction in upfront costs could encourage more transactions with a significant flow-on benefit to economic activity, similar to the proposed change in NSW.

The REIWA is calling for a $10,000 stamp duty concession for seniors over the age of 65 to encourage appropriate "rightsizing".

But the question remains: who might prefer stamp duty and who might prefer land tax?

For those planning to hold a property for a long time, paying a one-off stamp duty would be more appealing. This removes the annual land tax burden.

In NSW, the average stamp duty is $26,000, which increases for more expensive properties. In a good year, with around 200,000 transactions, the revenue exceeds $9 billion.

Yet from the initial announcement, the NSW Treasurer has indicated young property buyers will opt for the land tax scheme, deeming it "the Netflix of property tax".

However, most investors seem to be still unsure about the changes.

From our initial conversations and impressions, many see the choice as a positive, and with affordability being a large stumbling block for those entering the market, the land tax option seems appealing.

But we are yet to see how banks treat each scenario in their servicing calculations and how this will affect overall borrowing capacity. This will also be a major factor.

There is no doubt there is potential for the reform to make it a better proposition to buy an investment property in NSW. The initiative is clearly focused on reducing transaction costs, which is always a positive for investors.

It's likely the NSW government's consultation paper will be backed up by some further policy detail, which in the overall context of current market conditions will be positive for investors.

Is it time to ditch stamp duty?

Australia avoided a recession during the global financial crisis (GFC) due to a mixture of good luck and good policy.

Our proximity to Asia helped to moderate the economic downturn, while economic reforms implemented over the last few decades acted as a shock absorber to reduce their impact upon Australia.

Now, in the midst of another global recession, even if the Australian government successfully navigates the COVID-19 pandemic, a serious challenge remains for the economy.

Since the GFC, productivity gains in advanced economies have slowed. And these productivity gains lay the foundation of future growth in living standards.

With productivity growth expected to remain muted, it becomes increasingly important for policymakers to strive for reforms to economic institutions. And the tax system should be top of the list.

It is commonly agreed that property transaction taxes are highly inefficient. This was outlined in The Henry Review, which was commissioned by the government in 2008 and intended to guide Australia's tax system reforms over the next 10 to 20 years.

Property transaction taxes, incurred when a house is sold and more commonly known as stamp duty, are an important source of state government revenue.

Our research examines the cost and benefit of replacing stamp duty with either a recurrent property tax based on the value of the home or with an increase in consumption tax.

We've then analysed how Australians could be affected by these reforms.

Stamp duty reduces transactions in the housing market and prevents mutually beneficial gains.

Taxes like this also present a barrier for homeowners wanting to move when a residence no longer suits their needs, such as when a family outgrows their first family home.

Then there's mobility. Reduced mobility can have ramifications beyond the housing market. For example, it may be difficult for people to accept better jobs that are located too far from their current residence.

Stamp duty also increases the down payment required to purchase a home, making it more difficult for young households to enter the property market.

Over time, as house prices have increased the burden of stamp duty has become larger, and these problems have become more severe.

Finally, stamp duty is one of the most volatile taxes, as the revenue raised varies based on movements in the property market.

So, if the goal for state governments is to deliver a stable revenue stream, then stamp duty is not fit for modern purpose.

So, why do we still have stamp duty? The challenge of removing stamp duty is finding a viable alternative.

Although stamp duty is inefficient, removing it would realistically require either a reduction in government services or an increase in government revenue. So, state governments would eventually have to increase taxation from other sources or reduce their expenditure.

Australia already has low tax rates compared to many countries within the Organisation for Economic Co-operation and Development, so presumably, other sources of government revenue would have to be raised.

And here is the challenge for governments: even though stamp duty is highly inefficient, replacing stamp duty with an alternative tax will always be controversial as it will raise the tax burden on some people and lower it for others.

Our model shows that removing stamp duty would reduce the purchase price for home buyers, increase the sale price for sellers, increase the total number of transactions and reduce the degree of mismatch in the housing market.

We've also found find that the rate of homeownership would increase, particularly among younger segments of the population who currently have difficulty in saving for an initial house deposit. Our model predicts reforming the tax system could increase the homeownership rate among individuals under the age of 35 by three to four percentage points.

There would also be an increase in the rate of current homeowners moving to new homes which allows a more efficient allocation of housing as people are more willing to move in response to their changing circumstances.

Our economic model also allows us to address welfare issues.

First, in our model economy, we find people entering the economy prefer a tax system with stamp duty or a system with a property tax, or a system with increased consumption taxes. Here, our answer is unequivocal.

Young adults entering the economy would typically prefer a system with a recurrent property tax rather than a consumption tax or stamp duty.

Current homeowners would typically benefit from replacing stamp duty with consumption taxes rather than property taxes.

Why is this so? Well, over 65% of households in the Australian economy own property outright or are in the process of paying off a mortgage. For these households, moving to a property tax — which increases their tax burden — is less attractive than moving to a consumption tax.

Our economic model also suggests that the welfare effects will vary by demographic characteristics, income and homeownership.

Renters typically benefit more from the removal of stamp duty than homeowners. Houses become easier to purchase and this benefits groups that are currently excluded from homeownership by the greatest amount.

Perhaps surprisingly, we also found that older landlords will also tend to gain from the removal of stamp duty. They do so because this will in many cases increase the value of their housing portfolio, outweighing any cost associated with an increased tax burden.

This raises a challenge for governments.

In the long run, our research shows that a land or property tax is preferential to the current status quo. But it will be difficult to get broad-based support for the removal of stamp duty and its replacement with a property tax from current voters.

Some state and territory governments have already taken steps to eliminate stamp duty.

In the Australian Capital Territory, there's a 20-year plan for the transition from stamp duty to land taxes (which are similar in many ways to a property tax). This involves the gradual elimination of stamp duty and the gradual increase of land taxes.

The New South Wales' government has an alternative proposal. Households purchasing property in the future may be allowed to select either a recurring land tax or a one-off stamp duty levy. These are good policies that should increase the efficiency of the tax system and benefit future generations.

The gradual transition — either by increasing the length of the policy change or by allowing households to select into different tax payment systems — helps make these policies more palatable to the voting public and also provides a pathway for other state governments to follow.

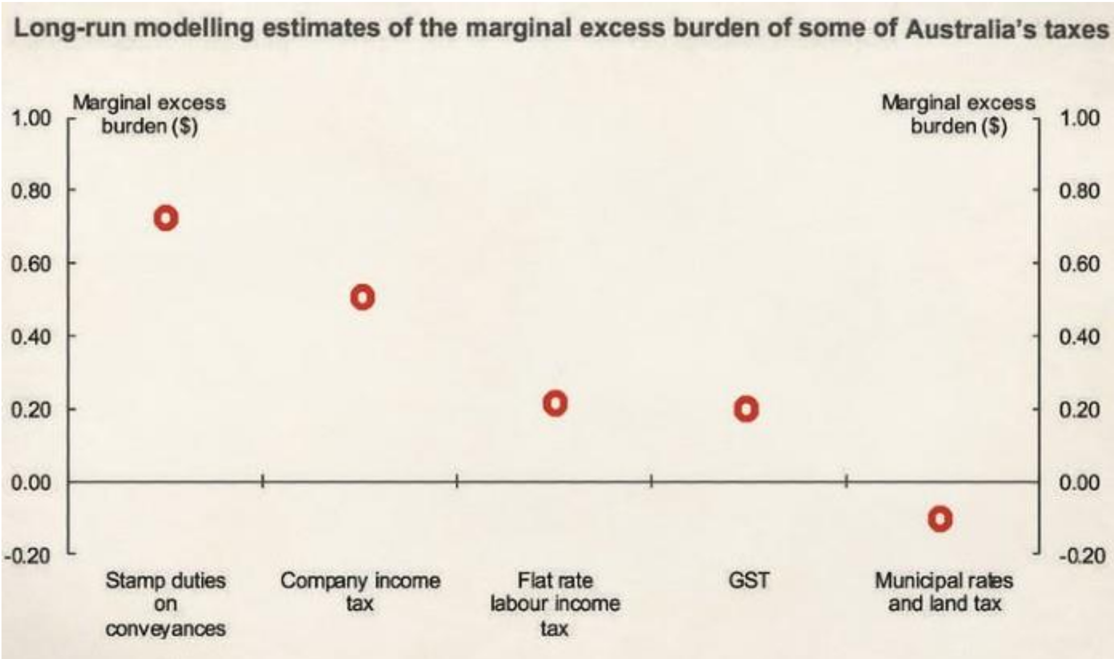
The losers — and surprising winners — from phasing out stamp duty

Stamp duty may be lowering sale prices for homeowners.

More than ever as we emerge from the crisis, we are going to have to get the most out of our economy.

Swapping stamp duty for land tax as the ACT government is doing (over 20 years) and the NSW government is planning (using an opt-in arrangement), is one of the best ways the tax system can help.

This graph, from the federal treasury's 2015 tax discussion paper makes the point.



It says the "marginal excess burden" (damage) done by real estate stamp duty amounts to 70 cents for each dollar raised.

It discourages people and businesses from changing addresses as often as they should, meaning workers live further away from their work than they would and are reluctant to move to where there is better work.

In contrast, Treasury found the marginal excess burden of land tax was negative. Land tax makes sure land was used for its most useful purpose and not left idle.

Efficiency-wise, it makes sense to swap one for the other, but as with all changes, there will be winners and losers, some of them surprising.

In our just-published study (copy attached), we use real-world data on living arrangements from the Melbourne Institute's Household, Income and Labour Dynamics in Australia survey and data on house prices and stamp duty rates from the Real Estate Institute Australia in an attempt to work out who the winners and losers will be.

Good for the young, and the old

We find that overall, the swap should reduce the purchase price for home buyers, increase the sale price for sellers, increase the total number of transactions, and reduce the degree of mismatch in housing.

It should also increase the rate of home ownership.

Young adults, particularly those who are currently having difficulty saving for a deposit, would be better off.

Current homeowners would generally be worse off.

Renters would benefit because they are currently excluded from home ownership.

Older landlords, perhaps surprisingly, would also benefit. In many cases, the increase in the value of their houses would outweigh the cost of the land tax.

Our findings raise a challenge for governments.

In the long run, the swap would improve the working of the economy, but in the short run, it will hurt many current voters.

A gradual transition — either through a very long phase in (of the kind adopted by the ACT) or by allowing households to select into different tax systems (as NSW is planning) would help make the switch more palatable.

But the sooner we start, the better.

'Holy grail' of taxing land owners who profit from 'stroke of a pen' proves elusive

Planning Minister Rob Stokes says major political challenges have hampered the NSW government in setting up a levy or tax on land values that skyrocket as a direct result of infrastructure projects.

Mr Stokes agreed that some of the uplift in land values due to government-funded projects – such as Sydney's second airport at Badgerys Creek – should go toward paying for the infrastructure required to support the extra development.

With the NSW government spending $107 billion on infrastructure over four years, a so-called value capture mechanism has often been touted as a way for the state to help fund projects by recouping some of the windfall gains made by landowners.

"It is the holy grail but, like the holy grail, it has eluded discovery," Mr Stokes said.

"Conceptually it's ideal. In practice, it's much harder to distil and involves every level of government working together."

A group representing eight councils in western Sydney has called for a review of public policy which, it argues, allows disproportionate private gains to be made from publicly funded works.

"We have already seen examples of enormous private windfalls from the land acquisition processes at Badgerys Creek," Western Sydney Regional Organisation of Councils president Barry Calvert said.

"The potential profits from land rezonings in the growth areas of western Sydney will be staggering. Both federal and state governments must act to promptly facilitate taxpayer investment in key developments from funding provided via value-capture mechanisms."

Federal Liberal MP John Alexander has championed a value-capture mechanism aimed at giving taxpayers a fair slice of major rises in land values as a result of government-funded projects.

Asked whether value capture should have been introduced earlier, Mr Stokes said there had been “massive missed opportunities going back to the 1970s”.

He said “these things are very, very difficult” and NSW Treasurer Dominic Perrottet was taking steps with a plan to abolish stamp duty in favour of a broad-based land tax.

“We have gotten very good, over time, at designing taxation over goods and services and income but the political hot potato has always been land. That’s where the windfalls have always been and that’s why it’s politically the most challenging area to take on,” Mr Stokes said.

He said one of his frustrations was that the market was able to judge where rezonings were likely to happen because strategic planning had improved over the years. “The problem with that, of course, is that the values have already been captured before the rezoning actually occurs. The better we get at planning, the earlier and earlier the value capture mechanism needs to be,” he said.

A British rail expert last year urged governments to establish a levy before preferred sites of train stations and other infrastructure were announced, because doing so afterwards was too late.

In the ACT, a betterment tax is levied at 75 per cent of the uplift in land value.

NSW Greens MP Jamie Parker said a betterment tax ensured that increases in land values resulting from a “stroke of a pen” by governments were not captured entirely by private interests.

“In NSW, we see hundreds of millions of windfall profits for no productive reason, just because the government has rezoned or the council has rezoned. The government needs to be capturing that for the community to fund these really important infrastructure priorities,” he said.