TAKING ON TAX:
REFORMING NSW PROPERTY TAXES

NSW
Business
Chamber

Thinking business

"NSW Business Chamber and NSW Council of Social Service join together in calling for the NSW Government to consider replacing conveyancing stamp duty with a broad-based land tax."

Foreword

by NSW Business Chamber and NSW Council of Social Service.

Stamp duty impacts on housing affordability and the efficiency of NSW taxes. That is why NSW Business Chamber and NSW Council of Social Service join together in calling for the NSW Government to consider replacing conveyancing stamp duty with a broad-based land tax (what we are calling 'the switch').

In 2015-16, conveyancing stamp duty is expected to generate more than $8.6bn for the NSW Government with a considerable share of this coming from residential property transactions. This is double the average received in the previous decade with the level of stamp duty payable on the median Sydney house price now more than $40 000, around twice what it would have been a decade earlier.

As broad and diverse stakeholders, the switch appeals to each of us for different reasons; but each agree that it is essential that stamp duty and land tax remain an active part of any conversation about tax reform.

NSW Business Chamber and NSW Council of Social Service joined together in November 2014 to look at options for state-based tax reform and to identify common ground. The reform of NSW property taxes, including stamp duty on property transfers and the potential to move to a broad-based land tax, was identified as an area where we thought we could come together.

Under the switch, property owners would be subject to a redesigned land tax, but would no longer pay stamp duty when purchasing a property. While NSW already has a land tax system in place, the current system is "narrow" and does not apply to owner occupied land. Under the switch a "broad" land tax would apply to owner occupied land in addition to those who already pay it. The switch could be designed as "budget neutral" so that it could be implemented independently of decisions about the revenue and expenditure needs of the Government.

To further explore the implications of the switch, NSW Business Chamber commissioned KPMG to model the impacts of the switch on the NSW economy, and consulted NSW Council of Social Service on the findings.

The modelling adds further weight to the argument for abolishing stamp duty on property and replacing it with a broad-based land tax. The modelling demonstrates significant benefits for NSW, including a potential boost of more than 1 per cent to Gross State Product, around 10 000 additional jobs, and more than $1400 dollars in additional consumption for the average household. With reference to the modelling and the broader evidence base, NSW Business Chamber and NSW Council of Social Service make the following observations about the switch:

- **Observation 1 - The economic benefits are significant:** the economic benefits to the community are large, including when compared with alternative tax reform proposals, meaning that it should remain front of mind when considering alternative tax reform options.

- **Observation 2 – The switch should be part of any conversation about solutions to housing affordability:** while it is only part of the solution to the significant housing affordability challenges we face here in NSW, a switch from stamp duty to land tax would improve housing affordability by making it easier for households to move as their needs change over time, enabling better use of the existing housing stock and reducing the upfront costs of home ownership.

- **Observation 3 – The bulk of the economic benefits comes from reducing conveyancing stamp duty rather than pursuing the "textbook perfect" land tax:** there is flexibility for a land tax to be designed so that it meets the needs of the community without compromising on the shared economic benefits of the switch.

"We recognise there will be a range of different views about the best model, but we have come together to propose the switch as a 'conversation starter' and to ensure conveyancing stamp duty and land tax remain on the table as part of the broader tax reform agenda."

- **Observation 4 - While the benefits are maximised by the switch being fully implemented, even small steps towards the switch are beneficial:** as with any significant reform, change has to be managed carefully and gradual implementation would allow stakeholders to adjust to a redesigned land tax regime.

- **Observation 5 – Reducing the Budget's exposure to the ups and downs of the property market will support better budget management now and into the future:** the switch will have the added benefit of stabilising property tax receipts at a time when record stamp duty cannot necessarily be relied on into the future.

While the modelling considers four specific land tax scenarios, these are intended to illustrate the scope of the economic benefits rather than to recommend a specific approach to redesigning land tax or implementing the switch. We recognise there will be a range of different views about the best model, but we have come together to propose the switch as a "conversation starter" and to ensure conveyancing stamp duty and land tax remain on the table as part of the broader tax reform agenda.

Nonetheless NSW Business Chamber and NSW Council of Social Service recognise the need for a viable approach to implementation, both in terms of the design of land tax as well as a mechanism to transition to a new regime. To achieve broad community support, the implementation plan would need to:

- consider the needs of those that have recently paid conveyancing stamp duty;

- manage the land tax liabilities of households on low incomes; and

- meet community expectations of fairness.

While more work needs to be done to determine how the switch is implemented, we believe that this is achievable if the government works with business, unions and the community sector to shape the reform. Indeed the South Australian and the Australian Capital Territory property tax reforms provide a possible template for steps that NSW could take toward implementing the switch. The 2010 Henry Tax Review also looked at options that could be used to inform the implementation of a broad-based land tax.

We know that this conversation is important for NSW – that's why we came together. And the fact that we were able to find common ground demonstrates the potential for achieving broad consensus on this complex issue.

NSW Business Chamber and NSW Council of Social Service are pleased to present the results of this new modelling.

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Economic Modelling of Property Tax Reform Options

Report prepared for the
NSW Business Chamber

February 2016

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Executive summary

A consensus appears to be emerging amongst stakeholders that there are many opportunities at all levels of Australian government to improve the tax system. Property tax reform is one component of the system where there appears to be potential for common ground amongst a range of stakeholders. The emerging consensus seems to be that conveyancing stamp duties (CSD) on property transactions should be abolished. CSDs account for a large portion of state government revenues. If such taxes are abolished an alternative source of revenue will be required by state governments to maintain existing services.

The NSW Business Chamber (Chamber) has commissioned KPMG to model the effects of replacing CSD on property with land taxes. The purpose of this analysis is to assist the Chamber in its assessment of the potential impacts of alternative property taxation policy options.

In this study, we use KPMG's regional computable general equilibrium model (KPMG-RCGE) to estimate the potential impacts on the NSW and Australian economies of four land tax reform scenarios. KPMG-RCGE uses the structure of the economy in 2009-10, as captured by the input-output tables published by the Australian Bureau of Statistics, as the starting point for computations. Each scenario is modelled with the assumption that the state government budget position is unaffected (i.e., budget neutrality).[1]

- **Scenario 1: Minimalist** – The current land tax structure (i.e. with the current exemptions and progressivity) is maintained and land tax rates are adjusted to maintain budget neutrality given the abolition of CSD.

- **Scenario 2: ex-PPR** – The land tax structure is modified to remove the Principal Place of Residence (PPR) exemption. Land tax rates in this modified structure are adjusted to maintain state budget neutrality.

- **Scenario 3: ex-PPR&Prog** – In addition to removing the Principal Place of Residence (PPR) exemption from the current land tax structure, the progressivity in that structure is also removed. Land tax rates adjust to maintain budget neutrality.

- **Scenario 4: Broad** – As per scenario 3 with an additional modification to the land tax structure that removes the primary production exemption. Land tax rates in this broad-based structure adjust to maintain state budget neutrality.

We analyse the implications of the four scenarios outlined above in two contexts. First, in the context where NSW adopts the reforms and the other states and territories maintain the status quo. Second, in the context where all state and territory governments implement the reforms in concert.

In the case where NSW goes it alone with the property tax reforms we find that NSW benefits and a small share of this benefit is at the expense of the rest of Australia. Table 1 shows that in the long run household consumption per household, expressed in 2014-15 dollars, is just over $1,400 higher than in the baseline (in the absence of policy change) under all four land tax arrangements. In each of the four scenarios, there are around 9,700 new jobs in NSW. The sectors that benefit most from the abolition of CSDs in NSW are *Residential Dwellings, Rental, Hiring & Real Estate Services and Construction*.

In the case where state and territory governments co-ordinate property tax reforms we find that NSW households benefit by more than the case where they implement the reforms alone. Table 2 shows that in the long run household consumption per household, expressed in 2014-15 dollars, is over $1,500 higher than in the baseline (in the absence of policy change) under all four land tax arrangements. The increase in employment in NSW is lower in these simulations because there is less incentive for households to move interstate when the policy reform is co-ordinated. The slightly lower increase in employment in NSW is also reflected in a slightly lower increase in gross state product. Table 2 shows that the benefits of the reforms to the rest of Australia are comparable to those for NSW.

Our results show that most of the economic benefits of the property tax reforms tested emanate from the abolition of CSDs. The alternative land tax arrangements make relatively small differences to the results. The GSP results capture the increased economic efficiency of land taxes as they are broadened. In the simulations where NSW implements reforms on its own, GSP per household increases by $1,556 per annum when CSDs are abolished and the current land tax structure is preserved with land tax rates adjusting to maintain budget neutrality. As the exemptions and progressivity arrangements are removed from the land tax structure, GSP per household increases by $1,684 per annum. When all states implement the property tax reforms in a co-ordinated manner we get similar results. The abolition of CSDs and implementation of a broad-based land tax that preserves budget neutrality in all states increase GSP per household by $1,605 per annum in NSW and by $1,698 per annum in the Rest of Australia.

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1 Note that budget neutrality encompasses the first-round effect of lost revenue and second-round effects.

Table 1: Selected Macro Results – NSW-only Property Tax Reform

	Scenario 1 Minimalist	Scenario 2 ex PPR	Scenario 3 ex PPR & Prog.	Scenario 4 Broad
NSW				
Household Consumption[1]	$1,451	$1,421	$1,437	$1,444
Gross State Product[1]	$1,556	$1,658	$1,681	$1,684
Employment[2]	9,743	9,699	9,819	9,856
Rest of Australia				
Household Consumption[1]	$22	$1	-$2	-$1
Gross State Product[1]	-$67	-$110	-$116	-$115
Employment[2]	-623	-1,054	-1,110	-1,094

Source: ABS and KPMG-RCGE.

Notes:
(1) Units are 2015 dollars per projected number of households in 2015.
(2) This represents the change in the number of jobs.

Table 2: Selected Macro Results – All States Reform Property Taxes

	Scenario 1 Minimalist	Scenario 2 ex PPR	Scenario 3 ex PPR & Prog.	Scenario 4 Broad
NSW				
Household Consumption[1]	$1,516	$1,544	$1,565	$1,562
Gross State Product[1]	$1,522	$1,590	$1,621	$1,605
Employment[2]	9,484	9,243	9,407	9,360
Rest of Australia				
Household Consumption[1]	$1,630	$1,591	$1,595	$1,597
Gross State Product[1]	$1,664	$1,677	$1,665	$1,698
Employment[2]	23,350	22,719	22,759	22,791

Source: ABS and KPMG-RCGE.

Notes:
(1) Units are 2015 dollars per projected number of households in 2015.
(2) This represents the change in the number of jobs.

1. Background

The NSW Business Chamber (hereafter the Chamber) has identified property taxes as an area of tax reform where there is potential for common ground among a range of stakeholders. The Chamber has commissioned KPMG to model the effects of replacing conveyancing stamp duty (CSD) on property with land taxes. The purpose of this modelling work is to assist the Chamber assess the potential impacts of alternative property tax policy options.

Scope

As set out in the Consultancy Agreement between the Chamber and KPMG, the scope of this project is to estimate the impact on the NSW and Australian economy of four alternative property taxation scenarios using KPMG's proprietary Regional Computable General Equilibrium model. Each scenario models a policy where the NSW state government abolishes stamp duty on CSD and simultaneously adjusts land taxes to ensure that the state government budget balance remains unaffected by the policy (i.e., budget neutrality).[2] The four scenarios differ in how the compensating adjustments to land taxes are modelled. Specifically, the four scenarios model the reform of land taxes as follows:

- **Scenario 1: Minimalist** – The current land tax structure (i.e. with the current exemptions and progressivity) is maintained and land tax rates are adjusted to maintain budget neutrality given the abolition of CSD.

- **Scenario 2: ex-PPR** – The land tax structure is modified to remove the Principal Place of Residence (PPR) exemption. Land tax rates in this modified structure are adjusted to maintain state budget neutrality.

- **Scenario 3: ex-PPR&Prog** – In addition to removing the Principal Place of Residence (PPR) exemption from the current land tax structure, the progressivity in that structure is also removed.

- **Scenario 4: Broad** – As per scenario 3 with an additional modification to the land tax structure that removes the primary production exemption.

These four scenarios represent a progression towards a broader land tax. By eliminating exemptions and

progressivity, the four scenarios modelled provide a decomposition of the impact of each of these features

The scenarios described above are modelled with reference to a business-as-usual (hereafter basecase) representation of the structure of the economy. For the purposes of this project KPMG's basecase representation of the economy has been modified to include additional details on the current stamp duty and property tax structures. The key extensions to the basecase include re-specifications of:

- **Stamp duty** – To the extent that data was available the modelling of stamp duties has been modified to separate out the tax-on-investment effects, the transactions (turnover) effects and the related labour mobility effects.

- **Land taxes on commercial land** – These have been modified to recognise the primary production exemption and to proxy progressivity through specification of average tax rates that differ by industry.

To provide some insights on the impacts of NSW going it alone on property tax reform versus the situation where all state and territory governments implement the same reforms together we have simulated each scenarios twice: once for NSW reforming on its own, and once with NSW reforming in concert with rest of Australia.

Report structure

The remainder of this report is structured as follows. Section 3 provides an overview of the NSW property tax system. We describe the nature of land taxes in NSW, the main economic implications of the current design and how they are modelled. Analogously, we describe the nature of NSW CSD, the main economic implications of the current design and how they are modelled. Section 4 provides an overview of the version of KPMG's Computable General Equilibrium Model that is used to model the alternative property tax scenarios. The simulation results are presented and discussed in section 5.

Each scenario models a policy where the NSW state government abolishes stamp duty on CSD and simultaneously adjusts land taxes to ensure that the state government budget balance remains unaffected by the policy.

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2 Note that budget neutrality encompasses the first-round effect of lost revenue and second-round effects.
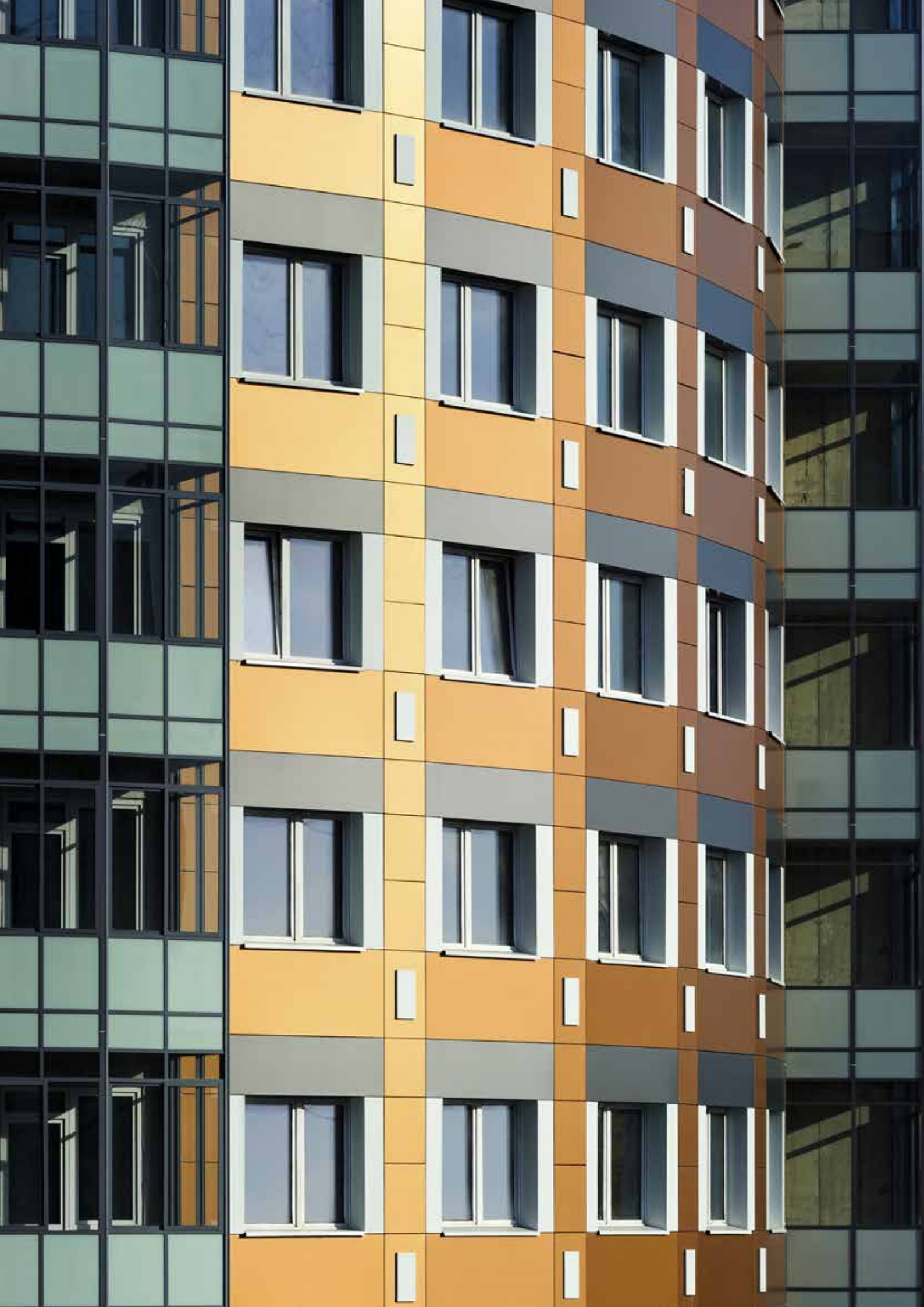
2. Property taxation

The Henry Tax Review brought attention to the high economic costs associated with some current taxes on commercial property, such as conveyancing stamp duty. Reforming property taxes by replacing relatively inefficient taxes with more efficient taxes can be expected to benefit the economy without necessarily sacrificing any tax revenue.

This section summarises the design and collections of CSD and land taxes in NSW and Australia. We also discuss the key economic issues associated with CSD and property taxes.

2.1 The current property tax system

Tables 2.1.1 and 2.1.2 show the revenues collected in 2009-10 and 2013-14 from CSD and property taxes by state Governments in NSW and Australia.

Table 2.1.1: State Government Property Taxes 2009-10 ($ million)

		Australia				NSW	
Conveyancing Stamp Duty		12,292				3,739	
Commercial	2,185				665		
Residential	10,107				3,074		
Land Tax		5,767				2,296	
Other Property Taxes		2,219				731	
Total Property Taxes			**20,278**				**6,766**
Other Tax Revenues			34,486				11,188
Total Tax Revenues			**54,764**				**17,954**

Source: ABS Category 5506.0 - Taxation Revenue, Australia, 2013-14 and NSW Office of State Revenue.

Table 2.1.2: State Government Property Taxes 2013-14 ($ million)

		Australia				NSW	
Conveyancing Stamp Duty		15,976				6,045	
Commercial	3,040				1,150		
Residential	12,936				4,895		
Land Tax		6,364				2,335	
Other Property Taxes		3,704				848	
Total Property Taxes			**26,044**				**9,228**
Other Tax Revenues			42,676				15,134
Total Tax Revenues			**68,720**				**24,362**

Source: ABS Category 5506.0 - Taxation Revenue, Australia, 2013-14 and NSW Office of State Revenue.

For NSW and for Australia as a whole, conveyancing stamp duty is currently the largest tax levied on the property sector in terms of revenue. In NSW CSD revenue has grown from 55% of property taxes in 2009-10 to around 65% in 2013-14. In fact, CSD revenue is also one of the largest individual components of NSW tax revenue. In NSW CSD revenue has grown from about 19% of total state tax revenues in 2009-10 to about 25% in 2013-14. For Australia as whole, CSD revenue has hovered around 60% of property taxes since 2009-10.

Land tax is the second largest source of property taxes. In NSW land tax revenue has fallen from 34% of property tax revenue in 2009-10 to around 25% in 2013-14, and from about 12% of total state tax revenue in 2009-10 to about 10% in 2013-14. For Australia as a whole, land taxes have fallen from about 28% of property tax revenue in 2009-10 to around 24% in 2013-14.

Between 2009-10 and 2013-14 CSD revenues increased by 62% in NSW while revenues from land taxes increased by only 2% over the same period. Table 2.1.3 shows that for NSW the number of dutiable residential transactions increased by about 14% between 2009-10 and 2013-14 whilst the transfer duties collected from these transaction increased by around 61% over the same period. This reflects mainly the strength in the property market in the more recent period: an increase in transactions of 14% accompanied by an increase in stamp duties collected of 61% indicates that the main driver of growth in CSD revenues over this period was increases in house prices.

Table 2.1.3: NSW Land-related Transfer Duties

	Residential		Non-Residential	
	Transactions (000's)	Value ($millions)	Transactions (000's)	Value ($millions)
2014-15	206	5,727	15	1,285
2013-14	202	4,722	13	1,110
2012-13	162	3,343	12	1,047
2011-12	144	2,736	11	596
2010-11	150	2,923	12	630
2009-10	177	2,938	14	635
2008-09	158	2,116	14	461
2007-08	165	2,810	25	793
2006-07	163	2,548	24	916
2005-06	156	2,294	21	687

Source: NSW Office of State Revenue

Table 2.1.4 reports CSDs and land taxes for NSW over a longer time frame. The table shows that in 2013-14 CSDs account for a relatively high proportion of total NSW taxes while land taxes account for a relatively low proportion. The table also shows that revenue from CSDs is relatively more volatile than revenue from land taxes, with the former ranging from 15.2% to 24.8% of NSW tax revenue and the latter ranging from 9.6% to 12.5% of NSW tax revenue.

Table 2.1.4: NSW Land-related Transfer Duties

	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14
	$m	$m	$m	$m	$m	$m	$m	$m	$m
CSDs	3,237	4,166	3,938	2,736	3,739	4,045	3,764	4,568	6,045
Land taxes	1,717	2,036	1,937	2,252	2,296	2,289	2,350	2,333	2,335
Total Taxation	16,057	17,854	18,675	17,954	19,280	20,549	20,731	22,054	24,362
Shares in total taxes									
CSDs	20.2%	23.3%	21.1%	15.2%	19.4%	19.7%	18.2%	20.7%	24.8%
Land taxes	10.7%	11.4%	10.4%	12.5%	11.9%	11.1%	11.3%	10.6%	9.6%

Source: ABS Category 5506.0 - Taxation Revenue, Australia, 2013-14

From a modelling point of view the volatility of CSD revenues poses a challenge. Analysis of this property tax policy should be framed in a long run context. If the 2013-14 snapshot of the structure of taxes (e.g., CSD revenues as a share of government revenues), and the structure of the economy more generally, is not representative then computations based on this snapshot may be biased. We have assessed that 2013-14 is not an ideal starting point for our computations. Instead, we have chosen to use 2009-10 as a starting point for our computations. Table 2.1.4 shows that the share of CSD receipts in total tax receipts in 2009-10 was very close to

to the long run average of around 20%. From a modelling perspective, basing simulations on a starting point where CSDs represent a significantly larger share of tax revenues than the long run average means that the economic benefits of removing the CSDs will appear to be higher and the compensating adjustments to land taxes will also be higher. From a policy perspective, it is important to recognise that changes to tax policy are designed to be permanent. Alternative policy options must be assessed on the basis of long run costs and benefits. Similarly, tax rates must be calibrated on the basis that they will be appropriate over the longer term.

The current designs of each of the property taxes analysed in this report are now discussed in turn. This provides background to understand the reforms to property taxation that are subsequently analysed in this report.

2.2 Land tax

Land taxes are levied on the commercial use of land, and on rental properties. All states and territories (except the Northern Territory) levy land tax on the unimproved value of a taxpayers aggregate holdings of land, excluding principal residences. Land used for primary production is exempt. Most states have a progressive land tax system and a tax-free threshold.

2010 NSW land tax regime

In 2010, NSW land tax payable was calculated on the combined value of all taxable land owned by a taxpayer above the land tax threshold of $376,000. The amount of land tax payable was calculated as $100 plus 1.6 per cent of the land value between the threshold and the premium threshold ($2,299,000), and 2 per cent thereafter. The land tax threshold did not apply for non-concessional companies and special trusts. For such land-holding entities, land tax was charged at a flat rate of 1.6 per cent of the taxable land value up to the premium threshold and 2 per cent thereafter.

2014 & 2015 land tax regime

In 2014 and 2015 the design of the NSW land tax regime remained the same as was in place in 2010. The only changes were in terms of the thresholds ($412,000 for 2014 and $432,000 for 2015). The premium threshold also increased ($2,519,000 in 2014 and $2,641,000 in 2015).

Table 2.2.1 gives an indication of how narrow the land tax base is made by the exemptions to land associated with principle places of residence and to primary production. Table 2.2.1 makes clear several key points:

i.   Residential zoned land accounts for over 72% of total land value in NSW;

ii. The impact of the PPR exemption is evident with only 11% of residential zoned land qualifying as taxable land;

iii. The exemption of primary producers from land tax is reflected in the fact that only about one third of the non-residential zoned land is taxable;

iv. Under the current arrangements, less than one fifth of land (by value) is taxable; and

v.   With NSW land tax revenues estimated to be $2.50 billion in 2014-15 and projected to be $2.66 billion in 2015-16 (NSW Budget Papers) we can infer that in 2015 the average rate of land tax for entities that pay land tax is around 1.3%.

vi. Some information about the impact of thresholds and progressivity of land taxes can be gleaned from table 2.2.2. The table shows the distribution across a number of value categories of entities that are potentially liable for land tax. For example, there are 19,135 entities with taxable land valued in the range $400,000 to $499,000. Analogously, there are 3,611 taxable entities with land holdings valued over $4,999,999.

Table 2.2.1: Summary Land Data for NSW for the 2015 Valuation Year

	Value ($bn)	Taxable Value ($bn)	Taxable %
Residential zoned land	820	93	11%
Non-residential zoned land	311	103	33%
Total land	**1,131**	**195**	**17%**

Source: NSW Office of State Revenue (OSR). The following notes are provided by OSR.

Notes:
(1) Data is based on all current land valuations for the 2015 valuation year, that is, current as at 01-Jan-2015. Data is as at 27-May-2015.
(2) Taxable land refers to the value of all 2015 valuations that are attached to an issued land tax assessment and do not have a current exemption.
(3) Residential valuations in the report are based on the zoning of the relevant land valuation not on the specific use of the property.
(4) Valuation values are as provided to OSR by Land and Property Information for the 2015 valuation year.

Table 2.2.2: Distribution of NSW Land Tax Payers by Aggregated Land Holdings 2015 Valuation Year

Aggregate taxable value ranges	No. of Entities[1]	Indicative Value of Holding[2]	Deduced Tax Revenue	Deduced Ave. Tax Rate
Under $100,000	2,381	$ 50,000	nil	
$100,000 - $199,999	3,163	$150,000	nil	
$200,000 - $299,999	2,223	$250,000	nil	
$300,000 - $399,999	1,677	$350,000	nil	
$400,000 - $499,999	19,135	$450,000	$7,424,380	0.09%
$500,000 - $599,999	25,428	$550,000	$50,550,864	0.36%
$600,000 - $699,999	19,017	$650,000	$68,232,996	0.55%
$700,000 - $799,999	13,581	$750,000	$70,458,228	0.69%
$800,000 - $899,999	9,671	$850,000	$65,646,748	0.80%
$900,000 - $999,999	7,267	$950,000	$60,955,596	0.88%
$1,000,000 - $4,999,999	36,744	$3,000,000	$1,566,176,256	1.42%
Over $4,999,999	3,611	$10,000,000	$659,455,264	1.83%
Grand Total	**143,898**		**$2,548,900,332**	

Notes:
(1) NSW Office of State Revenue data for the 2015 valuation year.
(2) KPMG assumption for ball-park reconciliation of budget land tax estimates and statutory land tax rates.

Table 2.2.2 also contains estimates of land tax revenues associated with each value category that we have deduced by making assumptions about the indicative value of each entity's land holding in each value category. For all value categories less than $1,000,000 we have assumed that the indicative value is the mid-point of the value category. For example, we have assumed that the indicative value of the taxable land held by the representative entity in the $800,000 - $899,999 category is $850,000. Using the thresholds and progressive rates specified for NSW in 2015 we deduce land tax revenue from this category to be $65,646,748. We then deduce an average land tax rate of 0.80% for that category. (i.e., 0.80% = $65,646,748/ [9,671x$850,000]). We make the following observations:

i. At least[3] 9,444 potentially taxable entities (holders of land that are not exempt from land tax) do not pay land tax because the value of their aggregated holdings fall below the $432,000 threshold;

ii. About 87% of land taxes are paid by the 40,355 entities with aggregated land holdings valued at over $1,000,000;

iii. The average rate of tax paid by entities with land holding of less than $1,000,000 ranges from 0.09% to 0.88%; and

iv. A weighted average of the tax rates for those that paid land taxes is about 1.2%.

Implications of current design

The current land tax system does have a relatively low economic cost – as measured by its excess burden (see inter alia KPMG Econtech's 2010 report to the Australian Treasury, KPMG, 2010). This is because it is levied on an immobile tax base. The total supply of land does not change in response to a change in the land tax rate, and thus land tax cannot affect the amount of land in use. Given these features, KPMG Econtech's 2010 report to the Australian Treasury estimated that for every dollar of revenue raised from the current land tax (averaged over all states), 6 cents of economic benefit is foregone.[4] This is low compared to other taxes on the property sector, such as CSDs.[5]

Although land taxes are relatively efficient there is scope to re-design the tax to make it more efficient and to ensure that the burden is not disproportionately increased on entities currently liable for land tax. The immobility of land means that a land tax can be designed so that decisions about the allocation of land are not affected by the tax. An efficient land tax will impact the value of the land it applies to, and not any other economic outcomes. When a land tax is applied, the pre-tax required rate of return on land (yield) must increase to cover the additional cost of the tax. However, because there is no change to the supply of land, this can only be achieved through a reduction in the value of land. If the tax is applied

3 Because of the gradation of the value categories some entities with holdings below the threshold value are captured in the $400,000 - $499,999 category.
4 That is, the average excess burden of the current land tax is estimated to be 6 cents per dollar of revenue raised. 'Consumer living standards' or 'consumer welfare' is the benefit derived by Australian households from their consumption, savings and leisure time.
5 As noted in KPMG (2010) the reported marginal excess burden of CSDs of 0.34 was likely to be an underestimate becase the impact of increased transactions was not modelled. In a subsequent study that took into account the transaction effects, KPMG (2011) estimated the marginal excess burden of CSDs to be 0.80.

uniformly across all land holders there will be no incentive to alter the usage of land. Put another way, the relative values of different parcels of land will not be distorted. Other things equal, an economically efficient land tax will not influence decisions about how land is used.[6]

To summarise, two features of the current land tax system have the potential to impact economic efficiency by influencing how land is used. Specifically,

- Certain land uses are **exempt** from land tax, such as land used for primary production or owner-occupied dwellings. This means that some industries will face lower rates of tax and have a cost advantage over industries facing higher rates. This will encourage the distribution of land towards those industries facing lower tax rates, resulting in an increase in the economic cost per dollar of land-tax revenue.

- Land tax is levied using a **progressive rate scale** where holdings up to a certain threshold are not taxed at all and where the rate of tax steps up above the premium threshold. The progressive rate is based on aggregate land holdings, which provides a disincentive to hold the optimal portfolio of land (size and/or value). This will raise the cost of production because businesses and landlords are not using technically efficient inputs of land in their production processes. Progressivity also weakens the revenue raising capacity of the tax, adding to the economic cost per dollar of land-tax revenue.

Our modelling of land taxes in KPMG-CGE is focussed on the efficiency aspects of such taxes. Although it is beyond the scope of this report to analyse distributional and equity issues, some comments on these issues are warranted. The Henry Tax Review highlighted these issues as follows:

"…owners of investment properties subject to land tax need an inducement to continue letting their property, as they could otherwise sell it to someone who wants to live in it themselves and not pay land tax. This inducement comes by effectively sharing some of the burden of the tax with the tenant, who may be a business or private renter. When this occurs, the incidence of land tax does not fall only on the holders of land — it also falls on the users of the land. A narrow land tax may therefore be relatively inefficient, and arguably, inequitable."
p. C2-2 Henry Tax Review (2009)

Therefore the current system of land tax may negatively impact on outcomes for renters to the extent that they bear the incidence of the existing land tax. This in turn depends on the prevailing supply and demand conditions in the market. Renters are also likely to be disadvantaged relative to owner-occupiers who are exempt from land tax under current arrangements.

The Henry Tax Review also argued that land tax is not a good instrument for achieving equity objectives because it is one of many assets that can be held in people's wealth portfolio. In particular, using exemptions to target equity objectives was unlikely to be effective because they reduce taxes for people without taking account of their means.

Land taxes have the potential to make housing more affordable to people who do not have taxable property in their portfolios and who are liquidity constrained in the short term (i.e., people with insufficient current savings to enter the property market). Imposition of a land tax lowers the value of land and, other things equal, the up-front cost of property; nevertheless, it also allows for the removal of stamp duties. The lower cost of entry into the property market will be offset over time by the annual land tax payments that the owner will make. This configuration of lower up-front costs and higher future tax payments may suit particular people who are at a stage in their income cycle where high up-front costs (e.g., deposits) are unaffordable.

KPMG-CGE modelling

In KPMG's Computable General Equilibrium model (KPMG-CGE), land tax is modelled as a tax on the value of land used in each industry. Land is a factor of production that is fixed in total supply. Thus, the modelling of land tax in KPMG-CGE can be characterised as a tax on a fixed factor. Consistent with economic theory, land taxes are relatively efficient (relatively low economic cost) in KPMG-CGE.

KPMG-CGE incorporates three types of land (agricultural, residential and industrial). Residential land is used by the Ownership of Dwellings sector. Agricultural land is used by the agricultural sectors and industrial land is used by the remaining sectors. On the supply side limited opportunities to transform land from one type to another are allowed in the long run. On the demand side industrial land is relatively highly substitutable between industries that use this type of land. Substitution between residential and other types of land is low, as is the degree of substitution allowed for agricultural land. Similarly, substitution between agricultural and other types of land is also limited.

Distortions arise from taxing different users of a particular type of land in different ways. For example, under the current land tax system in NSW, residential land used for a principal residence and land used by agricultural industries are both exempt from land tax.

In addition, the effective land tax rates in KPMG-CGE are different for different industries because of the effect of the land tax thresholds and the increasing marginal rates of land tax. Industries that tend to use aggregate land

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6 Other aspects of land tax reform, including assessments of fairness, are beyond the scope of this report. Assessments of the fairness of land tax reforms must be made in a broader context. Land is one of many income yielding assets that individuals and corporates can hold so the way the income tax system treats land income relative to other types of income is critically important in any assessment of fairness.

holdings of higher value will tend to have a higher effective rate of land tax. This introduces a point of differentiation in the model because industries with aggregate land holdings of lower value have a cost advantage over industries using aggregate holdings of higher value land.

This reflects the distortions that arise from taxing land based on aggregate holdings rather than on each individual parcel of land.

Table 2.2.3 sets out how we model land taxes in each of the four scenarios.

Table 2.2.3: Modelling Details for Each of the Four Property Tax Scenarios

Modelling Details for Each of the Four Property Tax Scenarios

Scenario 1
Minimalist

- Current land tax structure (i.e. with the current exemptions and progressivity) is modelled.
- Land tax rates adjust uniformly to ensure that the state budget balance remains unchanged in response to the abolition of stamp duty on conveyancing (i.e., land tax rates adjust to maintain state budget neutrality).
- Because we are dealing with sectors, rather than individual tax-paying entities, we don't model progressivity directly. The land tax rate that we infer for a sector is the average rate paid by the entities in that sector. In this scenario, progressivity is maintained by increasing the average rate for each sector by the same amount.
- In this simulation an increase in the average rate of land tax can be interpreted as an increase in the rate paid above the normal threshold and/or the rate paid above the premium threshold (it could also be interpreted as a decrease in one or both thresholds)

Scenario 2
ex-PPR

- The land tax structure is modified to remove the Principal Place of Residence (PPR) exemption. In NSW, the value of taxable residential zoned land is about 11% of the value of total residential zoned land. The value of taxable residential zoned land is about 47% of the value of total taxable land. We do not have data at the taxable entity level so cannot directly model how much residential land falls below the standard threshold and how much is above the premium threshold. If all residential land holders paid something close to the rate paid by the currently non-exempt residential land holders then this could amount to something like an additional $6b - $7b in land tax collections, which is more than 2.5 times the total amount of land taxes collected in 2013-14. We handle this by initialising the average rate of land tax paid by all residential land holders to the average rate paid by currently non-exempt residential land holders and then uniformly adjust all rates to ensure state budget neutrality.

Scenario 3
ex-PPR&Prog

- In addition to removing the Principal Place of Residence (PPR) exemption from the current land tax structure, in this scenario the progressivity in that structure is also removed. Effectively, when the land tax threshold is abolished, sectors which are not exempt from land tax now face the same land tax rate because the value of land used in these sectors no longer matters in determining their land tax liability. Therefore, we model the removal of the land tax threshold by insisting on a uniform tax rate on all non-exempt sectors.
- The uniform land tax rate is set at a level that ensures state budget neutrality.

Scenario 4
Broad

- As per scenario 3 with an additional modification to the land tax structure that removes the primary production exemption.
- All sectors in the economy now face a uniform land tax rate that is set at a level that ensures state budget neutrality.

2.3 Conveyancing stamp duty

Table 2.3.1: Conveyancing Stamp Duties in NSW

Threshold	Rate
$0 to $14,000	$1.25 for every $100 or part, (with $2 minimum)
$14,001 to $30,000	$175 plus $1.50 for every $100 or part , by which the dutiable value exceeds $14,000
$30,001 to $80,000	$415 plus $1.75 for every $100 or part, by which the dutiable value exceeds $30,000
$80,001 to $300,000	$1,290 plus $3.50 for every $100 or part, by which the dutiable value exceeds $80,000
$300,001 to $1m	$8,990 plus $4.50 for every $100 or part, by which the dutiable value exceeds $300,000
Over $1m	$40,490 plus $5.50 for every $100 or part, by which the dutiable value exceeds $1,000,000
Over $3m	Residential purchases over $3,000,000, $7.00 per $100 or part, by which the dutiable value exceeds $3,000,000.

Source: NSW Treasury: Interstate Comparison of Taxes 2014-15

In most Australian states, conveyancing stamp duty (CSD) is a transaction-based tax paid on the sale or transfer of land (including improvements) and on the sale or transfer of business assets.

States and territories levy a stamp duty on the transfer of both residential and commercial property. Different rates and thresholds apply depending on the property type, and concessions apply to first home buyers.

The rates and thresholds applicable in NSW are presented in the table below. Compared to the other states and territories, NSW has the highest CSD rate at its highest threshold (over $3m).

As reported in table 2.1.1 the NSW government collected about $3.74 billion in transfer duties in 2009-10. About 82% of these duties were collected from residential transfers and about 18% from non-residential transfers. Although NSW CSD revenues in 2013-14 were around 62% higher than in 2009-10 the proportion of residential to non-residential CSD revenue was broadly similar (i.e., about 19% and 81% for residential and non-residential transactions respectively).

Economics of conveyancing stamp duties

CSD can be conceptualised as a tax on two types of activity: first, investment (capital creation); and second, transactions (turnover of existing assets).

Investment

CSD are levied on the value of improvements to land (buildings and other structures). These duties raise the cost of investing in new residential and non-residential structures. Unlike land, capital is highly mobile in the longer term. Investment in structures is sensitive to the post-tax rate of return. In the short term stamp duties reduce the post-tax returns to structures. In the longer term the supply of funds can more freely move between industries and countries in search of the best (after tax) return. Thus, in the long run, the required post-tax rate of return on capital is effectively fixed on world capital markets. The economic cost of taxing structures through CSDs is that there will be less investment in structures than would be the case in the absence of CSDs.

For businesses, the higher cost of capital also shifts incentives away from using structures and towards using other factors of production. For households purchasing residential buildings, the increased cost of investment will also lower their housing consumption in favour of other forms of consumption.

Transactions

Conveyancing duties are also a tax on transactions. This introduces inertia into the economy because it discourages households and businesses from re-allocating assets from low value to high value use. The optimal location and physical structures required by a firm is likely to change over its life-cycle. Similarly, changes in technology, preferences and markets will change the optimal use of land and structures. Similar arguments can be made for households. The optimal location and dwelling structure for a household may change over the course of a family life-cycle. Changes in preferences (tastes) may also influence the optimal location and dwelling structure. In addition, the optimal location for a household is likely to be influenced by the availability of employment opportunities. Stamp duties may reduce the extent to which firms and households are willing to relocate, even when it would otherwise be beneficial for them to do so.

Van Ommeren (2008) reviews a selection of studies that find a significant negative impact on labour mobility from recurrent property taxes such stamp duty. Hilber and Lyytikainen (2012) also find similar effects on labour mobility from the real estate transfer tax in the UK. For Australia, Davidoff and Leigh (2013) estimate that a 10% increase in stamp duty lowers housing turnover by 6% over 3 years. Reducing housing mobility can reduce labour productivity by discouraging workers from taking up higher paying jobs elsewhere. Reducing housing turnover may decrease the efficiency of the housing stock by discouraging turnover that would otherwise occur; for instance, by discouraging young families to upsize their housing and by discouraging retiree households from downsizing (Glaeser and Luttmer, 2003).

As with land taxes our modelling work for stamp duties is focused on the efficiency aspects of the tax. Although it is beyond the scope of this report to analyse distributional and equity issues, we provide some general comments on this topic before turning to the details of how we model stamp duties. Other things equal, the removal of stamp duties, which are a tax on investment, will stimulate the supply of housing structures and put downward pressure on house prices. The empirical evidence on which of these two impacts will dominate is limited and is likely to be dependent on prevailing demand and supply conditions in the housing market.

Apart from transactions associated with new entrants to the market, a reasonable working assumption is that the majority of property transactions will be matched. That is, within a narrow time frame a seller of a property will also be a buyer of another property. For people already in the market the distributional consequences of stamp duties are likely to be dominated by the frequency of moving. Those that have to move frequently for work or family reasons will bear a bigger tax burden than those that move less frequently. This point is summarised in the Henry Tax Review as follows:

> *"Stamp duty is also inequitable as people who move more regularly – such as those needing to change homes for work – pay more tax than those who do not."*
> *p. C2-3 Henry Tax Review (2009)*

Because property is just one component of people's consumption bundle and one asset in their wealth portfolio, stamp duties are not particularly effective at targeting equity objectives. Even though the amount of stamp duty collected increases with the value of the property transacted, the tax falls disproportionately on people that have a preference for property. That is, it falls on people who allocate a larger share of their income on property rather than on people with the means to pay.

Stamp duties also have the potential to reduce access to property for people that are liquidity constrained. Insofar as stamp duties increase the up-front costs of accessing property, people that are credit constrained will be disadvantaged (see Henry Tax Review (2009), p. C2-3). New entrants to the market, particularly those at the early stages of their income cycle, are likely to be over-represented in this category.

The discussion above and in Section 2.2 of the distributional impacts of land taxes and stamp duties is equivocal due to the opposing effects on income distribution that each of these taxes separately create. If we consider the distributional effects of switching from stamp duty to land tax, the discussion becomes even more equivocal. It should be noted that it is not possible for us to make a definitive statement about the distributional impacts of switching from stamp duty to land tax beyond outlining the separate distributional effects of each tax.

KPMG-CGE modelling

KPMG-CGE models transfer duty on residential assets and business assets separately. For residential assets we have attempted to distinguish transfer duties collected on new assets from transfer duties collected on the turnover of existing assets. Transfer duties on new assets are modelled as a tax on investment by the Residential Building Construction sector. Transfer duties on the turnover of existing residential assets are modelled as a production tax on the Non-Residential Property Operators and Real Estate Services sector.

Commercial CSD are modelled as a tax on investment by the Non-residential Building Construction sector.

3. Overview of KPMG-CGE

The simulations contained in this report are run using a special purpose version of KPMG-CGE. The previous section described specific details about the modelling of land taxes and CSD in KPMG-CGE. In this section we provide an overview of KPMG-CGE before describing the modifications made to the model for this project and the key assumptions that we have adopted.

KPMG-CGE models the economy as a system of interrelated economic agents operating in competitive markets. Economic theory is used to specify the behaviour and market interactions of economic agents, including consumers, investors, producers and governments operating in domestic and foreign goods, capital and labour markets. Defining features of the theoretical structure of KPMG-CGE include:

- Optimising behaviour by households and businesses in the context of competitive markets with explicit resource constraints and budget constraints.

- The price mechanism operates to clear markets for goods and factors such as labour and capital (i.e. prices adjust so that supply equals demand); and

- At the margin, costs are equal to revenues in all economic activities.

The key data input used by KPMG-CGE is an input-output (IO) table which quantifies the flows of goods and services between producers and various users (e.g., intermediate inputs to other producers, inputs to capital creators, households, governments and foreigners) and the flows associated with primary factor inputs (i.e., labour, capital, land and natural resources). In KPMG-CGE the IO database is combined with the model's theoretical structure to quantify sophisticated economic behavioural responses, including to:

- price and wage adjustments driven by resource constraints;

- price and tax and/or government spending adjustments driven by budget constraints;

- allow for input substitution possibilities in production (e.g., allowing the combination of labour, capital, and other inputs required to produce a particular output to vary in response to relative price changes);

- capture a wide set of economic impacts driven by the responses of consumers, investors, foreigners and other agents to changes in prices, taxes, technical change and taste changes.

KPMG-CGE's theoretical structure and database facilitates detailed modelling of state and federal government fiscal accounts and balance sheets, including the accumulation of public assets and liabilities. Detailed government revenue flows are modelled, including a range of direct and indirect taxes, and income from government enterprise. Government spending includes public sector consumption, investment and the payment of various types of transfers (such as pensions and unemployment benefits).

3.1 Non-standard version of KPMG-CGE relevant to this project

Since the focus of this project is on NSW property tax reform we have developed KPMG-RCGE[7], a special version of KPMG-CGE that divides the Australian economy into two fully integrated economic regions; namely, NSW and the Rest of Australia (ROA). In KPMG-RCGE, each of the two regions is modelled at the same level of detail as the national economy in KPMG-CGE. Full integration between the two regional economies required the modelling of inter-state flows of goods and services, factors of production and population. The modification of the theoretical structure of KPMG-CGE to model the NSW and ROA economies separately also required a disaggregation of the KPMG-CGE National database to separately quantify the sales and cost structure of the two regional economies. In KPMG-RCGE the database for each of the NSW and ROA economies is as detailed as that for the National economy in KPMG-CGE with an added dimension capturing trade flows between the two regions.

KPMG-CGE models the economy as a system of interrelated economic agents operating in competitive markets. Economic theory is used to specify the behaviour and market interactions of economic agents, including consumers, investors, producers and governments operating in domestic and foreign goods, capital and labour markets.

7 The "R" in KPMG-RCGE stands for regional, indicating that the model used is a regional version of KPMG's CGE model.

3.2 Model setup

For each of the two regional economies in KPMG-RCGE 45 sectors are identified with each producing one good or service. KPMG-RCGE contains many more variables than equations. The model can determine values for as many variables as it has equations. In running the model we must select the sub-set of variables that the model will be allowed to determine (endogenous variables) with the remainder set outside the model (exogenous variables). The set of exogenous variables will include the policy variable of interest. In these simulations the policy variable is the rate of conveyancing stamp duty. In the simulations reported we set the value of this rate to zero (for NSW only in the first set of simulations and then for NSW and the Rest of Australia for the second set of simulations). The values of all other exogenous variables are assumed to remain unchanged from the baseline. The baseline is a characterisation of the structure of the economy in the absence of the policy shock. The choice exogenous variables and the nature of the baseline determine the economic environment (or economic context) that is assumed appropriate for analysing the policy shocks. Below, we discuss each of these choices in turn.

Economic environment

Tax policy reforms should be assessed in a long run context. This does not mean that short term structural adjustment issues emanating from a tax policy change are not important. Rather, it is a recognition that tax policy settings are designed to be stable and not subject to frequent change and that any proposed reforms must have demonstrable long term benefits. Although beyond the scope of this study, a policy change that is warranted by potential long run benefits can be designed to minimise short term adjustment costs. Our choice of exogenous variables is designed to configure KPMG-RCGE so that it represents the behaviour of the economy in the long run.

The key settings include:

- the economy-wide after-tax rate of return on capital is fixed at its baseline value;
- sectoral investment-capital ratios are held fixed at their baseline values;
- the number of working-age people is held fixed at the number in the baseline;
- the average propensity to consume out of household disposable income is held fixed at its baseline value;
- government budget balances are held fixed at their baseline values;
- technical change and consumer preferences are held fixed at their baseline values; and
- tax rates and government policy settings, other than conveyancing stamp duty rates and land tax rates, are held fixed at their baseline values.

Baseline

We have chosen to use the snapshot of the economy provided by the 2009-10 input-output database as our baseline. As explained in section 2.1 our assessment was that the configuration of property taxes in 2009-10 was more representative than in more recent years. A similar argument could be mounted for the structure of the economy. The impact of the mining boom and the terms of trade on the structure of the economy is more pronounced in recent years. Another compelling reason for using 2009-10 as our baseline is that we have a consistent set of data obtained from the ABS that disaggregates CSD and land taxes across sectors.

Tax policy reforms should be assessed in a long run context. This does not mean that short term structural adjustment issues emanating from a tax policy change are not important. Rather, it is a recognition that tax policy settings are designed to be stable and not subject to frequent change and that any proposed reforms must have demonstrable long term benefits.

4. Simulation results

The following subsections report the results from our simulations. We deal first with the results of the simulations where NSW alone implements the property tax reforms. Subsection 4.2 then examines the results where all the states implement the property tax reforms in concert. A notable feature of the results is that the elimination of CSD dominates the results and, from an economic efficiency point of view, the impacts of the various land tax configurations are similar, particularly at the macroeconomic level.

4.1 NSW-only property tax reform

Table 4.1.1 reports headline macroeconomic variables for the four simulations where NSW alone abolishes CSD. The numbers in this table should be interpreted as deviations from the baseline in the long run. For Household Consumption and Gross State Product (GSP) the values refer to 2014-15 dollars per household. For example, in scenario 1 we are projecting that in the long run Household Consumption per household, expressed in 2014-15 dollars, will be $1,451 higher than in the baseline (in the absence of the policy change). It is important to recognise that this represents a permanent increase in consumption per household. Analogously, in scenario 4 we are projecting that in the long run GSP per household, expressed in 2014-15 dollars, will be $1,684 higher than in the baseline.

The results in table 4.1.1 support the proposition that abolishing CSD is beneficial to the NSW economy. The impacts on the Rest of Australia (ROA) are generally negative but small in magnitude. This reflect the competitive advantage that NSW gets from unilaterally reforming its property tax system. The macroeconomic gains projected for NSW are not particularly sensitive to the configuration of the land taxes.

Table 4.1.1: Selected Macro Results – NSW-only Property Tax Reform

	Scenario 1 Minimalist	Scenario 2 ex PPR	Scenario 3 ex PPR & Prog.	Scenario 4 Broad
NSW				
Household Consumption[1]	$1,451	$1,421	$1,437	$1,444
Gross State Product[1]	$1,556	$1,658	$1,681	$1,684
Employment	9,743	9,699	9,819	9,856
Rest of Australia				
Household Consumption[1]	$22	$1	-$2	-$1
Gross State Product[1]	-$67	-$110	-$116	-$115
Employment	-623	-1,054	-1,110	-1,094

Source: ABS and KPMG-RCGE.

Notes:
(1) Units are 2015 dollars per projected number of households in 2015.

The first-round effect of abolishing CSD is to decrease the NSW state budget balance. However, the consequent increase in economic activity offsets this as the governments' tax revenue base expands (e.g., payroll tax base) and as its counter-cyclical outlays contract. In the simulations land taxes are used as the instrument to enforce state budget neutrality.

Table 4.1.2 summarises what happens to the average rate of land tax in NSW across the 4 simulations. It is important to note that these land tax rates are averaged across entities that pay land tax. In the baseline the average rate of land tax, for those that pay land tax, is 1.2%. In scenario 1 the existing land tax structure is maintained (i.e., we maintain existing exemptions and

progressivity) but the rates are allowed to adjust uniformly to ensure state budget neutrality is preserved. Scenario 1 makes clear the importance of the Principle Place of Residence (PPR) exemption. Under scenario 1, for both the go-it-alone and co-ordinated policy simulations, the increase in the average rate of land tax is large because only about 17% of land (by value) is taxable. The higher land tax rates recorded for NSW in the simulations where all states adopt the policy reform mainly reflects the lower level of economic activity for NSW in the later simulations, which results in less expansion in that state's tax base. The results for scenario 4 confirm that a broad based land tax, covering all landholdings, can maintain state budget neutrality with rates that are lower than required in those

structures that allow for exemptions. The removal of progressivity in land taxes, as we move from scenario 2 to scenario 3, has little impact on the average rate of land tax. Because our modelling of the progressivity component of land taxes is not detailed[8] our results for scenario 3 are driven by compositional changes and are likely to understate the impact of removing progressivity.

More detailed macroeconomic and sector results obtained from the four NSW-only simulations are presented in tables 4.1.3 and 4.1.4. The results reported in these tables are percentage deviations from baseline values of variables. For example, in scenario 2 NSW Gross State Product (GSP) is 1.02% higher than in the baseline.

Table 4.1.2: Average Land Tax Rates[1] – NSW-only Property Tax Reform

	Baseline	Scenario 1 Minimalist	Scenario 2 ex PPR	Scenario 3 ex PPR & Prog.	Scenario 4 Broad
NSW adopts policy					
Rate of Land Tax (average)	1.2%	5.1%	1.6%	1.6%	1.3%

Notes:
(1) Average rate for those entities that do pay land tax.

The macroeconomic results in table 4.1.3 also show little variation across the scenarios. The abolition of CSD gives investment a boost and reduces the cost of dwelling services, which is reflected in the lower CPI. The results also show a boost to after-tax real wages which impacts competitiveness and facilitates a switch of economic activity away from exporting and towards investment and consumption.

Table 4.1.4 reports the simulation results for value added at a sectoral level. The sectors that benefit most from the abolition of CSD in NSW are Residential Dwellings, Rental, Hiring & Real Estate Services and Construction. As explained earlier, CSD on transactions of new dwellings are modelled as taxes on investment in the Residential Building Construction sector and CSD on transactions of existing Dwellings are modelled as production taxes in the Rental, Hiring & Real Estate Services sector. The abolition of CSD reduces costs in the Rental, Hiring & Real Estate

Services and Construction sectors. The Residential Dwelling sector is very capital intensive and the main inputs that the sector uses to expand its capital stock are sourced from the Rental, Hiring & Real Estate Services and Construction sectors. The Residential Dwellings sector uses inputs from the Construction sector to maintain, modify or add structures. Inputs from the Rental, Hiring & Real Estate Services sector add to the capacity of the Residential Dwellings sector by best matching the requirements of households for dwelling services with the available stock of dwellings. Implicit in this modelling is that households can change the amount of dwelling services that they use by changing their investment in structures or by investing in Rental, Hiring & Real Estate Services to move to a more appropriate residence. With the costs of its two key inputs lowered by the abolition of CSD, the price of Residential Dwelling services decrease resulting in an increase in demand and an expansion in the sector.

8 As explained in section 2, we cannot model progressivity directly because we do not have information about the land holdings at the entity level.

Table 4.1.3: Macro Impacts of NSW Replacing Conveyancing Duties with Land Taxes: % deviations from the basecase.

	Scenario 1 Minimalist		Scenario 2 Ex PPR		Scenario 3 Ex PPR & Prog		Scenario 4 Broad	
	NSW	**Rest of Australia**	**NSW**	**Rest of Australia**	**NSW**	**Rest of Australia**	**NSW**	**Rest of Australia**
Household Consumption	1.48%	-0.01%	1.45%	-0.03%	1.46%	-0.03%	1.47%	-0.03%
Investment	2.39%	-0.12%	2.52%	-0.15%	2.55%	-0.15%	2.55%	-0.15%
General Government	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Foreign Exports	-1.52%	-0.49%	-1.19%	-0.51%	-1.19%	-0.52%	-1.20%	-0.52%
less Foreign Imports	0.70%	-0.01%	0.79%	-0.04%	0.80%	-0.04%	0.81%	-0.04%
Gross State Product	0.96%	-0.07%	1.02%	-0.09%	1.04%	-0.10%	1.04%	-0.09%
Employment	0.27%	-0.01%	0.27%	-0.01%	0.27%	-0.01%	0.27%	-0.01%
Real after-tax wage	1.79%	-0.05%	1.78%	-0.09%	1.81%	-0.09%	1.81%	-0.09%
CPI	-0.71%	0.12%	-0.62%	0.12%	-0.63%	0.13%	-0.62%	0.13%

Source: KPMG-RCGE.

Table 4.1.4: Impacts on Industry Value Added of NSW Replacing Conveyancing Duties with Land Taxes: % deviations from the basecase.

	Scenario 1 Minimalist		Scenario 2 Ex PPR		Scenario 3 Ex PPR & Prog.		Scenario 4 Broad	
	NSW	Rest of Australia	NSW	Rest of Australia	NSW	Rest of Australia	NSW	Rest of Australia
Agriculture, Forestry & Fishing	-0.24%	-0.12%	-0.17%	-0.13%	-0.17%	-0.13%	-0.21%	-0.13%
Mining	-0.61%	-0.37%	-0.35%	-0.39%	-0.32%	-0.40%	-0.26%	-0.40%
Manufacturing	-0.22%	-0.09%	-0.02%	-0.12%	-0.01%	-0.12%	-0.02%	-0.12%
Electricity, Gas, Water & Waste Services	0.65%	-0.02%	0.77%	-0.05%	0.80%	-0.06%	0.81%	-0.06%
Construction	1.37%	-0.03%	1.48%	-0.08%	1.51%	-0.08%	1.51%	-0.08%
Wholesale Trade	0.30%	-0.08%	0.43%	-0.11%	0.44%	-0.11%	0.43%	-0.11%
Retail Trade	0.53%	-0.01%	0.61%	-0.03%	0.62%	-0.04%	0.62%	-0.03%
Accommodation & Food Services	0.22%	-0.05%	0.37%	-0.07%	0.40%	-0.07%	0.40%	-0.07%
Transport, Postal & Warehousing	-0.02%	-0.08%	0.18%	-0.10%	0.19%	-0.11%	0.18%	-0.11%
Information Media & Telecommunications	0.57%	-0.04%	0.69%	-0.06%	0.71%	-0.07%	0.71%	-0.06%
Financial & Insurance Services	0.92%	0.00%	0.96%	-0.04%	0.97%	-0.04%	0.98%	-0.04%
Rental, Hiring & Real Estate Services	2.40%	-0.01%	2.54%	-0.06%	2.57%	-0.07%	2.57%	-0.07%
Professional, Scientific & Technical Services	0.58%	-0.07%	0.71%	-0.10%	0.72%	-0.10%	0.72%	-0.10%
Administrative & Support Services	0.48%	0.00%	0.62%	-0.02%	0.62%	-0.02%	0.62%	-0.02%
Public Administration & Safety	-0.03%	0.03%	-0.01%	0.02%	-0.01%	0.02%	-0.01%	0.03%
Education & Training	0.03%	-0.03%	0.12%	-0.04%	0.11%	-0.04%	0.10%	-0.04%
Health Care & Social assistance	0.21%	0.02%	0.31%	0.01%	0.30%	0.01%	0.29%	0.01%
Arts & Recreation Services	0.38%	0.01%	0.47%	-0.01%	0.49%	-0.01%	0.49%	-0.01%
Other Services	0.43%	0.01%	0.63%	-0.02%	0.62%	-0.03%	0.62%	-0.02%
Residential Dwellings	4.26%	-0.05%	3.76%	-0.08%	3.78%	-0.09%	3.80%	-0.08%

Source: KPMG-RCGE.

4.2 Co-ordinated property tax reform

Table 4.2.1 summarises the headline macroeconomic results for the four simulations where all states abolish CSD and implement alternative land tax structures to maintain budget neutrality. As with the NSW-alone results, there is very little variation across the simulations for NSW and ROA. In these simulations the differences between the results for NSW and ROA are not very large. On the basis of the consumption metric NSW benefits more from a co-ordinated approach to property tax reform than from the go-it-alone approach. This is because NSW benefits from the expansion in ROA. The NSW employment responses are lower under the co-ordinated policy reform approach because NSW cannot so easily attract resources, including labour, from ROA. Even though the NSW employment response is smaller under the co-ordinated policy approach the consumption response is greater mainly because real after-tax wages are stronger (see table 4.2.3).

Table 4.2.1: Selected Macro Results – All States Reform Property Taxes

	Scenario 1 Minimalist	Scenario 2 ex PPR	Scenario 3 ex PPR & Prog.	Scenario 4 Broad
NSW				
Household Consumption[1]	$1,516	$1,544	$1,565	$1,562
Gross State Product[1]	$1,522	$1,590	$1,621	$1,605
Employment	9,484	9,243	9,407	9,360
Rest of Australia				
Household Consumption[1]	$1,630	$1,591	$1,595	$1,597
Gross State Product[1]	$1,664	$1,677	$1,665	$1,698
Employment	23,350	22,719	22,759	22,791

Source: ABS and KPMG-RCGE.

Notes:
(1) Units are 2015 dollars per projected number of households in 2015.

Table 4.2.2 summarises what happens to the average rate of land tax in NSW across the 4 simulations where all states reform property taxes. In these simulations the average rates of land tax for NSW are higher than in the simulations where NSW implemented the policy on its own. This mainly reflects the lower level of economic activity for NSW in the later simulations, which results in less expansion in that state's tax bases.

Table 4.2.2: Average Land Tax Rates for NSW(1) – All States Reform Property Taxes

	Baseline	Scenario 1 Minimalist	Scenario 2 ex PPR	Scenario 3 ex PPR & Prog.	Scenario 4 Broad
All states adopt policy					
Rate of Land Tax (ave)	1.2%	5.4%	1.7%	1.7%	1.4%

Source: ABS and KPMG-RCGE.

Notes:
(1) Average rate for those entities that do pay land tax.

9 The differences in the employment numbers reflect largely differences in the scale of the two regions. NSW accounts for about 30% of national employment and ROA accounts for about 70%.

Table 4.2.3: Macro Impacts of All States Replacing Conveyancing Duties with Land Taxes: % deviations from the basecase.

	Scenario 1 Minimalist		Scenario 2 Ex PPR		Scenario 3 Ex PPR & Prog.		Scenario 4 Broad	
	NSW	Rest of Australia	NSW	Rest of Australia	NSW	Rest of Australia	NSW	Rest of Australia
Household Consumption	1.47%	1.64%	1.50%	1.60%	1.52%	1.61%	1.51%	1.61%
Investment	2.26%	2.21%	2.36%	2.25%	2.40%	2.24%	2.38%	2.28%
General Government								
Exports	-3.00%	-2.00%	-2.84%	-1.91%	-2.83%	-1.94%	-2.84%	-1.90%
less Imports	0.73%	0.70%	0.83%	0.73%	0.84%	0.72%	0.83%	0.74%
Gross State Product	0.87%	0.93%	0.91%	0.94%	0.93%	0.93%	0.92%	0.95%
Employment	0.26%	0.29%	0.25%	0.28%	0.26%	0.29%	0.26%	0.29%
Real after-tax wage	1.74%	1.96%	1.70%	1.91%	1.72%	1.91%	1.72%	1.92%
CPI	-0.32%	-0.77%	-0.19%	-0.69%	-0.20%	-0.71%	-0.19%	-0.68%

Source: KPMG-RCGE.

Table 4.2.4: Impacts on Industry Value Added of All States Replacing Conveyancing Duties with Land Taxes: % deviations from the basecase.

	Scenario 1 Minimalist		Scenario 2 Ex PPR		Scenario 3 Ex PPR & Prog.		Scenario 4 Broad	
	NSW	Rest of Australia	NSW	Rest of Australia	NSW	Rest of Australia	NSW	Rest of Australia
Agriculture, Forestry & Fishing	-0.60%	-0.44%	-0.58%	-0.43%	-0.58%	-0.44%	-0.66%	-0.55%
Mining	-1.73%	-1.06%	-1.62%	-0.98%	-1.58%	-1.00%	-1.56%	-0.90%
Manufacturing	-0.59%	-0.26%	-0.47%	-0.19%	-0.45%	-0.21%	-0.47%	-0.18%
Electricity, Gas, Water & Waste Services	0.66%	0.65%	0.78%	0.70%	0.82%	0.69%	0.81%	0.73%
Construction	1.33%	1.54%	1.41%	1.56%	1.44%	1.55%	1.43%	1.59%
Wholesale Trade	0.10%	0.20%	0.21%	0.25%	0.22%	0.23%	0.21%	0.25%
Retail Trade	0.52%	0.51%	0.62%	0.54%	0.63%	0.53%	0.63%	0.56%
Accommodation & Food Services	0.11%	0.23%	0.25%	0.29%	0.29%	0.28%	0.29%	0.32%
Transport, Postal & Warehousing	-0.29%	-0.03%	-0.14%	0.03%	-0.13%	0.01%	-0.14%	0.04%
Information Media & Telecommunications	0.52%	0.58%	0.64%	0.63%	0.66%	0.61%	0.65%	0.65%
Financial & Insurance Services	1.13%	1.27%	1.15%	1.26%	1.17%	1.26%	1.17%	1.27%
Rental, Hiring & Real Estate Services	2.79%	2.90%	2.90%	2.94%	2.93%	2.92%	2.92%	2.95%
Professional, Scientific & Technical Services	0.48%	0.43%	0.56%	0.47%	0.58%	0.46%	0.56%	0.49%
Administrative & Support Services	0.46%	0.57%	0.56%	0.62%	0.57%	0.60%	0.56%	0.63%
Public Administration & Safety	0.01%	0.06%	0.02%	0.06%	0.01%	0.06%	0.01%	0.06%
Education & Training	-0.11%	0.00%	-0.03%	0.06%	-0.04%	0.04%	-0.04%	0.06%
Health Care & Social assistance	0.23%	0.22%	0.34%	0.26%	0.34%	0.25%	0.32%	0.27%
Arts & Recreation Services	0.43%	0.48%	0.54%	0.53%	0.56%	0.51%	0.56%	0.54%
Other Services	0.39%	0.46%	0.57%	0.54%	0.57%	0.51%	0.55%	0.56%
Residential Dwellings	4.18%	6.24%	3.69%	5.74%	3.72%	5.84%	3.73%	5.69%

Source: KPMG-RCGE.

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• Public policy and advocacy.
• Reducing complexity to manage risk
• Empowering business through connections, knowledge and expertise.

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February 2016