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Tax Insights

NSW: Proposed Property Tax

Snapshot

On 17 November 2020, as part of the NSW Budget, the Treasurer announced a proposal to introduce a property tax regime that would provide taxpayers with a choice between paying a known amount of stamp duty at the time of purchase of a property, or an annual property tax charge instead. The proposed new property tax is intended to replace transfer duty on properties over a long period of time.

The conceptual framework for the new property tax would broadly consist of the following:

- A fixed amount plus an annual rate applied to the unimproved land value of an individual property (similar to that of council rates);
- The property tax annual rate would be subject to change based on increases to property values, or through increases to the rate at which the property tax is imposed;
- If the buyer chooses at the time of purchase to pay the property tax, it would replace the applicable stamp duty and land tax (if applicable);
- Once the property is subject to the property tax, the property tax obligation stays with the property and subsequent purchasers cannot opt out;
- If stamp duty has been paid on the existing property, the property tax will not apply to the property;
- The rate of the property tax will vary between commercial, owner occupied, residential and primary production land with lower rates applying to owner occupied residential and primary production land; and
- There will be an initial maximum price threshold for properties which will qualify for the new property tax, however, 80% of existing residential properties should be eligible from day one.

The Treasurer stated that this will provide stimulus and impetus for the people wanting to move, change jobs, or switch careers, upsize or downsize to match family size without the burden of stamp duty imposed on a property purchase and will provide an economic boost to the economy.

Whilst the proposed reform will be subject to public consultation until 15 March 2021, there are a number of interesting issues that taxpayers should consider before making a decision to opt into the property tax, if the legislation as ultimately passed mirrors what is proposed.

Accordingly, the comments below are necessarily general in nature, pending the consultation process and the finalisation of the Government policy.

Initial impact and concepts

Initial impact on residential property only

Due to the proposed initial maximum price threshold to fall within the property tax regime, commercial property, large parcels of land and high value property will remain in the stamp duty/land tax regime. This means both direct and indirect (landholder duty) transfers of these types of land will be subject to stamp duty. It is unclear when the property tax regime will be extended to property valued above the initial threshold, but this will likely be decided once Treasury has reviewed the revenue generated as the property tax regime progresses.

Opting in has a permanent impact

Under the proposed property tax, once a buyer opts in, the property then forever remains within the property tax regime. This removes any choice for a future purchaser. This has the potential to create a two-tier property regime and may impose an uncertainty on future property sales.

Use of unimproved value

The proposed property tax, like land tax, uses the unimproved value of land. This is the land value without improvements which is less than what stamp duty uses, being the market value of land and buildings. However, the unimproved value is determined by a valuation methodology that uses a concept of "comparative sales". This means that a sale of nearby property can alter a property's unimproved value. Even a purchaser's own acquisition can impact the unimproved value, which is an outcome that has occurred under the current land tax regime.

As an example, say there are a number of neighbouring vacant blocks of land that are similar, with all having an unimproved value of $500,000. A purchaser buys one block from the vendor for $1 million. Under the comparative sales methodology, that acquisition would be counted to likely increase the unimproved value for the subsequent property tax year for all neighbouring vacant blocks as well as the subject block.

Issues a taxpayer should consider when deciding to opt into the proposed property tax

The decision to opt into the proposed property tax may appear to be a simple numerical analysis in terms of a larger up front stamp duty cost vs a smaller annual property tax. However, there are other factors that a taxpayer may wish to consider before opting in if the property tax is implemented as proposed.

Affordability of annual property tax

Whether to opt into the proposed property tax regime may depend on the nature of the property. As an example, say there were two identical sites with the same unimproved value, with one having 100 apartments and the other a house. Each of the apartments will generally, have a lower unimproved value as the unimproved value is effectively spread across all apartments on the land. The site with the house will generally have a higher unimproved value as there is only one owner. As a result, this may impact on the affordability of a taxpayer to pay the annual property tax.

Likely changes in unimproved value

When deciding to opt into a property tax regime, it is important to consider the current unimproved value and potential events that may increase its value over time. Areas that have development opportunities may be susceptible to larger increases in unimproved value as a result
of the comparative sales methodology. We have seen large increases in unimproved values of land in the past where there is increased demand as a result of proposed infrastructure development. However, this concern may be balanced out if the acquisition is of an apartment or a house (see above).

Remaining in stamp duty/land tax regime may have benefit

In some cases, remaining within the stamp duty/land tax regime may have benefits for taxpayers, despite the upfront cost. For example, under the stamp duty legislation, the deceased estates exemption will continue to apply providing more efficient estate planning. Further, the land tax exemptions like the principal place of residence and primary production exemptions can still apply to the property.

Further, as the costs of the annual property tax become clearer in terms of the amounts and increases (both to the property value and the rate at which it is imposed), there may be advantages in remaining within the stamp duty regime to provide a seller with a greater pool of buyers. This would depend on how long a purchaser may wish to hold the property or the type of property (house versus apartment).

Conclusion

It should be noted that public consultation is being sought until 15 March 2021 and there may be changes to what is proposed. However, while a taxpayer may ultimately decide to opt into the property tax regime, if implemented as proposed, it is recommended that before locking a property into one particular option, taxpayers take a step back and consider their current and future intentions for the property to ensure they make the right choice for themselves and their priorities.

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