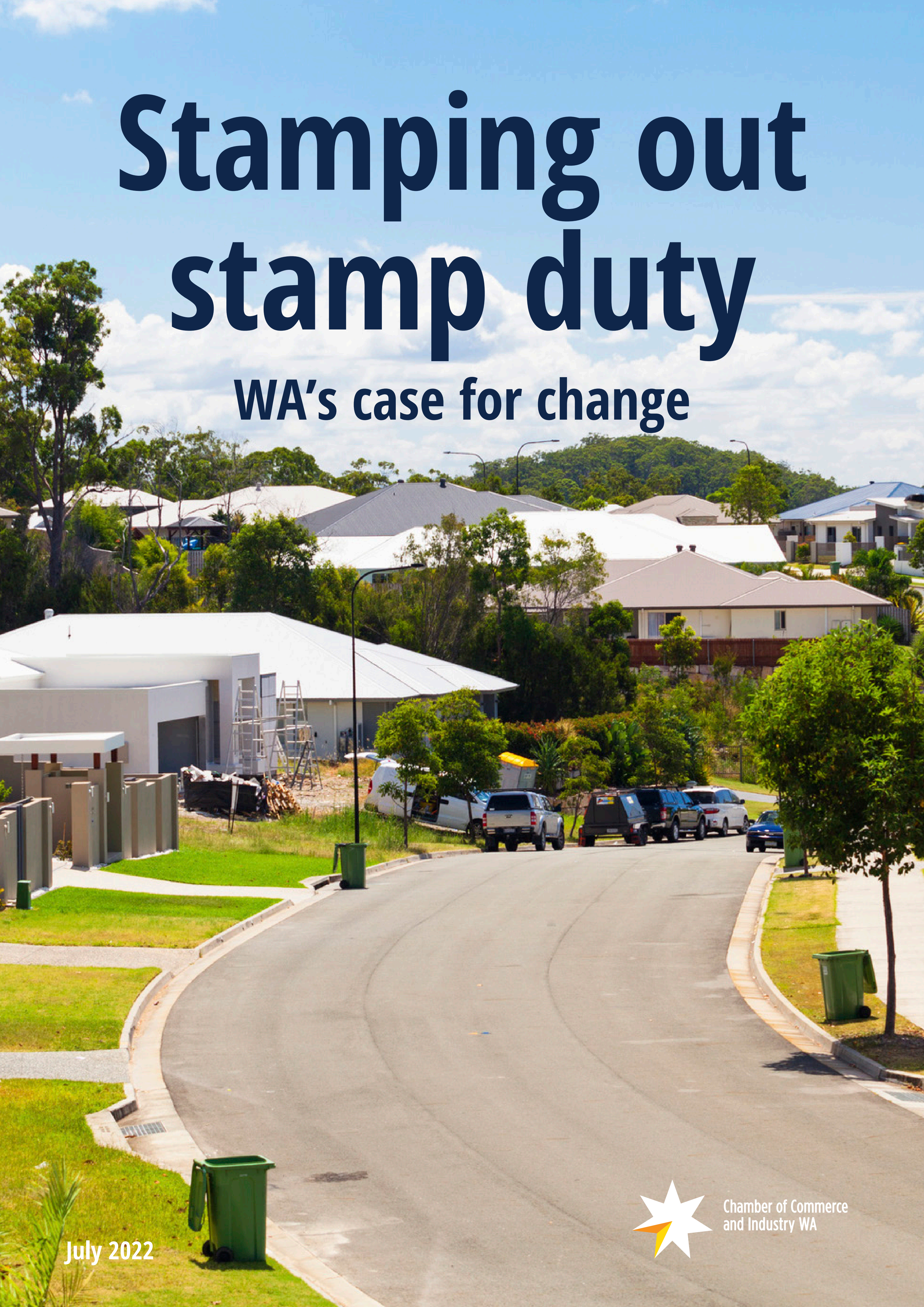
Stamping out stamp duty

WA's case for change



Chamber of Commerce and Industry WA

July 2022

Chamber of Commerce and Industry WA

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Executive Summary

As Western Australia (WA) emerges from COVID-19, attracting skilled workers and international capital will be critical to powering sustainable, long term economic growth. While the easing of border restrictions has removed many of the physical barriers preventing WA businesses from tapping into international markets, global competition for both labour and capital has intensified.

The upshot is that it's now tougher than ever for local businesses to attract and retain the talent and investment they need, posing key risks to WA's efforts to diversify.

We do not, however, have to accept our economic fate.

Those economies that undertake bold economic reform will separate themselves from the rest and prosper. To this end, every measure to inject dynamism and competitiveness into our economy must be taken.

One such measure that CCIWA has called for is the abolition of stamp duty on property transfers, and the introduction of a fairer, broad-based replacement tax on the property's Gross Rental Value. CCIWA strongly believes this reform will generate greater economic and social prosperity over the long term - a key objective of our policy development strategy.

Why? The benefits of reform are widespread

First, abolishing stamp duty would make it easier for people to move near jobs, family and schools, or to downsize later in life. With less commuting, there are benefits for the environment, and for business there are benefits in having a more mobile workforce.

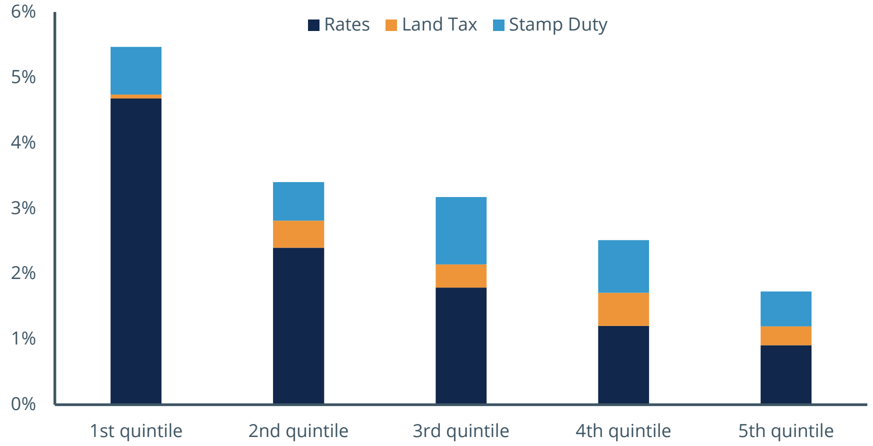
Enabling a more productive and efficient labour force will deliver broad economic benefits and help to ensure WA's economy remains globally competitive in the years to come.

Abolishing stamp duty would also lower a key barrier to entering the regional housing market, helping to address concerns that currently exist with FIFO workforces and housing affordability.

More broadly, an increase in housing turnover would stimulate household consumption typically associated with people moving, such as furniture and renovations. Indeed, the ANU's Centre for Applied Macroeconomic Analysis found that "removing stamp duty can raise the annual housing turnover rate by 50 percent, back to the level observed in the early 2000s[1]" when analysing the impact of reform on the Australian property market.

[1]ANU Centre for Applied Macroeconomic Analysis, Stamping out Stamp Duty: Property or Consumption Taxes?, January 2021

Household income allocated to property taxes



Note: CCIWA estimates using ANU Centre for Social Research and Methods model.

Second, there are important social benefits to reform; stamp duty is an inequitable and regressive tax, punishing those who need to move more throughout their lives to secure employment or other opportunities to improve their prosperity.

Reform would make it easier for people from lower socio-economic backgrounds to move into higher socio-economic areas, perhaps the most important factor in helping families break out of generational disadvantage.

This is because WA's property tax system hurts lower income households most.

Using a microsimulation model developed by the ANU Centre for Social Research and Methods, we can reveal unique estimates of the percentage of household income spent on property taxes, by income quintile.

Commissioned by CCIWA for this report, the model allows us to 'peer into the future' and identify what Western Australia could look like if stamp duty was successfully replaced with an annual property tax. As we explore later in the report, the model estimates the impact of reform on both total government revenue and household income.

These estimates show that the bottom 20 per cent of households by income (first quintile) pay around 5.5 per cent of their income in property-related taxes (rate, land tax and stamp duty). By comparison, the top 20 per cent (fifth quintile) pay only ~2 per cent.

Property taxes impose a higher burden on lower income households

Third, stamp duty reform would better enable our cities and town centres to evolve in the wake of COVID-19. With more people looking to work remotely in the post-COVID world, businesses may re-think how they design and structure conventional office layouts.

This creates an opportunity for new residential and commercial spaces to open, in so doing forming more dynamic and inviting places for people to visit. It would also help to influence the decisions of global and national businesses on where to locate their regional headquarters.

Abolishing stamp duty would help to facilitate all of this by removing barriers to asset regeneration. That is, enabling businesses and households to sell older and purchase newer property.

Fourth, there is a long-term benefit for the State Government: a greater reliance on broad-based property taxes would provide a more stable revenue source, especially important for WA given the cyclical nature of its economy due to its reliance on the resource sector and the royalty streams it provides.

Abolishing stamp duty has wide support, from the Urban Development Institute of Australia, St Vincent de Paul, to the Australian Council of Social Service. Respected organisations like the Commonwealth Treasury and Productivity Commission have each contributed to the case for change through a variety of independent studies. And when you look at the reform benefits, it's not hard to see why.

There is no time to wait

Reforms of this nature take years to get over the line, meaning we need to get started now. The ACT has swung into action and pushed ahead, and New South Wales have extended their 'opt in' reform to first home buyers. The evidence of the economic and social benefits such reform provides is unequivocal. WA cannot be left behind.

If we sit idle, we risk missing an important opportunity to supercharge WA's economic future, boost Western Australians' standard of living and enable our cities and town centres to launch into a new and exciting era – particularly as Australia's international borders have reopened to the world.

In this report, we explore practical pathways to reform, address the key challenges holding back progress, and build WA's economic and social case for change.

Leveraging outputs from the ANU's microsimulation model, we reinforce qualitative insights with robust technical analysis to showcase the significant benefits reform of this type would deliver.

The ANU's model reveals what a world without stamp duty could look like; it allows us to identify how reform would enhance Western Australia's economic and social fabric with a particular focus on improving the lives of our society's most vulnerable.

From here, it is critical that all key stakeholders - leaders across business, government and the community - work together to identify the most effective reform approach and 'build a bridge' to a better future.

To this end, it is imperative that we explore sustainable, equitable and efficient reform solutions that promote the interests of WA's business community and broader society.

There are two main reform options

The first is an 'opt-in' approach, whereby homeowners are given the choice to either pay stamp duty upfront or opt into an annual rates levy. While this approach overcomes nearly all political hurdles associated with reform, the recent NSW experience has shown that it is not viable without Commonwealth financial support plugging the significant funding gap. And while Western Australia is currently in a strong budget position, it should not fund reform on its own.

The second option is a 'straight swap' model, whereby stamp duty is replaced with an annual property levy at the next available opportunity. This delivers the benefits of reform quicker and creates a far smaller funding headache for government, but it has all the messy political issues outlined in this report. As such, it does not seem politically feasible.

The ACT has taken a different approach, opting to gradually phase out stamp duty over a 20 year period and replace it with higher council rates. The reform process began in 2012, and while the ACT has made progress reducing the stamp duty rate, it has struggled to reduce the absolute value of stamp duty collections and ensure the 'swap to council rates' is indeed revenue neutral. Given the inherent difficulty in projecting stamp duty collections and the complexity of achieving revenue neutrality via fixed adjustments to council rates, this approach does not appear to be politically or financially feasible outside the ACT bubble.

At this stage, the best option for government appears to be to pave the way for an 'opt-in' model by exploring the potential for securitisation of property income streams at the same time as engaging with the Commonwealth on reform funding mechanisms.

Ultimately, we hope findings from this report help to elevate the policy discourse in Western Australia and contribute to the successful development of implementable reform options.

The principal author is James Walsh, CCIWA Principal Economist

Key findings

WA's property tax system hurts lower income households most. The bottom **20 per cent** of households by income pay around **5.5 per cent** of their income in property-related taxes, while the **top 20 per cent** pay only **~2 per cent**.

Replacing stamp duty with a broad-based property levy in WA would **reduce** the average households' **tax burden by around $40**, with lower income households set to receive the **largest average tax reduction**.

Reform would help to **narrow** the property tax gap of **lower and higher** income households, promoting **greater fairness** across **income brackets**.

Reform would **significantly improve** budget stability and **assist** with **longer term decision-making**.

Reform would achieve **revenue neutrality**, with the Government expected to collect an additional **$2 million** in the **five years** post-reform **(0.03% of property tax revenue)**.

Why stamp duty is a shocker

Transfer duty on conveyances — more commonly known as stamp duty — is one of those long-standing, archaic taxes that is simply not fit for the modern world.

Stamp duty has its roots in 11th century England when William the Conqueror used land ownership records to develop a state taxation base. When it was first introduced in Australia (circa 1865), the composition of Australia's economy was very different; house prices were lower relative to income and moving around regularly was rare.

Fast forward 200 years, and unsurprisingly, times have changed.

Today, younger people are struggling to break into the property market, families are looking to move closer to jobs and schools, and older people or 'empty nesters' are more likely to want to downsize.

Stamp duty has put these ambitions out of reach for many Western Australians and is widely acknowledged as one of the worst taxes in Australia. Why?

Stamp duty is costly and inefficient

Stamp duty makes up around **20 per cent**[2] of the upfront cost of moving house, meaning it acts as a significant financial handbrake on households looking to move. For a full-time worker who earns the average wage in WA and saves 15% of their income, stamp duty adds 2.6 years to the time required to save a 20% deposit for a house (valued at the median WA property price).

Putting it another way, a Western Australian household which moved four times over the past 18 years (each time buying the median property price) would have paid **almost $50,000** more in stamp duty than a household that moved only once.

These costs create significant disincentives for households looking to move to places that align with their needs.

For instance, a young couple starting out might buy a home that is bigger than they need, because they don't want to move twice and incur a second round of stamp duty when their children are eventually born.

Additionally, it limits the ability of younger people in areas with higher property prices to find an affordable place while still living in the area and creates disincentives for their parents to downsize and remain close to family and friends.

For those from lower socio-economic backgrounds, stamp duty is a significant barrier to moving into higher socio-economic areas - keeping many in entrenched generational disadvantage.

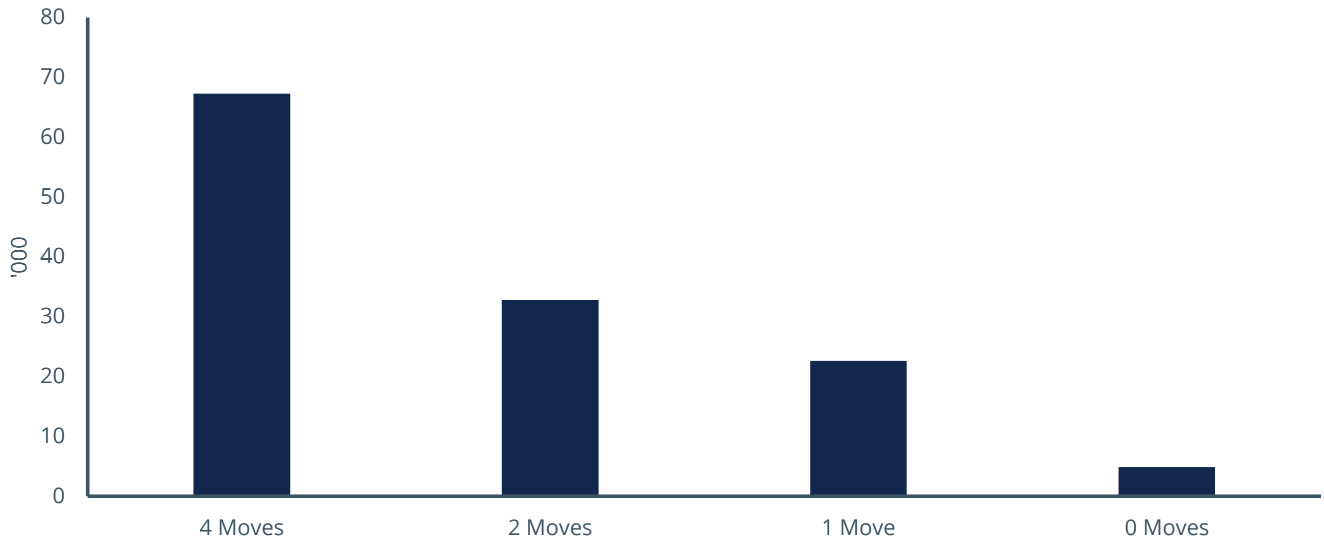
Many of these factors have climate change implications – the inefficient allocation of build infrastructure and greater transportation needs curtails progress toward achieving emissions reduction targets.

Eliminating stamp duty would provide Western Australians with greater ability to own a home where and when they want, all at a lower cost.

As the Reserve Bank of Australia Governor Philip Lowe noted in 2020, stamp duty is "a tax on mobility – on people moving location. If we're looking at an economy that's dynamic and vibrant, we want to remove taxes on mobility.[3]"

Effective Transfer Duty Paid

2002-2020, Perth



[2]NHFIC, Stamp Duty Reform: Benefits and Challenges, July 2021

Stamp duty is not fair

While the progressive nature of WA's transfer duty system means those purchasing higher valued properties pay more stamp duty than those purchasing less expensive properties, the majority of property transfers are for houses valued around $600,000[4] — in suburbs like Balcatta, Bassendean and Bibra Lake — meaning households in areas like these pay the bulk of transfer duty revenue. It could also reflect a stronger appetite from these households to move more throughout life, while those in more affluent suburbs (Cottesloe, Claremont, Peppermint Grove) tend to stay put for longer.

One of the major design flaws of stamp duty is the narrow base from which it is collected. Indeed, stamp duty adds well over $1 billion to the WA Government's bottom line each year despite being paid by roughly 4 per cent of households[5].

These households make a significant contribution to the delivery of critical infrastructure and essential public services, while longer-term homeowners enjoy the same services but make relatively smaller contributions via property taxation (despite also enjoying a once-in-a-generation land price windfall). It's just not fair.

> It is inefficient, inequitable and derails the stability of the government's revenue base.

Stamp duty revenue is unpredictable

Stamp duty is a volatile source of government revenue. It is exposed to the cyclical ups and downs of the property market, creating challenges for governments looking to make important budgeting decisions on long-lived assets that provide essential services like schools, hospitals and roads.

All up, stamp duty violates nearly every principle of effective taxation. It is inefficient, inequitable and derails the stability of the government's revenue base.

How does stamp duty work in Western Australia?

In most cases, whenever property and various business assets in Western Australia change hands, the buyer must pay an additional levy to the State Government (transfer duty).

First home buyers are levied a concessional rate, but on the whole, most residential transfers incur the following rates of duty

Dutiable value	Rate
$0 - $120,000	$1.90 per $100 or part thereof
$120,001 - $150,000	$2,280 + $2.85 per $100 or part thereof above $120,000
$150,001 - $360,000	$3,135 + $3.80 per $100 or part thereof above $150,000
$360,001 - $725,000	$11,115 + $4.75 per $100 or part thereof above $360,000
$725,001 +	$28,453 + $5.15 per $100 or part thereof above $725,000

[3]RBA Governor Philip Lowe, House of Representatives Economics Committee, Public Hearing Hansard, 14 August 2020, p 5.
[4]NHFIC, Stamp Duty Reform: Benefits and Challenges, July 2021
[5]Ibid.

The benefits of reform

The benefits of abolishing stamp duty (and replacing it with a broad-based property levy) are comprehensive.

Efficiency

- Makes it easier for people to move near jobs, family and schools, or for older people to downsize later in life.
- Reduces commute times, which in turn benefits the environment and WA's road system (less wear and tear).
- Enables households to move to properties that are best aligned to their needs, leading to a more efficient allocation of WA's property stock. This would also have climate mitigation dividend.

Fairness

- Makes it easier for lower-income households to break out of entrenched generational disadvantage.
- For those from areas with higher property prices, it supports younger people to buy their first house and parents to downsize and remain living in the area.
- Helps to close the property tax gap between lower income and higher income households.
- Broadens the property tax base, eliminating cross subsidisation associated with long-term homeowners (that would otherwise never pay stamp duty).

Government revenue stability

- Provides a stable source of Government revenue.
- Assists longer term budget decision-making.
- Indirectly boosts other revenue streams (e.g. GST) as the increased property turnover flows through to stronger household consumption on domestic items.

Community development

- Enables our towns and city centres to evolve in the wake of COVID-19, creating opportunities to form dynamic community hubs.
- Incentivises greater residential and commercial investment and asset regeneration.
- Assists WA households to relocate into Perth's CBD, lifting the City's vibe and making it a more attractive place to live and visit.

There is widespread support for reform, and the experts back it

It's not just CCIWA supporting reform. The benefits of transitioning away from stamp duty towards a broad-based property levy are well-documented by respected organisations and there is wide support across the community.

ACOSS, St Vincent de Paul and the UDIA have all expressed their support to transition away from stamp duty, and it's not hard to see why - the economic costs associated with stamp duty are in a league of their own.

Multiple independent organisations have produced estimates on the **economic cost of stamp duty**, and while these estimates do vary, they all find the economic damage associated with stamp duty is materially higher than that of a broad-based tax on land values (see chart).

For instance, the 2008 Henry Review found that the welfare loss from every additional dollar of stamp duty raised (34 cents) is more than three times that of the existing land tax arrangement (9 cents)[6].

In a research paper published in July 2021, the Commonwealth Government estimated that stamp duty wipes off 0.12 per cent[7] from WA's domestic economy each year - or $250 million. If this economic activity was retained, CCIWA estimates that around 20,000 jobs could be established and a further 5,500 indirectly supported.[8]

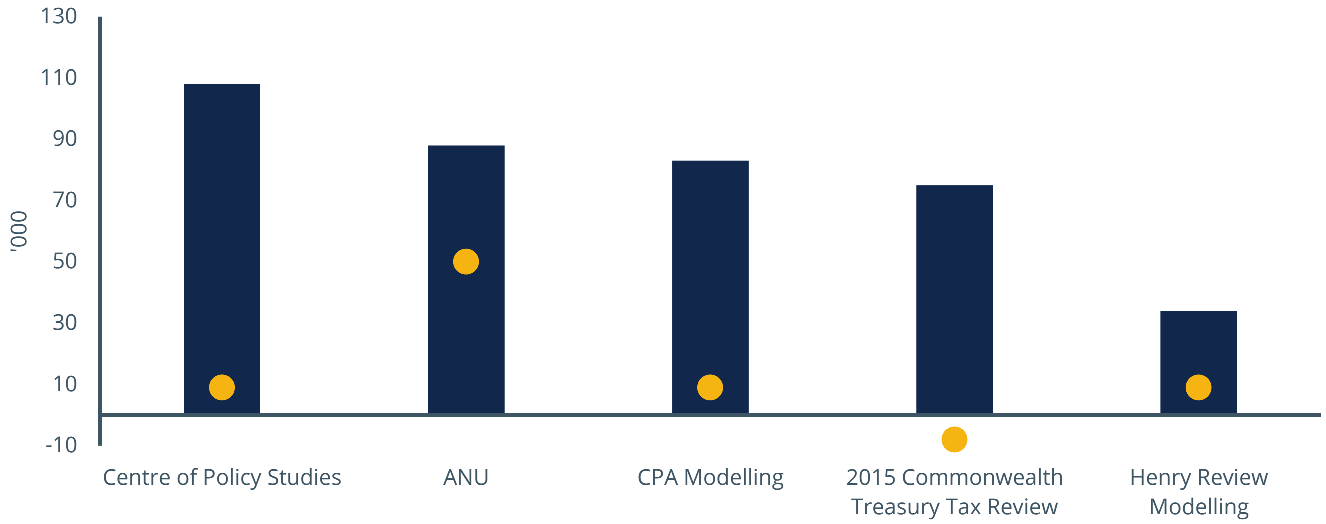
In December 2021, the International Monetary Fund (IMF) recommended that state governments transition away from stamp duties toward an annual tax based on land values. The IMF staff argued that "transitioning from a housing transfer stamp duty to a general land tax would improve efficiency by providing a more stable revenue source for states and territories, while promoting labour mobility"[9].

The OECD's most recent Economic Outlook (June 2022) noted that "further replacing stamp duty with a recurrent land tax...would result in a more sustainable tax base[10]", when commenting on opportunities to deliver medium term taxation reform in Australia.

In 2014, the independent Productivity Commission identified that "stamp duties on residential property add to the price of houses and can discourage people from moving to locations that may be closer to preferred jobs, family networks and schools[11]." In a separate report, they identify that "stamp duties on commercial property further discourage businesses from investing in existing land and capital"[12].

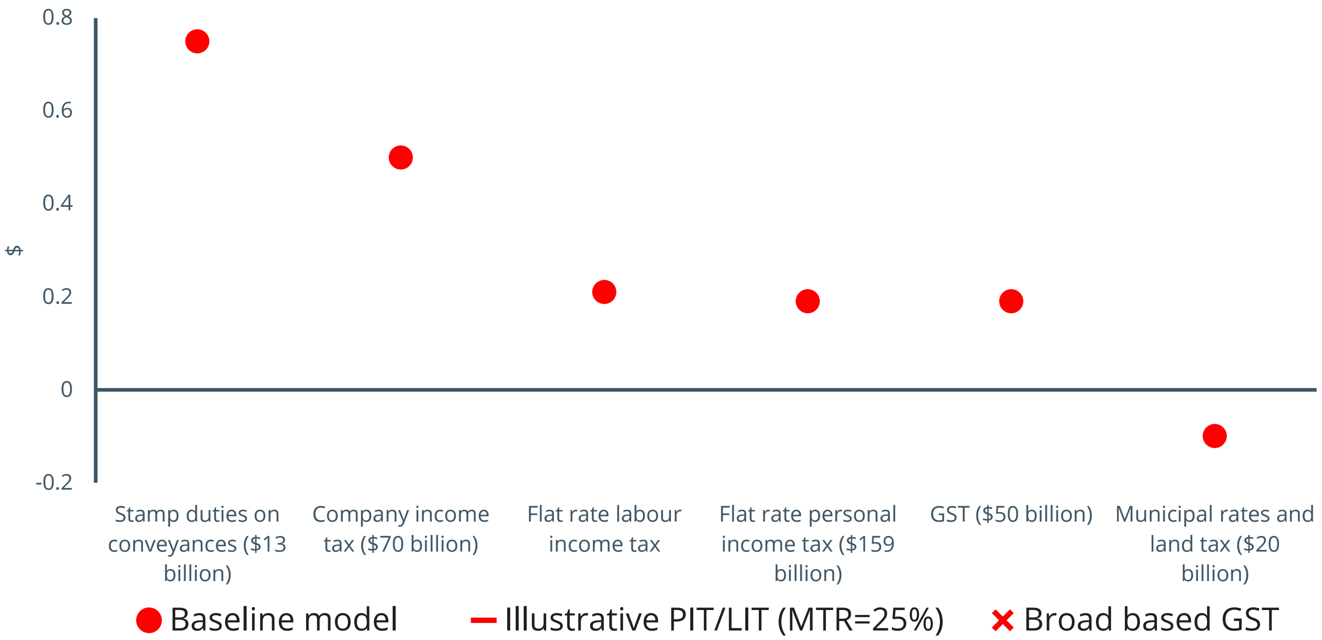
In 2015, Commonwealth Treasury

Welfare loss from raising an additional dollar in stamp duty and land tax



[6]Commonwealth Treasury, Australia's Future Tax System Review, 2008-2010
[7]NHFIC, Stamp Duty Reform: Benefits and Challenges, July 2021
[8]Estimates derived using economic multipliers.
[9]IMF, Australia: Staff Concluding Statement of the 2021 Article IV Discussions, September 2021

Marginal Excess Burden of Major Australian Taxes



argued that increases in stamp duties reduce property transfers and lead to "lower labour productivity and labour demand, which implies lower real wages and lower hours worked." In turn, they suggest "the economic incidence of a change in stamp duty tends to fall on workers"[13].

In the same study, Commonwealth Treasury found that conveyancing stamp duties have the highest marginal cost of the five major Australian taxes, while the most efficient tax is a broad-based land tax (see chart).

Marginal Excess Burden of Major Australian Taxes

As far as taxation reform goes, replacing stamp duty with a broad-based property tax is sitting at the top of the 'economic impact' pecking order. As mentioned, it will support our communities' most vulnerable households, supercharge WA's economy and provide the Government with a stable source of future revenue.

[10]OECD, Economic Outlook, June 2022
[11]Productivity Commission, Geographic Labour Mobility, 2014
[12]Productivity Commission, Realising the Productive Potential of Land, August 2017
[13]Commonwealth Treasury, Understanding the Economy-Wide Efficiency and Incidence of Major Australian Taxes, 2015.

Why we need to act now

It is essential that the Government considers moving on this reform as soon as possible. If we fail to act, we risk missing a unique and exciting opportunity to capture the wide-ranging benefits of moving away from stamp duty. In this section, we outline why there has never been a better time to get the reform engine started.

COVID-19: A unique opportunity

In the wake of COVID-19 and increasing prevalence of working from home, there is a unique opportunity to reinvent our City and other activity centres.

Not only would shifting away from stamp duty incentivise greater investment into our community hubs — creating inviting, dynamic places to visit — it would also provide households with greater opportunity to move to locations that align with their lifestyle preferences.

Budget stability

Over the past 12-18 months, stamp duty collections have been boosted by a significant pull-forward of future demand for residential homes — largely underpinned by record low interest rates and government support payments. Looking forward to the next few years, however, stamp duty revenues are expected to decline, and the outlook is plagued with uncertainty.

In the 2021-22 Budget, the Government acknowledged that “both residential property transactions and prices are susceptible to fluctuations in market sentiment and are therefore inherently difficult to forecast”.

Put another way, stamp duty is a volatile source of revenue that is difficult to predict. To this end, it damages the stability of WA’s budgetary position, creating headaches for decision-makers looking to fund essential services.

Strengthen WA’s economic trajectory for years to come

In the latest State Budget, WA Treasury expect WA’s economic growth to slow over the coming years, lifting the importance of undertaking meaningful, bold economic reform. Abolishing stamp duty on property transfers is a great place to start.

Strong outlook for the State’s finances

As we explore in the following section, some reform options lead to a revenue shortfall in the short term (e.g. the NSW ‘opt-in’ approach). While Western Australia’s strong financial position puts us in a fantastic position to move on this reform with confidence, WA should not fund reform on its own. Rather, we encourage the Government to engage closely with the Commonwealth throughout the reform process to identify possible revenue support mechanisms.

Assessing the options

There are three main criteria by which different options for property tax reform should be assessed.

Equity

The reform should help to address the inequities that already exist in WA's system of property taxes. It should narrow the property tax 'gap' and ensure that the most vulnerable members of our community are supported.

Efficiency

One of the main motivators for reform is to create a more efficient economy. As such, the extent to which options make it easier for people to move near jobs and to downsize is an important factor in judging their merits. It is also important to consider the impact on climate change, particularly via the efficient allocation of built infrastructure.

Government Revenue

Transfer duty is a volatile source of revenue that is difficult to predict. It is exposed to the cyclical ups and downs of the property market, creating challenges for governments looking to make important budgeting decisions. To this end, reform options should seek to improve revenue stability and sustainability over the long

So far, two other Australian jurisdictions have pushed ahead of the pack and committed to exploring options for reform – New South Wales and the ACT.

The NSW Approach

The NSW Government is exploring options to phase out stamp duty in favour of a broad-based property tax using an 'opt-in' arrangement. They have completed multiple rounds of public consultation to firm up the design and implementation of the proposed scheme.

Under the Government's proposed approach, buyers would have the option to either pay stamp duty at the point of sale (e.g., the existing system), or pay a much lower annual property tax.

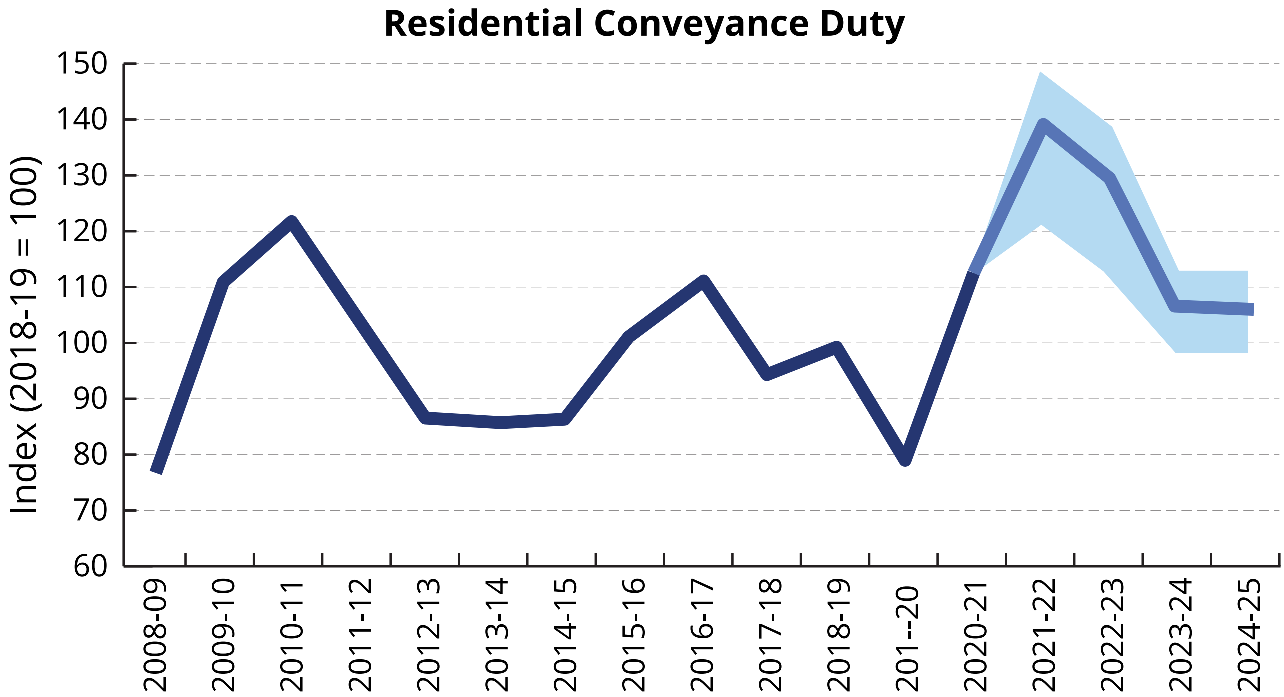
While the NSW Government acknowledged that the transition would likely reduce tax collections over the short-term, over the longer-term it will be revenue neutral (as more properties move onto the new scheme). All up, it is estimated that it will take around 23 years to turn over the entire housing stock onto the new broad-based land tax system.

In the most recent NSW Budget, the Government extended reform to first home buyers. That is, eligible first home buyers would be given the option to pay an annual property tax instead of transfer duty upfront (up to $1.5 million).

While this will benefit first home buyers who are looking to enter the property market, omitting the rest of the property market from the 'opt in' model greatly reduces the broad based benefits of reform. It is also a scaled back approach to what was initially proposed in the Government's July 2021 progress paper (to extend the 'opt-in' feature to a broader cohort of households).

Additionally, the Government has determined that properties will not be 'locked in' to the new system for subsequent purchases. This will create significant revenue challenges for the Government over the medium term and erode the widespread economic and social benefits associated with economy-wide reform.

The NSW Government has identified that overcoming the revenue shortfall is the primary barrier to extending this reform to a broader cohort of households. They note that securing Commonwealth Government funding will be an important factor to bridge the revenue gap.



The ACT Approach

The ACT has opted to gradually phase out stamp duty and replace it with higher council rates. The phasing out of stamp duty began in 2012 and is scheduled to occur over 20 years.

By funding the abolition of stamp duties through a levy imposed via the council rates base, the ACT Government was able to lower the average levy. If the approach was instead to increase existing land taxes, the average increase would have been much higher. This is because land taxes exclude a signification portion of land value.

In 2021, the ACT Government lifted the 'duty free' threshold for commercial transactions from $100,000 to $1.6 million – or more than 70 per cent of all commercial transactions.

They are now in 'Stage 3' of the reform program, scheduled to occur from 2021-22 to 2025-26. The Government has identified that "duty rates...are being set so that estimated revenue from residential general rates above the increase in the Wage Price Index is used to reduce forecast residential conveyance duty revenue by an equivalent amount".

Over the same time period, the ACT expect that "the commercial conveyance duty tax-free threshold will increase progressively from $1.5 million to $2 million in 2025-26."

Throughout the reform process, the ACT Government has struggled to reduce the absolute value of annual stamp duty collections and ensure the 'swap to council rates' is indeed revenue neutral. As shown in the chart below, the ACT's 2021-22 Budget identified that residential stamp duty collections have increased since the commencement of reform (2012), and the forward outlook remains uncertain and volatile (see error bands)[14]. Importantly, increases to council rates have occurred over this timeframe, which has underpinned a material rise in overall property tax collections.

The composition of Western Australia's economic and social environment is very different from that of New South Wales and the ACT. Our house prices are relatively lower, more of us live outside of the CBD and the State Government's financial position, albeit more exposed to cyclical volatility, is in good shape – having recently posted a record operating surplus.

With all this in mind, CCIWA recommends the Government explore a range of reform options - in consultation with industry and the broader community – to identify the best fit for the WA economy. These may include:

Opt-in approach

In line with the NSW approach, households would be given the option, when purchasing a property, to pay stamp duty, or to incur an annual property tax. The property levy could be applied to a property's Gross Rental Value in the same way that the Emergency Services Levy and WaterCorp wastewater charges are. It is essential that all property transactions (residential and commercial) are levied the same annual rate. That is, that commercial properties do not attract a materially higher annual levy.

This approach would help to overcome nearly all political arguments against reform and provide important flexibility for businesses and households with different operational/living requirements.

[14]ACT Budget 2021-22 Budget Outlook, *page 234*

The drawbacks of this approach are some of the widespread benefits of reform are delayed, and the State Government would face a funding shortfall over the medium term. To minimise this revenue shortfall, it is essential that properties remain locked into the new system after they have 'opted in'.

As mentioned, the NSW Government has initially extended the 'opt-in' approach to first home buyers. The Government has identified that the revenue shortfall associated with extending the reform to a broader cohort of households cannot be overcome without Commonwealth Government support.

It is therefore important that, should the WA Government consider the 'opt-in' approach, proactive engagement with the Commonwealth is undertaken well in advance to identify possible revenue support mechanisms. In addition, the Government could explore securitising the future stream of property levy payments to overcome the short term revenue challenges. That is, receiving an upfront payment from an investor in return for them receiving a portion of future property levy payments.

The Government could also explore the merits of a 'phased implementation' as part of a broader strategy to extend the opt-in reform economy-wide. Under this approach, reform could be initially targeted to those that would derive greatest utility from stamp duty reform. These could include lower income and regional households, first home buyers, and those aged 55+ looking to downsize.

Straight-swap reform

Under this approach, stamp duty would be abolished and a property levy applied to a property's Gross Rental Value. The property levy would be introduced simultaneously and set to deliver close to 1:1 replacement revenue over the medium term. To control for any material increases in revenue collections - should this occur - the Government could recalibrate the levy to a lower rate.

The 'straight swap' could be complemented by an array of short-term support measures to address the main social challenges identified in the next section. For instance, a concessions framework could be introduced, which may include a lower income threshold.

Grandfathered approach

Under the grandfathering approach (also known as switch-on-sale) a property levy is only introduced for a given property when the title changes hands. That is, either when the property is sold, or once all owners at the time of the introduction of the policy pass away. This is a version of the opt in approach but without providing households the choice on which taxation system to use.

This approach would help to address the concerns of people who have recently purchased a house, people who are asset rich and income poor, and older people who have paid taxes all their life and would feel unfairly treated if they have additional land tax levied on them.

The drawback of this approach - relative to the 'straight swap package' - is it creates an incentive for people to avoid moving to a new house, because they will then incur higher property levies. This would, in turn, lead to a significant revenue shortfall over the medium term which would be difficult to overcome.

Unpacking the challenges

There are a number of challenges to abolishing stamp duty in Western Australia, many of which must be addressed before reform can be progressed. The good news is that most can be resolved.

The challenges sit in two broad categories.

Revenue Challenges

Stamp duty is an important revenue source for state governments, and many of the existing and proposed reform approaches involve a shortfall of funding in the short to medium term.

As mentioned, there are a number of potential solutions to this, including State or Commonwealth borrowings filling the gap or securitising the future stream of property levy payments.

Stamp duty reform could also lead to a reduction in the States' GST distribution via increased property transfers, as detailed in the feature box below.

Impacts of reform on Western Australia's GST share

The Productivity Commission's 2018 report on Horizontal Fiscal Equalisation identified that stamp duty reform could lead to a reduction in GST collections, and that "the potential to lose GST payments could discourage States from pursuing efficiency-enhancing reforms[15]".

The Commission's report quantified the potential GST impacts of state tax reform (in 2016-17) via scenario analysis. One scenario involved cutting the rate of stamp duty in half and replacing 100% of lost revenue by a broad-based land tax (with reform implemented in a single year). They estimated that Western Australia could lose between $131 and $366 million from unilateral reform.

Should reform be phased in over an extended period, such as via the NSW opt-in model, the potential impact on GST is likely to be more gradual. Additionally, the Commonwealth Grants Commission's (CGC) use of a 3-year moving average to estimate each states' fiscal capacity (under the GST formula) would also help to smooth the GST impacts.

In commenting on the relationship between GST and stamp duty reform, the CGC noted that "a reduction in the rate of stamp duty on conveyances could see the observed tax base rise through an increase in property sales… any increase in a state's tax base increases its assessed revenue raising capacity relative to other states, which will in turn reduce the assessment of its relative GST requirement[16]".

However, the CGC identified that "if the reform policies of an individual state were having a material effect on its GST share then, under its policy neutrality principle, the Commission could seek to mitigate such effects". The policy neutrality principle aims to ensure that the assessment of a state's GST requirement is not affected by, and does not influence, individual state policy choices, such as changes to its tax mix[17].

Importantly, the CGC note that any response would have to be "permitted under the terms of reference issued for an update (or review) of the GST distribution, and the approach chosen would be determined in consultation with the Commonwealth and the states."

CCIWA strongly believes that no state should be worse off for undertaking productivity enhancing taxation reforms, such as the replacement of stamp duty with a broad based property levy. Rather, they should be better off. It is therefore important that governments work collaboratively with the Commonwealth Grants Commission and the Commonwealth Government to mitigate the potential impact of reform on GST collections, while preserving the structural integrity of the reforms enacted in 2018.

[15]Productivity Commission, Horizontal Fiscal Equalisation Inquiry Report, 2018
[16]Commonwealth Grants Commission, Occasional Paper 2 – GST Distribution and State Tax Reform, 2021.
[17]Ibid.

Social Challenges

There are also social challenges associated with members of the community likely to voice their opposition. These include:

People who have recently purchased a house

Recent buyers may feel unfairly treated if they are forced to pay an annual property tax after incorporating transfer duty into their mortgage structure. As a possible solution, the Government could credit back recent home buyers the total amount of duty paid over the past five years evenly over an extended (e.g. five year) period. The Commonwealth Government noted this option in a 2021 research paper which identified it "will not result in a cut to substituted land tax revenue[18]".

People planning to purchase a house

After announcing the reform, some households may choose to defer their decision to purchase a property until the reform is enacted. This could apply downward pressure on property prices.

To address this, the Government could allow for retrospective applications from the announcement of the reform to the date it is legislated.

Asset rich, income poor households

These households may face considerable financial pressure if forced to pay an annual property levy based on the properties' Gross Rental Value.

This challenge could be addressed via an 'opt-in' reform approach, where buyers are given the flexibility to either pay an annual rates levy, or an upfront stamp duty payment. It could also be addressed through the implementation of a concession framework, which may include a lower-income threshold. We incorporate this feature in our modelling outputs, as outlined in the following sections.

Older people who have paid taxes all their life and would feel unfairly treated if they have additional property tax levied on them

Seniors and retirees could be exempt from the broad-based levy through the implementation of a concession framework, or an 'opt-in' reform approach.

For other longer-term homeowners, however, it would be very difficult to justify the provision of tax concessions/support – particularly given the once-in-a-generation house price windfall these households have enjoyed over the past 20 years. To provide these homeowners with greater flexibility, an 'opt in' model could be explored.

People who now have a higher tax burden than they otherwise would have.

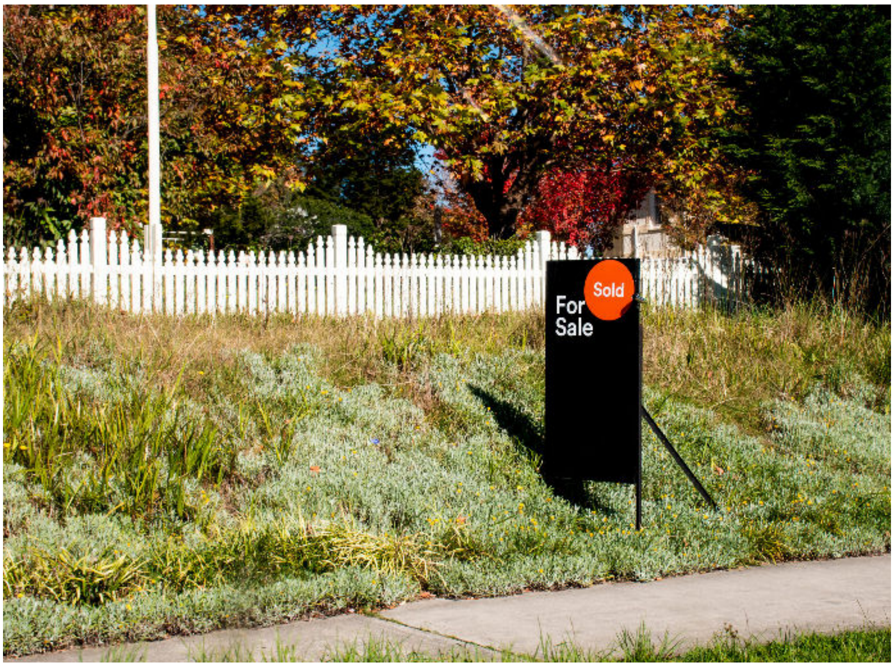
As mentioned above, some households may end up paying slightly more tax under the new system than they would previously. While this is largely unavoidable, the longer-term economic benefits associated with stamp duty reform would help to offset the increased tax burden for affected households. It would also ensure the property tax burden is borne by all households, not just the small proportion (4%) that move house. To provide these homeowners with greater flexibility, an 'opt in' model could be explored.

Landlords passing on the new broad-based property tax to rental tenants.

In WA, section 48 (1) of the Residential Tenancies Act (1987) prohibits landlords from passing taxes directly onto tenants. To provide additional reassurance that rents would not be affected by the reform, the Government could request quarterly monitoring reports by an independent pricing body – in line with the NSW proposal.

Over the longer-term, the reform will enable more households to enter the established housing market, in turn pushing down rents via reduced demand for rental properties. While a higher annual tax burden may prompt some landlords to realise their assets, the concomitant decline in rental demand would help to offset any reduction in rental supply.

The ANU Centre for Applied Macroeconomic Analysis arrived at a similar conclusion in a recent research paper:



[18]NHFIC, Stamp Duty Reform: Benefits and Challenges, July 2021

"As removing stamp duty favours home ownership, it reduces rental demand and raises the demand for owner-occupied and investment housing, leading to an increase in equilibrium housing price and a fall in equilibrium rent. This setup is consistent with the fact that in Australian housing market the provision of rental properties is dominated by households rather than institutional investors"[19].

Additionally, in a research report titled "Pathways to State Property Tax Reform", the Australian Housing and Urban Research Institute (AHURI) noted that "while the supply of rental stock may decline, this will be offset by falling demand for rental housing as home ownership rates increase[20]".

To provide landlords with greater flexibility, an 'opt-in' approach could be explored.

Businesses that own property assets

While most of the benefits of lower stamp duty are due to more efficient movement of households, removing duty on commercial property transactions would also deliver significant benefits, including via greater investment in the WA economy.

Given the critical role that businesses play in generating seven out of every eight jobs in WA, any proposed reform approach that includes commercial transactions must ensure the business community is left 'no worse off', and that commercial properties are not subjected to higher property rates (than what is levied on residential properties).

Any system that involves commercial properties must also include the provision of an 'opt-in' function – similar to the proposed approach in NSW – to provide established businesses and those with large property requirements (e.g. agriculture, manufacturing, warehousing) with important flexibility.

All told, not all of the above challenges can be designed away. To some extent there is a requirement for political argument and courage, noting however that the economic and social equity arguments are highly compelling.

[19]ANU Centre for Applied Macroeconomic Analysis, Stamping out Stamp Duty: Property or Consumption Taxes?, 2021
[20]AHURI, Pathways to State Property Tax Reform, 2017

A future without stamp duty – what could it look like?

In the following section, we use a detailed microsimulation model[21] developed by the Australian National University to showcase what Western Australia's future could look like if stamp duty was successfully replaced with an annual property tax. The model allows us to break down the household impacts by income quintile and illustrate the nature and extent of the reform benefits.

The findings progress the case for change and provide policymakers an evidence-based mandate to kickstart the reform process. From here, it is critical that all key stakeholders - leaders across business, government and the community - work together to identify the most effective reform approach and 'build a bridge' to a better future.

To this end, we urge the State Government – in consultation with industry - to explore sustainable, equitable and efficient reform options that promote the interests of WA's business community and broader society.

Modelling WA's Future – Unpacking the ANU's Microsimulation Model[22]

Model Parameters

In our modelled simulation, we estimate the impacts on household income and government revenue after transfer duty has been replaced with a broad-based property tax.

The annual levy is modelled at roughly 7.2 per cent of the properties' Gross Rental Value. For WA households with an average GRV

of around $22,100[23], the annual levy would amount to around $1,600 per year (as opposed to paying roughly $15,000 upfront in stamp duty[24]).

We sought to compare our approach to the 'first home buyer' reform option delivered in the most recent NSW Budget. However, given the NSW approach uses 'unimproved value' to anchor the rates levy, which is dependent on a range of difference factors – location, zoning, existing site conditions, proximity to infrastructure – it is difficult to estimate for the purposes of comparing 'apples with apples'. That said, for an average unimproved value of $500,000, first home buyers (owner occupier) would pay $1,900 per year under the proposed NSW scheme[25]. For an unimproved value of $400,000, households would pay $1,600 per year.

To demonstrate how a 'concession framework' could be used in Western Australia, we have estimated an effective lower income tax-free threshold of $100,000.

That is, households with an annual income of less than $100,000 are exempt from paying the annual property tax, which broadly reflects the annual pre-tax earnings of a dual-income household earning slightly above WA's minimum wage ($779 per week).

Impact on Government Revenue

Over a five year period, the State Government collects an additional $2 million in cumulative property taxes — or only ~0.03% of total property tax revenue.

Importantly, replacing stamp duty with a broad based property tax would improve the stability of Western Australia's budgetary position. Stamp duty is an incredibly volatile source of revenue, exposed to the cyclical ups-and-downs of the property cycle.

As shown in the following chart, replacing stamp duty with a broad based property tax would significantly improve budget stability and assist with longer term decision-

[21]Detailed information about the model can be found in the Appendix
[22]Key assumptions: Annual wages growth average 3.0 per cent, annual rental growth average 2.25 per cent, annual CPI growth average 2.5 per cent, annual property price growth average 2.7 per cent.
[23]Representative GRV based on median WA weekly rents ($425pw).
[24]Based on WA median selling price ($525,000)
[25]First home buyers are levied $400 + 0.3% of unimproved property value.

making. We compare the annual volatility of stamp duty (based on the 5 year period pre-COVID), to what our model has estimated over five years for a replacement broad-based property tax. The standard deviation (measure of volatility) of the rates levy is 24 times less than that of stamp duty.

While our modelled scenario estimates the revenue impacts after stamp duty has been replaced, some reform approaches elect to 'phase out' stamp duty over a prolonged timeframe – such as the 'opt-in' approach considered in NSW. These approaches create a revenue shortfall in the short to medium term.

Impact on Households

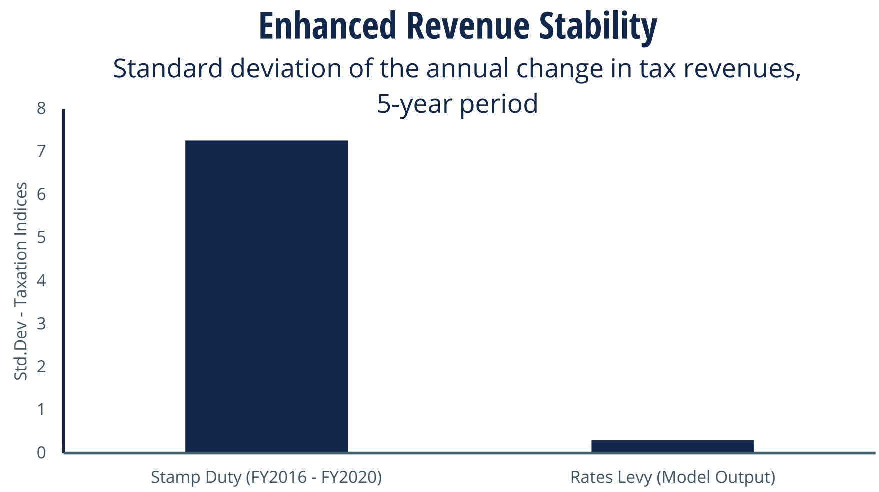
By introducing a tax-free threshold of $100,000, lower income households would have their property tax burden significantly reduced. For instance, the average household in the 1st income quintile (see chart) would pay around 4.7 per cent of their annual income in property tax under the 'reform' scenario – almost a full percentage point lower than what they are estimated to currently pay (5.5 per cent).

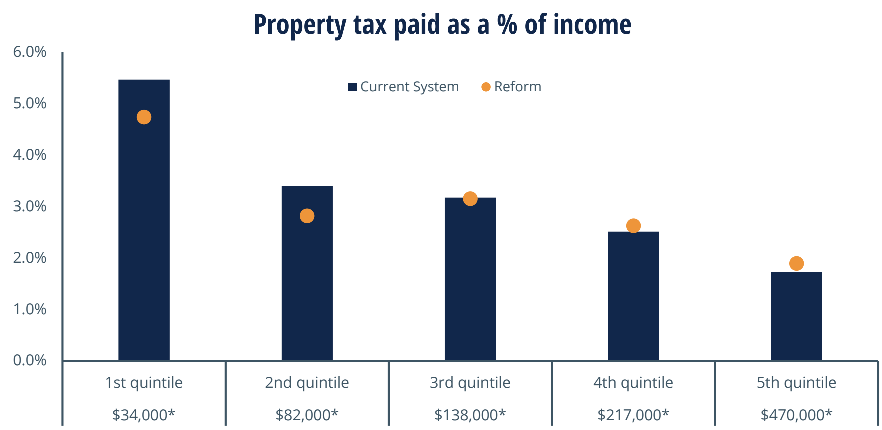
So, how does this translate into the dollar amount paid by the average Western Australian household?

On average, WA households in the first, second and third income quintiles would see a reduction in their annual property bill, while those in the upper income brackets would experience a slight increase.

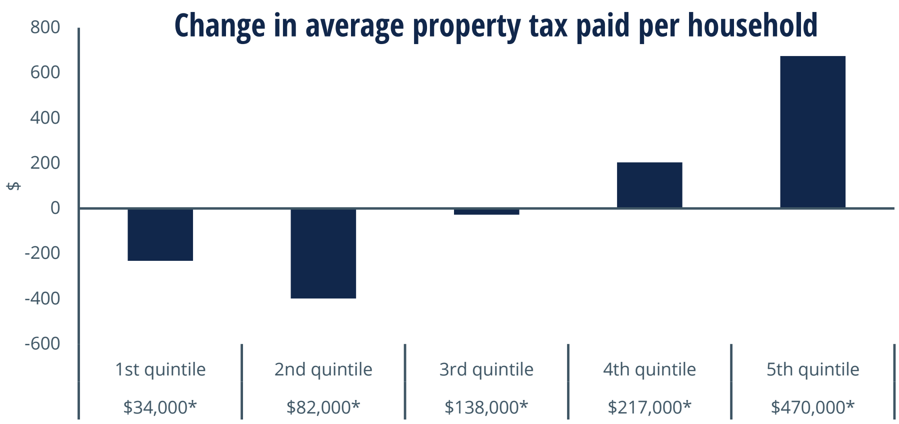
Households in the first quintile (with average incomes of around $35,000) would bank a $230 tax reduction on average, while those in the second quintile (~$82,000) would pay around $400 less in property taxes.

Put another way, reform would help to narrow the property tax gap of lower and higher income households, creating a more even distribution of the property tax burden across income brackets.





*average income within the quintile



*average income within the quintile

As mentioned, this would allow households to move to locations that best suit their lifestyle and assist lower income families break out of entrenched generational disadvantage.

More broadly, it would keep WA's economic fire burning for years to come and provide a stable source of revenue for future governments.

Technical note: For modelling purposes, we have estimated the year 2024-25 as the base period to illustrate 'what the future could look like' without stamp duty in WA. All estimated model inputs for this year were derived from structural economic and social assumptions coded into the ANU's microsimulation model.

Conclusion

If stamp duty reform were easy, it would already be done. But as this paper shows, while the challenges are big, the reform benefits are bigger. Indeed, this paper is the first of its kind, showing that the benefits of reform extend beyond efficiency, into the realm of equity.

Governments have two main options for reform. The first is to avoid many of the political challenges and proceed with an 'opt in' model. The recent NSW experience has shown however that achieving this reform is not possible without Commonwealth financial support plugging the significant funding gap. While Western Australia is currently in a strong budget position, it should not fund reform on its own.

The other option is a 'straight swap' model. This delivers the benefits of reform quicker and creates a far smaller funding headache for government. But it has all the messy political issues outlined in this report, and as such presents significant political challenges.

All up, the most feasible option for government appears to be to pave the way for an opt in model by exploring the potential to securitise income streams at the same time as it engages with the Commonwealth on reform options.

This work should start as soon as possible.

There has never been a more important time to kickstart the reform engine. As we emerge from COVID-19, undertaking bold economic reform will be critical to strengthening and diversifying WA's economy over the longer term. If we get it right, we will elevate WA's economic future, boost Western Australians' standard of living and enable our cities and town centres to launch into a new and exciting era.

For decades WA has been an economic powerhouse of the national economy, delivering extraordinary standards of living by global comparison. Stamp duty reform would keep us at the forefront of the nation, securing greater economic and social prosperity for current and future generations of Western Australians.

> This work should start as soon as possible. There has never been a more important time to get the reform engine started.

Appendix

About the model

The Australian National University's Centre for Social Research and Methods has developed a 'microsimulation' model - StateTaxMod - for testing the revenue and distributional consequences of change to property tax settings.

Microsimulation models are developed using a modelling technique that operates at the level of individual units such as people and households. Within the model, each unit is represented by a record containing a unique identifier and a set of associated attributes – e.g. a list of households with known composition, income, property value.

This technique is well suited to demographic investigations because events are generally the outcomes of complex, interdependent processes whose operation it is impossible to represent in solvable functional forms[26].

StateTaxMod was developed to model changes in property taxation mixes over time to determine effects on both total government revenue and gains/losses by households.

The data used is from the ABS Survey of Income and Housing 2017-18, which has been updated for each year to incorporate changes in incomes, prices and population. The survey has detailed information for each person, income unit and household, which enables the model to accurately simulate the complexity of the tax and transfer system.

The current stamp duty and alternative land tax arrangements were coded into the model and applied to the survey data.

The model allows the user to vary settings for a range of property taxes, including stamp duty, property rates, land tax, the RMIT and a rates levy. It also allows different tax rates to be set, as well as minimum and maximum payments, threshold amounts, income tests and policy phase ins.

Model Outputs

Impact on Household Income

Household Impacts	LG Rates	Land Tax	Stamp duty	TOTAL Base (Current System)	LG Rates	Land Tax	Stamp duty	Rates levy	TOTAL Alt (With Reform)
Tax % of income									
1st quintile	4.7%	0.1%	0.7%	**5.5%**	4.7%	0.1%	0.0%	0.0%	4.7%
2nd quintile	2.4%	0.4%	0.6%	**3.4%**	2.4%	0.4%	0.0%	0.0%	2.8%
3rd quintile	1.8%	0.4%	1.0%	**3.2%**	1.8%	0.4%	0.0%	1.0%	3.2%
4th quintile	1.2%	0.5%	0.8%	**2.5%**	1.2%	0.5%	0.0%	0.9%	2.6%
5th quintile	0.9%	0.3%	0.5%	**1.7%**	0.9%	0.3%	0.0%	0.7%	1.9%
Tax paid ($m)									
1st quintile	$341	$4	$53	**$399**	$341	$4	$0	$0	$346
2nd quintile	$424	$73	$104	**$602**	$424	$73	$0	$1	$499
3rd quintile	$534	$106	$307	**$947**	$534	$106	$0	$301	$941
4th quintile	$561	$236	$374	**$1,172**	$561	$236	$0	$427	$1,224
5th quintile	$912	$289	$531	**$1,732**	$912	$289	$0	$696	$1,897
Total income									
1st quintile	$7,299	$7,299	$7,299	**$7,299**	$7,299	$7,299	$7,299	$7,299	$7,299
2nd quintile	$17,704	$17,704	$17,704	**$17,704**	$17,704	$17,704	$17,704	$17,704	$17,704
3rd quintile	$29,850	$29,850	$29,850	**$29,850**	$29,850	$29,850	$29,850	$29,850	$29,850
4th quintile	$46,636	$46,636	$46,636	**$46,636**	$46,636	$46,636	$46,636	$46,636	$46,636
5th quintile	$100,210	$100,210	$100,210	**$100,210**	$100,210	$100,210	$100,210	$100,210	$100,210
Average tax/hh									
1st quintile	$1,457	$552	$12,699	**$1,703**	$1,457	$552	$0	$0	$1,476
2nd quintile	$1,637	$4,709	$16,223	**$2,323**	$1,637	$4,709	$0	$19	$1,924
3rd quintile	$2,044	$3,060	$20,686	**$3,624**	$2,044	$3,060	$0	$1,062	$3,598
4th quintile	$2,157	$6,599	$20,606	**$4,504**	$2,157	$6,599	$0	$1,449	$4,707
5th quintile	$3,500	$5,300	$36,322	**$6,645**	$3,500	$3,075	$0	$1,098	$7,278

[26] G. Santow, in International Encyclopedia of the Social & Behavioural Sciences, 2001