PROPERTY COUNCIL of Australia

Statewide Revaluation Initiative

Reviewing CBD land tax impacts and increasing South Australia's investment competitiveness.

Executive Summary

South Australia's relative success in navigating the pandemic has been acknowledged both domestically and internationally.

Having avoided lengthy and economically damaging lockdown periods witnessed interstate, the Economist recently recognised Adelaide as Australia's most liveable city placing it among the top three cities for this accolade globally.

Given South Australia's track record in pandemic management, in an environment where domestic and global capital seeks stable and competitive investment environments, South Australia currently possesses a persuasive business case.

A competitive tax environment is also a significant component of this business case.

Domestically, South Australia has achieved a comparative advantage. For example, the differences between property-based taxes in Victoria and South Australia now have become pronounced.

South Australia has abolished stamp duty on commercial transactions and reduced the top rate of land tax from 3.7 per cent to 2.4 per cent compared to Victoria's 2.55 per cent.

However, with the recent Statewide Valuation Initiative, the relative interstate competitive advantages achieved from the new lower land tax regime appears to be at risk.

In surveying our CBD membership base – landlords who have proactively sought out their FY22 site valuations – the Property Council has unveiled significant land value increases.

While increased property values are unsurprising, the magnitude and suddenness of these spikes naturally result in disproportionately large land tax bills, presenting major cash flow challenges. In many ways, these valuation uplifts feel like two decades of 'catch-up', but in one year.

Throughout the pandemic South Australian landlords, tenants and business owners have collaborated with Government in stoically bearing with COVID-19 activity restrictions to "slow the spread".

Beyond activity restrictions COVID-19 has challenged the traditional office model. Besides an increase in people working from home and downsizing in office space requirements, owners have worn unexpected costs associated with changes in office fit-outs, tenant relocations and an expectation to update amenity to meet standards associated with maintaining a healthy work environment.

The compounded impact of rental losses absorbed throughout the pandemic combined with cash flow issues due to delayed FY21 land tax rates – overlayed with the aforementioned land tax increases in FY22 and additional costs associated with adapting to the pandemic – cannot be understated.

In many cases, these land tax increases are not recoverable through rent and have a detrimental impact on cap rates with flow-on impacts for lending, which can undermine investment and growth. Where they are recoverable, landlords may be compelled to pass on these increases through leases. Anecdotally, it is suspected that many small businesses will not be able to survive this.

Property Council members recognise the need for a fair, sustainable and stable tax revenue source to undertake budget repair and fund the infrastructure required to stimulate growth beyond the election and in a post-pandemic environment.

This paper presents four policy options for the State Government's consideration.

These options are aimed at alleviation of the cash flow volatility arising from sudden land tax increases as well as how to retain and amplify South Australia's competitive advantage and investment attractiveness beyond the pandemic.

The Property Council has gathered case studies presented as "cameos" for the purpose of demonstrating the magnitude of year-on-year valuation and land tax liability spikes from Local Government Areas within the Adelaide CBD and its immediate periphery.

This paper then uses multi-criteria analysis to examine how the policy options presented might be assessed against considerations important to policy makers. The purpose here is not to lobby for tax concessions that markedly deteriorate the South Australian budget position, but rather arrive at a workable solution that assists the sector to cushion the impact of the Revaluation Initiative while achieving relative budget-neutrality and an improvement in the administration of land tax liabilities.

Nevertheless, further land tax rate reform should be considered to ensure Adelaide is not just the nation's most liveable city – but that South Australia becomes the best place in the country to invest.

With the March 2022 State Election fast approaching, the Property Council will continue to work with the State Government in good faith to find a solution to this challenge and smooth the impact of these tax increases.

In simple terms, this paper presents these valuation-land tax challenges and paves a policy pathway out.

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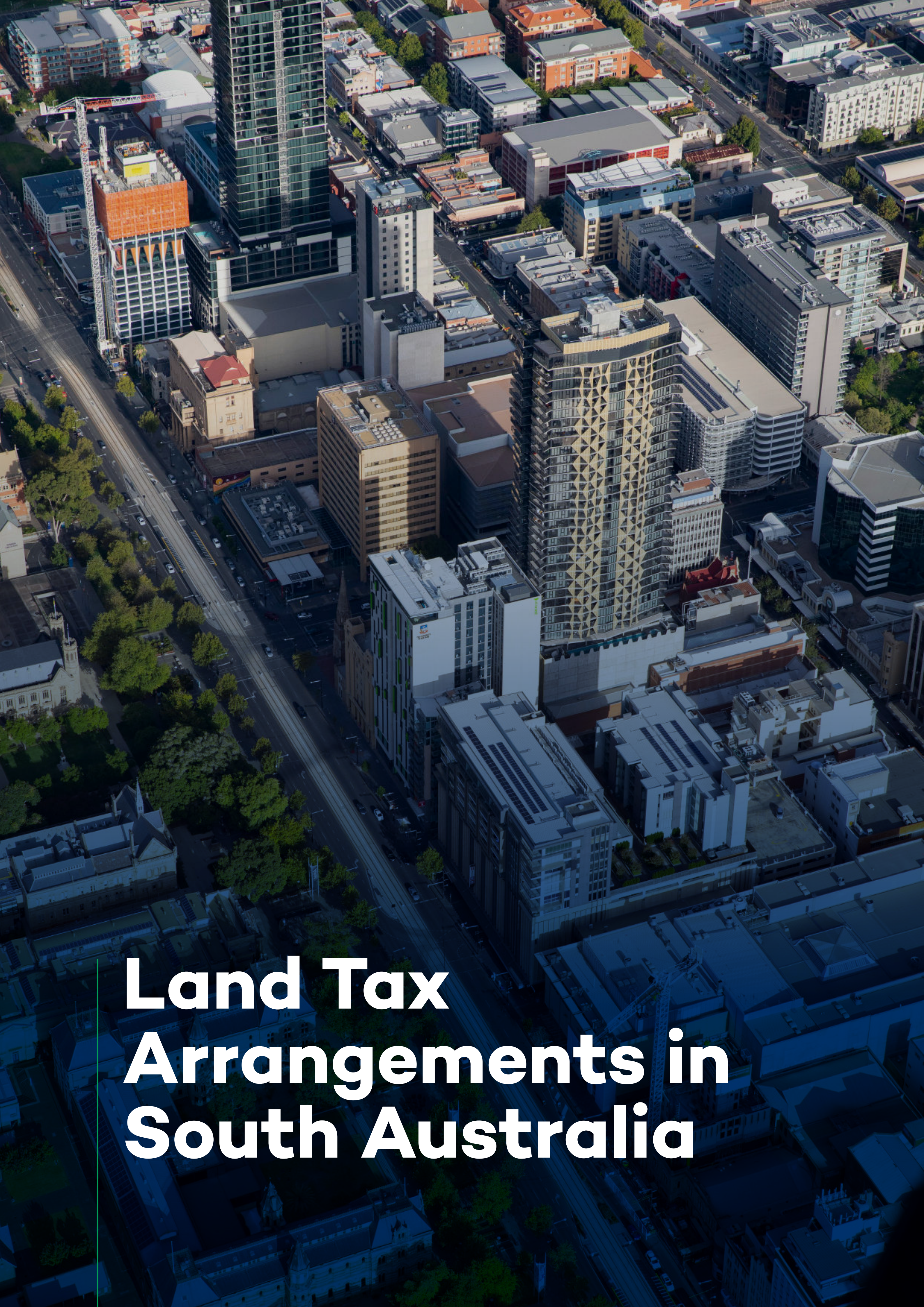
CONVENTION CENTRE



Land Tax Arrangements in South Australia

Land tax arrangements in South Australia have undergone significant changes over the last two years, most notably to the way properties held in trust are taxed.

To assist in managing the impact of these reforms on South Australian property investors, the Property Council of Australia was effective in lobbying the South Australian state government to reduce the top tax rate from **3.7 per cent**, down to **2.4 per cent** – a historic and significant reduction.

Despite these improvements in the economic efficiency of land tax arrangements – and in making some contributions towards improving the competitiveness of arrangements – the implementation of the current revaluation program has the potential to wipe out these recent gains and diminish competitiveness.

While the threshold increase has been a welcome relief for South Australian land holders, the investors that are likely to be most significantly impacted by the Valuer-General's revaluation initiative are those that have holdings well above the threshold. As such, these land holders will not substantively benefit from these reductions.

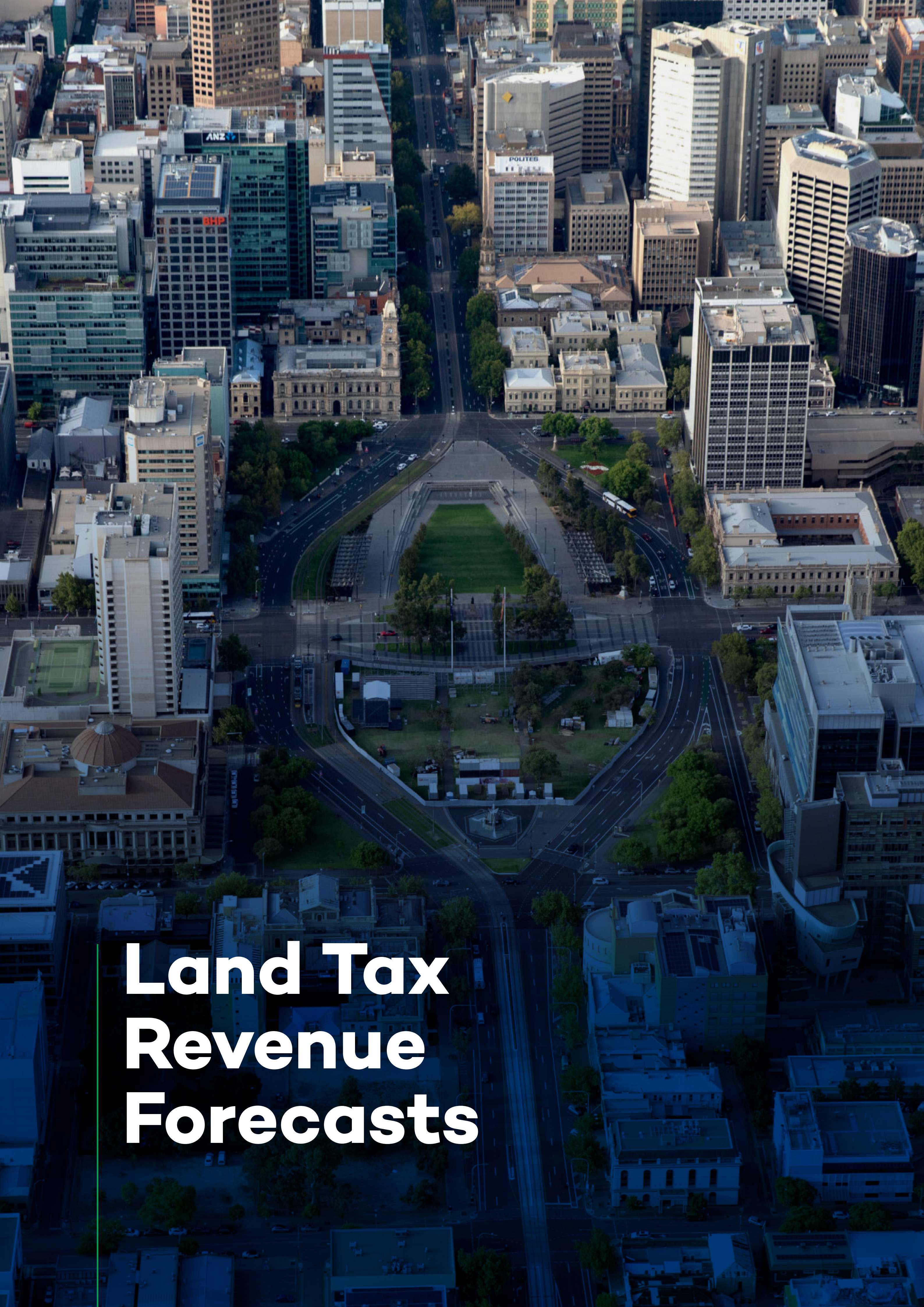
The affected land holders are predominantly the largest beneficiaries from the reduction in the top tax rate. However, the dramatic increase in land tax liabilities directly caused by significant upward revisions in the valuation of illiquid properties has created significant cash flow management challenges.

Land tax relief through the transition period between land tax arrangements has also been welcome for the property sector. However, again, these measures miss those most dramatically impacted by the revaluation initiative as it explicitly excludes those who have seen increased tax bills directly due to revaluations.

The revaluation initiative being undertaken by the Valuer-General has aimed to review and update the data forming the basis for the annual General Valuation.

The revaluation initiative is accepted as a sensible program that will help improve the accuracy of the annual General Valuation. However, the sudden shock of a substantial increase in land tax liabilities for significant land holders is a problem for South Australian property investors when it comes to cash flow management.

This is a problem that can and should be addressed through sensible, considered policy that aims to smooth the impact of this increase. This document will propose sensible policy that will allow the impact of dramatically increased land valuations to be smoothed over time, preventing negative externalities for the property sector at little or no cost to government.



Land Tax Revenue Forecasts

In the 2018-19 Budget, the South Australian State Government outlined that the revaluation initiative of the Valuer-General was expected to increase underlying land tax revenue by around **$19 million** by 2021-22.

Given revenue from private land taxes in 2021-22 was expected to be **$390 million** in the 2018-19 Budget, this would account for a total increase in land tax revenue of **4.9 per cent** off the back of the revaluation initiative.[1]

More recently, the 2021-22 Budget also outlines the expected growth in site values on average as a direct result of the revaluation initiative.

Residential site values are expected to grow by approximately **4.7 per cent** and non-residential by approximately **8.6 per cent**.

Overall, site values are expected to grow by **7 per cent** in 2021-22, and **3 per cent** per year going forward. The overall impact of the land tax initiative broadly on revenue is outlined in **Table 1**.[2]

Table 1: South Australian State Government 2021-22 total property tax revenue forecasts

	2020-21 Estimated result	2021-22 Budget	2022-23 Estimate	2023-24 Estimate	2024-25 Estimate
Total property taxes ($m)	781.3	818.8	829	847.5	869.6
Nominal growth (%)	-12	4.8	1.2	2.2	2.6
Real growth (%)	-13.3	3	-0.5	0.2	0.1
Policy adjusted underlying revenue ($m)	767.9	818.8	854.8	887.1	923.1
Nominal growth (%)	0.9	6.6	4.4	3.8	4.1
Real growth (%)	-0.6	4.8	2.6	1.7	1.5

This assumed increase is reflected in the revenue forecasts from private land tax in the 2021-22 Budget, where revenue from private land tax is expected to increase from the 2020-21 Budget to 2021-22 by almost 6.0 per cent. This is shown in **Table 2**.[3]

Table 2: South Australian State Government 2021-22 private land tax revenue forecasts, page 39, percentage changes calculated based on revenue figures in the table

	2020-21 Budget	2020-21 Estimated result	2021-22 Budget	2022-23 Estimate	2023-24 Estimate	2024-25 Estimate
Land tax - private	373	384	407	399	408	420
Percentage change from the 2020-21 estimated result (%)		-	6	-2.1	2.3	3.1

1 Government of South Australia, Department of Treasury and Finance, 2018-19 Budget Statement (page 43, 4 September 2018).
2 Government of South Australia, Department of Treasury and Finance, 2021-22 Budget Statement (page 39, 22 June 2021).
3 Ibid (page 39).

The Impact of the Revaluation Initiative

Throughout this document, given the complexity in the holdings of the various organisations and their individual properties, each land tax liability is assumed to be subject to land tax under the general land tax rates.

Sensitivity analysis shows that the difference in the increase in land tax liability from when the holdings are classed as trust holdings compared to general holdings is minimal. Treating holdings under the trust rates would yield slightly lower increases. However, this is likely offset by some of these organisations opting to pay the non-disclosure of the beneficiary fee.

Below are examples from Property Council members who have been subject to large increases in holding valuations across just a year-long period. This shows the magnitude of the increases in liabilities for certain Property Council members, highlighting the issues that the revaluation has caused for how landlords will manage cash flow for this financial year.

The term 'Cameo' can either refer to a group of properties held or managed by one organisation, or a group of properties where there is simply available data that has been used as an example of the revaluation initiative's impact on land tax liabilities for individual properties. Revaluations are calculated on a property-by-property basis, given the complex holding structures typically employed by high-value land holders.

Any reference to a financial year (FY) as FY2X should be considered as the financial year ending in year 202X. For example, FY22 refers to the 2021-22 financial year.

Cameo 1

The holdings of Cameo 1 have seen a significant upwards revision in the valuation of their properties, resulting in a 99 per cent and a 90 per cent increase in their tax liabilities on the two individual sites provided as examples. **Table 3** shows the impact the revaluation initiative has had on the CBD-based commercial real estate holdings of Cameo 1.

Table 3 clearly shows the impact that the revaluation initiative has had on the land tax liabilities of Cameo 1, and the problem this creates regarding cash flow for businesses like this. While it is likely that the revaluation of illiquid commercial properties such as these CBD-based office buildings was justified, it is a significant hit that can cause disruptions to commercial activities of organisations like Cameo 1.

Table 3: Cameo 1 land tax changes

Property LGA	FY21 Val ($)	FY22 Val ($)	Land tax liability FY21 ($)	Land tax liability FY22 ($)	Percentage change in land tax liability	Percentage change in valuation above indexation
Adelaide City Council	3,975,000	7,100,000	74,438	148,340	99%	72%
Adelaide City Council	2,875,000	4,725,000	48,038	91,340	90%	57%

Cameo 2

The revaluation of the properties shown under Cameo 2 have resulted in a significant increase in valuations of the sites, which has meant that their tax liabilities on the individual sites provided have more than doubled across the board. **Table 4** shows the impact the revaluation initiative has had on the CBD-based commercial real estate holdings of Cameo 2.

Table 4: Cameo 2 land tax changes

Property LGA	FY21 Val ($)	FY22 Val ($)	Land tax liability FY21 ($)	Land tax liability FY22 ($)	% change in land tax liability	% change in valuation above indexation
Adelaide City Council	2,400,000	4,900,000	36,638	95,540	161%	97%
Adelaide City Council	2,850,000	5,150,000	47,438	101,540	114%	74%
Adelaide City Council	2,900,000	7,325,000	48,638	153,740	216%	146%
Adelaide City Council	3,800,000	9,625,000	70,238	208,940	197%	146%

Cameo 3

The revaluation of Cameo 3's holdings have been reasonably large, however volatile, resulting in their tax liabilities on the individual sites significantly increasing for some, but barely shifting for one. **Table 5** shows the impact the revaluation initiative has had on the CBD-based commercial holdings of Cameo 3.

Table 5: Cameo 3 land tax changes

Property LGA	FY21 Val ($)	FY22 Val ($)	Land tax liability FY21 ($)	Land tax liability FY22 ($)	% change in land tax liability	% change in valuation above indexation
Adelaide City Council	5,100,000	10,250,000	107,890	230,466	114%	94%
Adelaide City Council	4,050,000	4,175,000	82,690	84,666	2%	-4%
Adelaide City Council	4,050,000	6,825,000	82,690	148,266	79%	62%

Cameo 4

Cameo 4 saw revaluations dramatically impact their land tax liabilities across the board. Most notably, the largest increase from a percentage point of view comes from those revaluations that pushed the lower value properties up into the higher tax brackets. Overall, these increases will prove to be difficult to manage from a cash flow perspective. The revaluations and their impacts on Cameo 4's land tax liability can be seen in **Table 6**.

Table 6: Cameo 4 land tax changes

Property LGA	FY21 Val ($)	FY22 Val ($)	Land tax liability FY21 ($)	Land tax liability FY22 ($)	% change in land tax liability	% change in valuation above indexation
Adelaide City Council	1,850,000	3,400,000	23,438	59,540	154%	77%
Adelaide City Council	3,330,000	6,525,000	58,958	134,540	128%	89%
Adelaide City Council	711,000	1,534,200	1,305	14,761	1031%	109%
Adelaide City Council	1,500,000	2,025,000	15,038	26,540	76%	28%
Adelaide City Council	1,650,000	2,175,000	18,638	30,140	62%	25%

Cameo 5

Cameo 5 also suffered large upward revisions in the values of their holdings, resulting in dramatic increases in their land tax liabilities. Similar to Cameo 4, the largest percentage increases came from pushing previously lower-value properties up into a higher tax bracket. There are also large absolute level increases in liabilities for higher-value properties. These figures can be seen in **Table 7**.

Table 7: Cameo 5 land tax changes

Property LGA	FY21 Val ($)	FY22 Val ($)	Land tax liability FY21 ($)	Land tax liability FY22 ($)	% change in land tax liability	% change in valuation above indexation
Adelaide City Council	3,950,000	6,350,000	73,838	130,340	77%	54%
City of Port Adelaide Enfield	840,000	1,150,000	2,828	6,340	124%	30%
City of Port Adelaide Enfield	940,000	1,200,000	4,078	7,340	80%	21%
City of Port Adelaide Enfield	1,175,000	1,350,000	7,938	10,340	30%	8%
City of Port Adelaide Enfield	680,000	850,000	1,150	2,410	110%	18%
Adelaide City Council	5,675,000	7,675,000	115,238	162,140	41%	28%
City of Port Adelaide Enfield	6,625,000	7,500,000	138,038	157,940	14%	6%

Cameo 6

Cameo 6 has had a somewhat more mixed impact from the revaluation initiative, with some properties having their valuations revised downwards. While this is welcome, and likely an indication of the increased accuracy and fairness of the dataset and methodology that the Valuer-General is now using, the revaluation initiative has still increased the tax bill overall for Cameo 6 by 32 per cent, or almost $180,000 across all properties. Cameo 6 revaluations and liabilities can be seen in **Table 8**.

It should be noted that the properties listed in **Table 8** are likely held across different individuals and organisations. As such, this total figure has been calculated based on the individual land tax liabilities on each property. It should also be interpreted purely as an example highlighting that decreases in valuations are not typically of a large enough magnitude to offset the significant increases caused by the revaluation initiative.

Table 8: Cameo 6 land tax changes

Property LGA	FY21 Val ($)	FY22 Val ($)	Land tax liability FY21 ($)	Land tax liability FY22 ($)	% change in land tax liability	% change in valuation above indexation
Adelaide City Council	2,550,000	7,625,000	40,238	160,940	300%	192%
Adelaide City Council	2,250,000	3,925,000	33,038	72,140	118%	67%
West Torrens	670,000	1,125,000	1,100	5,848	432%	61%
Adelaide City Council	3,950,000	5,625,000	73,838	112,940	53%	35%
West Torrens	1,050,000	1,300,000	5,453	9,340	71%	17%
Burnside	3,225,000	3,675,000	56,438	66,140	17%	7%
Port Adelaide Enfield	3,275,000	3,550,000	57,638	63,140	10%	1%
Charles Sturt	2,150,000	2,225,000	30,638	31,340	2%	-4%
West Torrens	1,875,000	1,875,000	24,038	22,940	-5%	-7%
West Torrens	620,000	620,000	850	690	-19%	-7%
West Torrens	2,625,000	2,425,000	42,038	36,140	-14%	-15%
Prospect	4,875,000	4,250,000	96,038	79,940	-17%	-20%
Adelaide City Council	4,825,000	4,025,000	94,838	74,540	-21%	-24%

Cameo 7

Given the relatively low valuations of some of Cameo 7's properties, the percentage increase of their tax liabilities for some properties has been extremely volatile, with the liability for one property increasing by more than 500 per cent. Again, this largely comes from a relatively lower-value property being pushed into a higher tax bracket. While this may not be a large absolute increase, the dramatic volatility will still prove to be an issue regarding cash flow management. These results can be seen in **Table 9**.

Table 9: Cameo 7 land tax changes

Property LGA	FY21 Val ($)	FY22 Val ($)	Land tax liability FY21 ($)	Land tax liability FY22 ($)	Percentage change in land tax liability	% change in valuation above indexation
Adelaide City Council	1,575,000	1,875,000	16,838	22,940	36%	12%
Adelaide City Council	1,400,000	3,300,000	12,638	57,140	352%	129%
Adelaide City Council	2,625,000	3,125,000	42,038	52,940	26%	12%
Adelaide City Council	920,000	1,950,000	3,828	24,740	546%	105%
West Torrens	1,250,000	1,625,000	9,438	16,940	79%	23%
Adelaide City Council	3,125,000	5,200,000	54,038	102,740	90%	59%
Adelaide City Council	2,400,000	3,500,000	36,638	61,940	69%	39%

Options for Managing the Implementation of the Initiative

The sudden impact of the Valuer-General's revaluation initiative will result in a significant hit to cash flow to many investors at a time when they can least afford it.

Along with the cash flow impact is the market valuation impact – an increase in land tax can only be passed onto a small number of tenants and is therefore absorbed by the landlord and thus reducing the net income of the property and resultant valuation.

Vacancies and rental or lease incentives for many commercial properties are at recent record highs in response to challenging market conditions, attributable in-part to stay-at-home and other public health orders imposed or recommended by the State Government.

Workforce occupancy in CBD commercial buildings has also been a present and ongoing challenge.

While it is acknowledged that land tax liabilities need to be calculated based on market site values, the sudden change in liabilities (driven by the way values are assessed) has the real potential to damage investor confidence at a time when South Australia should be doubling-down to attract investment off the back of its comparatively successful experience in managing the COVID-19 pandemic.

Instead of a sudden change in liabilities and hit to cash flow, the revaluation should be implemented in a way that allows investors to manage the change in their liabilities over a period of time to smooth the impact to cash flow and protect investor confidence.

There is room to do this, with the cameos outlined above showing significantly higher upward revisions in values, and hence liabilities (and tax receipts) than assumed in the 2021-22 State Budget. There is also likely room under existing Budget measures, with the 2021-22 State Budget outlining a $15.5 million underspend in the land tax relief fund for landlords and commercial owner occupiers.[4]

The Property Council is committed to working constructively and proactively with the State Government to deliver an economically efficient, pragmatic outcome that sees liabilities calculated at market rates, without the unhelpful and damaging hit to confidence that would result from a sudden change in land tax liabilities. Dramatic changes in land tax liabilities can deal a significant hit to property sector confidence. For example, in Victoria, following a significant increase in their top land tax rates, confidence in that jurisdiction has plummeted with Victoria dropping to the bottom of the ANZ/Property Council confidence survey for the 2021 September quarter.

The Property Council has developed a range of policy options for delivering this outcome and undertaken a multi-criteria assessment of options to provide a considered view of how to achieve the best outcome for the State and investors alike.

[4] Ibid (page 6).

Policy Options

The following options have been identified for the implementation of the revaluation initiative.

A Rebase thresholds to negate average property price increases, which would effectively and dramatically increase the threshold indexation to offset some of the larger increases in site valuations.

B Cap annual increases in tax liabilities regardless of the increase in the underlying site value, capping the maximum amount that the actual liability can increase as a result.

C Implement trailing average of holding values which would smooth the impact of a dramatic single year increase in the valuation of a site value and allow the liability to increase gradually over time.

D Implement a stepped increase in valuations – similar to capping the increase – but time-limited (instead of permanent) to account for the likely transitory nature of dramatically increased valuations across a single year period.

Policy Option A

Rebase thresholds to negate average property price increases

This option would involve an expansion of indexing arrangements under current legislation, whereby thresholds are adjusted by an index value calculated based on changes in average site values post-revaluation, rather than before. In other words, the threshold index could be increased significantly to assist in offsetting the increases in land tax liabilities that dramatic upward revisions of valuations have and will result in.

Effectively, this would mean that the impact of revaluations would be negated in perpetuity, unless the thresholds are subsequently readjusted. Land holders with revaluations greater than average would still incur an increased tax bill, but those at or below the average would not have any increase. In fact, those below the average would see a decrease. Thus, there are equity of outcomes considerations for this proposal. It is also somewhat counter-intuitive to the purpose of this policy proposal. This is because those that are going to be most affected by the revaluation initiative are the property holders who see the largest increase in the value of their property – this policy is essentially missing the target and giving a tax concession to the least affected.

The likely revenue impact would be a substantial write-down in revenues collected relative to the “no change” scenario. Based on the distribution of revenues observed in previous analyses, it is thought to be unlikely that this would result in a reduction in revenue in an absolute sense, but still a sizeable write-down. Write-downs in revenues recorded under the policy variation estimate included in the Budget would also be expected.

The cost of this policy measure will at least match or exceed ‘booked’ revenue, deteriorating net operating balance (NOB) and increasing general government sector (GGS) net debt. As such, this option will effectively wipe out any revenue uplift. This is because there is no change in revenue, therefore no additional volatility in revenue – a neutral result. Discovery of true revenue foregone is prevented without subsequent analysis. Therefore, accounting for this as a policy measure would be difficult without further, in-depth analysis.

It should also be acknowledged that the current top tax threshold has been legislated in the *Land Tax (Miscellaneous) Amendment Act 2019* to increase to $2 million for FY23. Because of this, there may be virtually negligible change to the existing policy.

Policy Option B

Cap annual increases in tax liabilities

Taxpayers' liabilities are assessed as current measure (reflecting revaluation). However, this policy proposes implementing a cap on the maximum increase in tax payable. To do this effectively, this cap would be constructed as a fixed rate cap on change in liabilities.

To implement this practically, this will need to be fixed at the average value of sites to prevent double counting the effect of indexation on liabilities. This will allow the liability to be reflected over time, with the cap imposed via policy or legislation, i.e. ex gratia relief administered via Revenue SA or via an instrument under new regulations.

The impact on revenue would likely be a write-down in revenues in an absolute sense, assuming the cap is set below the average increase in holdings values. However, this may not result in a write-down in forecast revenues under the policy measure, depending on whether the cap is set above the average increase in holding values assumed under the current policy measure.

The cost of this policy measure is essentially reflected in the difference between the cap rate being implemented, and the assumed rate under the current revaluation policy measure. If equal, this will be revenue neutral over time and in absolute terms. The cost of this measure will grow as the assumed rate falls away post-revaluation.

It is important to note that this policy is perhaps costly, depending on where the cap is set, and likely to be subject to criticism of the level of the cap, given the subjective nature of the decision on what level the cap should be set at. This will also be a significant reform to address a largely transitory issue, given that large updates to valuations are likely to become less prevalent as the Valuer-General's dataset is progressively updated over time, as outlined in the 2021-22 Budget.

Policy Option C

Implement trailing average of holding values

This policy measure would involve liabilities being calculated based on the average value of taxable holdings over a defined period – the Property Council's recommendation would be a three-year trailing average.

Changes in assessable interests would require liabilities to be calculated based on the average value of total interests within the assessment period. This means that interests would need to be assessed on a rolling basis and adjustments made accordingly.

The impact of the revaluation initiative would be smoothed over the assessment period, meaning their assessable interests would be lower than they would be otherwise after the end of the smoothing period (year 3 in this example).

The effect of this would be progressively smaller write-downs in booked revenues relative to the current policy measure in years 1 and 2, before reaching approximate parity in year 3. Individual years may exhibit more or less revenue, depending on volatility in valuations. However, this would be expected to average out over time.

The trailing average would also smooth the index value applied to thresholds, meaning a small transfer may occur between those that currently have more frequent changes in holdings values, specifically those above the top tax rate threshold, towards those having their holdings values reduced through the measure until year 3.

Whether this policy measure exceeds 'booked' revenue depends on average annual increases relative to assumed holding value increase in booked revenue. If the figure – approximated by compound annual growth rate (CAGR) – is less than the assumed rate in current measure, NOB will decline and GGS net debt will increase in 'in' years of forward estimates before trending towards neutral. In this instance, the policy measure will still be raising revenue relative to no change, but this will manifest as a revenue reduction from a Mid-Year Budget Review (MYBR) perspective.

This policy measure will assist in smoothing the change in revenue by approximately CAGR. The only uncertainty will come from upside, positive tail risk to budget.

This will eventually lead to the same outcome once the averaging period washes through, but those whose holdings move beyond average site value changes – but less than they would be under the current measure – wear a greater share of the burden. These taxpayers are expected to sit in the middle of the holdings value distribution.

Policy Option D

Implement a stepped increase in valuations

Essentially, this policy proposal is a revised version of the option that caps the increase in land tax liabilities.

However, this policy is time-limited to reflect the likely transitory nature of the revaluation initiative and its largest increased valuations of property values.

The same conclusions apply as with the capped increases, but with the liabilities in the revaluation year framed around the number of steps chosen – notionally two or three steps.

The cost of the policy measure is effectively the same as Option B, before snapping back to a neutral result after the final step has been implemented, so long as the transition periods are similar. NOB will be down in the short-term and GGS net debt will remain permanently increased as a result.

Where this policy proposal is potentially limited is that there seems to be no indication on how long the revaluation initiative will run, or how long the improved dataset and methodology will continue to put upward pressure on property valuations.

This means that this policy measure will likely require an extension or revision if significant upward pressure on valuations continues.

Assessment of Options

Each policy was assessed against seven criteria, organised under two categories (policy and strategic). Criteria were weighted evenly—to avoid any assumptions around the policy priorities of the government—with a score between 1 (low) and 3 (high) assigned to each criterion based on anticipated performance of the option against the criteria. A high rating indicates greater desirability of the policy option according to that criteria, from the perspective of the government.

Table 10: MCA analysis criteria, weighting, and score range

Criteria			Weighting	High	Low
1	**Policy**				
	1.1	Revenue measure impact	0.14	3	1
	1.2	Revenue volatility	0.14	3	1
	1.3	Revenue measure certainty	0.14	3	1
	1.4	Equity in outcomes	0.14	3	1
	1.5	Ease of implementation	0.14	3	1
2	**Strategic**				
	2.1	Extent of change from existing policy position	0.14	3	1
	2.2	Consistency with current platform	0.14	3	1

Table 11 shows the scores given to each policy against each of the criteria. While these are subjective rankings, scoring has been allocated on a consistent basis, to provide a consistent, considered approach to assessing options.

Table 11: Scoring of policy options against criteria

		Criteria						
Option		**1.1**	**1.2**	**1.3**	**1.4**	**1.5**	**2.1**	**2.2**
A	Rebase thresholds to negate average property price increases	1	2	1	1	3	1	1
B	Cap annual increases in tax liabilities	2	2	3	1	1	1	2
C	Implement trailing averages of holding values	3	3	2	3	1	2	2
D	Implement a stepped increase in valuations	2	3	2	2	1	2	3

A weighted score is then calculated based on the weightings attached to individual criteria (which was allocated evenly) and respective scores, with the results included in **Table 12**.

Table 12: Scoring of each policy option

Option		Total score	Weighted score
A	Rebase thresholds to negate average property price increases	10	1.43
B	Cap annual increases in tax liabilities	12	1.71
C	Implement trailing averages of holding values	16	2.29
D	Implement a stepped increase in valuations	15	2.14

Each of these policies needs to be assessed carefully on their impact on the State Government's Budget, and their effectiveness in achieving the Property Council's overall policy objective of smoothing the impact of the revaluation initiative for property holders.

It is recognised that the South Australian State Government has provided financial and policy support to the property sector through the COVID-19 pandemic, and the transition period between land tax arrangements. For example, South Australia's Code of Conduct for commercial leasing is nation leading.

As such, the motive of this policy document is to not to lobby for concessions for the property sector that create a liability for the State Government's Budget. It is more aimed at assisting landlords and investors in managing their cash flow to cushion the impact of the revaluation initiative.

Based on rankings and the stated purpose of the policies outlined in this document, **the Property Council recommends that the State Government investigates implementing Policy C, which uses a trailing average measure of holding values**. This policy will be effective in assisting landlords and investors to manage the transition period of significantly revised valuations from a cash flow perspective, while recognising the improved accuracy of the Valuer-General's determinations.

The trailing average policy proposal will likely be cost-neutral to Government and will assist Government in smoothing the increased revenue from the revaluation initiative over time, while giving South Australian property holders sufficient time to adjust to the new-normal and presenting a far more competitive market to inbound investors.

To provide an example of Policy C in action – and the impact that it will have on land tax liabilities for land holders – **Table 13** illustrates this policy in practice. Incorporating the assumed average growth in property valuations of 3 per cent following this initial increase – from the 2021-22 Budget – we can see that this policy is effective in smoothing the impact for land holders who have seen changes in their property's valuation.[5]

There is also an assumption that property values prior to the significant revaluation did not move. This is necessary given past valuation data was unavailable for the purposes of this policy proposal. **Table 13** uses the valuations of Cameo 6 to demonstrate the changes in land tax liabilities following the implementation of Policy C.

It should also be noted that while the percentage change over forward years are still significant, the actual underlying magnitude of these valuations are diminishing over time, assisting landlords in smoothing their cash flow impact.

[5] Ibid (page 40).

Table 13: Policy C impact on the land tax liabilities of Cameo 6 over the current and subsequent two financial years

	Valuations ($)		Current policy year to year land tax liability change (%)			Policy C year to year land tax liability change (%)		
Property LGA	**FY21**	**FY22**	**FY21 to FY22**	**FY22 to FY23**	**FY23 to FY24**	**FY21 to FY22**	**FY22 to FY23**	**FY23 to FY24**
Adelaide City Council	2,550,000	7,625,000	300%	-6%	3%	98%	34%	41%
Adelaide City Council	2,250,000	3,925,000	118%	-17%	3%	37%	-2%	32%
West Torrens	670,000	1,125,000	432%	3%	4%	87%	88%	51%
Adelaide City Council	3,950,000	5,625,000	53%	-10%	3%	17%	0%	18%
West Torrens	1,050,000	1,300,000	71%	4%	4%	10%	26%	24%
Burnside	3,225,000	3,675,000	17%	-19%	3%	4%	-18%	9%
Port Adelaide Enfield	3,275,000	3,550,000	10%	-20%	3%	2%	-20%	6%
Charles Sturt	2,150,000	2,225,000	2%	-43%	4%	-2%	-46%	5%
West Torrens	1,875,000	1,875,000	-5%	-6%	4%	-5%	-9%	2%
West Torrens	620,000	620,000	-19%	3%	3%	-19%	-6%	-2%
West Torrens	2,625,000	2,425,000	-14%	-37%	4%	-6%	-41%	-6%
Prospect	4,875,000	4,250,000	-17%	-15%	3%	-6%	-21%	-5%
Adelaide City Council	4,825,000	4,025,000	-21%	-16%	3%	-8%	-23%	-8%

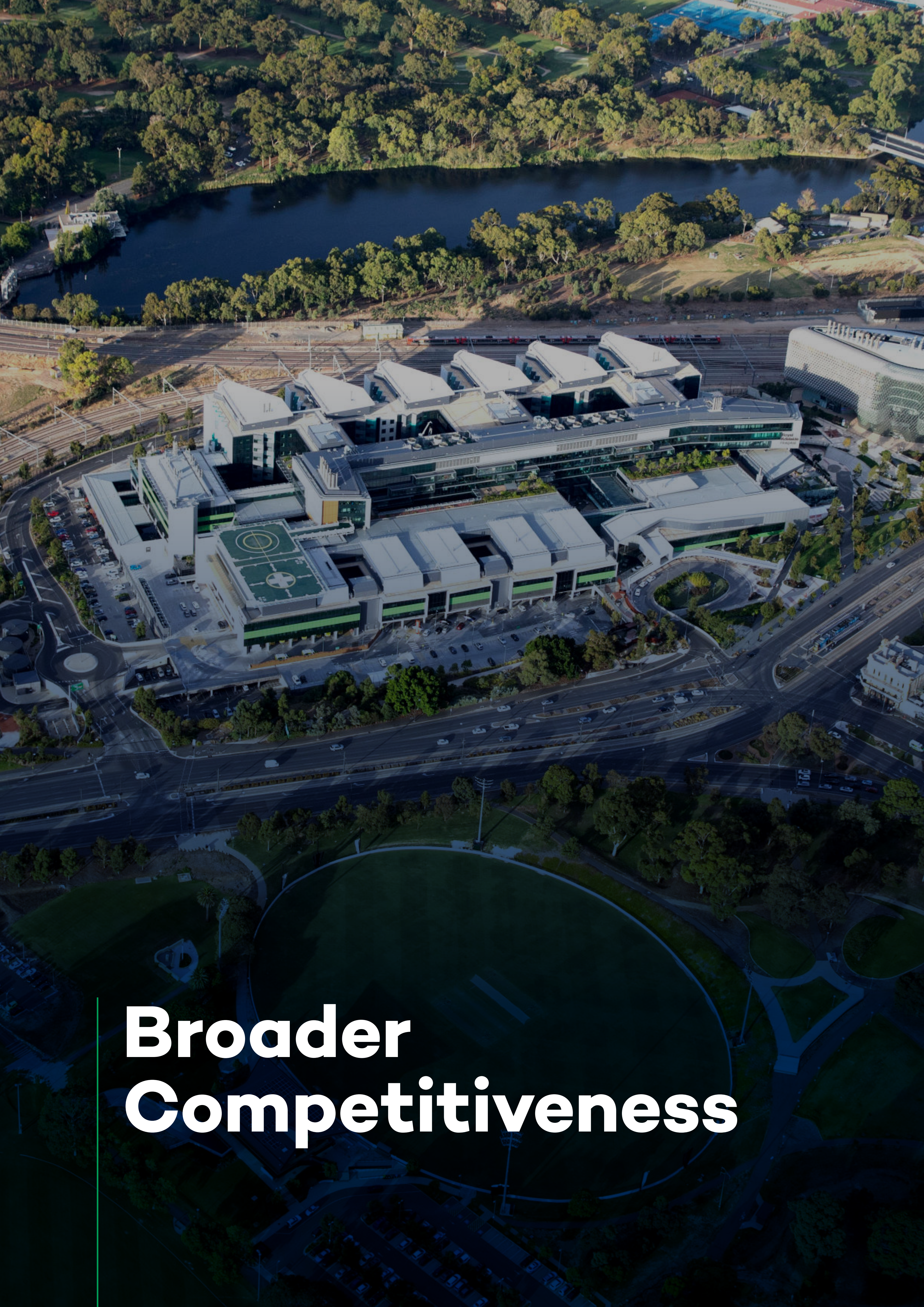
Property values around the $2 million mark at the time of the threshold increase saw significant drops in their liabilities.

Overall, **Table 13** clearly shows the effectiveness of Policy C in smoothing the land tax liabilities on those properties that were subject to significant upwards revisions in their valuations as a result of the revaluation initiative.

The figures shown in **Table 13** were calculated using the legislated increase in the top land tax rate threshold to $2 million for FY23.

Property prices under both policy models were increased at the estimated rate of 3 per cent - according to the 2021-22 Budget Papers – where Policy C valuations were increased in-line with Policy C's trailing average method as well as by the estimated 3 per cent each year.[6] Thresholds across future financial years were increased at the same 3 per cent rate. Flat fees were increased at 5 per cent per annum, approximately in-line with increases over the years preceding the 2019 land tax changes.

[6] Ibid (page 30).



Broader Competitiveness

The recommended option (Policy C – three-year trailing average for valuing sites) represents a sensible, cost-effective option for implementing the revaluation of land values.

To leverage this implementation, consideration also needs to be given to how to best use this change to drive improvements in the competitiveness of South Australia's land tax regime.

The priority for reform should be revising the top marginal rate of land tax, as it represents the most important lever for competitiveness in properties that will attract the largest share of investment in commercial and industrial property in the coming years. Investment in new commercial and industrial property will be critical to growing the productive capacity of the South Australian economy, and by doing so achieving the 3 per cent growth target to be met by Growth State.

With South Australia's interstate migration movement turning around over the past year, the State Government is well-placed to further encourage this trend to continue. A reduction in the top tax rate from 2.4 per cent to 1.9 per cent would see South Australia still maintain its significant revenue stream from land taxes, but drop it below the national average, as can be seen in **Chart 1**, sending a strong message to the property sector.

Importantly, a new rate of 1.9 per cent would make South Australia the most competitive state to invest on mainland Australia at the same time Adelaide has been recognised as the nation's most liveable city.

Chart 1: South Australian current and proposed maximum land tax rates, compared to current, or legislated future, maximum land tax rates of other jurisdictions, and the national average

Figure 1: Current and legislated future land tax rates around Australia.

Sources:

- Western Australia: Government of Western Australia, Department of Finance, About land tax <https://www.wa.gov.au/organisation/department-of-finance/land-tax>.
- Queensland: Queensland Government, Environment, land and water, Rates for companies and trustees <https://www.qld.gov.au/environment/land/tax/calculation/companies>.
- South Australia: Government of South Australia, RevenueSA, Rates and thresholds <https://www.revenuesa.sa.gov.au/landtax/rates-and-thresholds>; Land Tax (Miscellaneous) Amendment Bill South Australia (2019)
- New South Wales: NSW Government, Revenue NSW, Land tax <https://www.revenue.nsw.gov.au/taxes-duties-levies-royalties/land-tax#calculate>.
- Victoria: State Revenue Office Victoria, Land tax current rates <https://www.sro.vic.gov.au/land-tax-current-rates>; State Revenue Office Victoria, State Budget 2021-22 announcements <https://www.sro.vic.gov.au/state-budget-2021-22-announcements>.
- Tasmania: State Revenue Office of Tasmania, Rates of land tax <https://www.sro.tas.gov.au/land-tax/rates-of-land-tax>.

*Not including the additional 2 per cent absentee surcharge that will come into effect at the same time

While it is likely that the initiative of reducing South Australia's top land tax rate would have an impact on South Australian State Government revenue, it could reasonably be argued that this revenue will be regained in the medium- to long-term through increased economic activity and takings from a more active property sector.

If this shift to a more competitive land tax rate was to come into effect in FY24 – in conjunction with Policy C – this could have significant positive effects for the property sector. This impact is shown in **Table 14**, which shows the effect of this reduction in the top tax rate on the land tax liabilities of Cameo 1. This will free-up cash and help drive investment in the property sector. The same method and assumptions have been applied as in **Table 13**.

The only difference being the reduction in the top tax rate from 2.4 per cent to 1.9 per cent in FY24.

The second highest tax bracket then effectively becomes obsolete. As such, this has been taken out of this tax structure.

As can be seen in **Table 14**, Policy C is effective in smoothing the land tax liability of Cameo 1. On top of this, the reduction in the top tax rate then allows those increases in their land tax liability to level out sooner. Effectively, this prevents the shock of the revaluation initiative from causing a significant cash-flow issue for Cameo 1, but then speeds up the stabilisation process, freeing up capacity to expand investment.

Table 14: Policy C impact on the land tax liabilities of Cameo 1 over the current and subsequent two financial years, with a reduction in the top tax rate to 1.9 per cent for FY24

	Valuations ($)		Current policy year to year land tax liability change (%)			Policy C year to year land tax liability change, with top rate reduction in FY24 (%)		
Property LGA	**FY21**	**FY22**	**FY21 to FY22**	**FY22 to FY23**	**FY23 to FY24**	**FY21 to FY22**	**FY22 to FY23**	**FY23 to FY24**
Adelaide City Council	3,975,000	7,100,000	99%	-7%	3%	32%	12%	1%
Adelaide City Council	2,875,000	4,725,000	90%	-13%	3%	29%	1%	3%

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