ACT Government

Chief Minister and Treasury

GOVERNMENT RESPONSE TO MR SMYTH'S MOTION REGARDING ANALYSIS UNDERTAKEN ON TAXATION REFORM

Treasurer

Mr Andrew Barr MLA

October 2013

1. Executive Summary

On 19 September 2013, the ACT Legislative Assembly passed a motion regarding the tabling of taxation reform analysis undertaken by the ACT Government. The motion called on the Government to:

1) note the information provided in the 2012-13 and 2013-14 Budget Papers concerning the taxation reforms; and
2) in accordance with standing order 213A, calls on the government to table by 31 October 2013 any other analysis of the impacts that the taxation reforms implemented to date are expected to have over time.

This paper provides an overview of relevant modelling and analysis undertaken as part of the ACT Taxation Review and for the 2012-13 and 2013-14 Budgets.

2. ACT Taxation Review

The ACT Government commissioned the ACT Taxation Review in 2010. The Terms of Reference for the review included an examination of the overall efficacy of the tax system including:

- whether the mix of taxes currently levied is appropriate;
- whether the current ACT tax base is equitably and effectively distributed;
- options to ensure revenue certainty and sustainability of the tax base;
- whether reforms are required to improve efficiency and equity of the tax base; and
- completing a social impact assessment of any proposed reforms.

The Taxation Review was undertaken by Mr Ted Quinlan (chair), Professor Alan Duncan, and Ms Megan Smithies. The Panel undertook a comprehensive analysis of the Territory's taxation system in a wide range of contexts including, other jurisdictions' tax systems, the ACT's economic structure, its socio-demographic composition, expenditure needs, and Government policy objectives.

Both the ACT Review and the earlier Commonwealth Review (the Henry Review of 2010) concluded that the ACT's tax system – like all other jurisdictions – is inefficient and unsustainable.

The panel found that the ACT's taxation mix is not out of the norm, taking into account its circumstances. The report highlighted that the Territory's taxation system, like that of other States, is not sustainable in the long term. The panel made 27 recommendations in total on a range of different issues and highlighted the case for reform of the Territory's taxation system.

The Taxation Review found that the ACT has access to an efficient and broad land taxation base not readily available to other States i.e. general rates. The report contained a number of different options available to government to consider in transitioning towards a more stable revenue base over the long term.

The ACT Taxation Review was publically released on 7 May 2012.

Appendix A contains detail on the modelling and analysis undertaken as part of the ACT Taxation Review.

3. Taxation Reform: 2012-13 Budget

The ACT Government committed to undertaking significant reform to the Territory's taxation system over a 20 year period as part of the 2012-13 Budget. This reform will put the Territory on a strong footing for the future and provide flexibility to deal with our demographic changes and fiscal challenges and to respond to external economic circumstances.

The ACT Government was the first government in Australia to undertake such reform. However, it was recognised that reform was not a set and forget process but an ongoing process that requires adjustments, flexibility and responsiveness over the longer term. As such, the 2012-13 Budget announced that reform would be undertaken over a 20 year period to provide time for the market to adjust to the changes and to enable that the reform did not occur in an inequitable manner.

The Government committed to providing updated taxation reform figures annually, for the coming forward estimates periods, as part of the budget. Given the difficulty of predicting property prices, economic growth and interest rates over long time periods into the future, the Government has focussed on annual updates within rolling five year reform programs.

The ACT is in a unique position to pursue taxation reform. It has both the roles of a state and local government, and hence, has access to a broad based tax of general rates. The first tranche of major reforms announced included:

- abolishing duty on insurance policies over five years;
- abolishing conveyance duty over 20 years;
- abolishing commercial land tax;
- increasing the tax free threshold for payroll tax; and
- making residential land tax and the general rates system more progressive.

These reforms are being undertaken in a staged approach to allow ACT households and the economy time to adjust. The reforms will be funded through general rates to ensure revenue neutrality for the Budget overall, while preserving capacity for government services and ensuring future generations do not bear the higher economic costs of an unfair and inefficient tax system.

To assist households and cushion the impacts of taxation reform, a number of concession schemes were provided in the 2012-13 Budget. These measures included:

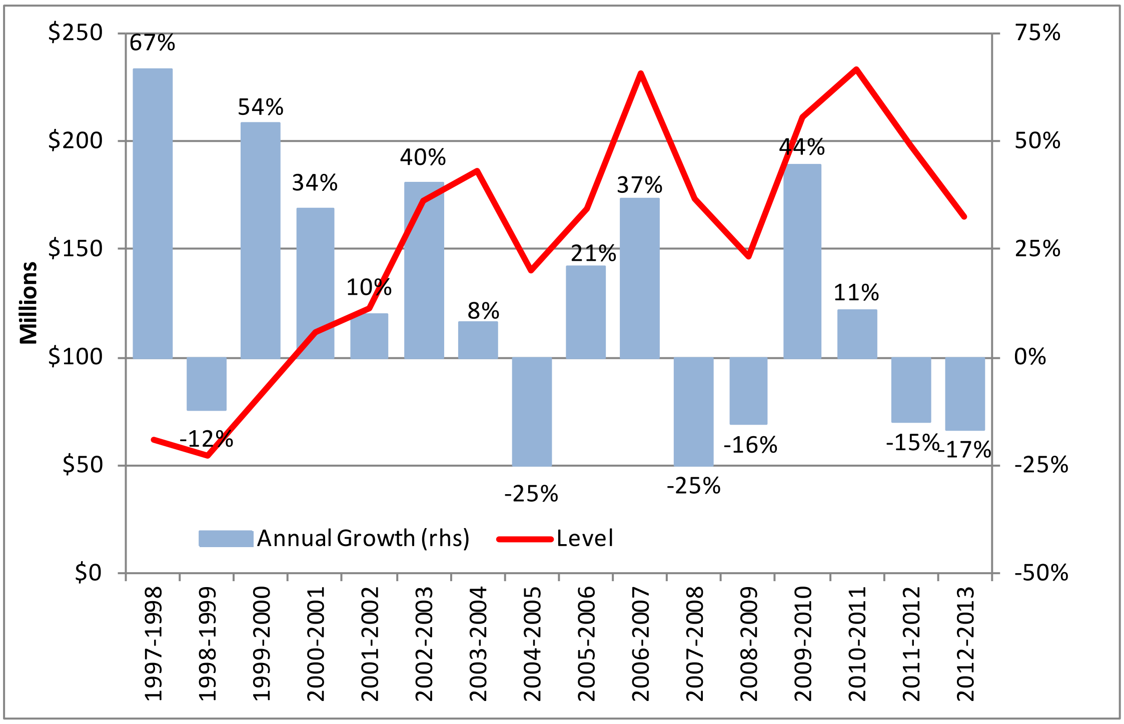
- expanding the Home Buyer Concession Scheme;
- extending the Pensioner Duty Concession Scheme;

- increasing the rates rebate scheme; and
- expanding the eligibility for the Rates Deferral Scheme.

Conveyance duty is an inefficient tax - it is transaction based, its incidence is uneven (impacting on a small percentage of the population only in any year period), and hence it has a distortionary economic burden. The amount of revenue raised fluctuates greatly from year to year, making it difficult to estimate future revenue with any degree of certainty and hence making budget planning difficult.

Chart 1 below shows the fluctuations in revenue conveyance revenue from 1997-98 to 2012-13. It shows that the revenue changed greatly from year to year, hence making it difficult to estimate future revenue. The budgets reliance on inefficient taxes will reduce over time. The cumulative economic benefit of improved economic efficiency was estimated to be $169 million in the first five years.

Chart 1: Residential Conveyance Duty: 1997-1998 to 2012-2013



Appendix B contains detail of the modelling and analysis undertaken as part of the 2012-13 Budget.

4. Taxation Reform: 2013-14 Budget

The ACT Government continued implementation of its taxation reform agenda in the 2013-14 Budget. Duty on general insurance premiums reduced from 8 per cent to 6 per cent and duty on life insurance premiums from 4 per cent to 3 per cent. Conveyance duty rates also reduced in line with the five year plan announced in the 2012-13 Budget. In addition, the reduction in conveyance duty was accelerated for properties valued at $1.65 million and above with the introduction of a flat rate of 5.5 per cent, taking into account the ACT having one of the highest rates in Australia to one of the lowest.

Reforms were also introduced to improve affordable housing in the Territory including:

- further expanding the Home Buyer Concession Scheme to provide greater levels of assistance to more households;
- retargeting and increasing the First Home Owners Grant (FHOG) to $12,500 for the purchase of new and substantially renovated properties; and
- a reduction of land tax on properties with average unimproved land values between $75,000 and $390,000.

Appendix C contains details of the modelling and analysis undertaken as part of the 2013-14 Budget.

5. Long Term (20 Year) Modelling

Modelling and analysis has been undertaken to consider the longer term pattern of revenue replacement between the residential revenue lines impacted by taxation reform.

This section outlines the long term modelling for residential general rates undertaken as part of the 2013-14 Budget. The **pre tax reform scenario analysis** (Section 5.1) outlines a range of possible long term revenue paths based on differing assumptions.

It is important to note that the trajectory of reform will not necessarily be linear and these projections are for estimation purposes only.

The analysis provides a range of possible target revenue paths. No single path is definitive; no single path was intended to be used as a defined reform approach or revenue replacement amount.

Rather the analysis provides tools by which to measure the overall progress and pace of the reforms and assess the efficacy of either accelerating or slowing the rate of individual reforms of taxation lines based on prevailing economic circumstances, broader fiscal strategy of the Government and the assessed financial capacity of ACT households and businesses.

The **tax reform scenario analysis** (Section 5.2) then considers, for the purpose of illustration, three of these paths – medium growth path, low growth path and high growth path. For each path, different options for the pace of tax reform are projected and the impact on average conveyance duty and average general rates estimated. The options are:

- immediate policy change;
- uniform path; and
- ten per cent revenue replacement path.

5.1 Pre Tax Reform Scenario Analysis

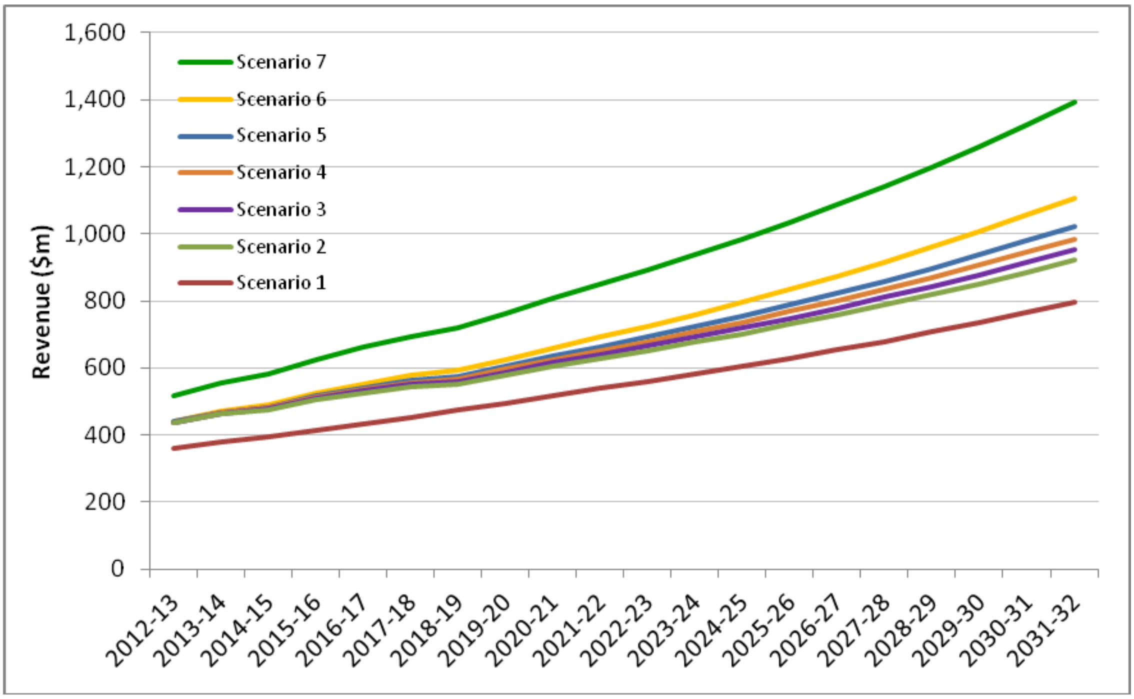
This section outlines the modelling of residential general rates pre tax reform. The pre tax reform models projected long-run revenue for general rates, insurance duty, conveyance duty and revenue in aggregate without taxation reform. The projections were based on a range of low, medium and high assumptions for long term population growth, property turnover, house price growth and wage price index. An overview of these assumptions is provided in the Table below. Attachment A contains further detail of the underlying assumptions relevant to each scenario.

Table 1: Pre tax reform assumptions for Scenarios 1-7

Scenario	WPI Annual Growth (%)	Population Annual Growth	Turnover to Stock Ratio	House Price Growth (%)
1	3	0.5%	6%	4.580
2	2.5	2012-13 to 2016-17: 1.5% p.a. 2017-18 to 2031-32: 1.03% p.a.	9% to 6% over 20 years	4.481
3	3	As above	9% to 6% over 20 years	4.481
4	3.5	As above	9% to 6% over 20 years	4.481
5	4	As above	9% to 6% over 20 years	4.481
6	5	As above	9% to 6% over 20 years	4.481
7	5	2%	12% to 9% over 20 years	4.479

These projected long term revenue paths are presented in Chart 2 below.

Chart 2: Projected Long Term Revenue over 20 years



The models were a basis to show a range of impacts – with more exaggerated impacts emerging from the extreme assumptions under scenarios 1 and 7. Each model is static (in that the assumptions are held constant over the 20 year period) and no single model is intended to reflect an actual outcome, but rather a range of possible outcomes over the period. The variables for which assumptions made will change constantly and can be difficult to estimate with certainty over the long term other than in trend terms.

The **medium growth** assumptions (Scenario 5) were used as a base line against which to measure the rates at which abolition of insurance duty and conveyance duty could be undertaken. The impacts under a low growth and high growth scenario (Scenario 1 and 7) were also considered.

Table 2 below shows the estimated revenue under the medium growth assumptions.

Table 2: Pre Tax Reform Projected Revenue under the Medium Growth Assumptions

	General Rates ($m)	**Conveyance Duty** ($m)	**Insurance Duty** ($m)	**Total** ($m)	(% change)
2011-12	183.6	209.2	28.0	420.8	
2012-13	191.0	218.6	29.4	439.0	4.3
2013-14	198.6	239.3	30.9	468.8	6.8
2014-15	206.6	245.6	32.4	484.6	3.4
2015-16	214.8	268.5	34.0	517.3	6.8
2016-17	223.4	282.6	35.7	541.7	4.7
2017-18	232.4	293.0	37.4	562.8	3.9
2018-19	241.6	295.1	39.3	576.0	2.3
2019-20	251.3	313.3	41.2	605.8	5.2
2020-21	261.4	332.4	43.3	637.0	5.2
2021-22	271.8	347.2	45.4	664.4	4.3
2022-23	282.7	362.7	47.6	693.1	4.3
2023-24	294.0	379.6	50.0	723.5	4.4
2024-25	305.8	397.0	52.5	755.2	4.4
2025-26	318.0	415.5	55.1	788.6	4.4
2026-27	330.7	434.8	57.8	823.3	4.4
2027-28	343.9	454.9	60.6	859.5	4.4
2028-29	357.7	476.5	63.6	897.8	4.5
2029-30	372.0	498.6	66.8	937.4	4.4
2030-31	386.9	522.2	70.1	979.1	4.4
2031-32	402.4	546.5	73.5	1,022.4	4.4

The pre tax reform projected revenue under each of the scenarios 1-7 are summarised in the table below. The full set of results are at Attachment A to this paper.

Table 3: Pre Tax Reform Projected Revenue under different scenarios

	2031-32 Projected results			
	General Rates	Conveyance Duty	Insurance Duty	Total
	($m)	($m)	($m)	($m)
Scenario 1	331.7	390.6	73.5	795.8
Scenario 2	300.9	546.5	73.5	920.9
Scenario 3	331.7	546.5	73.5	951.7
Scenario 4	365.4	546.5	73.5	985.4
Scenario 5	402.4	546.5	73.5	1,022.4
Scenario 6	487.2	546.5	73.5	1,107.2
Scenario 7	487.2	831.6	73.5	1,392.4

5.2 Tax Reform Scenario Analysis

The following section presents analysis undertaken on the medium growth scenario from Section 5.1. It investigates the impact of taxation reform under different assumptions, including:

- an immediate policy change;
- a uniform path; and
- a revenue replacement path.

Immediate policy change

This scenario considered the impact if all tax reform was implemented on 1 July 2012. That is, all inefficient taxes were abolished and immediately transferred to the general rates base. General rates increase by 139 per cent in 2012-13 and by 4 per cent per annum until 2031-32.

Table 4 below shows the impact on general rates from this model.

Table 4: Projected Revenue under a One-off Policy Change

	Conveyance Duty ($m)	Insurance Duty ($m)	General Rates ($m)	General Rates (% change)
2011-12	209.2	28.0	183.6	
2012-13	0.0	0.0	439.0	139
2013-14	0.0	0.0	456.5	4
2014-15	0.0	0.0	474.8	4
2015-16	0.0	0.0	493.8	4
2016-17	0.0	0.0	513.5	4
2017-18	0.0	0.0	534.1	4
2018-19	0.0	0.0	555.4	4
2019-20	0.0	0.0	577.7	4
2020-21	0.0	0.0	600.8	4
2021-22	0.0	0.0	624.8	4
2022-23	0.0	0.0	649.8	4
2023-24	0.0	0.0	675.8	4
2024-25	0.0	0.0	702.8	4
2025-26	0.0	0.0	730.9	4
2026-27	0.0	0.0	760.2	4
2027-28	0.0	0.0	790.6	4
2028-29	0.0	0.0	822.2	4
2029-30	0.0	0.0	855.1	4
2030-31	0.0	0.0	889.3	4
2031-32	0.0	0.0	924.9	4

Uniform path

This scenario considered the impact if tax reform is implemented in a uniform manner. That is, if residential conveyance is reduced by 5 per cent per annum and insurance duty is reduced by 20 per cent per annum.

This uniform path, reflects the aspirations of longer term tax reform – that residential conveyance duty is abolished over 20 years, and insurance duty is abolished by 1 July 2016.

This path was not definitive; it is not intended to be used as a defined reform approach or revenue replacement amount. Rather it provided a tool by which to measure the overall progress and pace of the reforms and assess the efficacy of either accelerating or slowing the rate of individual reforms of taxation lines based on prevailing economic circumstances, broader fiscal strategy of the Government and the assessed financial capacity of ACT households and businesses. Table 5 below shows the impact on general rates from this model.

Table 5: Projected Revenue under the Uniform Path

	Conveyance Duty ($m)	Insurance Duty[1] ($m)	General Rates ($m)	General Rates (% change)	Total ($m)	Total (% change)
2011-12						
2012-13	207.7	23.5	207.8	13	439.0	
2013-14	215.4	18.5	234.9	13	468.8	6.8
2014-15	208.8	13.0	262.8	12	484.6	3.4
2015-16	214.8	6.8	295.7	13	517.3	6.8
2016-17	211.9	0	329.7	12	541.7	4.7
2017-18	205.1		357.4	8	562.5	3.8
2018-19	191.8		383.5	7	575.3	2.3
2019-20	188.0		416.7	9	604.7	5.1
2020-21	182.8		452.7	9	635.5	5.1
2021-22	173.6		488.8	8	662.4	4.2
2022-23	163.2		527.3	8	690.6	4.3
2023-24	151.8		568.7	8	720.5	4.3
2024-25	138.9		612.6	8	751.6	4.3
2025-26	124.7		659.6	8	784.3	4.4
2026-27	108.7		709.6	8	818.3	4.3
2027-28	91.0		762.8	7	853.8	4.3
2028-29	71.5		819.8	7	891.3	4.4
2029-30	49.9		880.2	7	930.1	4.3
2030-31	26.1		944.7	7	970.8	4.4
2031-32	0		1,013.1	7	1,013.1	4.4

The total revenue from general rates, conveyance revenue and insurance duty under this tax reform scenario is slightly lower than the pre-tax reform revenue (see Table 1). This occurs as conveyance revenue is assumed to increase at a higher rate than general rates in the medium growth scenario (around 5 per cent capturing CPI, growth of property values and other factors). When conveyance duty is replaced by general rates, it grows at the assumed growth rate for this revenue line (around 4 per cent WPI).

This analysis is presented in Chart 3 below.

[1] Insurance Duty decreases uniformly over 5 years from the base case.

Chart 3: Projected Cumulative Revenue under the Uniform Path

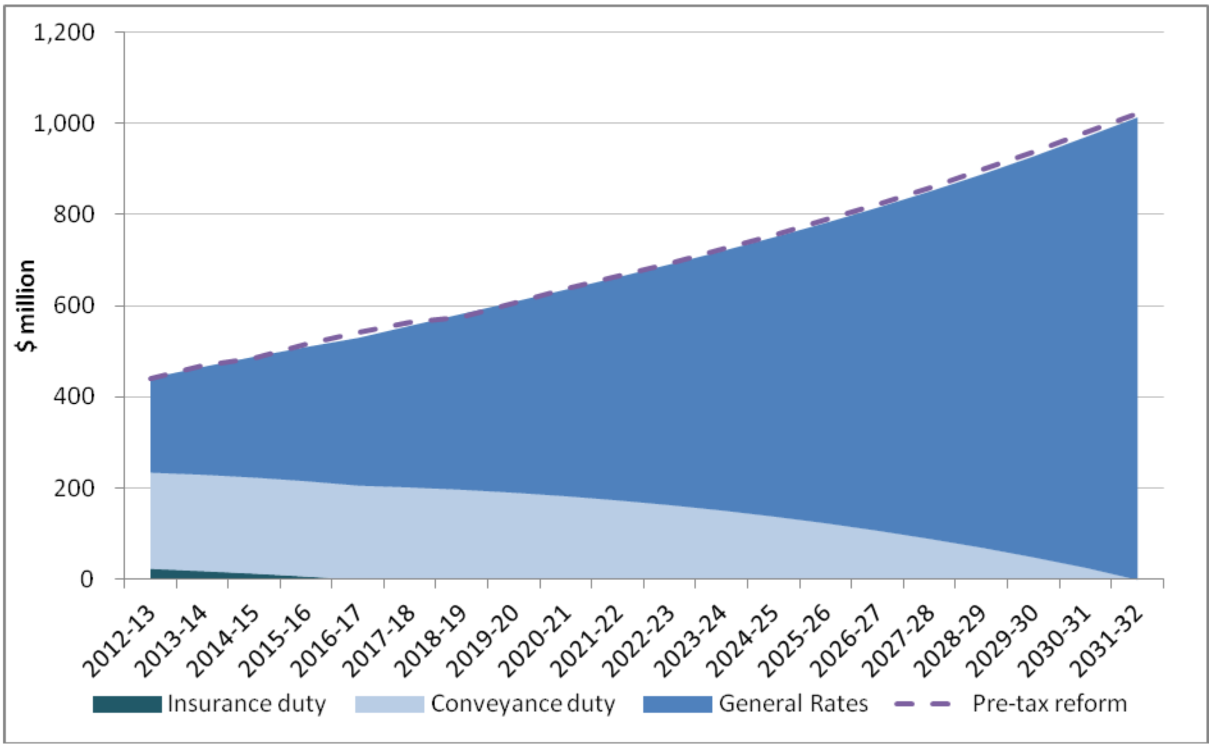


Chart 3 shows the difference between general rates with reform compared to general rates without reform. It shows the impact of the abolition of insurance and conveyance duty on general rates over the 20 year period.

Revenue replacement path

The objective of the 10 per cent revenue replacement scenario was to reduce the impact on residential general rates over the first 5 years while insurance duty is being abolished.

Hence, the increase in general rates revenue was adjusted for an average level of increase of 10 per cent from 2013-14 to 2016-17. This scenario means the offset of conveyance duty is slightly lower than the uniform path would suggest, but is increased over the remaining 15 years once insurance duty is fully abolished.

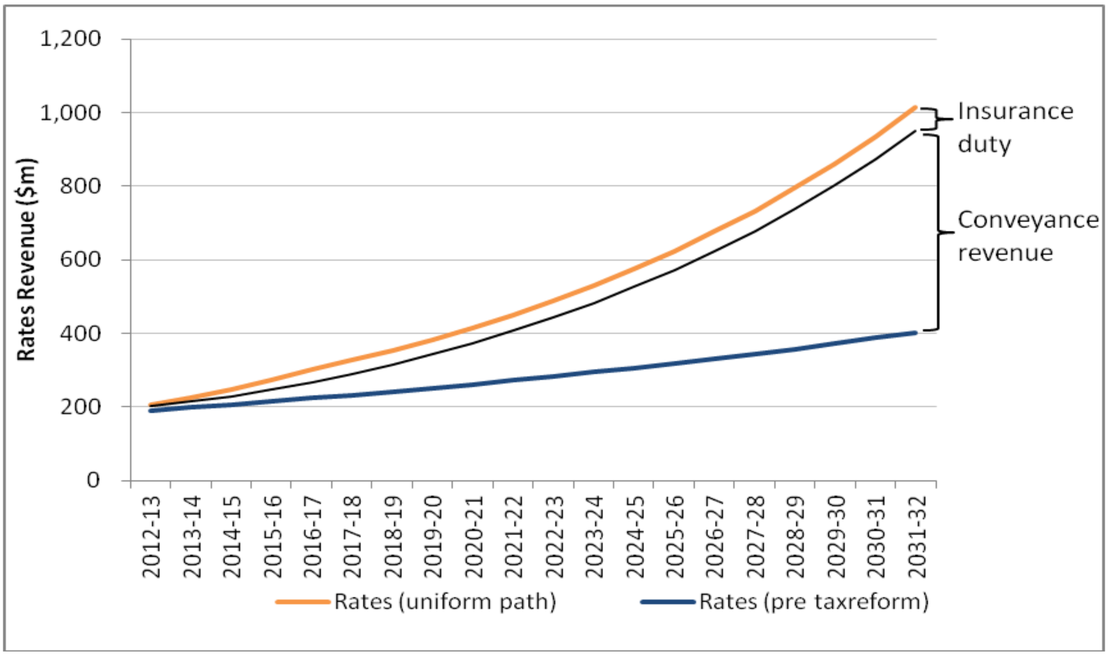
Table 6 below shows the impact on general rates from this model.

Table 6: Projected Revenue Replacement Path (10% for 5 years)

	Conveyance duty ($m)	Insurance duty ($m)	General ($m)	Rates (% change)	Total ($m)	(% change)
2011-12						
2012-13	208.4	23.5	205.4		437.3	
2013-14	224.3	18.5	225.9	10	468.8	7.2
2014-15	223.1	13.0	248.5	10	484.6	3.4
2015-16	237.1	6.8	273.4	10	517.3	6.8
2016-17	240.9	0.0	300.7	10	541.7	4.7
2017-18	236.4		326.1	8	562.5	3.8
2018-19	221.8		353.6	8	575.3	2.3
2019-20	221.3		383.4	8	604.7	5.1
2020-21	219.8		415.7	8	635.5	5.1
2021-22	211.6		450.8	8	662.4	4.2
2022-23	201.7		488.8	8	690.6	4.3
2023-24	190.4		530.0	8	720.5	4.3
2024-25	176.8		574.8	8	751.6	4.3
2025-26	161.0		623.2	8	784.3	4.4
2026-27	142.5		675.8	8	818.3	4.3
2027-28	121.0		732.8	8	853.8	4.3
2028-29	96.7		794.6	8	891.3	4.4
2029-30	68.4		861.6	8	930.0	4.3
2030-31	36.5		934.3	8	970.8	4.4
2031-32	0.0		1,013.1	8	1,013.1	4.4

This analysis is presented in Chart 4 below.

Chart 4: Projected general rates revenue – Components



The same analysis was also undertaken for the Low and High growth scenarios – details are provided at Attachment B.

A summary table of the results based on the low, medium and high scenarios is provided in the table below.

Table 7: Projected replacement revenue - Summary of results for low, medium and high growth scenarios

	Low growth Scenario 1		Medium Growth Scenario 5		High Growth Scenario 7	
	2012-13 ($m)	**2031-32 ($m)**	**2012-13 ($m)**	**2031-32 ($m)**	**2012-13 ($m)**	**2031-32 ($m)**
Conveyance Duty	130.2	0.0	208.4	0.0	287.8	0.0
Insurance Duty	23.5	0.0	23.5	0.0	23.5	0.0
General Rates	205.4	777.8	205.4	1,013.1	205.4	1,393.0
Total	**359.1**	**777.8**	**437.4**	**1,013.1**	**516.7**	**1,393.0**

Impact on average stamp duty and average general rates

For illustration purposes, this section considers the impact on average stamp duty and average general rates for the medium growth scenario (scenario 5).

Medium Growth scenario

Immediate policy change

An immediate policy change, to immediately abolish insurance and conveyance duty, illustrates the effect of tax reform most clearly.

On this basis, the average general rates before tax reform of $1,350 in 2012-13 increased as a result of the immediate transfer of the inefficient duties to $3,090 – an increase of 2.3 times the pre tax reform level.

Conveyance duty is a tax which applies selectively to individuals based on their choice to transact in the property market – under the reform program it is being shifted to a tax base which applies the burden equitably across all rate payers. Insurance duty, while also selective, is more broadly spread across most property owners already. In comparing the impact of this shift in tax, the movement of conveyance duty could better be measured against the pre-existing base of general rates plus insurance duty.

The increase for the average household on this basis, above that under the pre-tax reform levels was 2.1 times (or slightly more than a doubling).

<u>20 year reform path</u>

This section illustrates the impact of transferring insurance duty over 5 years and conveyance duty over 20 years. The uniform path and the revenue replacement path involve a slightly different rate of transfer, however, by the end of the 20-year period, general rates will have increased to the same level, necessarily.

If the model's estimate of revenue in 2031-32 eventuates, the average general rates as a result from the transfer of the inefficient duties will be $2,940 (in 2012-13 dollars) – an increase of 2.2 times the 2012-13 pre tax reform level of average general rates. Measured against a base of general rates and insurance duty, as explained above, the higher general rates at the end of the 20 year reform for the average household, is 1.9 times the 2012-13 pre-tax reform average general rates.

5.3 Case Studies – Individual Perspectives

In aggregate, the shifting of the tax bases is being undertaken on a revenue neutral basis. However, the impact on an individual will differ depending on their particular circumstance.

This section considers the impact on an individual under a range of scenarios.
While the general rates paid by an individual will increase, this is a consequence of shifting inefficient taxes into the general rates base and hence consideration needs to be given to the reduction in tax in other areas to determine the overall impact on the individual.

The case studies presented below consider an individual who purchases a house at different stages through the tax reform program and estimates the aggregate impact on that individual across the relevant tax lines which are the subject of the reform.

Three scenarios are considered, to show the differential impacts by value of property – lower quartile, median value and upper quartile property – and within each scenario, three different timings of house purchase are considered.

Note that for all scenarios the individual would be in broadly the same financial situation regardless of the stage during the reform program at which they purchased their property.

Case Study 1 – Lower Quartile Property Value

<u>*Assumptions:*</u>

- *House price is $411,000 (REIA Market Facts June quarter 2012) with an AUV of $227,000.*
- *The house purchase and conveyance duty are covered by a mortgage, over 20 years, at an average rate of 7.5 per cent per annum.*
- *The typical period for holding a property is ten years.*

Consider the impact on an individual if they purchase the property outlined above at different stages through the tax reform program – consider Year 1, Year 5 and Year 10.
In the first year of the tax reform programme, this individual would pay **$39,940** in aggregate over the ten year holding period for the property, across the relevant tax lines:

- Conveyance duty of $13,823;
- Insurance duty of $75 over the ten years;
- General rates of $16,999 over the ten years; and
- additional interest cost over the ten years (due to conveyance duty paid through the mortgage) of $9,043.

(Or alternatively, you could consider it as opportunity cost on the potential investment of that amount over the ten years, at an assumed investment return of 5 per cent, is $8,693)

At Year 5 of the tax reform programme, the individual would pay **$37,550** in aggregate over the ten year holding period for the property, across the relevant tax lines:

- Conveyance duty of $9,900;
- Insurance duty of $5 over the ten years;
- General rates of $21,168 over the ten years; and
- additional interest cost over the ten years (due to conveyance duty paid through the mortgage) of $6,477.

(Or alternatively, you could consider it as opportunity cost on the potential investment of that amount over the ten years, at an assumed average investment return of 5 per cent, is $6,226).

At Year 10 of the tax reform program the individual would pay **$38,038** in aggregate over the ten year holding period for the property, across the relevant tax lines:

- Conveyance duty of $6,584;
- Insurance duty of $nil;
- General rates of $27,146 over the ten years; and
- additional interest cost over the ten year (due to conveyance duty paid through the mortgage) of $4,308.

(Or alternatively, you could consider it as opportunity cost on the potential investment of that amount over the ten years, at an assumed investment return of 5 per cent, is $4,141).

Case Study 2 – Median Property Value

<u>*Assumptions:*</u>

- *House price is $494,100 (REIA Market Facts June quarter 2012) with an AUV of $273,000.*
- *The house purchase and conveyance duty are covered by a mortgage, over 20 years, at an average rate of 7.5 per cent per annum.*
- *The typical period for holding a property is ten years.*

Consider the impact on an individual if they purchase the property outlined above at different stages through the tax reform programme – consider Year 1, Year 5 and Year 10. In the first year of the tax reform programme, this individual would pay **$48,351** in aggregate over the ten year holding period for the property, across the relevant tax lines:

- Conveyance duty of $17,770;
- Insurance duty of $75 over the ten years;
- General rates of $18,881 over the ten years; and
- additional interest cost over the ten years (due to conveyance duty paid through the mortgage) of $11,626.

(Or alternatively, you could consider it as opportunity cost on the potential investment of that amount over the ten years, at an assumed investment return of 5 per cent, is $11,175).

At Year 5 of the tax reform programme, the individual would pay **$45,391** in aggregate over the ten year holding period for the property, across the relevant tax lines:

- Conveyance duty of $13,224;
- Insurance duty of $5 over the ten years;
- General rates of $23,511 over the ten years; and
- additional interest cost over the ten year (due to conveyance duty paid through the mortgage) of $8,652.

(Or alternatively, you could consider it as opportunity cost on the potential investment of that amount over the ten years, at an assumed average investment return of 5 per cent, is $8,317).

At Year 10 of the tax reform program (assuming the reform continues according to the 10 per cent path outlined above, since conveyance duty rates have not been defined beyond 5 years), the individual would pay **$44,773** in aggregate over the ten year holding period for the property, across the relevant tax lines:

- Conveyance duty of $8,840;
- Insurance duty of $0 over the ten years;
- General rates of $30,150 over the ten years; and
- additional interest cost over the ten year (due to conveyance duty paid through the mortgage) of $5,783.

(Or alternatively, you could consider it as opportunity cost on the potential investment of that amount over the ten years, at an assumed investment return of 5 per cent, is $5,559).

Case Study 3 – Upper Quartile Property Value

<u>Assumptions:</u>

- *House price is $590,000 (REIA Market Facts June quarter 2012) with an AUV of $326,000.*
- *The house purchase and conveyance duty are covered by a mortgage, over 20 years, at an average rate of 7.5 per cent per annum.*
- *The typical period for holding a property is ten years.*

Consider the impact on an individual if they purchase the property outlined above at different stages through the tax reform programme – consider Year 1, Year 5 and Year 10. In the first year of the tax reform programme, this individual would pay **$59,176** in aggregate over the ten year holding period for the property, across the relevant tax lines:

- Conveyance duty of $23,000;
- Insurance duty of $75 over the ten years;
- General rates of $21,054 over the ten years; and
- additional interest cost over the ten years (due to conveyance duty paid through the mortgage) of $15,047.

(Or alternatively, you could consider it as opportunity cost on the potential investment of that amount over the ten years, at an assumed investment return of 5 per cent, is $14,465).

At Year 5 of the tax reform programme, the individual would pay **$55,932** in aggregate over the ten year holding period for the property, across the relevant tax lines:

- Conveyance duty of $17,960;
- Insurance duty of $5 over the ten years;
- General rates of $26,217 over the ten years; and
- additional interest cost over the ten year (due to conveyance duty paid through the mortgage) of $11,750.

(Or alternatively, you could consider it as opportunity cost on the potential investment of that amount over the ten years, at an assumed investment return of 5 per cent, is $11,295).

At Year 10 of the tax reform program (assuming the reform continues according to the 10 per cent path outlined above, since conveyance duty rates have not been defined beyond 5 years), the individual would pay **$53,613** in aggregate over the ten year holding period for the property, across the relevant tax lines:

- Conveyance duty of $12,086;
- Insurance duty of $0 over the ten years;
- General rates of $33,620 over the ten years; and
- additional interest cost over the ten year (due to conveyance duty paid through the mortgage) of $7,907.

(Or alternatively, you could consider it as opportunity cost on the potential investment of that amount over the ten years, at an assumed average investment return of 5 per cent, is $7,601).

5.4 Whole of Government Budget Analysis

The above analysis considered the shifting of taxes between conveyance and insurance duty to general rates over a 20 year period given assumed levels of growth of those lines and importantly, maintaining revenue neutrality.

As pointed out earlier, it's important to note the tax reform program must have regard for the broader budget context, and remain flexible to respond to the external impacts on the budget which will occur, but cannot be predicted, over a twenty year period.

The tax reform program should be implemented to be consistent with, and to support where appropriate, the government's overall fiscal strategy.

Own tax revenue is a significant component of Budget revenue, and the general rates and conveyance components are a significant part of own tax revenue. The other significant component of revenue is Commonwealth government grants, which include GST revenues. The own tax revenue reform program should consider the potential for changing circumstances in regard to Commonwealth funding.

To illustrate this, hypothetical scenarios can be considered:

- GST revenue is a major component of Commonwealth funding and consequently ACT Revenue is particular sensitive to GST. A change in the ACT's relativity from the current 1.2 to say 1.4 would result in an increase in revenue from this source of about $150m in 2014-15 which is about 30 per cent of revenue across these three lines

- A 2 per cent cut in ACT Government expenditure while preserving National Partnership and Specific Purpose Funding Commonwealth grants would free up about $80 million in 2014-15.

While these scenarios are purely hypothetical, they serve to illustrate the importance of the broader budget and fiscal context in designing a program of tax reform over an extended period. The government, if presented with such a scenario at any stage during the 20 year tax reform program, could consider a range of options in managing its budget and advancing tax reform.

Attachment A: Further information regarding the Pre Tax Reform Scenario Analysis

Attachment A provides further information regarding the assumptions and results of the pre- tax reform scenario analysis.

Table A1 below shows the different assumptions under Scenarios 1-7.

Table A1: Assumptions and Estimated Total Revenue under Different Scenarios over the 20-Year Period

Scenario	WPI Annual Growth (%)	Population Annual Growth	Turnover to Stock Ratio	House Price Growth (%)	Total Revenue ($m)
1	3	0.5%	6%	4.580	795.8
2	2.5	• 2012-13 to 2016-17: 1.5% p.a. • 2017-18 to 2031-32: 1.03% p.a.	Declining from 9% to 6% over the 20 year	4.481	920.9
3	3	• 2012-13 to 2016-17: 1.5% p.a. • 2017-18 to 2031-32: 1.03% p.a.	Declining from 9% to 6% over the 20 year	4.481	951.7
4	3.5	• 2012-13 to 2016-17: 1.5% p.a. • 2017-18 to 2031-32: 1.03% p.a.	Declining from 9% to 6% over the 20 year	4.481	985.4
5	4	• 2012-13 to 2016-17: 1.5% p.a. • 2017-18 to 2031-32: 1.03% p.a.	Declining from 9% to 6% over the 20 year	4.481	1,022.4
6	5	• 2012-13 to 2016-17: 1.5% p.a. • 2017-18 to 2031-32: 1.03% p.a.	Declining from 9% to 6% over the 20 year	4.481	1,107.2
7	5	2%	Declining from 12% to 9% over the 20 year	4.479	1,392.4

The results for Pre Tax Reform Projected Revenue under each scenarios 1-7 are presented in the Tables below.

Table A2: Scenario One - Low

	Rates ($m)	**Conveyance duty** ($m)	**Insurance duty** ($m)	**Total** ($m)	**Total Growth Rate** (%)
2011-12	183.6	209.2	28.0	420.8	
2012-13	189.1	142.2	29.4	360.8	-14.3
2013-14	194.8	152.0	30.9	377.7	4.7
2014-15	200.7	161.9	32.4	395.0	4.6
2015-16	206.7	172.6	34.0	413.3	4.6
2016-17	212.9	184.1	35.7	432.7	4.7
2017-18	219.3	196.2	37.4	452.9	4.7
2018-19	225.8	208.8	39.3	474.0	4.6
2019-20	232.6	222.1	41.2	495.9	4.6
2020-21	239.6	236.0	43.3	518.9	4.6
2021-22	246.8	246.8	45.4	539.0	3.9
2022-23	254.2	258.2	47.6	560.0	3.9
2023-24	261.8	270.1	50.0	581.9	3.9
2024-25	269.7	282.6	52.5	604.8	3.9
2025-26	277.8	295.8	55.1	628.6	3.9
2026-27	286.1	309.7	57.8	653.6	4.0
2027-28	294.7	324.3	60.6	679.6	4.0
2028-29	303.5	339.6	63.6	706.8	4.0
2029-30	312.6	355.8	66.8	735.1	4.0
2030-31	322.0	372.7	70.1	764.8	4.0
2031-32	331.7	390.6	73.5	795.8	4.1

Table A3: Scenario Two

	Rates ($m)	Conveyance duty ($m)	Insurance duty ($m)	Total ($m)	Total Growth Rate (%)
2011-12	183.6	209.2	28.0	420.8	
2012-13	188.2	218.6	29.4	436.2	3.7
2013-14	192.9	239.3	30.9	463.1	6.2
2014-15	197.8	245.6	32.4	475.8	2.7
2015-16	202.7	268.5	34.0	505.2	6.2
2016-17	207.8	282.6	35.7	526.0	4.1
2017-18	213.0	293.0	37.4	543.4	3.3
2018-19	218.3	295.1	39.3	552.7	1.7
2019-20	223.7	313.3	41.2	578.2	4.6
2020-21	229.3	332.4	43.3	605.0	4.6
2021-22	235.1	347.2	45.4	627.7	3.7
2022-23	240.9	362.7	47.6	651.3	3.8
2023-24	247.0	379.6	50.0	676.5	3.9
2024-25	253.1	397.0	52.5	702.6	3.9
2025-26	259.5	415.5	55.1	730.0	3.9
2026-27	266.0	434.8	57.8	758.6	3.9
2027-28	272.6	454.9	60.6	788.2	3.9
2028-29	279.4	476.5	63.6	819.5	4.0
2029-30	286.4	498.6	66.8	851.8	3.9
2030-31	293.6	522.2	70.1	885.8	4.0
2031-32	300.9	546.5	73.5	920.9	4.0

Table A4: Scenario Three

	Rates ($m)	Conveyance duty ($m)	Insurance duty ($m)	Total ($m)	Total Growth Rate (%)
2011-12	183.6	209.2	28.0	420.8	
2012-13	189.1	218.6	29.4	437.1	3.9
2013-14	194.8	239.3	30.9	465.0	6.4
2014-15	200.7	245.6	32.4	478.7	2.9
2015-16	206.7	268.5	34.0	509.2	6.4
2016-17	212.9	282.6	35.7	531.1	4.3
2017-18	219.3	293.0	37.4	549.7	3.5
2018-19	225.8	295.1	39.3	560.2	1.9
2019-20	232.6	313.3	41.2	587.1	4.8
2020-21	239.6	332.4	43.3	615.3	4.8
2021-22	246.8	347.2	45.4	639.4	3.9
2022-23	254.2	362.7	47.6	664.6	3.9
2023-24	261.8	379.6	50.0	691.4	4.0
2024-25	269.7	397.0	52.5	719.1	4.0
2025-26	277.8	415.5	55.1	748.3	4.1
2026-27	286.1	434.8	57.8	778.7	4.1
2027-28	294.7	454.9	60.6	810.2	4.1
2028-29	303.5	476.5	63.6	843.6	4.1
2029-30	312.6	498.6	66.8	878.0	4.1
2030-31	322.0	522.2	70.1	914.2	4.1
2031-32	331.7	546.5	73.5	951.7	4.1

Table A5: Scenario Four

	Rates ($m)	Conveyance duty ($m)	Insurance duty ($m)	Total ($m)	Total Growth Rate (%)
2011-12	183.6	209.2	28.0	420.8	
2012-13	190.1	218.6	29.4	438.1	4.1
2013-14	196.7	239.3	30.9	466.9	6.6
2014-15	203.6	245.6	32.4	481.6	3.2
2015-16	210.7	268.5	34.0	513.2	6.6
2016-17	218.1	282.6	35.7	536.3	4.5
2017-18	225.7	293.0	37.4	556.2	3.7
2018-19	233.6	295.1	39.3	568.0	2.1
2019-20	241.8	313.3	41.2	596.3	5.0
2020-21	250.3	332.4	43.3	625.9	5.0
2021-22	259.0	347.2	45.4	651.6	4.1
2022-23	268.1	362.7	47.6	678.5	4.1
2023-24	277.5	379.6	50.0	707.0	4.2
2024-25	287.2	397.0	52.5	736.7	4.2
2025-26	297.2	415.5	55.1	767.8	4.2
2026-27	307.6	434.8	57.8	800.2	4.2
2027-28	318.4	454.9	60.6	834.0	4.2
2028-29	329.6	476.5	63.6	869.7	4.3
2029-30	341.1	498.6	66.8	906.5	4.2
2030-31	353.0	522.2	70.1	945.3	4.3
2031-32	365.4	546.5	73.5	985.4	4.2

Table A6: Scenario Five - Medium

	Rates ($m)	Conveyance duty ($m)	Insurance duty ($m)	Total ($m)	Total Growth Rate (%)
2011-12	183.6	209.2	28.0	420.8	
2012-13	191.0	218.6	29.4	439.0	4.3
2013-14	198.6	239.3	30.9	468.8	6.8
2014-15	206.6	245.6	32.4	484.6	3.4
2015-16	214.8	268.5	34.0	517.3	6.8
2016-17	223.4	282.6	35.7	541.7	4.7
2017-18	232.4	293.0	37.4	562.8	3.9
2018-19	241.6	295.1	39.3	576.0	2.3
2019-20	251.3	313.3	41.2	605.8	5.2
2020-21	261.4	332.4	43.3	637.0	5.2
2021-22	271.8	347.2	45.4	664.4	4.3
2022-23	282.7	362.7	47.6	693.1	4.3
2023-24	294.0	379.6	50.0	723.5	4.4
2024-25	305.8	397.0	52.5	755.2	4.4
2025-26	318.0	415.5	55.1	788.6	4.4
2026-27	330.7	434.8	57.8	823.3	4.4
2027-28	343.9	454.9	60.6	859.5	4.4
2028-29	357.7	476.5	63.6	897.8	4.5
2029-30	372.0	498.6	66.8	937.4	4.4
2030-31	386.9	522.2	70.1	979.1	4.4
2031-32	402.4	546.5	73.5	1,022.4	4.4

Table A7: Scenario Six

	Rates ($m)	Conveyance duty ($m)	Insurance duty ($m)	Total ($m)	Total Growth Rate (%)
2011-12	183.6	209.2	28.0	420.8	
2012-13	192.8	218.6	29.4	440.8	4.7
2013-14	202.5	239.3	30.9	472.6	7.2
2014-15	212.6	245.6	32.4	490.6	3.8
2015-16	223.2	268.5	34.0	525.7	7.2
2016-17	234.4	282.6	35.7	552.6	5.1
2017-18	246.1	293.0	37.4	576.6	4.3
2018-19	258.4	295.1	39.3	592.8	2.8
2019-20	271.3	313.3	41.2	625.8	5.6
2020-21	284.9	332.4	43.3	660.5	5.5
2021-22	299.1	347.2	45.4	691.7	4.7
2022-23	314.1	362.7	47.6	724.5	4.7
2023-24	329.8	379.6	50.0	759.3	4.8
2024-25	346.3	397.0	52.5	795.7	4.8
2025-26	363.6	415.5	55.1	834.1	4.8
2026-27	381.8	434.8	57.8	874.4	4.8
2027-28	400.8	454.9	60.6	916.4	4.8
2028-29	420.9	476.5	63.6	961.0	4.9
2029-30	441.9	498.6	66.8	1,007.3	4.8
2030-31	464.0	522.2	70.1	1,056.3	4.9
2031-32	487.2	546.5	73.5	1,107.2	4.8

Table A8: Scenario Seven - High

	Rates ($m)	Conveyance duty ($m)	Insurance duty ($m)	Scenario 6 ($m)	Total Growth Rate (%)
2011-12	183.6	209.2	28.0	420.8	
2012-13	192.8	296.1	29.4	518.3	23.2
2013-14	202.5	323.5	30.9	556.8	7.4
2014-15	212.6	337.3	32.4	582.3	4.6
2015-16	223.2	368.3	34.0	625.5	7.4
2016-17	234.4	391.1	35.7	661.2	5.7
2017-18	246.1	410.7	37.4	694.2	5.0
2018-19	258.4	422.2	39.3	719.8	3.7
2019-20	271.3	450.3	41.2	762.8	6.0
2020-21	284.9	480.0	43.3	808.2	5.9
2021-22	299.1	504.1	45.4	848.6	5.0
2022-23	314.1	529.4	47.6	891.1	5.0
2023-24	329.8	556.6	50.0	936.4	5.1
2024-25	346.3	585.0	52.5	983.7	5.1
2025-26	363.6	615.2	55.1	1,033.8	5.1
2026-27	381.8	646.8	57.8	1,086.3	5.1
2027-28	400.8	679.9	60.6	1,141.4	5.1
2028-29	420.9	715.3	63.6	1,199.8	5.1
2029-30	441.9	752.0	66.8	1,260.7	5.1
2030-31	464.0	791.0	70.1	1,325.1	5.1
2031-32	487.2	831.6	73.5	1,392.4	5.1

Attachment B: Further information regarding the Tax Reform Scenario Analysis

The following tables show the projected revenue replacement path for a range of different scenarios, including low growth (Table B1), medium growth (Table B2) and high growth (Table B3).

Table B1: Low Growth Scenario

	Conveyance Duty	Insurance Duty	Rates		Total Revenue	
	($m)	($m)	($m)	(% change)	($m)	(% change)
2011-12						
2012-13	130.2	23.5	205.4		359.1	
2013-14	133.2	18.5	225.9	10	377.7	5.2
2014-15	133.5	13.0	248.5	10	395.0	4.6
2015-16	133.1	6.8	273.4	10	413.3	4.6
2016-17	132.0	0.0	300.7	10	432.7	4.7
2017-18	132.2		320.4	7	452.6	4.6
2018-19	131.9		341.3	7	473.3	4.6
2019-20	131.2		363.7	7	494.8	4.6
2020-21	129.9		387.4	7	517.3	4.5
2021-22	124.2		412.8	7	537.0	3.8
2022-23	117.7		439.8	7	557.5	3.8
2023-24	110.3		468.6	7	578.9	3.8
2024-25	101.9		499.2	7	601.1	3.8
2025-26	92.5		531.9	7	624.4	3.9
2026-27	81.9		566.6	7	648.6	3.9
2027-28	70.2		603.7	7	673.9	3.9
2028-29	57.0		643.2	7	700.2	3.9
2029-30	42.5		685.3	7	727.8	3.9
2030-31	26.4		730.1	7	756.5	3.9
2031-32	0.0		777.8	7	777.8	2.8

Table B2: Medium Growth Scenario

	Conveyance Duty	Insurance Duty	Rates		Total Revenue	
	($m)	($m)	($m)	(% change)	($m)	(% change)
2011-12						
2012-13	208.4	23.5	205.4		437.3	
2013-14	224.3	18.5	225.9	10	468.8	7.2
2014-15	223.1	13.0	248.5	10	484.6	3.4
2015-16	237.1	6.8	273.4	10	517.3	6.8
2016-17	240.9	0.0	300.7	10	541.7	4.7
2017-18	236.4		326.1	8	562.5	3.8
2018-19	221.8		353.6	8	575.3	2.3
2019-20	221.3		383.4	8	604.7	5.1
2020-21	219.8		415.7	8	635.5	5.1
2021-22	211.6		450.8	8	662.4	4.2
2022-23	201.7		488.8	8	690.6	4.3
2023-24	190.4		530.0	8	720.5	4.3
2024-25	176.8		574.8	8	751.6	4.3
2025-26	161.0		623.2	8	784.3	4.4
2026-27	142.5		675.8	8	818.3	4.3
2027-28	121.0		732.8	8	853.8	4.3
2028-29	96.7		794.6	8	891.3	4.4
2029-30	68.4		861.6	8	930.0	4.3
2030-31	36.5		934.3	8	970.8	4.4
2031-32	0.0		1,013.1	8	1,013.1	4.4

Table B3: High Growth Scenario

	Conveyance Duty	Insurance Duty	Rates		Total Revenue	
	($m)	($m)	($m)	(% change)	($m)	(% change)
2011-12						
2012-13	287.8	23.5	205.4		516.7	
2013-14	312.4	18.5	225.9	10	556.8	7.8
2014-15	320.8	13.0	248.5	10	582.3	4.6
2015-16	345.3	6.8	273.4	10	625.5	7.4
2016-17	360.5	0.0	300.7	10	661.2	5.7
2017-18	360.8		333.1	11	693.9	5.0
2018-19	350.2		368.9	11	719.1	3.6
2019-20	353.1		408.6	11	761.7	5.9
2020-21	354.0		452.6	11	806.6	5.9
2021-22	345.3		501.3	11	846.6	5.0
2022-23	333.4		555.2	11	888.6	5.0
2023-24	318.3		615.0	11	933.3	5.0
2024-25	298.9		681.2	11	980.1	5.0
2025-26	275.1		754.5	11	1,029.5	5.0
2026-27	245.7		835.6	11	1,081.3	5.0
2027-28	210.1		925.6	11	1,135.7	5.0
2028-29	168.1		1,025.2	11	1,193.3	5.1
2029-30	117.8		1,135.5	11	1,253.3	5.0
2030-31	59.1		1,257.7	11	1,316.8	5.1
2031-32	0.0		1,393.0	11	1,393.0	5.8