What the Henry Review means for the property sector

The comprehensive review of the Australian taxation system contained plenty of recommendations but resulted in little action from the Federal Government. For property investors the playing field remains largely unchanged.

Titled 'Australia's Future Tax System', the Henry Review report spanned almost 1,000 pages and included 138 recommendations for taxation reform. The Review is arguably the most thorough assessment of the Australian taxation system and processes undertaken. The response from the Federal Government to the Henry Review has been characterised by a distinct lack of recognition for the vast majority of these recommendations.

The most significant recommendations to be supported by the Government were announced together with the report release on Sunday May 2. These included:

- A reduction in the company tax rate progressively from 30% to 28% by 2014/15.
- Superannuation reforms, including shifting the compulsory employer contribution from 9% to 12% by 2019/20 and a $500 annual superannuation bonus for workers earning under $37,000 per annum
- A 40% tax on profits from the resources sector (known as the Resource Super Profits Tax (RSPT)) which should funnel $12 billion in revenue to the Government over the first two years it is implemented.
- Establishment of a new infrastructure fund which will support state infrastructure projects.

The Henry Review had the potential to change the way Australian's view the property market as an investment class The big ticket recommendations for the property sector were associated with negative gearing, capital gains tax and stamp duty reform – all of which remained virtually untouched in the Federal Government's response to the review.

The Henry Review recommended replacing personal taxation discounts such as negative gearing and the 50% capital gains discount with a broader reaching 40% discount on interest income, net residential rental property income, capital gains and some interest expenses (recommendations 14 to 17). In the Federal Government's response these recommendations were largely ignored.

Investors can continue to use negative gearing to offset losses on their investment property against their personal income tax and capital gains are still subject to a 50% discount if the asset is held longer than one year.

It should come as no surprise that these tax discounts remained untouched, particularly in an election year. One only has to cast their mind back to 1985 when Treasurer Paul Keating attempted to tamper with negative gearing, replacing the policy with a system that offset net losses against future profits. The result was that investment in property declined significantly and with no introduction of new rental stock, rental rates shot upwards. Two years later the policy was wound back.

With Australia being largely reliant on private investors to introduce new rental stock, the resulting reduction in new rental supply that would result from a downturn in investment would likely be fuel to the fire of an already undersupplied rental market.

The Review also recommended major changes to stamp duty provisions, where state based stamp duties would be replaced by a more efficient and broader based land tax system. The recommended land tax system would apply to all land holdings and use a sliding scale for assessment based on value per square metre. In this way, more valuable land would be taxed at higher rates and concessions would be given to low value and agricultural land where the dollar value per square metre is likely to be relatively low. Additionally, land tax would be applicable to individual properties rather than across aggregated land holdings.
The Government has not commented on this recommendation, apart from stating that the family home would be exempt from any land tax. Removing stamp duties will not be a decision the Government makes lightly, considering that stamp duty makes up about 34% of State Government property taxes (which in turn comprise about 45% of the entire State Government revenue base).

Another key section from the Henry Review relates to housing affordability and housing assistance. The review proposes:

- “a review of institutional arrangements (including administration) to ensure zoning and planning do not unnecessarily inhibit housing supply and housing affordability”; and
- a review of infrastructure charges / developer charges to ensure they appropriately price infrastructure contributions from developers to ensure unnecessary costs are avoided, transparency of these charges is improved and reductions in regulation are introduced that will streamline the development time frame.
- an increase in the maximum rate of rental assistance and a provision for escalations in rental assistance to be indexed to rental rates rather than CPI.

All of these recommendations have been ignored in the Federal Governments response to the Henry Review.

Whilst the Government’s response seems to lack a great deal of support for the recommendations contained in the ‘Australia’s Future Tax System’ report, it is still early days. There are likely to be further announcements as the Government releases budget papers next week. In particular, the Government is expected to announce further intentions for tax simplification and savings incentives such as tax breaks on bank savings.

Overall for the property sector, it is largely ‘business as usual’ and potentially a case of ‘watch this space’.