Submission No. 63 - Mr David King - received 23/03/2018 - authorised for publication 28/03/2018.

SUBMISSION ON CHANGES TO CALCULATION OF RATES BY THE ACT GOVERNMENT

The following is a brief submission concerning the changes to the method the ACT Government uses to calculate the variable charge for rates for units in the ACT for 2017-18 and subsequent years. I maintain that the method now applied in the *Rates Act 2018* is inequitable, discriminates unfairly against unit owners and is illogical.

In my case, the overall effect has been fairly modest in 2017-18, about $330, an increase of about 25 per cent on the previous year. Most of this – about $300 – was due to the change in the valuation-based charge. However, it will be at least $100 higher next year due to the removal of the $100 rebate for units. The valuation-based component of my rates more than doubled (a 212 per cent increase).

This does not change the fact the change is irrational and unfairly discriminates against units, for the following reasons.

PREVIOUS SYSTEM

Rates are a tax on the land component of a property. They are determined on the unimproved capital value (actually site value I think) of the land. Under the system used before 2017-18, rates included a fixed charge and a variable charge (the valuation-based charge) and now include various other fixed components – the fire and emergency services levy and safer families levy (ignored for the purposes of this submission).

The valuation-based charge for residential properties is based on a progressive rate scale (as is the scale for commercial properties, although its rates are higher). There was a tax-free threshold in the past, although it appears that it was abolished some time ago. However, the bottom rate that applies up to $150,000 (the threshold is not indexed) at 0.2960 per cent is still somewhat lower than the next rate of 0.408 per cent that applies from $150,000 to $300,000 and so on. The ACT Government increased the rates in 2017-18 over 2016-17 and the fixed charge.

Previously what the Rates Act did (broadly) for units, was divide the total unimproved value of the property by the number of units on the property and then apply the rates scale to the quotient to determine the individual's rates liability. So, ignoring that unit entitlements could vary somewhat per apartment and unit entitlements were the actual divisor, if a property had a total unimproved value of $5 million and there were 50 units on the property (roughly the situation in my case, by the way), each unit owner had an unimproved capital value of $100,000. So each unit owner had a full tax-free threshold (when it existed) and enjoyed the full benefit of the lower rate scale. This (arguably) may not have been perfect but it was a fair and reasonable way to divide up the property and logically defensible. Each unit holder was treated the same way as every other property owner. It would be difficult to conceive of a fairer way to apply rates (or land tax) in a practical way.

THE NEW SYSTEM

What the new system does is treat developments with units on them as a single property and apply the rate scale to its total unimproved capital value and then divide this total rate liability by the number of unit owners to arrive at the individual's liability. In the example above, it is as if I owned a property with a $5 million unimproved capital value and my rates were determined on this basis. Then my considerably higher calculated rates liability is divided by 50 (as some sort of numerical concession) to determine my actual rates liability. I maintain this is ridiculous.

The effect of this calculation is that I obtain the benefit of only 1/50th of the lower rates threshold. If there were a tax-free threshold, I would obtain the benefit of only a 1/50th of the tax-free threshold. To suggest I own all of the common property (eg the backyard, stairwells, garbage room etc, which in my case may comprise say 2/3 of the total property, even more so, that I own all of the property, is ridiculous. I do not have exclusive use or exclusive possession of the common property and its land content. I have to share it with the other residents, which reduces its value (improved and unimproved) to me. Dividing the property up initially into 50 units recognised this in a reasonable way.

The land content of my small unit is small. That I should have only a fraction of the lower rate scales with my small unit and even smaller land content, simply because I live with other people in a separately titled development, is inequitable and arbitrary.

Note, as I understand it – I have only skimmed through the relevant part of the Rates Act so I cannot state with certainty – the ACT Government does not apply this treatment to houses that have multiple owners but are on a single property title. (Simply for the reason that they are on a single title?)

ACT GOVERNMNET'S RATIONALE

When I questioned my 2017-18 rates assessment – I confess I was initially surprised at it and could not believe rates were determined in this way –the ACT Revenue Office told me (essentially) the change in method was because the Government thought units did not pay enough rates. Some units paid less rates that vacant land, although the vacant land was worth less, and some units paid less rates that some houses of apparently lower market value. However, this is only to be expected. Rates are a tax on the unimproved land content of property. They are not a tax on the value of a property. If they were, I would object to it but the rates would at least be determined differently – by applying the same rates schedule to all properties – or a person's interest(s), aggregated or not, in his property. (The details do not concern us). This is not what is being done here.

It is understandable that the unimproved value/site value of vacant land in some areas would be higher than the unimproved value of some units (but not their market value). The vacant land does not have a residence on it so it may sell for less than land with units or a house on it. When the vacant land has been rezoned for residential uses and has houses or units on it, its unimproved capital value may increase considerably.

Further, it is to be expected that some houses may have a higher land content than some units and but a lower market value than some units. They may be in a less attractive location. The market value of a house or unit is determined by a range of factors (eg location/ distance from the city, size, closeness to other neighbourhood amenities, etc .) There is a trade off between location and size (among other factors). A large house far from the city may have a low market value for that reason but the size of the land (which obviously providers a compensatory benefit to the owners) may mean it has a higher unimproved capital value and hence higher rates. In other words, I may pay lower rates compared to some other property of lower total market value (unlikely but let us grant the possibility) because I choose to put up with the inconvenience of living in a small unit (but which is closer to the city). In my case, perhaps because my unit is so small, the outcome of the trade offs may be that the much lower land content outweighs the contribution of its more desirable (arguably) position for the purposes of rates determination. If rates used a different land value (eg some sort of 'improved value'), the outcome might be different in relation to some houses of allegedly lower market value. However, it would be wrong to say that I am getting more benefit

from my land than the owner of a large block of land of allegedly lower market value but paying less rates for that benefit.

I also note that the ACT Government apparently does not consider these arguments relevant in the analogous case of a multiple owner house ie a house say worth $5 million with 10 owners. In this case it appears each individual owner has his rates liability determined by applying the rates scale to his individual interest in the property.

There are also other possible anomalies.

ANOTHER RATIONALE

There may be another reason that the ACT Government chose to change the method for determining rates for units in this way. It may be concerned at the number of units being built on existing blocks of land. If each unit owner is given an individual rate scale that applies to his unit's proportional interest in the property, then relative to the rates liability that would arise if the property had a single owner, the rates on the property could fall (eg instead of rates being assessed on a $10 million unimproved value property, the rates would be assessed on a say 100 properties of $100,000 value. Because of the progressive rates scale, this would result in a lower total rates assessment.) The ACT Government could be concerned that this could cause a significant fall in the rate of growth of rates if repeated on a large scale. This is hard to believe given the size of the fixed charges in a rate assessment (the fixed charge component, the fire and emergency services levy and the safer families levy.)

- Furthermore, the ACT Government also announced in the 2017-18 Budget a new means of charging for unit titling so that it is now a fixed charge of $30,000 per unit. This would be equal, in present value terms, to my 2016-17 valuation based charge for over 100 years, and probably a broadly similar amount for other unit owners.
- This may be expected to be the outcome of high population growth for Canberra and the need to accommodate the greater number of people, with units (and smaller houses) being apparently the preferred means of doing so. Overall, ACT Government would be expected to benefit, probably also in revenue terms. More units on land means a parcel of land when it is developed and sold by the Government to developers will fetch a higher sale price than if it were used for houses alone and, for the time being, stamp duty would be higher.
- Rates thresholds are not indexed and a higher population and more units would be expected to lead to increases in unimproved values and a form of 'bracket creep'.
- There are also alternatives to the current methods. The fixed charge could be increased and the rates scale made less progressive (which the ACT Government has also done, to some extent). A rebate could be given for low income earners. More radically, a flat rate scale could be applied to the unimproved value of all properties or a flat charge to all properties, with rebates for lower income earners. Compared to the current system, some people may be made worse off than they were by the ACT Government's 2017-18 changes and some people better off. However, the system would be fairer – more akin to a rate increase than a rate distortion. This is not the place to discuss alternative changes but to note alternatives to deal with this possible rationale exist.