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SOUTH AUSTRALIA STAMP DUTY REFORMS

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Introduction

Stamp duty is a barrier to investment in property, and has become a more significant one when there is a rapid increase in capital values. In recent years the SA Government has changed parts of the stamp duty legislation with the aim to increase business investment in the state. There have been two significant reforms regarding stamp duty over the last five years. The first to be implemented was an exemption and a partial exemption for off the plan apartments which commenced in 2012. The second and more recent change is the staged abolishment of stamp duty for a range of asset classes which was announced as part of the 2015/2016 budget.

The paper will explore both of these reforms and the affect these reforms have had on the property market to date. We will also explore the possible future implications for these reforms.

What are the reforms for commercial property?

The most recent reforms to stamp duty announced in 2015 is the staged abolishment of stamp duty for several asset classes. This is a staged step down of stamp duty over a three year period which is applicable for:

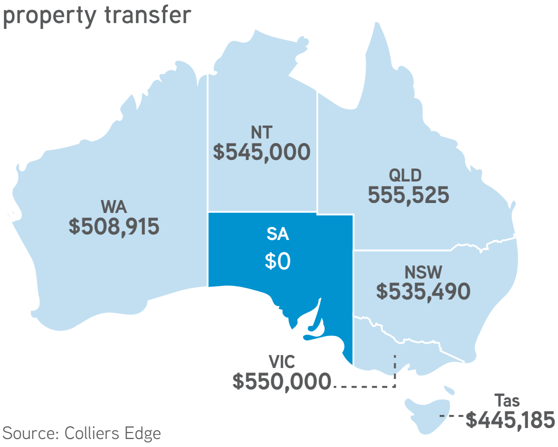
- non-residential, non primary production real property transactions
- non-real property transfers
- Corporate restructures
- transfer of mining tenements

These changes are not applicable to any residential or primary production use with stamp duty for these asset classes remaining unchanged. The only exception is for off the plan apartments which will be covered later in this paper. Looking more closely this will include the sale of business (either full or partial interest), and changes/transfer of either whole or partial share of a partnership. This however is not applicable to any land (except commercial use) or motor vehicles as part of the business sale. Stamp duty on these items remains unchanged.

The first cut to stamp duty was effective 7 December 2015, which saw stamp duty reduced by a third. The second cut is effective 1 July 2017 and the final cut which will see no stamp duty applicable for the above asset classes will be effective 1 July 2018. This will make South Australia the lowest tax jurisdiction for commercial transactions in Australia. This has seen South Australia become one of the most competitive places in Australia to do business. The map on page 2 shows the differences in stamp duty when applied to a $10 million commercial asset purchase.

The more recent changes to commercial property stamp duty are still in the early stages with only the first third of the reduction in stamp duty effective. The second round to reductions is due in June 2017 with the final round of abolishment in 2018. It is worth noting that these changes are part of a framework put in place by the State government to encourage investment into the South Australian economy. Other changes to the taxation system include changes to payroll tax and increasing the threshold for land tax. Some of the other initiatives being investigated are 10 gigabyte city, Carbon neutral Adelaide and the economic investment fund to encourage businesses to relocate to South Australia. All of these changes has made South Australia one of the most competitive places to do business.

2018 Stamp Duty applicable on a $10 million property transfer



Source: Colliers Edge

What are the implications for commercial property assets?

Although these changes are likely to stimulate the other areas which include non-real property transfers, corporate restructures and transfer of mining tenements are likely to stimulate further investment and corporate restructures, the main focus of the implications we will explore is in the commercial property sector.

There are several advantages to removing stamp duty which include:

- Removing the disincentive to trade an asset;
- Less barriers to purchase property and,
- Less transaction cost involved in all commercial property transactions.

This is likely to encourage assets to be traded more freely and therefore could increase the volume of transactions within the commercial property sector over the medium term. It is however worth noting that transaction volumes could be affected around the time that the step down in stamp duty is likely to occur. In the months leading up to step down in stamp duty it is likely to delay investment in 2017 and then again in 2018. Correspondingly, it is expected that there is an increase in activity likely post the step down in stamp duty payable. All of these implications are short term, but could be a disruptor for commercial property markets in the month's pre and post implementation.

It is also possible that there could be an uplift in capital values after the step down in stamp duty. This is due to purchasers delaying purchasing property until post 30 June 2017 or 2018 which pushes demand past the implementation date. When this occurs some of the savings in stamp duty could be offset by the uplift in capital value. Conversely there may be some pressure on capital values pre the implementation as purchasers hold off on purchasing property in this period. If a vendor has a particular need to sell before the next cut in stamp duty this may require a level of discounting to encourage purchasers to bring forward their purchase decisions. This is due to the possible increase in demand post the step downs in stamp duty.

South Australian commercial property has not experienced the same level of yield tightening as seen in some of the east coast markets and therefore is a very attractive option for investment as it is one of the highest yielding in the country. Combining the savings in stamp duty with the high yields on offer, this is likely to see more domestic and offshore capital interest in the Adelaide market. This increase in demand may conversely drive up capital values and therefore see yields start to tighten in the Adelaide market.

One of the main reasons for this policy change is to encourage further investment in business. However some of the short term implications could mean a delay in investment flows in the months leading up to the next round of cuts. Medium to long term it is expected that these changes will have a positive impact on commercial property markets and business investment by reducing the costs and red tape involved in these transactions. This will help to encourage more investment in the commercial property sector and is likely to encourage higher transaction volumes over the longer term. The short term implications however will need to be managed over the next two years.

What are the reforms?

There have been two major reforms to stamp duty over the last four years. The first change was regarding off the plan apartments which occurred in May 2012. This provided a full exemption to stamp duty for apartments under $500,000. Above this $500,000 threshold a partial concession was offered. Between 2012 to June 2016 there were geographic restrictions. Initially this was got the city council of Adelaide and which was then extended further to include the inner rim council regions. As of 30 June 2016 these geographic restrictions have been lifted so it is now applicable state wide. The aim of these changes are two-fold. The first was to remove the additional tax burden which was applied to purchasing an apartment rather than a new subdivision and building a home. The second was to meet the infill targets from the 30 year plan which was released in 2009. This plan was aiming to have 70 per cent of new housing development as infill with the remaining 30 per cent. The 30 year plan which was released in 2009 and an update in 2016 aims to see 70 per cent infill with 30 per cent green-field development. This is to help build density which will then be able to support further investment in transport infrastructure such as extensions of the tram networks. Current density ratios in the inner rim and CBD are unlikely to be dense enough to justify the investment in successful transport tram networks which are in cities such as San Francisco.

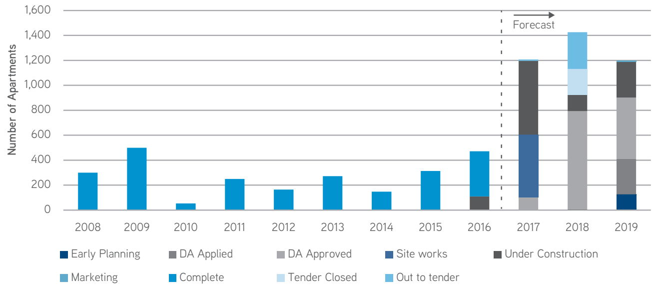
What are the implications for the off the plan apartments?

The aim of the stamp duty exemption when first implemented was to remove any unfair tax advantage that green-field development had over off the plan apartments. Before the exemption, a green-field development had stamp duty applied to the land component with a construction contract. An apartment sale however saw stamp duty applicable to the total sale price. This tax treatment meant purchasers of an off the plan apartment had stamp duty which was thousands of dollars higher than a house and land package on the fringe. This stifled development of higher density projects and was in conflict with the objectives of the 30 year plan to have a higher infill development. As these exceptions have been in place for four years, the impact of this change can be assessed through an analysis of the construction activity within the Adelaide CBD. It is also worth noting that at the time of the stamp duty exemptions were put in place the City of Adelaide also implemented changes to their development plan. These changes increased building heights and reduced some of the restrictions regarding car parking. The combination of both changes to planning and the exemption of stamp duty for apartments supported demand for new construction of apartments in the Adelaide CBD.

Although the stamp duty exemptions were effective in mid-2012, the effects on supply were not evident until 2014. This is due to the lag time between the pre-commitment to purchase an off the plan apartment to the completion of construction which can be 18 months or more. Additionally, not all projects which have DA Approval will commence construction with a number of reasons such as the ability to finance the construction, presales targets not being met and the project not being economically feasible.

Chart 1 examines the completion of new apartments to the Adelaide CBD market since 2008. Although the volume of apartments receiving DA Approval increased during 2013/2014 the increases in supply start to become evidence in 2015 with 313 apartments added to supply. Forecasts for 2016 expect 471 apartments to be completed with a further 1207 apartments in 2017. This is a particularly high pipeline of supply, but this is significantly boosted due to the construction of urbanest at 228-230 North Terrace which is 505 rooms.

Adelaide CBD apartment pipeline



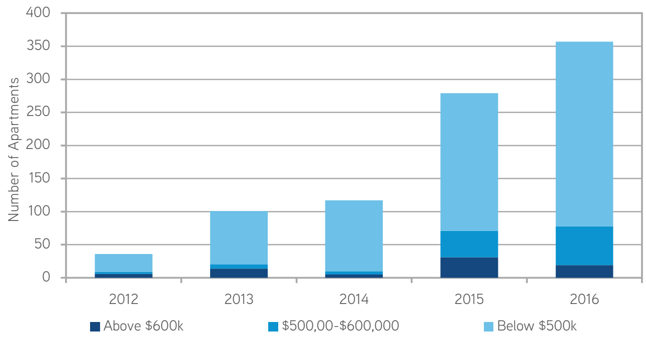
Source: Colliers Edge

There is a strong pipeline of supply proposed from 2017 to 2019 and if all projects commence and complete in the estimated time frames 3,833 apartments would be delivered to supply. It is however unlikely that this many apartments would be completed in this period, as it would require demand for off the plan apartments to more than double to absorb this many apartments in a year. Although we are expecting an increase in demand as the Adelaide apartment market begins to mature, it is unlikely that it will keep pace with this level of supply.

Looking wider than the CBD there has been more recent changes in planning to meet infill targets outlined in the 30 year plan. The extension of the stamp duty exemptions included some of the inner rim suburbs since October 2013 which has resulted in an increase in the number of inner rim projects proposed. One of the large infill project which has been successful is the Bowden project. Renewal SA have managed the land release which has been sold in 'super lots' to developers. These lot sales have resulted in a mix of medium and high density projects being completed over the last three years.

An analysis of sales for new apartments in the CBD over the time period of the implementation of the exemptions has demonstrated that although the stamp duty exemptions initially stimulated demand below the $500,000 price point, as demand has grown so have the proportion of apartments above the $500,000 price point. A closer analysis has shown that this is mostly apartments in the $500,000 to $600,000 price bracket. We would expect a similar trend in the metro markets, with this exemption stimulating demand at the lower end of the market, but over time this will see the price points and the demand in the apartment market starts to mature.

Adelaide CBD new apartment sales by price bracket



Source: Colliers Edge

Conclusions

The changes to stamp duty for apartments have shown that they are an effective way to be a catalyst for further development and investment. This is demonstrated through the success of the stamp duty exemptions for off the plan apartments. It is expected that with the extension of the stamp duty exemptions state wide that this will continue to encourage development of in fill projects and help to accelerate the maturity of the apartment market in South Australia. There are many benefits to this, in particular that it allows for greater densities which is likely to lead to more investment transport networks such as tram line extensions into other suburban locations.

The abolishment of stamp duty for commercial property and business sales is a positive step to encourage further investment. Although there are some short term implications for investment volumes, these changes are likely to lead to greater demand for assets in the Adelaide market and therefore could support further growth in capital values.