21 October 2021

The Hon David Davis MLC
Shadow Treasurer of Victoria

By email: david.davis@parliament.vic.gov.au

The Hon Ryan Smith MP
Shadow Minister for Planning and Heritage
Shadow Minister for Housing

By email: ryan.smith@parliament.vic.gov.au

Dear Shadow Treasurer and Shadow Minister

Windfall Gains Tax and State Taxation and Other Acts Further Amendment Bill 2021

I write to you about the *Windfall Gains Tax and State Taxation and Other Acts Further Amendment Bill 2021* (**Bill**), introduced by the Treasurer to the Legislative Assembly on 12 October.

As you are aware, UDIA Victoria opposes the Windfall Gains Tax, which is a tax on investment and housing supply. The Windfall Gains Tax will materially and negatively impact project viability, housing affordability, the creation of employment precincts and economic activity throughout Victoria.

We also note the rezoning tax's likely unintended consequences which will disproportionately affect housing supply and affordability in regional Victoria and limit urban regeneration throughout Melbourne's middle-ring, contrary to core planning strategies such as *Plan Melbourne*.

UDIA Victoria modelling shows that on the basis of just seven case studies, each project will be rendered unviable and will not proceed. This will reduce housing supply by 6,696 dwellings (including over 300 affordable, social or disabled access dwellings), cost over 20,000 direct jobs and nearly 100,000 indirect jobs and reduce Victoria's economic output by nearly $7.5 billion. Importantly, **we estimate that this will cost the State Budget $170 million in foregone Stamp Duty receipts, with a total economic loss to the State of $7.7 billion**.

The Government has not provided any modelling whatsoever, let alone modelling to rebut this.

Although we ask the Opposition to oppose Parts 1 to 6 of the Bill, as well as any consequential provisions, we also ask for your support to prepare and table a series of amendments to improve the Bill if it proceeds to Committee Stage in the Legislative Council.

The basis for those amendments is set out below.

Proposed amendment 1: Capping the tax in regional Victoria at no more than GAIC

The imposition of a Windfall Gains Tax will have significant and adverse consequences on both housing supply and affordability, as well as the creation of new employment precincts across regional Victoria.

Data prepared by Research4, one of Australia's leading residential greenfield market research houses, shows that housing affordability across regional Victoria has reduced significantly in recent years. In Geelong it has reduced by 85 per cent since 2018, in Ballarat it has reduced by 55 per cent since 2019 and in Warragul it has reduced by 45 per cent since 2020.

Housing demand in regional Victoria has been steadily increasing in recent years, a trend that was brought forward significantly with the onset of the coronavirus pandemic and the well understood demographic shifts as people reconsidered their housing requirements. Without a commensurate increase in housing supply across regional Victoria, current land supply levels are extremely low. Research4 suggests that greenfield land supply in Bendigo is now as low as 4.2 years while a recent report prepared by Ethos Urban shows that available land supply in Greater Geelong will be exhausted in between 2.3 and 2.8 years.

The imposition of a Windfall Gains Tax across regional Victoria will not dampen demand for new homes across the State, although it will stifle supply. The only possible outcome is that regional house prices will rise further, pushing affordability out of the reach of more Victorians and locking regional Victorians out of buying a home in the towns they have grown up in.

Analysis by UDIA Victoria members indicates that a 50 per cent uplift tax on a hypothetical 20-hectare site in regional Victoria will equate to a tax rate of approximately $250,000 per hectare.[1] This is more than double the GAIC levied in metropolitan Melbourne. We agree that land subject to GAIC should be exempt from the application of the tax, although as a matter of equity, a failure to cap the rezoning tax at the GAIC rate will place regional Victoria at a competitive disadvantage to Melbourne's growth corridors.

It is appropriate and necessary for a cap to be placed on the quantum of the tax that applies in regional Victoria so that at a 'worst case scenario' the tax is no more than the GAIC on a per hectare basis. This is a simple equation that can be implemented upon levying the tax. The uplift simply need be divided by the area of the subject property. If the amount is less than the cap per hectare, then the tax remains as assessed. If the amount exceeds the cap per hectare, then the cap is applied. Like GAIC, we accept that the cap should be indexed.

Proposed amendment two: hypothecation of revenue

Although the Government announced that the tax will return a share of the profits from rezonings to the community for vital infrastructure,[2] the Bill provides no mechanism to do so, nor accountability on how the Government should use that revenue.

The Bill should establish a dedicated fund, into which revenue raised by the tax is paid, with a clear purpose to invest in infrastructure to benefit the local communities from which the revenue is raised. This fund should ring fence revenue to be spent in a particular locality on an LGA basis.

Proposed amendment three: extending transitional provisions to exempt all pre-existing agreements

The transitional provisions at clause 39 exempt land that is rezoned by a WGT event if the land is subject to a contract of sale entered into before 15 May 2021, or an option to enter into a contract of sale granted before 15 May 2021. Guidance provided by the Treasurer in advance of the introduction of the Bill states:

> *Development agreements will not be subject to the transitional arrangement, regardless of whether they were entered into prior to 15 May 2021. Development agreements are not covered as they do not involve a transaction of the land between a landowner and a developer.*

[1] Note that a case study from leading accounting firm, Pitcher Partners, has put this figure as high as $415,000 per hectare.

[2] https://www.premier.vic.gov.au/windfall-gains-tax-benefit-victorian-community.

This position neglects that, whether or not a transaction of the land, a Development Agreement (and other agreements, such as Joint Venture Agreements) are legally binding arrangements in which the parties have assumed rights and obligations. In many cases, these will involve significant financial implications. Any legally binding arrangement entered into prior to 15 May 2021, like contracts of sale and option agreements, were struck on commercial terms and in an environment that did not contemplate the Windfall Gains Tax. It is also important to consider that many contracts of sale or option agreements may have been entered into after 15 May 2021, but on the basis that another agreement was negotiated and executed prior to that date – for example, an Exclusivity Deed, Heads of Agreement or Letter of Offer. Each of these documents would be entered into based on financial models, feasibility analyses and negotiations that took place prior to the announcement of the Windfall Gains Tax. There are several cases in which a court has found a preliminary agreement to be binding if it contained all of the elements of a legally binding contract (see *Sinclair Scott & Co Ltd v Naughton* (1929) 43 CLR 310, *Baulkham Hills Private Hospital Pty Ltd v GR Securities Pty Ltd* (1986) 40 NSWLR 622 and *PRA Electrical Pty Ltd v Perseverance Exploration Pty Ltd* [2007] VSCA 310).

A failure to exempt all pre-existing arrangements means that the tax will operate retrospectively, damaging investor confidence in Victoria's already fragile economy.

Proposed amendment four: extending transitional provisions to remove to occurrence of settlement prior to a rezoning event

Clause 39 also requires that, for a contract of sale entered into before, or option to enter into a contract of sale granted before, 15 May 2021 to be exempt from the tax, that contract or option must not have settled before the WGT event (the rezoning) occurred.

Consistent with our position in relation to proposed amendment three, whether or not settlement has occurred prior to rezoning is irrelevant to whether a landowner has entered into a bona-fide transaction, struck on commercial terms and based on prevailing taxation laws and conditions.

There is no justification as to why pre-existing arrangements that have settled before a rezoning should be captured by this tax. If the Government's justification is that a party to an agreement can withdraw from that agreement prior to settlement, then this is misconceived as financial penalties may attach (for instance, the forfeiting of an often significant deposit).

An analogous situation is where the Government sought to impose a new direct 50 per cent tax on the purchase of a new home. In the case of two homes side by side and sold at auction on the same day for $1 million each, the respective purchasers would likely have paid a deposit of $100,000 each. If the Government only exempted a purchase that had settled at a certain date, it would result in one purchase being exempt from the tax while the other is not. Although true that the purchaser who is yet to settle could choose not to proceed to settlement, they will forfeit a $100,000 deposit for doing so. This position, like the position for a developer in respect of the Windfall Gains Tax, is unconscionable and cannot be justified.

Proposed amendment five: extending transitional provisions to bring forward the point in the planning process at which a proponent-led rezoning attracts an exemption

Clause 40 of the Bill states:

40 Exemptions in relation to rezonings underway before 15 May 2021

(1) Windfall gains tax is not imposed on land that is rezoned by a WGT event if the Commissioner is satisfied that—

(a) *the planning scheme amendment constituting the rezoning was prepared by a Council; and*

(b) *a request for the amendment was created and registered in the Amendment Tracking System by the Council before 15 May 2021; and*

(c) *before 15 May 2021 the owner of the land—*

(i) *approached the Council to request the rezoning; and*

(ii) *paid for, was liable to pay for, or had otherwise performed or procured relevant work in relation to the rezoning; or*

(iii) *paid, or was liable to pay, relevant costs to support consideration of the rezoning; and*

(d) *the total value of the relevant work and relevant costs referred to in paragraph (c)(ii) and (iii) was not less than the threshold amount.* (emphasis added)

The time at which a request for an amendment is created and registered in the Amendment Tracking System is too late in the planning process and neglects the fact that the Victorian planning system is such that it can take many years for a project to reach this stage – at which time a landowner has incurred significant cost (direct expenditure, holding costs and time that could have been invested into other projects).

For the same reasons it would not be appropriate that the trigger point in the planning process be the point at which a council formally seeks approval for a planning scheme amendment. Reaching this point requires numerous discussions and negotiations with the relevant council prior to officers even agreeing to put the amendment request to Council. UDIA Victoria members have identified that it can currently take between three and five years from first discussions to negotiate a position prior to a formal submission with a request to authorisation to exhibit (the point at which the "request for amendment" is registered).

It the context of transitional arrangements, it ought to be enough that a landowner has "substantially commenced" a rezoning process. We understand that this trigger needs to be measurable. Accordingly, we propose that "substantial commencement" be defined plainly, with reference to correspondence about a Planning Scheme Amendment for the subject land having been submitted along with supporting documentation. We note feedback from our members in which they have engaged extensively with a relevant council (including participation in over 20 meetings) so that a formal Planning Scheme Amendment would be lodged only once all the issues had been resolved (the alternative being to lodge an amendment without council input and not to council's satisfaction, resulting in extensive post-lodgement negotiation and against good industry practice).

If this correspondence was submitted prior to 15 May 2021 and remains on foot until approval (that is, strategic justification was established and the application was not rejected), then it should be exempt from the tax.

Proposed amendment six: extending transitional provisions to exempt proponent-led rezonings undertaken by an owner or someone acting on an owner's behalf

Clause 40(1)(c) of the Bill set out above requires certain actions be taken by the owner of the land to attract an exemption from the tax.

In practice, the vast majority of proponent-led rezonings that would otherwise be captured by this transitional provision will be where a developer leads the rezoning application on behalf of a landowner

under a Development Agreement. That the actions required in clause 40(1)(c) have been undertaken on the owner's behalf by another party does not change the substance of those actions, but merely reflect contractual arrangements in place and the obligations of parties under those agreements.

The requirement that "the owner of the land" approached the Council, paid for, performed or procured relevant work and paid relevant costs in clause 40(1)(c) of the Bill will severely restrict the operation of this transitional provision.

This clause should be amended to acknowledge that the actions required by the owner of the land in clause 40(1)(c) can have been taken by the owner, or any person on behalf of the owner.

Proposed amendment seven: extending transitional provisions to expand the definition of "relevant work" in clause 40(3)

Exemptions in relation to rezonings underway before 15 May 2021 require that "relevant work" has been paid for, performed or procured in relation to the rezoning.

Clause 40(3) defines "relevant work" as follows:

> ***relevant work*** *means professional analysis or assessment that, in the Commissioner's opinion, is necessarily performed in preparing for or seeking a rezoning of land including but not limited to—*
>
> *(a) surveying analysis; and*
>
> *(b) engineering analysis; and*
>
> *(c) traffic analysis; and*
>
> *(d) master planning analysis; and*
>
> *(e) Aboriginal cultural heritage assessment; and*
>
> *(f) architectural analysis; and*
>
> *(g) environmental analysis—*
>
> *but not including works done to the land itself, such as remediation or land clearing;*

Through its consultation process the Government stated that the tax is "capturing the economic value created by a Government decision to enable a higher and better use". This is incorrect. It is far more accurate to say that a Government decision to enable a higher and better use *releases* the value that is most often created by the significant time and expense incurred by a developer to bring a site to the point of rezoning, at significant commercial risk. The Government's position assumes that all value improvement attributable to development costs expended before the CIV1 valuation are reflected in the CIV1 valuation. That is not the case. In fact, none of the value created from those costs may be reflected in the CIV1 valuation in some circumstances. The pre-rezoning development costs put the Government in a position to decide whether to rezone the land based on the merits created in expending those costs. The rezoning decision that triggers the value uplift between CIV1 and CIV2 is a realisation event for value already accumulated and embedded (unrealised) in the land because of the developer's early work. Although the rezoning decision creates some value, it is erroneous and misleading to say that it creates all value.

Land speculators make profits on rezonings with relatively little investment of time or resources, and without any economic value add in the process. By contrast, developers purchase land for the purpose of development – creating jobs, housing, employment precincts and communities. Developing a project

takes several years, cost millions of dollars in holding, remediation, land clearing and planning costs. Developers carry significant project risk, invest enormous sums, pay significant local, state and federal taxes (more than any other industry), and, by doing so, deliver enormous economic and social benefits to Victoria.

The exclusion of remediation and land clearing works from the definition of "relevant work" fails to acknowledge that these works are often required to facilitate a Planning Scheme Amendment, with recent EPA requirements often making this a pre-condition to the lodgement of an amendment.

For the same reasons, remediation and land clearing works must be made allowable deductions when regulations are established.

Proposed amendment eight: extending transitional provisions to include events occurring prior to the introduction of the Bill

As outlined in respect of our proposed amendments three to seven, the relevant date for transitional provisions in the Bill is 15 May 2021, which is the day on which the Windfall Gains Tax was announced.

The Treasurer's media release announcing the Windfall Gains Tax said:

> *When governments make planning decisions to rezone ex-industrial land, or create new residential estates, property developers can make massive windfall profits overnight.*
>
> *A new windfall gains tax on these profits will claw back an estimated $40 million a year, ensuring these gains are shared with the community and invested in public transport, schools and other vital infrastructure.*
>
> *Developers and speculators will face a windfall gains tax of up to 50 per cent applied to planning decisions to rezone land from 1 July 2022, ensuring multi-million dollar overnight profits are shared with the community.*
>
> *The total value uplift from a rezoning decision will be taxed at 50 per cent for windfalls above $500,000, with the tax phasing in from $100,000 – ensuring the vast majority of land holders will not be affected. Land subject to the Growth Areas Infrastructure Contribution will also not be affected.*[3]

Between 15 May and 12 October, the date on which the Bill was introduced in the Legislative Assembly, no further detail was publicly available. Although industry associations, including UDIA Victoria, were privy to targeted consultation, this consultation was confidential and we took that obligation seriously. The limited information provided to us (which did still not outline the full detail of the Bill) was not shared. Industry participants were provided with four sentences of detail about arguably to biggest tax changed faced by the urban development industry in more than a decade.

It is unreasonable to suggest that market participants ought to have stalled or cancelled transactions from 15 May 2021 based on the very limited detail available, or else be captured by the tax. The relevant time at which those market participants were able to make any informed decision about the future of a transaction was the point at which detail became available to them.

Accordingly, the relevant date in respect of both the exemption for proponent-led rezonings in train or for pre-existing arrangements should be 31 December 2021 or, at the earliest, 12 October 2021.

Proposed amendment nine: period for objection

[3] This was the entire reference to the Windfall Gains Tax, although there were further references to other issues (for example, increases to the rate of stamp duty and land tax).

Clauses 89 – 92 of the Bill contemplate a regime under which a taxpayer may object to a valuation (CIV1 or CIV2) for the purposes of an assessment of Windfall Gains Tax. An objection must be lodged within 60 days. This period should be extended to 180 days.

The 60-day period is too short and fails to recognise the time required to prepare an assessment with reasons as to why a valuation is not valid. These reasons can be complex and technical in nature, with a thorough process required to accurately determine the development potential of a parcel of land or the costs required to make that land developable – both critical aspects in determining its true value. Developers pay significant sums (often in the hundreds of thousands of dollars) conducting due diligence on a site to best estimate its true commercial value. Site-specific valuations can vary significantly between sites which can be closely located and ostensibly look the same. Even with extensive due diligence, there remain cases where a developer is unable to fully assess the site conditions and later discovers an unknown source of contamination that needs to be remediated at significant cost.

Proposed amendment ten: grouping provisions

Members of a group of related corporations, trusts or a combination of related corporations and trusts, are jointly and severally liable for the Windfall Gains Tax on all the land held by members of the group that is rezoned by the relevant WGT event. The effect of making members of a corporate group 'jointly' and 'severally' liable for WGT incurred by one or more members of the group is that each group member (irrespective of whether it owns land subject to Windfall Gains Tax) is liable for the entire tax obligation until it is paid by one (or more) of the group members. The SRO can choose to pursue the member with the WGT liability, or other members of the group that do not have the liability (and may not even own land). The extension of liability for Windfall Gains Tax to group members that do not have a WGT liability, or even hold land, is a significant departure from current land tax practice or GAIC practice. Moreover, it will mean in practice that different lenders to different group members will be concerned that the member's asset base over which they have security could be adversely diminished by a liability for Windfall Gains Tax that emanates from another group member. In practice they will therefore insist upon WGT Sharing Agreements and WGT Funding Agreements widely used in connection with income tax consolidation.

We do not expect that the Government has adequately considered the practical implications for group lenders and other creditors of making members of corporate and trust groups jointly and severally liable for Windfall Gains Tax. The matter has been considered, we suspect, purely from a Government recovery perspective. However, the practice of accommodating for this outcome will inevitably add cost and uncertainty to doing business in Victoria.

These provisions should be amended to reflect the practice currently adopted by the land tax and GAIC regimes.

Preparation of amendments and meeting with UDIA Victoria Board and Advisory Group

We ask that you instruct Parliamentary Counsel to prepare amendments to rectify the deficiencies in the Bill, as set out in this letter.

I am happy to provide a more detailed briefing on these issues to provide you with greater insights into their importance or to provide further technical details. In this respect, I would be happy to convene a briefing for the both of you to discuss these issues with the UDIA Victoria Board and a specialist group of our members that have convened to form an Advisory Group to respond to the Windfall Gains Tax.

I can be contacted on 0416 443 555 or at matthew@udiavic.com.au to arrange this briefing.

Yours faithfully

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