Victoria Budget Announcement 2021-22

A review of the Victorian Budget's major business implications

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Executive summary

The 2021-22 Victorian Budget sees further investment from the government, with some additional revenue-raising measures.

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The Victorian Government's budget for 2021-22 projects a net operating deficit of $17.4 billion for 2020-21 and a further deficit of $11.6 billion for 2021-22. Government net debt is not expected to exceed 27 percent of gross state product at any stage over the period from 2021 to 2025.

Alongside a $7.1 billion commitment to improving healthcare infrastructure and services, a prominent feature of the Budget's expenditure program is the announcement of $3.8 billion allocated to the transformation of mental health and wellbeing support in Victoria. More than 20 percent of this is targeted at supporting children, young people and families.

The government notes that the Royal Commission into Victoria's mental health system estimated the annual economic cost to Victoria of poor mental health at $14.2 billion. The Budget includes a proposed levy on employers with a national payroll greater than $10 million. The levy would be 'ring-fenced' to funding mental health support services in Victoria and would apply from 1 January 2022.

The Budget's investment of $3.2 billion in transport infrastructure includes new trains and support for the increased take-up of 'zero emission' vehicles.

The Budget includes proposed increases to stamp duty (for properties valued at more than $2 million) and land tax (for taxable landholdings valued at more than $1.8 million).

Revenue-raising measures have generally been absent from federal and state budgets over the last 12 months and so these increases will be a surprise to some. However, the government clearly feels that it is time to re-set the balance between revenue and spending measures and has looked at where the perceived ability to pay may be greatest. The extent to which the burden of these tax increases would ultimately fall on consumers remains to be seen.

There is also a proposed new tax, to apply from 1 July 2022 on 'windfall' gains of more than $100,000 in value that arise from planning decisions to re-zone land. There is an evident connection here between the size of the windfall gain (and therefore the amount of government revenue raised from the tax) and the amount of re-zoning that government bodies allow to occur.

It makes sense for the government to focus in this Budget on enhancing healthcare and mental health support services, whose importance to the community has stood out during the pandemic. Productivity-enhancing tax reform must, however, come to the fore soon if the state is to best position itself to achieve its aspirations for the living standards of residents.

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Economic analysis

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The underlying philosophical position of the Victorian State Budget is clearly one of redistribution, with the wealthiest being taxed to fund a range of social and health initiatives that will be predominantly provided for the poorest and most vulnerable in society.

This is not a misplaced ideal and is fundamentally the basis of Australia's progressive income tax system. It also recognises that the lower-paid and the vulnerable have felt a more severe impact from the pandemic than other sections of the community. However, there is room for reasonable people to differ on when is the optimum time to apply the proposed new funding mechanisms included in the budget to help pay for such reforms. Should they be implemented over the next 12 months, or after another year or two to enable the state's economy to consolidate in the meantime?

In considering the new measures contained in the Budget we think it is important to consider that the coronavirus pandemic, unfortunately, is likely to have a way to run. It is also worth considering that the recovery in the Victorian economy, which was particularly hard-hit because of the extended lockdowns, is lagging other parts of the country. In such an environment the challenge facing the government is to not over-burden the private sector while still managing to run a credible budget that can support important programs, like the mental health initiative, and also continue to provide short term stimulus to accelerate the economy's recovery from the coronavirus shock.

The budget still relies heavily on raising revenue from economically relatively inefficient taxes to fund the provision of new services and to reduce the deficit. The fiscal position will need to be managed very carefully and we believe that the circumstances are compelling for the government to review the efficiency and effectiveness of state taxes. In managing the budget going forward there is no doubt that there will be a strong focus on the spending side of the budget. We believe there should also be a strong focus on reforming the tax system so that a more efficient and sustainable tax mix can ensue.

A more efficient tax mix will ensure that the tax burden on low- and middle-income households is as low as possible and that the tax burden on Victorian businesses does not blunt their competitiveness.

Infrastructure spending is important for supporting future productivity growth and can also be timed to assist the recovery that is underway. It is important, however, to ensure that there is sufficient capacity in the economy to deliver these projects without generating unnecessary price pressures in the construction sector, which may crowd out other private sector investments.

The public sector has necessarily expanded. As the economy continues to recover, federal and state governments will need to carefully balance skilled migration, border management and their own workforce needs to ensure that Australian businesses are not held back by labour shortages and higher costs just as their requirements are growing.

Key Insights

- The Victorian Government has handed down a Budget that seeks to redress many social and community problems, including investing in mental health, additional support for health care and young children, albeit it does it while imposing new and deeper taxes at a time when many businesses, investors and homeowners are still recovering from the coronavirus-induced economic downturn.
- The Victorian Government should look to reform its tax system so its reliance on inefficient taxes, like stamp duties and payroll taxes, is reduced.

Property Tax

The government has announced a range of measures and introduced the *State Taxation and Mental Health Acts Amendment Bill 2021* (Vic) (**Budget Bill**) which expands the tax base and increases rates while also seeking to stimulate purchases of lower value properties.

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Land tax changes

Key changes to the Victorian land tax regime have been announced, to apply from 1 January 2022. These changes increase rates at the upper end while increasing the tax-free threshold for the lower end of the market:

- Both the general land tax and surcharge land tax rates will increase by:
  - 0.25 percent for taxable land with a site value in excess of $1.8 million
  - 0.30 percent for taxable land with a site value in excess of $3 million.
- The tax-free threshold for general land tax is to increase from $250,000 to $300,000.

A vacant residential land tax (VRLT) exemption for up to two years will be introduced for newly completed residential properties. The current land tax exemption for clubs and associations will cease for gender-exclusive clubs.

Transfer duty changes

With effect from 1 July, the Budget Bill also proposes to introduce:

- A 1 percent increase in the general rate of duty for transactions with a dutiable value in excess of $2 million. The new rate will be $110,000 plus 6.5 percent of the dutiable value above that amount.
- An increase in the transfer duty threshold to $1 million for off-the-plan contracts entered into from 1 July 2021 to 30 June 2023 for all home buyers (noting the principal place of residence test must be satisfied).
- Temporary transfer duty concessions for the purchase of newly constructed residential property in City of Melbourne with a dutiable value up to $1 million. Purchases of new property constructed at least 12 months prior will be exempt for contracts entered into from 21 May 2021 and before 1 July 2022. A 50 percent concession will apply on the purchase of newly constructed residential property less than 12 months old on contracts entered into from 1 July 2021 and before 1 July 2022.

New Windfall gains tax

The most unexpected measure is a new 'windfall gains tax' to apply from 1 July 2022, where rezoning of land leads to a "windfall". The tax will apply at rates of up to 50 percent of the gain, phasing in from $100,000 and applying at the maximum rate to gains over $500,000. However, rezoning to and from the Urban Growth Zone within the existing GAIC areas will be excluded from the tax, as will a rezoning to Public Land Zones. The provisions for this new tax have not been included in the Budget Bill and we await the detail for implementation.

Key Insights

- There are both increases and expansions of the property taxes which will target property buyers and owners at price points that are rapidly becoming mid-range in Melbourne.
- Duty concessions aimed at new residential properties and off-the-plan purchases are intended to assist first-home buyers in getting a foothold in the property market, while developers hit by the exodus of inner city buyers will welcome duty and VRLT concessions as providing relief and incentives.

Summary of key expenditure / revenue items

This table summarises the Budget's larger expenditure measures, and also shows the more significant revenue-raising and revenue-reduction proposals. Figures are rounded to the nearest $0.1 billion.

Key expenditure items	$ billion
Investment in hospital infrastructure and services, emergency departments and Ambulance Victoria	5.0
Transforming the mental health system	3.8
Public transport services and infrastructure	3.2
School infrastructure including upgrades, expansions, and building of new schools	1.6
State public health response to the COVID-19 pandemic	1.3
Supporting children and families, including help for vulnerable families	1.2
Reducing the impact of bushfires on Victorian communities	0.8
School programs and support for teaching workforce	0.7
New road safety strategy, including new technologies and infrastructure upgrades	0.4
Providing support to victim survivors and addressing family violence	0.4

Key revenue raising measures	$ billion*
Mental Health and Wellbeing Levy for businesses with national payrolls above $10 million per year.	2.9
Increase land tax rates for high-value landholdings	1.5
Premium duty rate on land transfer duty for high-value properties	0.8
Increased penalty unit value	0.3
Windfall gains tax for high-value landholdings	0.1

Key tax relief measures	$ billion*
Increase the tax-free threshold for land tax	0.1
Temporary land transfer duty concession for new residential property within the Melbourne local government area with a dutiable value of up to $1 million	0.1
*Over the forward estimates period	

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