

INQUIRY INTO LAND VALUATION SYSTEM

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Date Received: 8/03/2013

Our ref: R90/0400.smcb Out-21287

8 March 2013

Mr Matt Kean MP
Chair
Joint Standing Committee on the Office of the Valuer General
Parliament House
Macquarie Street
SYDNEY NSW 2000

Dear Mr Kean

Inquiry into the Land Valuation System

I write to provide Local Government NSW's comments to the Joint Standing Committee Inquiry into the NSW Land Valuation System.

Local Government NSW (LGNSW) is the peak body for councils in NSW, representing all the 152 NSW general-purpose councils, the special-purpose county councils and the NSW Aboriginal Land Council.

LGNSW welcomes the opportunity to provide comments to the review.

Introduction

NSW Local Government is a major stakeholder in the land valuation system. Councils rely on the valuation system for the determination of council rate assessments. NSW councils raised around \$3.3 billion in rates in 2012. Councils also rely on the services of the Office of the Valuer General (OVG) for other purposes including the determination of just terms compensation in the case of compulsory land acquisitions.

Councils pay for the services they receive and Local Government is one of the principal sources of revenue for the OVG, the other major client being the NSW Office of State Revenue (OSR). Local Government is acutely aware of the performance of the NSW valuation system and the strengths and weaknesses of the rating methodology currently applied in NSW.

This submission focusses on the need to introduce a market value based valuation methodology while providing comments on the general performance of the valuation system from a Local Government perspective and on a number of specific issues.

LGNSW Engagement with OVG

LGNSW is a long term member of the Land Valuation Advisory Group (LVAG) and attends its regular meetings. The LVAG comprises representatives of property industry groups, the OSR and LGNSW. The group monitors the quality of land values and provides a channel for communication between the Valuer General and property industry stakeholders. LGNSW finds the LVAG a valuable forum for raising issues of concern to Local Government.

LGNSW is also represented on the tender panel for contracts for the provision of land valuation services. LGNSW has been a member of this panel since the introduction of private contracting for valuation services for rating and taxing in NSW.

LGNSW also benefits from direct consultations with the Valuer General as required.

Performance of Valuation System

Close engagement with the valuation system has placed LGNSW in a good position to comment on the performance of the system over the past decade or more. LGNSW have witnessed a prolonged period of continuous improvement overall. This commenced with implementation of recommendations of the *Report of Inquiry into Operation of Valuation of Land Act, 1999* (the Walton Report) and the recommendations of subsequent reviews including the Ombudsman's report entitled *Improving the quality of land valuations issued by the Valuer General, 2005* and the Joint Standing Committee on the Office of the Valuer General's *Report on the Inquiry into the provisions of the Valuation of Land Act 1916, 2010*.

On the whole, administration of the present land valuation system appears to be working reasonably well for the purposes of Local Government rating. There has been a marked reduction in the number of objections received and in the number of successful objections over recent years. The number of objections steadily declined from 6769 in 2007 to 3513 in 2011. Objections represent a minute proportion of the 2.4 million valuations undertaken. Feedback received by LGNSW from councils on the quality of valuation services is generally positive with most indicating progressive improvement.

LGNSW has also witnessed major improvements in contract management, objection processes and communication with key stakeholders and the broader community.

This is not to say that there aren't exceptions or room for further systemic improvement. LGNSW is aware of problems arising from poor contract performance in the Central West of the NSW. The Perilya case, discussed later in this paper, raises concerns about mine valuation methodology. However, the main deficiency from a LGNSW perspective is the continued use of land value rather than a market value for the majority of property valuations. This is discussed in more detail in the following section.

Valuation Methodology

LGNSW agrees that, as the basis of a taxation system, the valuation system needs to be transparent, efficient, predictable and equitable. To that end, LGNSW advocates the adoption of Improved Capital Valuation (ICV) methodology to replace land value as the basis for rating and taxing valuations.

LGNSW maintains that adoption of ICV or other market based methodologies such as Gross Rental Value (GRV), would significantly improve equity in the rating system. The current land valuation system creates a number of anomalies, particularly in relation to strata holdings and multiple tenancies on single lots. It is pleasing that this matter has already been recognised in the Inquiry Issues Paper. As the Issues Paper notes, "while the market value of a strata title may be quite high, the taxable land value attributed to the titleholder may be low because the land value is spread across the strata titleholders on the property". This results in non-strata property owners carrying an inequitable share of council rates. In the absence of rate pegging, it would also deprive councils and communities of income. The bias in favour of strata holdings is already a significant problem in many high density Local Government areas and is getting worse as strata development becomes increasingly prevalent.

The issue of equity does not only apply to council rates, it applies to land tax and will apply in relation to the broad based property levy that is being proposed to fund emergency services in NSW. Equity is arguably the strongest reason for changing the valuation methodology.

The concept of land value is also poorly understood by the general public when applied to anything other than vacant land. It is difficult for owners of properties with houses, apartments, commercial or industrial buildings to reconcile 'land value' with the more familiar real estate market values. ICV is more reflective of market value and is much more easily benchmarked against current real estate prices. ICV would therefore provide a higher degree of transparency.

It is also likely that ICV would prove to be more efficient once the costs of transition have been absorbed. For example, it should be simpler to base valuations on market sales data without the need to discount capital improvements. Further, it may also help reduce distortions.

It is less clear whether ICV would be more predictable than other methodologies for the majority of residential properties. This would require comprehensive comparative studies. Land valuation is at best an imprecise science. Land values are subject to market fluctuations with some categories of property being more volatile than others. Some properties also have particular characteristics that make valuation more complex and vulnerable to error or dispute.

There has been a growing consensus in favour of moving to market value based valuations. The major stumbling block appears to be the cost involved in doing so. There is a considerable investment in the systems that support the current methodology and there would be significant one-off costs involved in transitioning to a new methodology. LGNSW believes that the costs are warranted in the long run. Rates are a major source of funding for Local Government and land tax represents a large and increasing share of NSW government revenue. It is important that the property taxation system has an equitable, transparent and efficient basis and it appears that a change in methodology is required to deliver this.

Land tax revenues are growing faster than total council rate revenues in NSW.

Local Government Rates v Land Tax

It should be understood that land valuations do not affect council rate revenue in the same way they affect NSW Government land tax revenue. The rate pegging regime in NSW effectively prevents council rate revenue from rising in line with property values. The rate peg determined annually by the Independent Pricing and Regulatory Tribunal of NSW (IPART), sets the maximum amount by which a council's general income (largely rates), may be increased, regardless of land valuation movements. This process includes adjustment for growth in rateable properties. The rate peg is determined by a Local Government Cost Index. The rate peg to apply in the 2013/14 financial year was determined at 3.4%. To increase rates beyond the rate peg, councils may apply for a special rate variation, also determined by IPART and also independent of land valuation.

Revaluations primarily serve to redistribute the rate burden in a Local Government Area. This assists in maintaining an equitable distribution of rates, not to increase general income.

In contrast, land tax collections vary in direct relation with land values and increases in land values also work to push additional property holdings, adjusted by indexation, over the land tax thresholds.

Mine Valuations

LGNSW has raised its concerns about the judgement in *Perilya Broken Hill v Valuer General* [2012] with the Premier, the Minister for Finance and Services and the Minister for Local Government.

As this judgement is subject to an appeal, LGNSW is not in a position to form a view on the current mine valuation methodology or its application.

If the appeal is unsuccessful there will obviously be an urgent need for a review of mine valuation methodology and practice.

Objections

LGNSW has concerns over uncertainties associated with the dual objections process pursuant to section 35 of the *Valuation of Land Act (NSW) 1916*.

Section 35 provides that, except in certain circumstances, an objection must be lodged with the Valuer General, in accordance with the regulations, not later than 60 days after:

- (a) the date of service of the notice of valuation under section 29 (i.e. for council rating), or
- (b) in the case of a valuation for the purposes of the *Land Tax Management Act (NSW) 1956*, the date of service of the relevant land tax assessment under section 14 of the *Taxation Administration Act (NSW) 1996*.

LGNSW supports the argument made by the NSW Revenue Professionals that having two opportunities to lodge an objection creates a problem for councils where an objection is upheld against a valuation used by the OSR that has already been in use by a council for rating purposes for some time.

Review of the *Valuation of Land Act (NSW) 1916*

LGNSW supports the recommendation of the Joint Standing Committee on the Office of the Valuer General's *Report into the provisions of the Valuation of Land Act 1916*, 2010, that a comprehensive review of the Act be undertaken.

Conclusion

The valuation system underpins the growing land based taxation system in NSW. It is essential that a taxation system has a sound basis on the fundamental taxation principles of equity, efficiency, transparency and administrative simplicity. On the whole, administration of the present land valuation system appears to be working reasonably well for the purposes of Local Government rating. However, LGNSW maintains that the current land valuation system would be improved by transitioning to a market value based valuation methodology such as ICV. LGNSW also supports a comprehensive review of the *Valuation of Land Act (NSW) 1916* to make it fit for purpose in the 21st century.

For further information about LGNSW's comments, please contact Mr Shaun McBride at [REDACTED] or [REDACTED]

Yours sincerely

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Director - Policy