

The Effects of GST (Goods and Services Tax) on Construction Capital Costs and Housing Property Prices

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Abstract

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Following the implementation of GST in Malaysia on 1 April 2015, it was predicted that construction capital costs and housing property prices will increase accordingly. Examining the GST effects associated with construction capital costs and its influences towards the housing developers and housing property prices is this study's primary objective. This study also aims to highlight the developers' point of view regarding how GST impacts upon them as well as the housing prices of further future proposal of initiatives. The findings are obtained by surveying the opinion of 36 housing developers and an experienced property consultant under the employment of Henry Butcher (International Asset Consultant) in Penang, Malaysia. It was concluded that building materials and land acquisition are the major construction capital costs affected by the GST implementation while capital flow turnover is the post and significant consequence that developers now face which subsequently led to an increment of housing property prices. Ultimately, the end buyers are the ones who bear the brunt of the price increment where the government plays the central role within this scenario.

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1. Introduction

Following the implementation of GST in Malaysia, the primary group affected due to this broad-based consumption tax are the consumers (Warsame, 2006). According to the Malaysian Deputy

2. Impacts of GST on Construction Capital Costs

Building material costs are the major components in construction development costs while GST implementation has been identified to have inflated the construction material prices within a year of implementation (Breen *et al.* 2002, Burgess, 1998 and Daliae, 1999).

Findings as shown in Table 1 indicate that all building materials set the highest cost increase after GST implementation is not surprising as prior to GST implementation only second schedule materials were being charged 5% of sales and service tax (SST). On the other hand, GST had also led to an increment to the land acquisition cost although supply of land for housing properties is exempted from GST. Hence, the argument of Dato' Subromaniam Holsay saying that the "biggest cost components" which is land being exempted from GST would lead to cost saving for housing developers is imprecise. Besides, marketing costs has also been raised after GST implementation which may be a result of developers outsourcing marketing agents to help them boost the sales of property while the agents are entitled to as much as 5% of the project's Gross Development Value, leading to higher marketing costs for the developers. Moreover, labour cost as indicated at Table 1 does not get a significant GST impact as neither increase nor decrease.

Table 1. GST Impact on Construction Capital Costs.

No.	Construction cost	Mean Score	Frequency	Rank
<u>Construction Site Cost</u>				
1	Land Acquisition	3.74	High	9
2	Title Insurance	3.58	High	18
3	Site Demolition	3.52	High	29
4	Transfer Taxes	3.52	High	30
5	Commission & Fees	3.42	Medium	34
6	Feasibility/Survey	3.42	Medium	35
<u>Construction Hard Cost – Building Materials</u>				
1	Timber	4.10	High	1
2	Aggregates	4.03	High	2
3	Bricks	4.03	High	3
4	Cement	4.00	High	4
5	Roofing Materials	4.00	High	5
6	Glass	3.97	High	6
7	Ready Mix Concrete	3.97	High	7
8	Iron/Steel Reinforcement/ Bar	3.90	High	8
<u>Construction Hard Cost – Labour</u>				
1	Bricklayer	3.52	High	24
2	Tiller	3.52	High	31
3	Roofer	3.52	High	28
4	Plumber	3.52	High	27
5	Painter	3.52	High	26
6	Concretor	3.48	Medium	32
7	Steel Barbender	3.45	Medium	33
8	Structural Steel Worker	3.42	Medium	36
9	Plasterer	3.39	Medium	39
10	Carpenter (Formwork)	3.39	Medium	37
11	General Labour	3.39	Medium	38
12	Carpenter (Joinery)	3.35	Medium	40
<u>Construction Hard Cost – Equipment and Machinery</u>				
1	Excavator / Backhoe	3.65	High	10
2	Marble / Granite Polisher	3.61	High	14

3	Concrete Mixer	3.61	High	12
4	Concrete Vibrator c/w Poker	3.58	High	15
5	Mobile Crane	3.58	High	17
6	Bar Cutter / Bender	3.55	High	20
7	Power Trowel	3.55	High	23
<u>Construction Soft Cost</u>				
1	Marketing Fees	3.65	High	11
2	Insurance Fees	3.61	High	13
3	Legal Fees	3.58	High	16
4	Others	3.55	High	22
5	Engineering Fees	3.55	High	21
6	Architectural Fees	3.55	High	19
7	Loan / Interim Fees	3.52	High	25

3. Impact of GST on Housing Developers & Housing Property Prices

GST implementations in reality will not directly affect the business profitability but instead affects one's living cost and eventually one's purchasing power (Grigore and Gurau, 2013). Due to the lack of purchasing power, it will indirectly led to a waning sales of property as the development costs is brought up by 6% where the 6% charged is for the price of the final product which is housing property prices.

For a developer, their projects include residential properties and also commercial properties. Sales of commercial properties being charged an additional 6% of standard rate and developers are able to claim back the 6% from the government within one month. Hence, developer cash flow should not face any issue. However, all of the developers surveyed have not yet received any payback from the government after GST implementation due to the government system being temporarily offline, calculation error and the authorities still in the learning process of the new system.

Although housing properties are exempted from GST, the late tax claim refund from the government for the commercial properties will result in difficulties within an organisation's overall cash flow which is the critical circumstance that all respondents are facing (Englund *et al.*, 1995 and Zainal *et al.*, 2015). In order to cover for the losses within the tax claiming time frame, developers will then increase the final property price. As consequences, the housing property prices are then increased due to the limitation of exempted tax and late claims though not as much as 6%.

Once the housing property prices increase due to GST implementation eventually the end buyers will bear and suffer the price increment. The main reason is due to developers' entrepreneur objective which aims for profit maximisation. Although GST is said to be absorbed by housing developers on surface, but in reality, the final housing prices have already increased although only more than 3.41% and not 6%.

In conclusion, GST does affect housing developers in terms of cash flow (financial tightening) and work overload. Cash flow turnover leads to developer's increasing the output prices while the ones who bear the price increment are the end buyers who act as the last consumer within a supply chain whereas the complexity of the claiming procedure results in one's work overload and confusion.

4. Initiatives and Suggestions for Malaysian Housing Developers

Transferring all the cost increment to the end buyers is the priority decision among all of the developers. However such a measure will result in an increment of the housing property prices and thus is unadvisable. The initiative of using in-house sources which is recommended by MCT Executive Director is not an effective solution to soften the GST impact either as professional soft costs are just a small portion in a project. However, such small portioned savings can help an organisation to allocate their resources onto other operational fields.

On the other hand, promotions such as giving discounts between 5-10% for those buyers who can pay their instalments within a single payment is necessary in order to push up sales rate although developers will still sustain some losses. Additionally, the late claiming issues can be overcome if an organisation establishes a GST specialist department to handle all GST related issues. Although investment in a new department may be costly initially, however it can provide a positive return in the long run. Yet, all the suggestions above are not the most effective as that particular solution lies within the government's role because government is the one who can ensure that the GST implementation can be ran efficiently. Once everything is proceeding smoothly, then only anything can be settled easily.

Hence, for this moment, the most urgent issue which the government should tackle first is to list all the claimable guidelines clearly and make the claiming process faster so to ensure an organisation's cash flow can be proceeded smoothly. However, if the government would not abolish the GST implementation, then they must at least make housing properties less than RM500k into zero-rated tax items. Moreover, subsidies can also be provided for the developers as the Gross Development Value can be reduced while Gross Development Costs can be decreased automatically. For example, Prima and MyHome projects are the projects receiving subsidies from the federal government.

Meanwhile, the local government can alter certain policies or reduce other taxes such as stamp duty to help in lowering the GST impact (Obst *et al.*, 1999). Due to subsidies and increase in population density per hectare of land, housing developers would be able to build more economic houses and thus property prices would become cheaper while the sales rate becomes greater. As a side note from the findings, it was found that Malaysian NGOs within the construction field have no obvious function other than to act as the informer who passes along messages.

In conclusion, the ones who can directly help in lowering the GST impact on the housing developers are the federal and local governments. The federal government needs to improve itself and cooperate with the developers to ensure that all related can benefit from this tax implementation.

5. Conclusion

Overall, building materials and land acquisition costs are the major construction cost components to receive the most significant impact due to GST implementation. On the other hand, cost increment due to GST and exempted taxes have caused various issues in the developers' business capital flow. In order to maintain profit and cover the risk of losses developers have resorted to raising the housing prices where the end buyers will ultimately bear the price increment. Therefore the government should

wisen up and strives to transform the critical scenario for the developers and housing buyers into a win-win situation.

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