
Design of the interest limitation rule and additional bright-line rules

3 messages

APIA Admin <admin@apia.org.nz>

11 July 2021 at 13:00

To: Policy Webmaster <policy.webmaster@ird.govt.nz>

Cc: brooke.vanvelden@parliament.govt.nz, Nicola.Willis@parliament.govt.nz

Sir/Madam

1. Background

1.1. This submission is made on behalf of members of the Auckland Property Investors' Association Incorporated ("APIA"). We are an independent and non-profit organisation that provides education and networking opportunities for property investors and have been operating since 1995.

1.2. We based this submission on our members' responses to a survey we conducted on the subject matter of this consultation. The matters raised in this submission represent a high-level overview of our members' perspective on best design suggestions for the interest limitation rule and additional bright-line rules.

1.3. We preface these remarks by stating to you explicitly that **our organisation is against the introduction of interest limitation**. Not only is it an unprincipled approach to taxation in general, but it will also lead to long-term and negative financial effects on landlords, their tenants, and first home buyers. These effects include, and are not limited to:

- increase in compliance and administrative cost that outweigh the benefits of an overly complicated tax system;
- cost recuperation by landlords in the form of sharper rent increases creating additional cost pressure on tenants who are saving for their first homes;
- market distortion and unnecessary competition for first home buyers as a result of promoting investors' demand in the new-build market.

1.4. We are also of the view that given the seismic shift of this policy seeks to tax treat investment properties, **it is imprudent to shorten the usual 6-month consultation period to a mere 4.5 weeks**. This shortened timeframe is grossly insufficient for the government to design a robust policy.

1.5. Nevertheless, we are cognisant that the scope of the consultation does not extend to whether interest limitation *should* be policy but rather *how interest limitation as policy can best be designed*. On that basis, we make these recommendations:

2. On the definition of a *new-build*

2.1. On renovating an uninhabitable dwelling so that it becomes habitable

2.1.1. **On whether a *new-build* should include renovating an uninhabitable dwelling so that it becomes habitable: we think yes.** Bringing a previously uninhabitable property up to habitable standards (major/extensive renovation) materially adds to the housing stock whereas a minor renovation does not. Difficulty relating to differentiating between major and minor renovation should not, in effect, disadvantage any property investor who undertakes such work especially when you are prepared to overlook the same administrative difficulty and accept a one-for-one dwelling replacement as sufficient for a simple new build (second bullet point, paragraph 7.5, pages 73-74 of the discussion document).

2.1.2. On whether there is some tool that could be used to identify when a dwelling that is completely uninhabitable has been improved significantly, such that it has added to housing supply: suggestions from our members include

- relying on before and after inspection reports by local councils or registered valuers;
- referencing the building consent process and issuance of Code of Compliance Certificate ("CCC");
- a specific statutory provision giving definitions to *uninhabitable dwelling* and *habitable dwelling* for the purpose of determining eligibility for exemption from interest limitation; and
- incorporating the Healthy Homes Standards in defining what is *habitable*.

2.1.3. Granting major renovation work of this nature the status of a *new build* could create the perverse incentive for existing owners to allow a property to fall into disrepair. To promote the supply of healthy

and safe rental housing, **we suggest that new-build status of this nature be granted only to owners who acquire a property in an uninhabitable state** (and subsequently brings it up to habitable standards) and not those who have, in the time of their ownership, allowed a habitable dwelling to fall into a state of uninhabitable disrepair and subsequently restore the same property back to a habitable standard.

3. On new build exemption from interest limitation

3.1. On your general rule to apply exemption only to new builds that receive CCC on or after 27th March 2021: **our members' view is that the designated milestone date (27th March 2021) is arbitrary.** Not only does it undercut the integrity of the tax system its application would also lead to an increase in compliance and administrative costs for those investors who transacted on or around that date. These investors should not be unfairly disadvantaged (or advantaged). Given that the intent of the policy is to increase the supply of housing and considering the unexpected nature of the government's announcement of its housing policy on 23rd March 2021 (rendering little chance for investors in a midst of a transaction to mitigate their tax loss) our view is that that it would be appropriate for **the new build exemption to cover any dwelling that receives its CCC on or after 1 April 2020.**

3.2. On whether new build exemption should apply only to early owners, or to both early owners and subsequent purchasers: our members' preference is for the former, **that exemption be only applied to early owners.** However, should the exemption be also granted to subsequent purchasers, we consider it appropriate for the **exemption to expire 10 years from CCC issuance applicable to both early owners and subsequent purchasers.**

3.3. 60% of our members **disagree with the proposed continued investment rule** that seeks to truncate a new-build's eligibility for exemption from interest limitation by the mere act of the owner moving into the property (even if it is for a short period of time). Given the severe shortage of rental properties, it would be imprudent to restrict (new-build) owners' ability to accommodate and meet their changing circumstances by financially disincentivising them to return a one-time owner-occupied new-build back into the rental pool. We think the policy would be more able to achieve its stated objective of promoting access to housing (whether by ownership or by renting) if the exemption to interest limitation is restored once an owner-occupied new-build property is returned into the rental market within the period of exemption.

4. On interest allocation

4.1. On the treatment of new loans drawn down post-27th March 2021 that, in effect, refinances a pre-27 March 2021 loan, our members' strong preference (89.3%) is for the **new loan to benefit from a specific provision** (which we understand to be that the new loan would receive the same tax/interest limitation treatment as if it is the original pre-27 March 2021 loan).

4.2. On the proposed approach to a high water mark: **we disagree with the approach and recommend that the total limit of the revolving credit on 27th March 2021 benefit from the specific provision** (see paragraph 4.1. above). A high water mark test that is underwritten by an arbitrary date (27th March 2021, see paragraph 3.1 above) fails to account for the seasonality or conventional business cycle of property investing (which can be broadly predicted by the due dates of GST, provisional tax, insurance and rates). Should 27th March 2021 fall at a low point of an investors' borrowings then that investor is unfairly disadvantaged by this arbitrary date.

4.3. On suggestions as to any commercial reasons for a NZD loan to be restructured to a foreign currency loan, our members' feedback are the following

- to take advantage of a lower interest rate/more favourable financing terms;
- to facilitate the purchasing of an overseas property which may include collateralising an NZ property; and
- to minimise the actual cost of repayments by utilising exchange rate movements.

5. Thank you for the opportunity to give feedback on the design of the interest limitation rule and additional bright-line rules. Should you consider it appropriate and necessary, representatives from our organisation will be available to elaborate on matters raised above.

Sincerely,
Kristin Sutherland
President of the Auckland Property Investors' Association Incorporated



Your like-minded community of property investors. From beginner to experienced.

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Policy Webmaster <Policy.Webmaster@ird.govt.nz>
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11 July 2021 at 18:52

[IN CONFIDENCE RELEASE EXTERNAL]

Hi Kristin

Thank you for your submission on the discussion document – *Design of the interest limitation rule and additional bright-line rules*.

We will be considering all submissions that come in over the consultation period as we prepare the final design of the proposals. If you have indicated it is okay to do so, we may contact you to discuss the points raised.

Our next steps include:

- considering your submission,
- reporting to Ministers on submissions and recommending any changes, and
- progressing any changes the Government agrees to through the parliamentary process.

Any changes progressed through the parliamentary process would be subject to parliamentary debate and select committee scrutiny, including consideration of public submissions.

Submissions may be the subject of a request under the Official Information Act 1982, which may result in their publication. The withholding of responses on the grounds of privacy, or for any other reason, will be determined in accordance with that Act. If you consider that any part of your submission should properly be withheld under the Act please let us know, if you have not already done so.

Many thanks once again for taking the time to submit on this discussion document.

Policy Webmaster

Policy and Regulatory Stewardship

Inland Revenue

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23 July 2021 at 12:42

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