# Submission to

# Productivity Commission

# on the

# Local Government Funding and

# Financing Draft Report

**Date: 16 September 2019**

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Tourism Industry Aotearoa (TIA) welcomes the opportunity to submit on the draft report by the Productivity Commission (the Commission) on Local Government funding and financing.

This submission is filed without prejudice to TIA's future position. Our ability to prepare a comprehensive submission responding to the draft report relied on the provision by the Commission of information relevant to the connection between the draft report and the benefits that would accrue. If any information is provided at a later date, TIA reserve the right to comment further.

## EXECUTIVE SUMMARY

1. TIA welcomes the opportunity to submit on the draft report by the Productivity Commission on Local Government funding and financing and we thank the Commission staff for their willingness to engage. While we concur with some of the tourism-related analysis provided in the draft report we are disappointed in the recommendations to address the impacts of regional tourism growth. In this submission we focus on the tourism-related aspects of that draft report.

2. The Commission has proposed a patchwork of funding solutions - user pays, bed taxes, and IVL funding. These fail on a number of fronts for local government funding and financing, most importantly against the Commission's stated principles of efficiency, equity and fairness, and sustainability.

3. It is our view that the Commission's draft report took a dismissive view of the tourism industry, seemingly arguing that our members simply needed to run their businesses better. The Productivity Commission has taken the path of least resistance rather than providing a thoughtful and detailed analysis of the issues and complexities of local government funding.

4. TIA's proposal is that Central Government makes an annual calculation equivalent to 20% of the GST already collected from international visitors and distributes these funds via a Trust to Local Government to address local tourism-related needs, with the allocation determined by the measured level of visitor impact on each territorial local authority.

5. New Zealand doesn't need new taxes. What we need is to find ways to better share the taxes and charges we already collect.

## INTRODUCTION

6. TIA is the peak body for the tourism industry in New Zealand. With over 1,600 members, TIA represents a range of tourism-related activities including hospitality, accommodation, adventure and other activities, attractions and retail, airports and airlines, transport, as well as related tourism services.

7. The primary role of TIA is to be the voice of the tourism industry. This includes working for members on advocacy, policy, communication, events, membership and

business capability. The team is based in Wellington and is led by Chief Executive, Chris Roberts.

8. Any enquiries relating to this paper should in the first instance be referred to Sam MacKinnon, TIA Policy Analyst at sam.mackinnon@tia.org.nz or by phone on 021 026 72441.

## GENERAL COMMENTS

**We concur with parts of the analysis provided in the draft report.**

9. One particular point we endorse is the observation that tourism is a significant direct contributor to the Government through the tax system.

*"Deloitte estimate that in the year ending March 2018 central government collected about $1 billion in income tax, $353 million in company tax and $264 million in motor vehicle taxes, attributable to international tourism. But unlike other export industries, tourism also directly contributes a large amount of GST to central government revenue. In 2017–18, international tourists generated $1.7 billion in GST. Many councils perceive a disconnect between council costs from tourism and central government benefit from tourism."* [1]

10. It is also worth noting the Commission's analysis around day visitors:

*"The guest night figures do not capture visitors who may be visiting or passing through one district, but staying in another district. Mackenzie, Buller and Matamata-Piako are examples of districts where the number of visitors passing through to visit popular tourist sites (e.g. Church of the Good Shepherd in Tekapo, the Punakaiki rocks on the West Coast, and the Hobbiton movie set in Matamata) is likely to far exceed the number of visitors staying one or more nights. Yet day visitors also put pressure on local infrastructure, including roads, car parks and public toilets."* [2]

11. However, given the analysis above it seems incongruous that the Commission would suggest that an accommodation tax is the best approach to levy tourists, especially for those regions with a high number of day tourists. Tourism is New Zealand's biggest export, and unlike most other export industries pays GST. This is why our view is that an amount equivalent to 20% of the annual GST international visitors pay should be returned to local government in order to alleviate funding pressures, rather than implementing extra costs on tourism businesses to pass onto their customers.

12. We also acknowledge the Commission's finding 7.3, and the subsequent recommendation 7.1:

[1] Productivity Commission Local Government Funding and Financing Draft Report, pg. 80.
[2] Ibid, pg. 81.

F7.3: *Differentials and the uniform annual general charge are not transparent in allocating the burden of rates to those who benefit from council services. Targeted rates provide a more direct connection between the funding and the beneficiaries of services; and therefore are a much more transparent way of giving effect to the benefit principle.*

R7.1: *The Local Government (Rating) Act 2002 should be amended to remove rates differentials and uniform annual general charges. Councils should have five years to implement their removal.*[3]

13. This aligns with our view that differentials lack transparency and for businesses result in a higher rate payment for little if any direct benefit. We support Recommendation 7.1.

14. In those cases where there is a clear connection between funding and the beneficiary then a targeted rate may be justified. We say this with caution however, as accommodation operators in Auckland are currently burdened with a targeted rate requiring them to pay approximately $14m annually towards destination marketing costs. They are not the sole beneficiary of those services and receive only 7% of the visitor spend in the region.[4] Requirements for implementing targeted rates on businesses need to be established and agreed with the business sector to ensure they do not become the new method of non-descript revenue gathering. To support this the business sector needs to be engaged early in the design process, and not just in the final consultation of the annual or long-term planning process.

**It is our view that the Commission took a dismissive view of the industry, seemingly arguing that our members needed to run their businesses better.**

15. One of the Commission's main concerns is around the perception of subsidising the industry. The following comments are unnecessary as the issue is about local government funding, not how tourist operators should run their businesses.

*"All businesses have costs that their customers are expected to cover. To understand the problem of tourism funding pressures, a good place to start is to note that a successful private business produces goods and services that customers value more highly (indicated by their willingness to pay) than the resource costs of producing those goods and services. A basic tenet of economic efficiency is that if a business cannot achieve this surplus of providing value over cost, then it is making poor use of resources which would be better deployed elsewhere in the economy.*

*Tourism should be no exception to this basic tenet. Often no problem exists as tourists, either directly or through the tourist industry, pay for and cover the costs of the goods and services they receive. To identify where the problem lies, it is*

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[3] Productivity Commission Local Government Funding and Financing Draft Report, pg 194.

[4] Monthly Regional Tourism Estimates YE June2019

*necessary to analyse the different types of goods and services that residents and tourists consume and how the costs of providing them are recovered."* [5]

16. With regards to the Commission's principled objection that "*no other industry is, or expects to be, subsidised by receiving a GST rebate*" it is our view that the Commission has chosen to put more emphasis on 'GST rebate' than 'subsidy'. Accepting that subsidy is interpreted in a wider context, not specifically related to a GST rebate, there are many examples of government providing subsidies, grants, incentives and discounts to a specific industry.

17. For instance, it was recently announced that the Government's Interim Climate Change Commission has proposed bringing agriculture into the Emissions Trading Scheme (ETS) from 2025 but under a 95 percent discount rate, which means farmers will only meet the cost of 5 percent of their emissions. Recognising that agriculture presents a challenge for New Zealand to reach our target of net zero emissions by 2050, a Government agency has proposed what is essentially an agricultural subsidy to entice the agri-sector to join the ETS.

18. Another example of what is effectively a subsidy for the agri-sector is the large-scale irrigation projects that have been crown-funded. Crown Irrigation Investments Limited was established in 2013 to enable the development and construction of off-farm regional irrigation infrastructure where it identifies irrigation scheme proposals that have the potential to generate long-term economic benefits from irrigation for New Zealand. While funding will be wound-up in the first part of 2018, according to the Briefing for Incoming Ministers on 31 October 2017, CIIL has invested $27.5 million via grants in large-scale irrigation schemes. Since then, CIIL news releases have shown a further $134.4 million in loans to some of these projects. These projects have primarily benefitted dairy, beef and lamb, horticulture and viticulture farming, thus essentially subsidising an industry that would have struggled to fund these investments under normal commercial conditions.

19. Furthermore, the film industry has been receiving subsidies for many years. International productions are eligible for a cash grant of 20% of Qualifying New Zealand Production Expenditure (QNZPE) with a 5% Uplift available for a smaller number of productions that are invited to apply and can demonstrate significant additional economic benefits to New Zealand. Post, digital and visual effects productions can access a grant of 20% of QNZPE up to QNZPE of $25 million, and 18% of QNZPE for QNZPE above $25 million. According to StatisticsNZ, latest statistics on the film sector showed that gross revenue was $3.3 billion per annum and the sector employed a total of 29,700 jobs (both salaried and contracted). By comparison, tourism draws in $39.1 billion per annum and directly employs 216,000 people and another 149,000 indirectly in New Zealand – almost 1 in 7 jobs.

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[5] Ibid, pg 173.

20. The reality is that most industries have received support from Central Government at some stage. In that light, the distribution of a portion of government's GST to tourism is no different than the investment into strong biosecurity systems which primarily benefits the agriculture and horticulture sectors. All of the above are worthwhile investments but support specific sectors and do not have differing arguments from the tourism industry for the wider public good they provide.

**The International Visitor Levy (IVL) is not intended to be a complete source of funding for local government.**

21. The Commission states:

*"Some small tourist spots such as Tekapo and Punakaiki do not offer much accommodation and many of their visitors stay for less than a day. An accommodation levy would not work in such places because it would be unlikely to raise enough revenue to cover the costs caused by tourists. Such places would need to use other options such as introducing more user pays (e.g. paid car parking and public toilets, access charges to scenic spots) or receiving a portion of the new international visitor levy collected at the New Zealand border."* [6]

22. However, it is clear that the IVL is not an alternative source of funding to an accommodation levy for local government, as referenced in the Commission's draft report.

23. The Government has stated in the published outline of investment priorities for the IVL that they will favour 'national solutions for infrastructure issues'.[7] Some initial projects have been funded, none of which are led by councils.[8] The Government's clear intention is to have a small number of targeted investments that will deliver on national objectives. An Investment Plan is to be issued by November but it is now clear that the IVL cannot be considered a source of funding for areas with low accommodation and high day visitor numbers.

**User pays systems are unlikely to provide sufficient funds for regional tourism growth**

24. While the Commission advocates for a broader use of user pays in many areas, there is a lack of detail on what that looks like. Common forms of user pays for visitors include parking fees and admission charges e.g. pools. These systems are well embedded in our towns and cities, paid for by locals and visitors alike. There are very

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[6] Productivity Commission Local Government Funding and Financing Draft Report, pg 177.

[7] International Visitor Conservation and Tourism Levy - Investment Priorities; https://www.mbie.govt.nz/assets/international-visitor-conservation-and-tourism-levy-investment-priorities.pdf

[8] "First IVL projects to support sustainable tourism and conservation", Beehive Press Release 14 August 2019; https://www.beehive.govt.nz/release/first-ivl-projects-support-sustainable-tourism-and-conservation

few examples of user pays for local and mixed-use infrastructure where locals would be exempt from the fee.

25. While we support the principle of user pays for its fairness, the reality is there appears to be little appetite from local government to implement it. This is likely due to a range of reasons. It's another tax on locals, the income derived may not support the operating costs to manage the infrastructure, and a fee can cause unintended side effects e.g. if they don't want to pay for using the toilet.

**It is our view that the Productivity Commission has taken the path of least resistance in advocating for an accommodation levy.**

26. We believe there has been a severe lack of analysis into possible funding options to support regional tourism costs. The report's comment below illustrates this point:

    *"The government is already considering a legislative change to allow Queenstown Lakes District Council to introduce such a levy following a local referendum.* ***There is no reason why the option should be limited only to one district*** *– the ability to introduce an accommodation levy would reduce cost pressure in tourism hot spots around the country."* [9]

27. Other parts of the report confirm that a bed tax was the starting point for the Commission, not the reasonable conclusion they reached.

28. In addition, the report notes *'the best options to directly recover the tourists' share of the costs of mixed-use services are through greater use of user pays, and accommodation levies. These are the only options that target the right group, do not involve an industry subsidy, and meet the other funding principles outlined above'*. In our view those proposals fail on two of the five principles the Commission is using to assess options – fairness and efficiency.

29. Our main objection to a bed tax is on the principle of equality. Levying a tax on commercial accommodation is an easy target, and technology may now allow this to be extended to some peer to peer accommodation like Airbnb. However, a bed tax unfairly targets one sector, who host only a minority of total visitors.

30. The Productivity Commission has shown an unfortunate and significant lack of understanding of the nature of the visitor economy. Not all visitors are tourists, and not all visitors stay the night in a hotel, Airbnb or other paid accommodation. But all visitors are consumers of resources and services in the place they visit.

31. A June 2019 report by Horwarth HTL calculates that there were 140 million overnight visitor stays in 2018 (domestic and international combined, split roughly 50/50). Only 35% of these nights were spent in commercial or peer to peer accommodation. The

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[9] Local Government Funding Draft Report, pg. 252.

rest was in private homes, student accommodation, freedom camping and other non-paid accommodation.

32. A bed tax misses almost two-thirds of the visitors travelling around New Zealand.

33. There also seems to be an assumption that the costs won't impact the accommodation sector – they are simply the vehicle by which the tax is collected. However, it is incorrect to assume that the bed tax only impacts the person paying for the bed. Accommodation demand is relatively elastic, increasing and decreasing with changes in room rate. If a bed tax is added to the rate, accommodation providers may be forced to drop their rates to retain business, especially for group business which is particularly price-sensitive. When the Border Clearance Levy was introduced in 2016, airlines were unable to pass the full cost of the levy on to passengers due to the competitive nature of the sector. We expect the same to occur for the accommodation sector, particularly in current market conditions where international visitor growth has slowed to approximately 1% in 2019.

34. As you can appreciate, we and the industry have given much thought to the options available for local government funding, particularly around funding of tourism and mixed-use infrastructure. This has included the McKinsey report commissioned by some of our members, and through the design sprint we undertook with industry and regional tourism representatives. We have arrived at our position – Central Government makes an annual calculation equivalent to 20% of the GST already collected from international visitors and distributes these funds via a Trust to Local Government to address local tourism-related needs – following extensive research on viable and equitable solutions, and in-depth discussion by our Board.

35. While we concur that not all of the options laid out in the draft report were practical solutions, we believe there could have been a more genuine attempt to address or identify funding models that could solve or assist with tourism infrastructure funding. The proposed mix of funding options is a patchwork of solutions that will be confusing for visitors and local government alike, and do no favours to the reputation of New Zealand tourism.

**The Commission's dismissal of Option Three (Rebating a proportion of GST)**

36. We wish to specifically critique the Commission's dismissal of option three.

37. As stated in the report:

"*As noted, several submitters supported the third option (councils in tourist areas receive a portion of GST from tourist spending). However, it is not possible to identify GST by location or by the identity of the final consumer (e.g., GST on a rental car hire is not related to where the car is driven or for what purpose – tourism, personal non-tourism, or business). A more principled objection to this option is that no other industry is, or expects to be, subsidised by receiving a GST rebate. Implementing such a rebate would violate the principle that businesses should cover their costs.*

*A possible justification sometimes offered for this option is that international tourists do not have free use of many expensive services that taxes pay for, such as schools and hospitals. Even so, international tourists do benefit from some services (such as ACC, police and rescue services, and national conservation services) while travelling in New Zealand. International tourists also do not pay income taxes in New Zealand. In addition, the justification fails entirely for domestic tourists who make up a large proportion of the total." [10]*

38. From our view, the Commission hasn't shown a willingness to pursue this option further. To state "it is not possible to identify GST by location or by the identity of the final consumer" is to take a superficial view of possible methodologies to arrive at a reasonable dollar figure. StatisticsNZ have data outlining the regional spend of both international and domestic tourists, which would provide a provisional figure of tourist spend in order to "identify the final consumer". In addition, TIA have developed a proposed regional distribution system for GST to be redistributed to the regions.

**Our Own Position**

39. As made clear above, TIA does not support an accommodation levy or 'bed tax'. Through our own processes, we have investigated the merits of an accommodation levy or 'bed tax' as potential options to alleviate local government stresses around tourism infrastructure. As noted earlier a bed tax fails on the principles of equity and fairness – principles which the draft report highlights as important to assessing the adequacy of funding and financing options.

40. TIA's proposal is that Central Government makes an annual calculation equivalent to 20% of the GST already collected from international visitors. This amount would be $335m based on 2018 data.

41. These funds would be distributed to councils via a Trust to address local tourism-related needs, with the allocation determined by the measured level of visitor impact on each territorial local authority. Appendix 2 provides what each territorial authority would receive in annual funding based on the funding model, using 2018 data. The measure of visitor impact is based on total visitor nights per region (territorial authority) as an indicator of where tourism pressures may lie.

42. We would appreciate you updating the draft report (Pg 173) to acknowledge our position - to set aside an amount <u>equivalent to</u> 20% of the GST collected from international tourist spending.

43. One of the strengths of our proposed model is that it meets the tax principle of sufficiency. We believe an amount of $335m p.a. (equivalent to 20% of the GST collected from international visitors in 2018) will address current and future local

[10] Local Government Funding Draft Report, pg 176.

demand. The amount would adjust each year relative to the total number of international visitors.

44. In April 2017, TIA commissioned Deloitte to survey local councils to understand the scale and depth of local and mixed-use infrastructure requirements to meet forecasted tourism demand. 47 councils responded, whose regions collectively received 95% of visitor expenditure. The subsequent report identified 673 Local and Mixed-Use projects. A rough order of cost was estimated for 525 (78%) of the 673 projects, totalling $1.46 billion.

45. Our proposed model focuses on more than funding local mixed-use infrastructure. We are aiming to support the growth and development of tourism across all regions through their destination management plans. An allocation of $335m p.a. from Central Government to support local visitor economies is not unrealistic and can be achieved through a reprioritisation of current government priorities for regional development. In particular, we encourage a reallocation of the $1b p.a. Provincial Growth Fund (PGF) to regional tourism needs when the initial 3-year fund period draws to a close in 2021.

46. New Zealand doesn't need new taxes. What we need is to find ways to better share the taxes and charges we already collect.

Follow up process

47. TIA wishes to participate further in any follow-up process, including any formal meetings, to ensure that the potential impacts on tourism are adequately represented.

**BACKGROUND**

48. Tourism for New Zealand is big business as the country's largest export sector. It is a major contributor to the New Zealand economy that will always be here and won't easily go offshore. Tourism takes the lead in promoting New Zealand to the world. The brand positioning built by a vibrant tourism industry has become an important source of national confidence and identity and a front window for "Brand New Zealand". Indeed, the clean and pure offering that is synonymous with New Zealand tourism has been widely adopted and used to promote New Zealand exports in a range of other industries as well.

49. The tourism industry delivers the following value to New Zealand's economy:

- Tourism in New Zealand is a $107 million per day and $39.1 billion a year industry. Tourism delivers around $44 million in foreign exchange to the New Zealand economy each day of the year. Domestic tourism contributes another $63 million in economic activity every day.

- The tourism industry directly and indirectly supports 13.5% of the total number of people employed in New Zealand. That means 365,316 people are working in the visitor economy.

- Tourism is New Zealand's biggest export industry, earning $16.2 billion or 20.6% of New Zealand's foreign exchange earnings (year ended March 2018).

Tourism 2025 and Beyond

50. Tourism 2025 and Beyond is the New Zealand tourism industry's growth framework. It has been created by industry, for industry and keeps the tourism industry's focus firmly on growing our value to individuals, communities, the environment, the economy and our visitors. Its development is led by Tourism Industry Aotearoa.

51. Tourism 2025 and Beyond was launched in May 2019 and has a vision of 'Growing a sustainable tourism industry that benefits New Zealanders.' It is closely aligned with the New Zealand-Aotearoa Government Tourism Strategy and takes a balanced scorecard perspective to:

    - Make sure our visitors are having great experiences
    - Make sure our communities are happy with and benefitting from tourism
    - Make sure our environment benefits from tourism, and
    - Bring economic success.

End.

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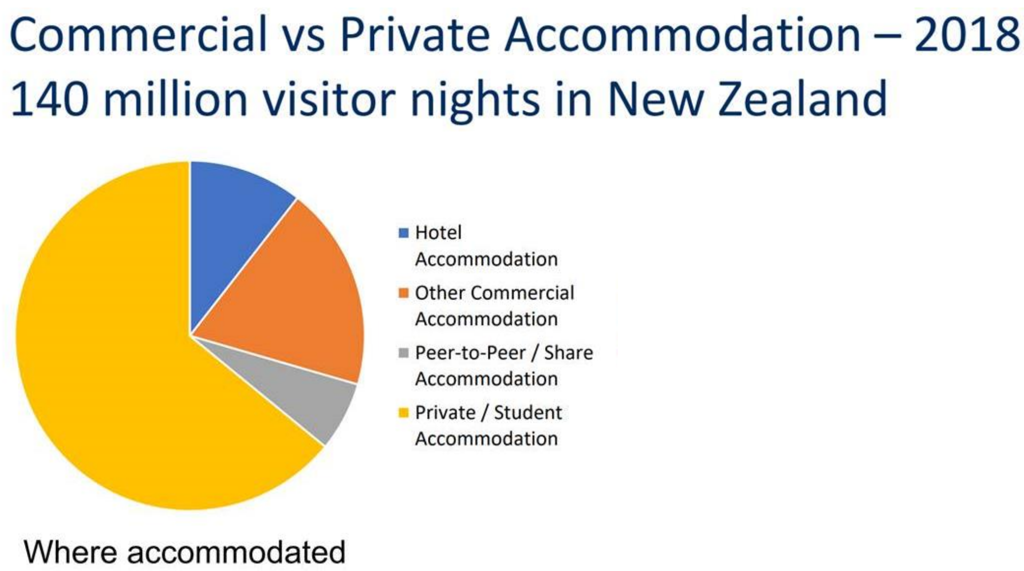
**Appendix 1: Horwath presentation to Hotel Industry Conference, June 2019.**

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## Appendix 2: TIA Regional Tourism Funding - Proposed Distribution System

It is the recommendation of the TIA Board that Central Government makes an annual calculation equivalent to 20% of the GST already collected from international visitors and distributes these funds via a Trust to Local Government to address local tourism-related needs, with the allocation determined by the measured level of visitor impact on each territorial local authority.

The table below provides what each territorial authority would receive in annual funding based on the funding model, using 2018 data. The measure of visitor impact is based on total visitor nights per region[11] (territorial authority).

| Territorial Authority[12] | Proportion of International Visitor GST attributed[13] |
|---|---|
| Far North District | $ 10,707,276 |
| Whangarei District | $ 4,703,160 |
| Kaipara District | $ 1,131,075 |
| Auckland Council | $ 62,163,455 |
| Thames-Coromandel District | $ 6,554,086 |
| Hauraki District | $ 1,175,125 |
| Waikato District | $ 1,407,004 |
| Matamata-Piako District | $ 900,489 |
| Hamilton City | $ 6,310,746 |
| Waipa District | $ 1,350,116 |
| Otorohanga District | $ 300,278 |
| South Waikato District | $ 372,150 |
| Waitomo District | $ 1,282,548 |
| Taupo District | $ 9,810,714 |
| Western Bay of Plenty District | $ 2,366,939 |
| Tauranga City | $ 7,988,056 |
| Rotorua District | $ 19,547,283 |
| Whakatane and Kawerau Districts | $ 2,463,127 |
| Opotiki District | $ 1,089,693 |
| Gisborne District | $ 2,281,465 |
| Wairoa District | $ 407,315 |
| Hastings District | $ 3,351,751 |
| Napier City | $ 6,339,198 |

[11] Guest Nights data source - Accommodation Survey / Commercial Accommodation Monitor (CAM) (YE March 2018)

[12] Analysis based on 66/67 Territorial Authorities - Chatham Islands excluded as CAM data not available. Whakatane/Kawerau & Carterton/South Wairarapa combined as per provision of CAM data

[13] GST data source - Tourism Satellite Account (YE March 2018). Based on 20% of $1,675m

| | |
|---|---|
| Central Hawke's Bay District | $ 162,800 |
| New Plymouth District | $ 4,363,816 |
| Stratford District | $ 358,482 |
| South Taranaki District | $ 838,508 |
| Ruapehu District | $ 4,073,129 |
| Whanganui District | $ 1,622,126 |
| Rangitikei District | $ 310,019 |
| Manawatu District | $ 443,595 |
| Palmerston North City | $ 3,456,305 |
| Tararua District | $ 357,408 |
| Horowhenua District | $ 764,949 |
| Kapiti Coast District | $ 1,514,762 |
| Porirua City | $ 573,219 |
| Upper Hutt City | $ 502,488 |
| Lower Hutt City | $ 2,106,415 |
| Wellington City | $ 19,519,342 |
| Masterton District | $ 1,278,126 |
| Carterton and South Wairarapa Districts | $ 804,535 |
| Tasman District | $ 6,159,592 |
| Nelson City | $ 6,322,752 |
| Marlborough District | $ 6,651,457 |
| Kaikoura District | $ 2,453,981 |
| Buller District | $ 2,328,527 |
| Grey District | $ 2,287,657 |
| Westland District | $ 7,149,749 |
| Hurunui District | $ 3,260,841 |
| Waimakariri District | $ 974,224 |
| Christchurch City | $ 24,929,918 |
| Selwyn District | $ 684,535 |
| Ashburton District | $ 1,751,415 |
| Timaru District | $ 2,635,450 |
| Mackenzie District | $ 7,027,945 |
| Waimate District | $ 354,992 |
| Waitaki District | $ 3,504,357 |
| Central Otago District | $ 2,817,640 |
| Queenstown-Lakes District | $ 38,161,186 |
| Dunedin City | $ 7,919,909 |
| Clutha District | $ 755,367 |
| Southland District | $ 7,014,411 |
| Gore District | $ 387,681 |
| Invercargill City | $ 2,413,447 |
| **Total** | **$ 335,000,109** |

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