

30 August 2019

Murray Sherwin
Chair of the Productivity Commission
Online submission

Dear Chairman,

Tax on vacant residential land – Local government funding and financing enquiry

Chartered Accountants Australia and New Zealand (CA ANZ) welcomes the opportunity to comment on the Productivity Commission's consideration of a tax on vacant residential land as part of the *Local government funding and financing: Draft report*. We would be happy to discuss our submission with you in further detail.

While we recognise the significant amount of work undertaken by the Productivity Commission in preparing its draft report, our comments are restricted to those areas addressing tax on vacant residential land and we hope our comments will assist in compiling your final report to the Minister of Finance in November.

Overview

CA ANZ would caution against rushing to introduce a vacant residential land tax. Government must first clearly develop their problem definition, and who a vacant residential land tax would seek to target. There is a high risk that a vacant residential land tax would have unintended consequences for a wide range of taxpayers. If a proposed tax means to capture developers who may currently hold large parcels of vacant

residential land for future development (land banking) then it should be targeted accordingly. In addition, there may be other more appropriate mechanisms available to Government.

Defining 'vacant land' for the purposes of a vacant residential land tax would be complex, likely with a number of exclusions and exceptions required. Complexity also brings with it costs of compliance and administration, an erosion of taxpayer certainty, and can affect whether taxpayers perceive the tax as being broadly fair. If a vacant residential land tax is considered by Government, we recommend that a definition is set nationally and should only be applied by local governments where there is an identified shortage of land and a desire for housing. We also recommend that de minimis thresholds are considered to reduce the inappropriate application and overreach of a proposed tax.

Other factors which affect housing supply and affordability in New Zealand, such as the Resource Management Act, unitary and zoning plans, and access to financing and funding must be considered in tandem with a proposed vacant residential land tax.

Problem Definition

In our view there is no clear evidence that a vacant residential land tax would directly achieve a reduction in housing costs or significantly increase supply of residential land in high demand areas.

The Minister of Finance, in his letter of 29 April 2019, asked the Productivity Commission to consider whether a tax on vacant land would be a useful mechanism to improve the supply of available housing for New Zealanders.

When considering the supply of land for housing in New Zealand we first make two key observations.

Firstly, New Zealand has a shortage of available residential land for housing in high demand areas such as Auckland, Wellington and Queenstown¹. However, we query whether there is a shortage of available land at a national level. This needs to be considered when proposing a vacant land tax and whether, or how, such a tax is targeted, as a tax levied on regions where there is no shortage of available land, or a desire for housing development could be perceived as unfair.

Secondly, supply of land is only one factor when considering housing supply and affordability. The Tax Working Group in their interim report² observed that supply of land is only one factor of housing affordability and supply, high building costs and access to finance for developers are also significant factors. There is therefore not a linear correlation between land supply and housing supply and affordability.

Government needs to clearly define the intended scope of a vacant land tax and, if the intention is to increase supply of residential land, whether the tax will have the desired effect. If a vacant land tax is proposed it must be accompanied by a thorough review of other key factors, including the Resource Management Act, and unitary and zoning plans. This needs to be accompanied by thorough analysis of where there is a demand for vacant land supply.

Defining ‘vacant land’ and associated issues

If a vacant residential land tax is proposed, we outline some key questions regarding defining ‘vacant land’ which should be considered. While these questions highlight the complexity of defining vacant residential land, the list is far from exhaustive. Consultation with relevant stakeholders should be undertaken at the policy design stage to further scope these issues.

If Government does pursue a vacant residential land tax, the policy trade-off will be between a complex definition which minimises the opportunities for avoidance, and policy which is simple to apply, administer

¹ For example, the 2013 census data showed that 44% of our population were based in Auckland and Wellington. A more current estimate will be available when the results of the 2018 census are available.

http://nzdotstat.stats.govt.nz/wbos/Index.aspx?_ga=2.199122543.1378277644.1567024553-995490251.1566871665#

² <https://taxworkinggroup.govt.nz/resources/future-tax-interim-report.html#section-13>

and comply with. As we have stated, Government must identify during the problem definition phase which taxpayers a proposed tax would intend to capture to limit the overreach and complexity of the tax.

A national level definition of vacant land would provide clear guidance to local government and taxpayers. Government needs to decide whether a vacant land tax would apply nationally with local government able to set the rate, ideally within a band relative to the need for land supply, or whether a more targeted approach would be adopted where the tax would apply only to areas identified as being under pressure. If a vacant residential land tax is proposed, CA ANZ would urge that the tax only be applied if and when regions have been identified as having both a high demand for new housing and lack of available land.

Regardless, CA ANZ suggests a de minimis threshold be considered, such as applying the tax only to properties exceeding an acre (or 4000 m²), to reduce the risk of overreach and to exclude property where activities are being carried out (such as gardening or grazing). A de minimis would resolve or avoid some of the issues we identify below but does limit the scope of land which could be used to increase housing supply and the revenue return.

Using existing definitions of vacant land, the scope of a proposed tax could extend to capture holiday homes as they are typically unoccupied for a large period of time. Including a de minimis would largely avoid this issue.

Land holdings on the urban rural boundary pose an additional challenge and may conflict with other Government objectives. We note Government has recently signalled its intention to protect valuable, productive agricultural land such as market gardens. This land is currently being eroded by urban sprawl in large areas of the country but would also be considered a prime option for residential development due to its proximity to existing infrastructure. This adds an additional layer of complexity to defining and administering a vacant land tax.

As we expect defining vacant land to be complex, and likely to include a number of exclusions or exceptions, significant taxpayer education would be required to support compliance and to ensure taxpayers could correct or amend the vacant land assessment if required.

Vacant residential land tax questions:

- How would a vacant residential land tax be applied where taxpayers intend to develop the land but have not yet been granted consent to do so?

This point requires careful consideration. Resource consent and planning processes are long and costly, and it is not uncommon for this to take months or even years, especially for larger developments. In our view a tax applied to vacant land without significant improvements to the resource consent and planning processes, may disincentivise property developers from commencing new projects and therefore slow the supply of available new housing.

- It must also be economic for the land owner to bring the land to market. Is it fair to tax land that may be 'vacant' but difficult or unsuitable to develop? Such as cliff-side properties, natural waterways, easements and service access points. Would special provisions be included for land damaged by earthquakes or other natural disasters such as subsidence or soil liquefaction?
- Would the tax be defined by the area of the vacant land or applied at a flat rate?
- If the tax is determined by the rate multiplied by land area, taxpayers in the regions or on the urban boundary where land holdings are typically larger would carry a greater cost of the tax, but there may be less of a desire for housing supply. This needs to be considered against the taxpayer's ability to pay, and the demand for new housing in that region.
- How would the definitions account for hobby farmers or gardeners, or lifestyle blocks?
- How would cross-lease titles be treated?
- CA ANZ believes the definition of 'vacant land' for the purposes of a vacant residential land tax should be set at a national level. Would the tax be perceived as fair, if local authorities could come to their own

definition when at the fringes of each authority taxpayers could be paying different rates of tax for comparable properties?

- Who would assess whether the land was 'vacant'? This would impose a significant enforcement burden on councils and/or local government or would require self-assessment and possibly associated compliance costs for the taxpayer.
- What options could be available to the taxpayer to dispute an assessment when they have an intent to develop the land, or the land is otherwise productive? What would be the administrative process and burden to do so?

Incentivising productive use of land

New Zealanders tend to view land as a safe investment, often with the intention to transfer the land to children or family later in life. Many want the freedom to have a vegetable plot, or to keep animals, or space for their children to play and would not view their property as vacant. Again, including a de minimis threshold would largely avoid the over-application of a vacant land definition.

While this behaviour could be included in what Government seeks to address by proposing a vacant land tax, these behaviours are deeply ingrained in our society. We question whether the introduction of such a tax would be effective in changing these thoughts and behaviours.

The rate of tax needs to be weighed against the cost to the taxpayer (and their desire) for subdividing or developing their land. The costs and time associated with subdivision and development are significant, especially for 'mum and dad' property owners who are not in the business of developing land. If the imposition of the tax is seen as the lesser of the costs, a vacant land tax is not likely to increase supply of land at the detriment of those taxpayers.

Behavioural Change

Revenue collection does not appear to be the primary motivation for implementing a vacant land tax. Rather, such a tax is supposed to act as a behavioural mechanism to incentivise taxpayers to sell, subdivide or develop their property. As we have discussed above, this is not a straightforward mechanism and many factors will determine whether the imposition of a tax is a sufficient incentive for taxpayers to develop their property. To change behaviour and increase land supply, the imposition of a tax would need to be so sufficient to result in sale or development of the land. This degree of taxation would likely be viewed as unfair in situations where taxpayers do not want to sell or develop, do not have the funds to do so, or the income to absorb the tax.

Regarding utilising tax to modify taxpayer behaviour, CA ANZ noted in our submission to the Tax Working Group that other criteria such as; the coherence, fairness, simplicity and efficiency of the tax system, and the rights and fundamental freedoms in the Bill of Rights Act (1990) must also be considered³.

Some behavioural taxes, like those applied to tobacco, are clearly distortionary and are still considered appropriate despite the key taxation pillars, because they achieve their desired outcomes and these outcomes are appropriately measured. This reinforces the need for a clear problem definition to be stated for the introduction of a vacant residential land tax.

A vacant residential land tax also needs to be considered in light of existing tax mechanisms and how these influence taxpayer behaviours and decisions.

Current mechanisms intended to restrict property speculation, such as the brightline test and the '10-year rules', encourage taxpayers to hold onto land, as selling, subdividing or modifying the land within a defined period (subject to limited exclusions), incurs tax⁴.

Inland Revenue's tax policy work programme is also set to review the integrity of these rules, in particular for developers and habitual renovators.

³ Chartered Accountants Australia and New Zealand (2018). Submission to the Tax Working Group on the Future of Taxation. Page 3. A copy of our submission can be found [here](#).

⁴ The Tax Working Group interim report provides a succinct summary of these mechanism. Paragraphs 13 – 18, Chapter 9. <https://taxworkinggroup.govt.nz/resources/future-tax-interim-report-html#section-13>

Without suitable consideration for existing regimes, a vacant residential land tax could leave taxpayers in a situation where they are penalised for selling land, and they are penalised for holding it. This does not create a clear impetus for taxpayers to modify their behaviours to 'free up' vacant residential land for housing supply.

Revenue Collection

The revenue collection capabilities of the tax will be heavily dependent on its design. However, revenue benefits need to be carefully considered alongside the compliance and administration costs of such a tax (particularly if this responsibility is to fall with local government) and the efficacy of the tax.

Imposing a vacant land tax on residential land

It is noted elsewhere in the *Local government funding and financing: Draft report* that the elderly are often disproportionately impacted by changes to rates due to many being on a fixed superannuation income. As we are faced with an aging population the ability of this group to pay the tax is an important factor.

While it would be simpler, and arguably fairer, to impose a vacant residential land tax on an unrealised basis this approach creates issues when the taxpayer does not have the cashflow to pay it. If a vacant residential land tax is also subject to the ability for taxpayers to seek relief or reduction due to their being on a low or fixed income, or deferred until the sale of the property, this will delay or reduce the flow of revenue for local authorities to invest in infrastructure to support housing expansion and development.

Imposing the tax on a realisation basis would largely avoid these issues. However, a realisation basis would significantly diminish the effectiveness of a vacant residential land tax to increase the supply of land as the tax would only become a motivating factor at the time of sale or development. There would be little incentive for taxpayers to sell or develop sooner than they otherwise intended as they could expect to absorb the cost of the tax from any rise in property value. Complexity could also arise using a

realisation basis in situations where the land is 'vacant' for a period of time, then put to a use for a period, then sold.

The efficacy of a vacant residential land tax is inextricably tied to Government's problem definition and the legislative definition as to what constitutes 'vacant land'. These questions must be carefully scoped before further policy consultation can be effectively carried out. We are happy to discuss our submission with the Productivity Commission in more detail and would like to participate in any further consultation regarding the design and implementation of a proposed vacant land tax.

Yours sincerely



John Cuthbertson, CA
NZ Tax Leader, CA ANZ



Greg Haddon, FCA
Chair, CA ANZ Tax Advisory Group

Appendix 1

Chartered Accountants Australia and New Zealand

Chartered Accountants Australia and New Zealand is a professional body comprised of over 120,000 diverse, talented and financially astute members who utilise their skills every day to make a difference for businesses the world over.

Members are known for their professional integrity, principled judgment, financial discipline and a forward-looking approach to business which contributes to the prosperity of our nations.

We focus on the education and lifelong learning of our members and engage in advocacy and thought leadership in areas of public interest that impact the economy and domestic and international markets.

We are a member of the International Federation of Accountants and are connected globally through the 800,000-strong Global Accounting Alliance and Chartered Accountants Worldwide which brings together leading Institutes in Australia, England and Wales, Ireland, New Zealand, Scotland and South Africa to support and promote over 320,000 Chartered Accountants in more than 180 countries.

We also have a strategic alliance with the Association of Chartered Certified Accountants. The alliance represents 788,000 current and next generation accounting professionals across 181 countries and is one of the largest accounting alliances in the world providing the full range of accounting qualifications to students and business.

General Position

In formulating its submissions, Chartered Accountants Australia and New Zealand takes a best practice, public policy perspective. That is, we endeavour to provide comment on a “what is best for New Zealand” basis.

We recognise Government's legitimate right to set tax policy direction. We comment on those policies, and also make comment on their practical implementation. Our public policy perspective means we endeavour to provide comment free from self-interest or sectorial bias.

Research confirms that in practice the best tax system is one with a broad tax base and low tax rates. Such an approach restricts the conditions that make tax avoidance attractive.

Our guiding principles in formulating this submission are that New Zealand's tax system must not impede New Zealand's international competitiveness; growth of the New Zealand economy; and innovation and entrepreneurship.

Recognising there are judgments and trade-offs, taxes should, as far as possible:

- be simple in their application;
- provide certainty in their application;
- be perceived as broadly fair;
- minimise the costs of compliance and administration;
- minimise distortions to the economic behaviour of individuals and businesses;
- utilise businesses' own accounting systems as the data source for calculation;
- align the obligations with the businesses' own cash flows; and
- be imposed at an overall rate which allows adequate retention of investment funds within businesses.

We believe one of the pillars of an effective and efficient tax system is taxpayer certainty. This will increase voluntary compliance, decrease administration costs, and deliver positive economic benefits. Tax legislation

must be as clear in its policy intent and application. Further, any identified errors post-enactment should be corrected without delay.

In Chartered Accountants Australia and New Zealand's view tax legislation should not be retrospective unless it corrects an anomaly to ensure taxpayers pay no more tax than Parliament intended. Retrospective application dates undermine the principle of taxpayer certainty and the Generic Tax Policy Process.