**Appendix 1**

***Chapter 2 – Residential property subject to interest limitation***

- We generally agree with the principles outlined in paragraphs 2.10 to 2.12, that land and buildings that are not suitable for owner-occupier housing should not captured by the new rules. We strongly agree with the proposed exemptions for farmland, business premises, retirement villages and rest homes and employee accommodation.

- In relation to the exempted property types, we note that there may be a period prior to the construction of these types of properties where funds have been borrowed but the land is vacant or is being developed into one of these types of properties. It should be made clear that all interest related to these developments is fully deductible (either under the developer exemption or otherwise).

- In addition to the above, we consider properties that are part of a "build-to-rent" ("BTR") scheme should be entirely excluded from the new rules. BTR has the potential to positively impact the supply of high-quality, stable residential rental accommodation. Whilst BTR would be excluded under the "developer" or "new build" exemptions, if the new build exemption cannot apply in perpetuity across multiple owners of BTR, then it affects the liquidity of BTR projects for initial investors, which in turn negatively impacts on the commercial viability of BTR investments for developers. Excluding BTR schemes from the new rules would enable the schemes to be more comparable for institutional investors to the UK, US and Australian markets where BTR supply of rental housing has grown significantly. We submit that BTR properties should be entirely excluded from the new rules as a BTR property is not one which is generally available for an owner-occupier to acquire.

- In terms of a full exclusion, we note that a BTR property could be a defined term in the tax legislation which would reduce the risk of taxpayers claiming the exclusion on properties not intended to be excluded from the proposals. For example, the Royal Institution of Chartered Surveyors defines BTR in the UK with the following characteristics:

    - Accommodation will typically comprise at least 50 self-contained dwellings.
    - The dwellings will be separately let but held in unified ownership.
    - Management and oversight will be under a single entity.
    - The building(s) may be specifically designed for BTR purposes, and may include shared amenities such as common areas, gym facilities or a swimming pool.

*Chapter 3 – Entities affected by interest limitation*

- We agree with the primary limitation of the new rules to close companies, however we submit that this should also be expanded to also exclude widely held companies and/or listed companies on a major stock exchange.

- Under the proposals, we expect an increased level of compliance costs will be incurred if the FB Group is required to undertake detailed calculations to evidence it is not a 'residential investment property-rich' company.

- We understand the Government and Officials may have a concern that landlords might establish widely held companies that collectively own a portfolio of residential rental properties. This scenario seems unrealistic for all manner of practical reasons (such as individual property owners being able to agree relative property values and ownership percentages). Unless the level of residential property was at such a scale that the company was large enough to have professional management in place (e.g. hundreds, if not thousands of properties) the administrative costs of managing the properties and shareholder relationships would likely exceed any benefits of interest deductions.

- Ultimately there is the general anti-avoidance rule if parties are entering into artificial and contrived arrangements to defeat the rules. The policy design of the rules should not be driven by avoidance concerns as this may result in unworkable policy.

*Does treating new builds and residential property covered by the development exemption as "residential investment property" for purposes of the "residential investment property-rich" threshold cause issues for any developer companies? If so, what are those issues?*

- The requirement to include exempt property in the calculations will materially increase compliance costs for the FB Group with no corresponding benefit, as ultimately the property will be covered by an exemption.

- The formula to calculate the residential investment property percentage is proposed to apply on a tax consolidated group basis. We propose groups of companies should have the option of calculating the test on an accounting group basis including all companies in the NZ group to reduce compliance costs (similar to the test for thin capitalisation).

*Do you prefer to use accounting or tax book values for calculating the residential investment property percentage for assets other than land, improvements and depreciable property? Why?*

  - We submit that accounting values should be an option to minimise compliance costs across all asset categories. There is support for this basis in the Controlled Foreign Company regime, which allows for testing to be done based on audited IFRS accounts.

- In a large group such as the FB Group, a requirement to include a market value for all residential property would create a burdensome requirement to analyse each individual title, as most property is carried based on historical cost in the audited financial accounts.  The proposal to include depreciable property based on the adjusted tax value would also create additional compliance costs. A taxpayer should be allowed the option of using accounting book values.

*Are there other organisations that should not be subject to the interest limitation proposal?*

- As noted above, we submit that widely held companies, or alternatively companies listed on a recognised stock exchange, should be excluded from the application of these proposals.  Close companies and listed companies may differ in a variety of aspects with regards to funding:

    - Listed companies typically have large scale funding facilities used to fund ongoing business activities and the facilities may not be directed towards any particular asset. Whilst closely held companies may see borrowings secured against specific property assets, this may not be the case for larger listed companies. For example, the FB Group borrows certain funds based on a negative pledge arrangement. The negative pledge includes a cross guarantee between several wholly owned subsidiaries and ensures that external senior indebtedness ranks equally in all respects and includes the covenant that security can be given only in very limited circumstances. This means interest on debt cannot be directly traced to a particular asset.
    - Large scale borrowings (i.e. greater than NZ$100 million) may be fixed for an extended period of time (e.g. borrowing under a US Private Placement can allow for 10+ year debt) which would make the proposal to trace interest towards the cost of acquiring residential property difficult, if not impossible, to apply in practice.

***Chapter 6 – Development and related activities***

*Are there other types of developments or activity which should be covered under this exemption?*

- We disagree with the comments made in section 6.11 of the discussion document that "*it is anticipated that almost everyone who develops residential property will hold the property on revenue account under section CB 7 because they are in one of the above businesses*." Many taxpayers developing residential property could be developing the property for their own long-term hold as rental property, and they will not hold the property as revenue account property under CB 7 of the Act. For example, retirement villages will not be held on revenue account.  Although the proposals are to exempt retirement villages once constructed, it should be made clear that all interest related to the development of a retirement village prior to the completion of construction is fully deductible (either under the developer exemption or otherwise).

*Do you agree with the proposed criteria for the development exemption to apply?*

- The FB Group agrees with the proposed criteria for the development exemption to apply. As land developers are assisting in adding to the housing stock of New Zealand, they should be entitled to full interest deductions.

***Chapter 8 – New build exemption from interest limitation***

*Should the new build exemption apply only to early owners, or to both early owners and subsequent purchasers?*

- We submit that the new build exemption should apply to every owner (early and all subsequent owners).

*What application period for the exemption do you think best achieves the objective of incentivising (or not disincentivising) continued investment in new housing?*

- The Group submits that the application period should be for a minimum period of 30 years to align to the expected time taken to pay off a residential investment property based on current market values. In the event our submission to exclude BTR entirely is not accepted, the application period needs to ensure that taxpayers undertaking BTR developments are not disincentivised by the lack of future interest deductions.

***Chapter 14 – Administration***

We submit that the proposals contained in Chapter 14 would materially increase compliance costs for the FB Group with no noticeable benefit being delivered to Inland Revenue, particularly where interest will be fully deductible.

*Are there issues with adding new fields to income tax return forms for total interest incurred in relation to land used for income-earning purposes and the amount of this interest that has been deducted?*

- We submit that this proposal is impractical when applied to a large taxpayer such as the FB Group. Isolation of interest costs in relation to land used for income-earning purposes, particularly if that interest is fully deductible, would increase compliance costs with no perceptible benefit to Inland Revenue.

**From:** s 9(2)(a) [redacted]
**To:** Policy Webmaster
**Subject:** Design of the interest limitation rule and additional bright-line rules
**Date:** Monday, 12 July 2021 10:59:29 AM
**Attachments:** s 9(2)(b)(ii) [redacted]

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Morning

I attach a submission on the discussion document on interest deductibility.

A key focus of my submission is on minimising taxpayer compliance costs.

In the time available I have only focussed on selected areas / issues in the document.

I am happy to make further submissions if that would assist.

Could you please acknowledge receipt of this submission.

Regards

s [redacted]

Kind regards,

s 9(2)(a) [redacted]

173 Spey Street, Invercargill 9810, New Zealand
Private Bag 90106, Invercargill 9840, New Zealand



s 9(2)(a) [redacted]

# Submission on Interest Deductibility

## Introduction

I make the submissions below to provide constructive suggestions as to how the rules could be improved from a compliance cost and administrative perspective. In preparing this submission I have focused on selected areas and issues. I am happy to make supplementary submissions if Officials have questions on the matters raised.

A key concern I have is that this tax law will have to be applied by many people who will not have tax advisors / specialists or who use small accounting firms with no specialist tax expertise. The rules need to be designed and drafted to be able to be applied by non-tax professionals. The main body of rules needs to be expressed simply and consistently with the policy objectives sought. For example, the fact the rules apply to all interest incurred (not just interest on the purchase a property) adds more complexity than is necessary to achieve the policy objectives - the rules on revolving credit are an example.

Having different approaches to defining short and long-term accommodation for income tax and GST does not assist either revenue type. To the extent the rules are trying to define the same matter – the same approaches should be used in both revenue statutes. This will also strengthen compliance. For example, many business people prepare and file GST returns and understand GST at a level needed to comply. People in the business of providing short-term accommodation are more likely to understand the GST rules than rules in the Income Tax Act.

Another option to achieve simplicity is to leave people with only one rental property out of these rules, as was done with the aviation engine overhaul reforms. This may also provide a balance with the argument that supplies of rentals will constrict following the impact of the rules, as is apparently happening in the UK (I didn't research this). It will also simplify application of the rules and work with the exclusion of developers and new builds as if a person only has one rental – and the rules exclude that rental – then you have achieved simplicity and encouraged development – albeit by only one property. Nevertheless, if a person has two or more rentals, the costs of complying with these proposals will be better balanced.

In some areas the proposals are over thought. For example, in the areas of substitution and serviced apartments and the rules for what a new build is and how long it will be a new build. Serviced apartments, for example, are short-stay operations. Below I propose a simple way of resolving the issues in the paper – but the bigger picture point is that if legislation is going to go down every rabbit hole (chasing short-term accommodation that is used as long-term accommodation for example) the rules will contain unnecessary statutory largesse with diminished returns to the key policy objectives. In other words – the approach to design and drafting needs to reflect the policy objectives: there is a diminishing degree of utility (improvement to the policy objectives) with the degree of legislative detail that will be required to make some of these rules work as proposed in the discussion document. Compliance costs for taxpayers must be a key consideration in the design of these rules. This is the case also for Inland Revenue's administration obligations.

## Chapter 1

## Policy objectives

Income tax laws should not be used as a tool for a Government's social policy objectives – rather they should be used to raise the funds to support those objectives. The policy promoted in this document fails at the first hurdle, as did prior Government's policies in trying to use the tax system to discourage certain activities, such as the bright-lines rules themselves, sections 129 (which recovered deductions of property sold within 10 years) and 188A (that limited certain farming losses to $10,000) of the ITA 1976. Taxes on smoking and alcohol are further examples of failures if the objectives were to lower or stop the consumption and use of alcohol and tobacco.

Further, applying the revenue to the consolidated fund for Government spending purposes implies that this policy is not wholly directed at housing, but is partially a revenue raising policy. If Government is serious about its objectives in chapter 1 – the revenue raised (tax savings) should be hypothecated into related Government policy spending. For example, the revenue could be directed to the Government's Housing programmes such as Kianga Ora for example.

Even if one were to take this policy proposal at face value – i.e. everything else aside – it is a band-aid on a wider policy matter. For decades New Zealand salary and wage earners have lived in a low to moderate wage and salary environment. The only safe savings vehicle for many Kiwi's was land and housing. After decades of encouraging people to save through land ownership – the economic implications of changing those settings are unknown and thus the consequential outcomes of these changes may create yet more issues.

For example, the proposals are likely to create inefficiencies as investors shift to other forms of savings, such as commercial property, land banking, foreign land acquisition, and equities in property entities such as Australian property syndicates. A simple example is borrowing to purchase shares in a listed PIE that invests in property – commercial or residential.

The odd outcomes arising from excluding people renting rooms in their home for "flat mates" or "borders" generates inefficiency as tax advisers recommend restructuring family arrangements to generate interest deductibility. This is another good illustration of why social policy should not be delivered through the income tax system.

Any law that provides more work for tax advisors, accountants, and lawyers is always going to be inefficient or give rise to inefficiencies. Taxpayers who can afford to get advice to avoid these rules will benefit – leaving the rules to apply as a tax on those that cannot afford professional advisors: as socially motivated taxes often do.

Administration – In the current environment the necessary complexity of the rules is going to be difficult to administer for Inland Revenue.  While tags in tax returns will be able to alert Inland Revenue to the fact a taxpayer is required to comply with these rules – Inland Revenue is going to have to have some human resource available to check taxpayer positions. Inland Revenue received direct Government funding some years ago to target property subject to Subpart CB – perhaps this approach needs to be revisited to assist with the administration of these rules?

With the introduction of these rules, we will have three key legislative regimes targeting rental expenses – all tripping over themselves. The MUA rental loss ring-fencing rules cross over the general rental loss ring-fencing rules and will again cross over these rules. To an extent, denying interest deductions crosses over both the MUA rules and the rules on rental loss ring fencing: making these all but redundant. To be effective, rules need to be understood. Overwriting the MUA rules and the rental loss ring fencing rules with these rules will create comprehension and misunderstanding. This adds to compliance and administrative issues. Government needs to review the application of its existing suite of property-related rules to ensure they interact appropriately and minimize taxpayer compliance costs.

Finally, I note that if Government wanted to use the tax system to regulate demand for property, the better solution is to subject certain properties to tax – rather than interfere with fundamental tax principles by denying deductibility for expenses that have nexus with income. So, for example, an approach similar to that in paragraph 5.35 could apply. That is, a simple asset classification regime that required taxpayers to declare if a property that is not their main home is on capital or revenue account. People owning property for rental income purposes will likely be on capital account. Capital account treatment will contain rental loss ring-fencing rules and rules for interest deductions but will not tax the property on sale. People owning property principally for income derivation purposes are unlikely to object to rental-loss ring fencing as they will more than likely have positive net rental income. If a person wanted rental expenses and losses deductible (subject to timing rules perhaps), the property needs to be designated as on revenue account and all gains on sale taxable. These rules would be simpler by comparison, largely self-policing and have a better basis in tax policy. The discussion document at paragraph 5.43 sought alternative options and I would advance this proposal in that context.

## Chapter 2

### Property subject to the rules

Foreign land should be excluded from the Bright-line test also as this is outside any influence on domestic housing and further adds confusion when included under one arm of closely-related rules and excluded under the other.

Any premises provided by an employer for employees (other than non-PAYE shareholder employees) should not be subject to interest limitation rules.

Dual-use (business premises and residential) – you will have to expect a certain amount of reconfiguration to business use to avoid these rules, ie shops with residential apartments above could be reconfigured to have some or all of the residential areas converted to office space or other business activity use to ensure they fall within the business premises exception. This type of behaviour is another example of the inefficiencies created by these rules.

I have discussed the exceptions for flat mates and borders above. This is a prime example of why social and tax policy should not be mixed. Excluding boardinghouses also brings risks at the margins as these facilities are not exclusively short-term accommodation in nature.

Carve out for student accommodation as defined in the Residential Tenancies Act is appropriate in this context. However, the risk is that this is broadened and a sub-class of residential rental property outside these rules created. It is not necessary and should not be done.

Substitutibility – There will always be issues at the margin. Trying to cover off all opportunities to substitute short-term for long-term accommodation is a ghost-hunting exercise and risks yet more unnecessary statutory largesse. Further, this is unlikely to result in advancing the policy objectives. The same applies for the proposals as regards serviced apartments. However, to overcome some of these matters – the definition should use the GST boundary. That is, putting the $60,000 turnover threshold for GST aside, if the activity of using an apartment or other accommodation type to generate revenue is such that it should be GST registered it will be short-term. People dressing long-term as short term risk being required to be registered for GST. For example, if I turn my student flat rental into a "boarding house" I will be subject to GST if above the threshold. If I turn my regular apartment into a serviced-apartment, would that give rise to taxable supplies but for the threshold of $60,000? I may find I have a need to GST register. Applying boundaries in such a way as there is a natural tension means that, to an extent, they are self-policing.

## Chapter 4

## Interest allocation

As a general principal a tracing approach, as outlined in the discussion document, is the starting point. However, it has its limits – which lead to the rules that companies use for interest deductibility. These issues are still inherent in the fungibility of money today.

Switching off interest deductions on money borrowed to fund overdraft facilities, or to fund repairs and maintenance is not consistent with the Government policies stated at the outset of the document, viz to "ensure that every New Zealander has a safe, warm, dry, and affordable home to call their own – whether they are renters or owners."

So property owners who borrow to upgrade insulation, double window glazing and related repairs will be required to absorb the cost in full despite the nexus with assessable income. This is counter intuitive. Not only do borrowings to undertake repairs and maintenance not add to the demand for residential property, but denying interest as a deduction adds to the cost of maintenance on domestic rentals. As with the proposal that allows interest deductions on new builds, interest should be allowed as a deduction when an existing property owner borrows to undertake maintenance. For that matter, borrowings to fund all outgoings on a residential rental should be available for the reason that there is no inconsistency with Government policy and it is a legitimate deduction. This may also overcome some of the complexity discussed in tracing interest – for example, when a revolving credit facility is used as discussed at para 4.27.

As an alternative, the rules (IR Policy) for repairs and maintenance in place now are also counter intuitive to Government policy objectives. That is, Government elected to encourage home insulation by subsidising this. However, in many instances this cost for a landlord is a capital outlay, i.e. it is added to the value of the house for which no depreciation relief is available. If Government is serious about encouraging warm homes – rental or otherwise – it needs to put policies in place that work together – not against one another. For example, they could have opted to make a depreciation category available for certain insulation options – and in that way encouraged rental owners to make the outlay. Having this on the asset schedule is also good means of tracking age and when replacement may be due.

The problem identified in paragraph 9 is dealt with now through the accounting system – if it is a business bank account, private drawings will be coded as such and treated as private. Depending on materiality an adjustment may be made for the interest. However, it is acknowledged that small amounts taken as drawings may not be. For example, a business owner purchases some work boots for staff from SafteyProtectorWear – while there the business owner acquires a new pair of dress boots for himself. The store will process the full transaction. The business owner will remove the dress boots from deductible business and GST expenses, but the interest on the overdraft will not be adjusted.

Para 4.14 – I agree with the principle that a new loan takes on the characteristics on a loan it replaces. However, this as a rule can give rise to the problems discussed in *Roberts and Smith*. For example, a trust that owns a farm that has been farmed by mum and dad for 50 years has limited debt. Mum and dad want to retire. To facilitate this the trust borrows $3m from its bank to pay out mum and dad's current account and loans to the trust so they can build a new home away from the farm and have sufficient funds to retire on. Mum and dad also have two rental properties. If the trust borrowings are used by mum and dad to reduce trust debt to mum and dad this is replacing debt with debt. Are the borrowings that are paid to mum and dad to build a new home deductible? However, if mum and dad use these funds to retire debt on the rental properties does this trace back to the trust borrowings? Other examples are not hard to think of. For example, if mum and dad instead had the farm in the company and the borrowings were used to pay mum and dad for shares and as part of the arrangement the payment of a dividend to avoid loss of ICs – is the borrowing to repay the dividend affected by this proposal if used by the shareholders to acquire residential property or retire debt on residential property?

Footnote 17 implies some of the very simple arrangements used by business owners (through trusts, company and partnerships and the like) could be subject to the GAAR. In many instances businesses borrow to acquire assets from associated entities. This could be part of a family restructure to retire the business owners as above, or to exit business owners in a dispute. If these rules are to be a code, they should not need to fall back on the GAAR in all but the most extreme instances. Rather, the legislation should manage these risks: either it is okay (i.e. no GAAR breach) to borrow to purchase business assets (per footnote 17) when the funds are ultimately used for residential purposes or otherwise or it is not. On the other hand, were the legislation not a code but rather a series of rules, then the need to fall back on the GAAR to fill in gaps is understandable. Further, leaving matters for the courts to decide is poor policy. If Officials cannot work these issues through – how do they expect taxpayers to?

The proposal to allow either apportionment or stacking of loans seems a reasonable approach to the complexities of tracing. However, as above, some complexity can be reduced by allowing interest deductibility for borrowings for expenses that give rise to legitimate deductions to be aligned with pre-27 March deductions – although I note my primary submission on this point is that it is deductible in full. As noted, this could be minimised a little by allowing people with one rental to continue to get full deductibility.

## Chapter 5

## Disposal of property

Properties on revenue account should qualify for full deductions. If the BL tests is the test that treats the property as revenue account – then the deduction will be deferred to point of sale as it is now. If the nature of the property is such that it is caught under other time-based rules in the Act – again a deduction could be deferred until disposal. However for people in business and associated people caught under the property sales rules, interest deductions should arise as a matter of course. There can be no basis in tax policy denying deductions against business income.

I comment briefly on the options:

Option A risks driving people outside the tax system. Many people already believe that a gain on property is beyond tax. Denying interest deductions altogether when a property is on revenue account will not assist compliance.

Option B is consistent with revenue account expenditure rules.

Option C is inconsistent with New Zealand's global / gross approach to taxation

Option D consistent with existing rules on rental losses and more acceptable than denying the deduction completely.

Options E & F – If a property is on revenue account, all interest should be deductible as there is no defined basis for trying to split the deduction between rentals and taxable gain. The main issue is the timing of the deduction. In terms of arbitrage concerns, options to deal with this would include deeming an income amount to arise annually (for example, like the FIF rules deemed rate of return approach), or like the FDR approach. A base price adjustment could be undertaken when the property is sold to square up any gain or loss.

## Chapter 6

## Developers

The proposal is to exclude the proposals for interest denial for people who develop property.

Above, I suggested allowing people who have one rental property to be excluded from these proposals. On that basis, if someone undertook a one-off development, such as your example 22, they would be outside these proposals.

In considering who should qualify as a developer the consultation document does not touch on GST. The tests for when someone is taxable on land sales for income tax versus a need to GST register differ. The income tax rules are quite prescriptive in that a person could be assessed under the business income head in s CB 1, the profit-making undertaking or scheme s CB 3, intention or purpose of sale s CB 6, business relating to land s CB 7, land development or subdivision business s CB 10, or under the subdividers rule in s CB 12 or finally under a major development or division s CB 13. The principal rule in the GST context, on the other hand, is whether there is a taxable activity. While the law post *Newman* is clear that a one-off development is not subject to GST, the law is vague as to where the boundary is. For example, if I undertake a development that involves three, is that sufficient to constitute a taxable activity – what if I do two developments now and two in three years time?

In the context of these proposals I would submit that for anyone to be considered a developer, they would have to be GST registered: either because they have sufficient development activity to constitute a taxable activity or they intend to have a sufficient level of activity.

In relation to the points at the end of the chapter I make the following observation:

Dealers and developers are not always mutually exclusive – a person in business as a land dealer may also have some degree of development activity occurring. Bear in mind also people can structure affairs to be a development entity, i.e. a dealer may for a subsidiary company to undertake a land development. Further, if I make losses in initial years as a developer, I can subvent these to my dealing operations?

Bringing in remediation-type work risks the integrity of the rules. For example, instead of renting out my 6-bedroom student flat, I undertake some development to turn it into 3 x 2bedroom flats and I have my interest deductibility back.

In terms of the final two points, these issues illustrate the difficulties with fungibility of money. For commercial developers most business lending from traditional banking sources will be able to be substantiated. However, transactions between associated entities contain few commercial constraints. For example, if I set up a development company along side my rental activities, I can advance funds (for example by selling properties to the development company with a loan back) from the rental company to the development company and transform interest from non-deductible to deductible. Either you need some hard-wired rules to prevent over debt capitalising a development entity – or you take the view that as long as anu interest incurred in a development entity is fully taxable in the related lending entity (i.e. not just soaking up losses) then do you care? However, what is not a good policy outcome is to leave these situations to the GAAR.

## Chapter 7

### Definition of new build

The rules on new builds need to be kept at a manageable level: that is clear to taxpayers and administrable by Inland Revenue.

In this context, for integrity and simplicity, I propose that the definition of a new build is not extended to existing dwellings that have work undertaken on them to increase size or habitability.

## Chapter 8

### New build exemption

As with chapter 7 – rules on the new build need to be simple to comply with and administrable by IRD.

Presumably the new build exemption is to encourage investors to build new housing stock. This being the case, the new build rule should apply only to investment properties built for that purpose: for example, similar to the exclusion from the land sale rules. If the property is sold the new build exemption ceases to apply.

I note that if Government went down an asset classification path – the need for new build exemption could still work in that context, ie owners on capital account would get an interest deduction.

The interest exemption would, presumably, be tied to the funds borrowed to build the property. Extra borrowings presumably won't qualify – although I note borrowings to maintain or repair a property should be deductible for the reasons set out earlier in this submission.

## Chapter 9

### New builds and the bright-line rule

The new build bright-line rule should be limited to land acquired, dwellings built and disposed of within a 5-year period. The land on which the new build sits would have to have a separate title or cross lease arrangement.

However, it is worth noting that this will not stop the general rules in ss CB 6 and CB 12 applying. People who plan to build and sell the property within the 5-year bright-line period could well have a purpose or intention of sale. Thus, if Government were really serious about encouraging new builds it would switch off the rules in ss CB 6 and CB 12 as they relates to new builds.

A point on code of compliance certification. The question of whether a property is a new build is a matter fact. While a ccc is generally indicative of a new build this is not always the case. So the rules could incorporate a ccc in the definition (for example by using an inclusive definition), but should otherwise define a new build by reference to factors normally associated with new builds, e.g. no previous occupation, improvements recently added to rating valuation etc.

## Chapter 10

## Roll-over relief

I support the provision of roll-over relief for situations when land is transferred between closely associated entities. I also support the proposals as they relate the land acquired by trustees when a trust is settled. In family trusts in New Zealand, many trusts have children, and grandchildren and children of grandchildren as beneficiaries. Following the introduction of the Trusts Act 2019 many trust deeds are being reviewed to narrow down the beneficiaries.

On a related matter, I note that it is disappointing that the associated person's rules only seem to apply to tax transactions by associated persons.

It is disappointing that no roll-over relief in the context of the bright-line rules is provided when property is transferred by a trust to a beneficiary who is closely associated with the settlor or a descendant of the settlor, for example. As a matter of law, if a named beneficiary has a beneficial interest in the property, there should be no bright-line application in any event.

I also highlight an interpretation issue with the present laws. If a deceased person has property held in a trust- and on passing (under the memorandum of wishes) this property passes to a beneficiary of the trust, some advisors would say that the rules for property passing on death apply – but all that has happened is that property has passed from a trust established as an inter vivos trust (not a trust arising as a consequence of death). As I submitted above, transfers from trusts to beneficiaries should have roll-over relief when there is a tight association – that is, the disposal should not give rise to a fresh bright-line tax issue.

I note also the comment on s GC 1. In most cases we have struck when Mum and Dad assist their children into a home by acquiring it in their name and subsequently transferring freehold ownership to a child, the relationship is a bare trust relationship – that is Mum and Dad have bare legal title in their names – not full legal and beneficial interests. This gives an outcome consistent with the Government's objectives. Roll-over relief could however be provided for these situations on the same basis as discussed above, i.e. when property is transferred between close associates it should not restart the bright-line period for that property. While this was manageable when the rules were two years, and even with 5 years, the ten year rule is now a barrier to what should be a non-taxable event. Mum and Dad should not have to wait until death to be able to transfer title without bright-line implications.

Joint tenants and tenants in common. Under current law there is some confusion when a joint tenancy situation arises – that is whether there is a disposal or not. If a person disposes of property to a partnership, case law would say you have a disposal. Certainly you have a disposal of property if you dispose of, say, 50% of a property to another person as tenants in common. In practice, tenants in common would prevail, i.e. be the likely basis on which the interests in land are registered, when there is a business relationship – as per your examples 36 and 37. Joint tenants would be more likely the case in a relationship in the nature of marriage, for example.

For the purposes of tax law the issue is wider than just these proposals and the bright-line tests. This matter should be clarified for the purposes of the Income Tax Act as a whole. The rules for partnerships are relevant also in this context, i.e. when disposing of an asset to a partnership a nominal disposition arises. Is Government proposing relief from depreciation recovery as well – per the proposals for partnerships and LTCs? Further, what is a partnership in this context? For example, if Mum and Dad acquire a property as tenants in common – is this a partnership – or do they need to have a partnership deed? The risk in making exceptions for these things in the context of the bright-line and interest deductibility tests is that you end up with different outcomes under other areas of the Act.

## Chapters 12 and 13

I commented above in opening submissions on the interaction of the bright-line rule, the interest deduction rules and the mixed-use asset rules. My key submission point is that with rental loss ring-fencing rules – the mixed use asset rules are all but otiose. The expenditure apportionment rule could stay (and be simplified) – but the rest is not necessary.

The interest limitation rules essentially subsume the rental loss ring-fencing rules. Once the transitional period has expired, the ring fencing rules only have application to repairs and maintenance – and as above – why are we denying deductibility to repairs and maintenance when Government wants to see more spent on rental properties to improve the warmth and functionality of these – policy should work together not against one another.

## Chapter 14

## Administration

These proposals will be very difficult to interrelate with IRD's systems driven approach to tax administration. Complexity is likely to mean compliance is going to be up and down depending on a person's ability to afford advice.

The administration of rules of this nature will require some level of human resource to be applied by Inland Revenue. Auditing through the media and by way of mass email correspondence triggered from boxes ticked in a tax return is unlikely to achieve the right outcomes. In this context I would have thought Inland Revenue as a good case for additional funding to administer the rules effectively – or otherwise risk a shambles.

The proposals in the discussion document are likely to push compliance costs on to taxpayers. While the addition of compliance costs with these rules is inevitable, any additional data collected needs to be data that is requited and used. In this context it is not clear why Inland Revenue need details of all interest incurred? If interest is not deductible why should taxpayers need to calculate this? If this is to monitor and assist, for example, a hypothecation determination by Inland Revenue, this could be understood. Otherwise, why should taxpayers who are being denied a tax deduction still incur the costs of calculating this.

In relation to tax return boxes, Inland Revenue still haven't sorted the issue with foreign income and New Zealand tax credits. It would be good to see some age-old issues tidied up.

## Bright-line rules point

With the BL rule now at 10 years – the case for income carry back exists. The former s 129A of the ITA 1976 did this when expenditure on certain activities was clawed back if sold within 10 years. People who sell a property in, say, year 9, should be able to spread the income back.

**From:** s 9(2)(a) [redacted]
**To:** Policy Webmaster
**Cc:** s9(2)(a) [redacted]
**Subject:** Design of the interest limitation rule and additional bright-line rules
**Date:** Monday, 12 July 2021 11:29:05 AM

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To whom it may concern:

My wife and I work full time jobs s 9(2)(a) [redacted] Since 2015 we have acquired 10 properties with a total of 16 rental incomes, in s 9(2)(a) [redacted] For the most part this has been possible as we have leveraged off our personal home which we bought in 2006.

All our properties are relatively high cashflow properties and our tenants are low income earners. We show compassion where we can to our tenants, letting them exit fixed term tenancies early when they need to, trying to keep rents approx 10% under market, fixing issues quickly, improving the properties as much as we can, among other things.

Whether it is a popular idea or not, we need to treat our investment like a business because our biggest financial responsibility is to the bank, without whom we would not have a business.

For this reason I firmly disagree with the proposed interest deductibility change. Prior to its announcement, property investors entered the market with a certain understanding of how the rules worked with regards to expense deductibility. The banks have financed the investments with the same understanding.

This rule change affects the structure of how tax is calculated and results in scenarios where an investor's tax bill can actually be larger than their cashflow. I find this incredible, and I have two big concerns about it:

1. It will undermine the confidence that banks have in rental property investments, which will limit finance available in this market. This will affect supply where some investors exit the market, which will impact rents.

2. In reality cashflow shortfalls will need to be met by tenants. This will have a devastating effect on rents and on the lives of tenants.

Property investors have made decisions, taken risks and given guarantees to banks to get themselves into a situation where they are bankable and are less likely to be a burden on the state in the future. Some investors talk about keeping rents low, absorbing costs as they increase, doing this for years and ending up with rents significantly under market and tenants who are happy to stay. Effectively, they are sharing their investment with their tenants. While they are free to do what they wish, I strongly disagree with this practice. If it was framed this way to banks who are financing the investments, they would probably not be happy with the idea either.

It is manifestly wrong for the government to expect investors to give the fruits of their efforts and risks to anyone else. I suspect most investors would agree with this, and this is why rents will increase because of this rule change. Who in their right mind would buy a house as an investment so that they can then keep paying their own money for someone to live in it?

If the government is so interested in helping tenants become first home buyers, then why are they working so hard to add significant costs to their living situations, pushing that goal further out of reach? Similarly for tenants who will never own their own home, why is the government so intent on making their lives miserable as well by adding more and more costs to the business of supplying the home to them?

In summary, I believe this rule change should be scrapped entirely so as to actually protect the people it was never really going to help. AT THE VERY LEAST, as self-serving as it might sound, consider limiting its reach to new purchases only, to protect the interests of banks who have financed previous purchases under the old rules, of investors who made their financial decisions under the old rules also, and of tenants who will face significant rent increases if the majority of investors nationwide are hit with a new cost all at the same time.

Regards
s 9(2)(a) .

| | |
|---|---|
| **From:** | s 9(2)(a) |
| **To:** | Policy Webmaster |
| **Subject:** | Design of the interest limitation rule and additional bright- line rules |
| **Date:** | Monday, 12 July 2021 11:30:13 AM |

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To whom it may concern

- I disagree with the proposed interest limitation rules
- Capital account property holders who are caught with the taxable sale should be able to deduct interest for the whole period of ownership in the year of sale
- Date of commencement for new build should be the earliest date possible in the process of developing, and I suggest from date the existing tenant moves out.
- Rollover relief should be included and should be broadened to include LTC elections and all related party transfers, including share transfers. This should also be back dated to 29/3/18

I disagree with the proposed interest limitation rules. It does nothing at all to help with the supply of housing, and does nothing to achieve one of the governments key housing objectives, which is to ensure “affordable home to call their own”. I certainly believe rents will increase over time as more existing rentals are sold to personal house owners.

CAPITAL ACCOUNT PROPERTY HOLDERS
If a long term hold rental property is sold, and is caught by the brightline rules or other taxing provisions, then interest should be fully deductible in the year of sale. The long term hold investor is already paying a very large amount of tax if the sale is taxable, and if interest was not an allowable deduction, tax would then be at a very unreasonable level and would severely unfairly penalize the property owner. If interest was not deductible for a taxable sale, it could see an owner paying more tax then the gain they made which is non sensical.

DATE OF COMMENCEMENT FOR NEW BUILDS
Interest deductions should be allowed from when the tenant moves out from the old property. This should be the first stage in an older rental property becoming a new build. Or the interest should be allowable from when the older property is demolished.

ROLLOVER RELIEF
I do agree that there needs to be rollover relief now that Brightline has been extended to 5 and then 10 years. This should cover all related party transactions, and the following should receive rollover relief
- Becoming an LTC should also be excluded from a brightline sale, as becoming an LTC can simplify ownership for a Company and reduce unnecessary compliance costs.
- Sole trader or partnership to LTC, Trust, Company or LP
- LTC share changes, between related parties, including to Trusts and between individuals

Roll over relief should also be back dated to 29/3/18 as there are a lot of rental property owners who unintentionally have been caught by these very complicated rules

143 pages of discussion document, shows this is way too complicated and will be an unfair burden on taxpayers to comply with the rules. The new rules need to be simple and easy and fair for all!!

Thanks
s 9(2)(a)

**From:** s 9(2)(a) [redacted]
**To:** Policy Webmaster
**Subject:** "Design of the interest limitation rule and additional bright-line rules"
**Date:** Monday, 12 July 2021 11:39:14 AM

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Hi There

I have been a private landlord of various properties since 2016 and worked in the property industry for the last 15 years. I currently own two rental properties s 9(2)(a) [redacted]

I currently do not make any profit off my residential portfolio. They are a passive investment. My tenants currently just cover the expenses and mortgage payments. Any minor profit is usually put towards maintenance or upgrades. The plan is for these to eventually make an income stream for our retirement at which point as they will be making a profit and we fully expect to pay tax.

There has already been significant costs associated with Healthy Homes and Residential Tenancy Act changes put on Landlords. A number of people are still paying off these expenses particularly those investors starting out.  I fail to see how you can make people pay tax when they aren't actually making any profit. The only way through this is to increase rents or sell the property. Neither benefit tenants. I am a good landlord and would only ever rent out a warm place that I'm prepared to live in myself. My tenants are unlikely to ever own their own home and I'm not sure they actually want to. Not everyone wants to own a home some prefer renting. All these changes will do is increase the rental shortage as more investors pull out and make it even harder for renters to find a place as in the end you will always have people needing to rent.

Every other business you can deduct interest expense and it is baffling why residential property business is treated any differently.

My position is that the Government should not progress these changes and should instead consider other mechanisms by which to reduce demand and increase supply in the housing market such as:

- increase interest rates
- encourage higher density building
- restrict the export of building materials. Timber costs are escalating locally due to the timber being export overseas at a higher price. Build costs escalating drive up prices or restrict building.

I do think excluding new builds from these changes is a good decision so that it does not stall supply.

IRD Officials can contact me should they wish to discuss the above comments

Kind Regards

s 9(2)(a)

**PUB-0361**

**From:** s 9(2)(a)
**To:** Policy Webmaster
**Subject:** Design of the interest limitation rule and additional bright-line rules
**Date:** Monday, 12 July 2021 11:54:56 AM

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Name : s 9(2)(a)

Background: Property investor trying to provide for my retirement and my family.

Recommendations :

- I disagree with the entire legislative change and think that it undermines the entire NZ tax system, which allows business expenses to be claimed against business income. It singles out a single asset class and complicates what was a relatively robust tax system. I think that the proposal should be scrapped in its entirety.

- Chapter 5 – a deduction should be allowed at the time of sale if the sale is taxable, as all the income from investing in the property is taxed. I think that the entire interest paid should be able to be claimed as a deduction, even if this results in a loss. This loss should be carried forward in the entity that incurs it. Again, this aligns with the rest of the NZ tax system.

- Chapter 6 – Development exemption. Major renovations to a property (remedial work), which includes adding a bedroom to the property, should be covered under this exemption. A bedroom is adding to the housing supply in the market and the renovation is extending the life of the property. To make this easier to define what the renovation involves, investors could provide evidence to accountants or IRD of updating the property file with council, to prove the extra bedroom has indeed been added. This would then qualify this property for the
'complex new build' category. And allow continued interest deductibility for this property.

- Chapter 7 – the adding of another bedroom, which is increasing the capacity of existing housing stock, and hence adding the housing supply (like splitting an existing dwelling into multiple dwellings but keeping the same overall number of bedrooms) should be classified as a complex new build.

- Chapter 8 – the new build exception should apply to both early owners and subsequent owners for a fixed period of 20 years from the date the new builds CCC is issued. If this does not occur the market will be impacted with near new properties significantly dropping in value relative to the new properties.

- Chapter 9 – new fields should not be added to income tax forms – this will further complicate an already complicated process, and further increase compliance cost for residential property investors. Tax law in NZ is complicated enough for the average investor, this adds further complexity to the system.

Further detail and history:

Impact- the impact this proposed change has on me personally is both mental and financial. Financially it reduces my ability to provide rental properties for future tenants, hence reducing rental property availability and as with any supply and demand equation, this will increase rents for residential property in NZ. As most of my tenants are first home buyers saving for their first home, this legislation will make it harder for them to buy a home as they will be paying more in rent. They will have to rent for longer to save their deposit. This seems to go against the intention of the proposed legislation "to tilt the playing field away from property investors and towards first home buyers".

Financially, not allowing the complex build exception for adding extra bedrooms (which cost to do), disincentives me from doing this type of renovation, thus I do not provide more housing supply for to the market. Adding bedrooms, for example my normal renovation takes a 2-bedroom property and makes it a 3-bedroom property, opens this property up to families and larger flatting groups, when a 2-bedroom property would not have sufficed. This renovation allows more people to occupy existing space and hence increases housing supply. As cities in NZ grow into world class cities, residents are happy to live in smaller dwellings, to be closer to their work or leisure activities.

Mentally the proposed legislation adds confusion and complicates the tax system in NZ, from one that was world class to one that is complicated and difficult to navigate and singles out specific asset classes. This makes me worry about what changes may be next if the government is willing to undermine the entire tax system. It makes me worry about investing in NZ further. NZ does need private investors in the residential property market, and this legislation scares me away from investing further. This will further reduce supply of housing, which will increase both rents and property prices, which is in opposition to the objective of this proposed legislation.

I am happy to be contacted to discuss this further. s 9(2)(a)

Kind Regards, s 9(2)(a)

| | |
|---|---|
| **From:** | s 9(2)(a) [redacted] |
| **To:** | Policy Webmaster |
| **Cc:** | s9(2)(a) [redacted] |
| **Subject:** | Re: Design of the interest limitation rule and additional bright-line rules |
| **Date:** | Monday, 12 July 2021 12:10:45 PM |
| **Attachments:** | image.png<br>image.png |

To whom it may concern:

This is my second email/submission regarding the interest deductibility changes. The first is copied below FYI. I wanted to demonstrate the analysis of a rental purchase, to highlight the impact of this rule change.

Under the old rules a rental property purchase might have looked like this. These are real numbers from a purchase we made in s 9(2)(a) [redacted]

s 9(2)(a) [redacted]

The gross return is 9.8%, which is very high. The rents (4 units) were approx $30pw under market at the time of purchase. The property needs a lot of work on the outside, but is ok on the inside. I have added heatpumps and ventilation for Healthy Homes. I have financed this property on interest only lending initially, so my cashflow is quite a bit higher for now.

Now I will do the same numbers, were I to look at buying this property now:

s 9(2)(a)

[redacted]

Note how the tax has almost doubled, and the cashflow on P&I has gone negative. Where previously the rent provided a surplus that could fund improvements to the property (or could pay the interest on funds borrowed for improvements) a purchaser would be looking to the tenants for additional cashflow just to stay afloat, let alone to fund any maintenance or improvements.

The way the government has taken a property with a tremendous 9.8% return and cashflow of over $5,600 and turned it into a loss-making venture is incredible. They are wanting to collect $6,494 extra in tax while ignoring the reality of where that money comes from.

At under $200,000 per unit I don't think you could argue that I paid too much for these. This property is not a "first home buyer" property. Changes affecting the financial viability of investments like these as demonstrated above will not serve tenants well, as their rent costs will have to go up.

I hope this makes sense. Again, please consider either scrapping this rule change or limiting its scope to properties purchased after its announcement only.

Regards
s 9(2)(a) [redacted]

On Mon, Jul 12, 2021 at 11:28 AM s 9(2)(a) [redacted] wrote:

> To whom it may concern:
>
> My wife and I work full time jobs s 9(2)(a) [redacted] Since 2015 we have acquired 10 properties with a total of 16 rental incomes, in s 9(2)(a) [redacted] For the most part this has been possible as we have leveraged off our personal home which we bought in 2006.
>
> All our properties are relatively high cashflow properties and our tenants are low income earners. We show compassion where we can to our tenants, letting them exit fixed term tenancies early when they need to, trying to keep rents approx 10% under market, fixing issues quickly, improving the properties as much as we can, among other things.
>
> Whether it is a popular idea or not, we need to treat our investment like a business because our biggest financial responsibility is to the bank, without whom we would not have a business.
>
> For this reason I firmly disagree with the proposed interest deductibility change. Prior to its announcement, property investors entered the market with a certain understanding of how the rules worked with regards to expense deductibility. The banks have financed the investments with the same understanding.
>
> This rule change affects the structure of how tax is calculated and results in scenarios where an investor's tax bill can actually be larger than their cashflow. I find this incredible, and I have two big concerns about it:
>
> 1. It will undermine the confidence that banks have in rental property investments, which will limit finance available in this market. This will affect supply where some investors exit the market, which will impact rents.
>
> 2. In reality cashflow shortfalls will need to be met by tenants. This will have a devastating effect on rents and on the lives of tenants.
>
> Property investors have made decisions, taken risks and given guarantees to banks to get themselves into a situation where they are bankable and are less likely to be a burden on the state in the future. Some investors talk about keeping rents low, absorbing costs as they increase, doing this for years and ending up with rents significantly under market and tenants who are happy to stay. Effectively, they are sharing their investment with their tenants. While they are free to do what they wish, I strongly disagree with this practice. If it was framed this way to banks who are financing the investments, they would probably not be happy with the idea either.
>
> It is manifestly wrong for the government to expect investors to give the fruits of their efforts and risks to anyone else. I suspect most investors would agree with this, and this is why rents will increase because of this rule change. Who in their right mind would buy a house as an investment so that they can then keep paying their own money for someone to live in it?

If the government is so interested in helping tenants become first home buyers, then why are they working so hard to add significant costs to their living situations, pushing that goal further out of reach? Similarly for tenants who will never own their own home, why is the government so intent on making their lives miserable as well by adding more and more costs to the business of supplying the home to them?

In summary, I believe this rule change should be scrapped entirely so as to actually protect the people it was never really going to help. AT THE VERY LEAST, as self-serving as it might sound, consider limiting its reach to new purchases only, to protect the interests of banks who have financed previous purchases under the old rules, of investors who made their financial decisions under the old rules also, and of tenants who will face significant rent increases if the majority of investors nationwide are hit with a new cost all at the same time.

Regards
s 9(2)(a)

**From:** s 9(2)(a) [redacted]
**To:** Policy Webmaster
**Subject:** Design of the interest limitation rule and additional brightline rules
**Date:** Monday, 12 July 2021 12:15:09 PM

To whom it may concern,

I have been investing in NZ residential real estate since 1999, and in s 9(2)(a) [redacted] My opinions below are based on my experience as s 9(2)(a) [redacted]

I believe that the interest limitation rule and additional brightline rules should be scrapped in their entirety as it is highly unlikely to achieve what the government intends for it to achieve, and could instead cause dire unintended consequences.

The government has stated on numerous occasions that they want to reduce property speculation, and make it easier for first home buyers to enter the property market. Here are my thoughts about why I believe that the interest limitation rule and the additional brightline rules will actually increase speculation, rather than reduce it, and make it harder for first home buyers and tenants to get ahead financially:

- Under the original brightline rules (2 years, then extended to 5 years), if someone was in the business of trading/speculating/flipping property (i.e. buying with the intention of selling for a capital gain), then any property that was purchased for long term buy and hold was "tainted" which meant that effectively the brightline on their buy and hold properties was extended to 10 years. This was a significant deterrent for many of our clients, who as a result, chose not to trade in property, but instead to invest in long term rental properties. With the extension of the brightline rules to 10 years, this effectively removes that deterrent, and we have had many of our experienced buy & hold investors who have recently expressed an interest in incorporating a trading/speculating/flipping strategy.
- The government has actively encouraged investors to purchase new build properties by leaving the brightline on these properties at 5 years, and by announcing that the interest portion of the mortgages on those new build properties will be tax deductible (although further details are yet to be clarified). This has increased demand for new builds, at a time when demand for new builds was already enhanced by the exemption from the RBNZ rules for minimum deposits (new builds have a lower required deposit). This increased demand in a period where there is limited supply has increased prices in the new build market, decreasing rental returns, and further increasing the number of previously purely buy & hold investors who are now interested in trading property in order to make a profit to pay down the mortgage on their long term rental properties in order to improve the after tax cash flow.
- Increased prices in the new build market tend to have a flow on effect of increasing prices in the existing property market, thereby increasing the difficulty for first home buyers to enter the market, which would be an unintended consequence of these tax changes.
- The interest limitation rule has increased financial pressure on many Mum & Dad investors, who now feel that in addition to the increased costs they have faced with regards to Healthy Homes Specifications, and increased risk as landlords if they find themselves with a problematic tenant (as they can no longer give 90 notice without cause in order to evict such tenant), they simply can't afford to keep their rental property. According to an MBIE report in February 2021, approximately 78% of investors own one rental, which suggests that by far the majority of property investors in this country are Mum & Dad investors. We know from our weekly training sessions with the public, that most people are interested in property investing in order to improve their financial position for retirement (so they are less reliant on government support). We also know that the majority of these Mum & Dad investors are average income earners (e.g. teachers, nurses, police etc). By making it more expensive to provide rental accommodation, it increases the chance that there will be fewer of these Mum & Dad investors who will be able to afford to invest in property. Fewer private investors means fewer rental properties available in the rental market, and as (according to the NZ Property Investor Federation's submission to the government in March 2020) 87% of tenants rent from a private landlord or trust, that could be a significant problem for the government since over 30% of NZ's population live in rented accommodation. This increased imbalance between supply and demand is likely to result in further surges of market rent, making it more unaffordable for tenants, and harder for tenants to save a house deposit.
- If the government continues down this path, it is unlikely to reduce people's desire to improve their financial position, but it is instead likely to mean that the only people who will be able to afford to purchase investment properties and provide private rental accommodation will be people on high incomes. I find it hard to believe that this government truly wants to see the rich get richer and the poor get poorer.

Warm Regards,
Debbie

s 9(2)(a) [redacted]

s 9(2)(a)

[redacted]

PUB-0364

**From:** s 9(2)(a) [redacted]
**To:** Policy Webmaster
**Subject:** Submission on the Changes to interest deductibility on residential property income
**Date:** Monday, 12 July 2021 12:32:15 PM

Dear Submission Recipient,

Background
My name is s 9(2)(a) [redacted]

Still keenly interested in tax law after practicing the administration of it for a long time, I would like to make a submission on the new proposed Changes to Interest Deductibility on Residential Property Income.

I do not own a domestic rental property.

Submission
I recall the current Minister of Finance making a statement earlier in the year when this change was proposed………….. "because Mum & Dad homeowners cannot deduct their mortgage interest against their income, then it is not fair that a domestic home investor should be able to deduct interest".

To me, this statement is simply not theoretically or factually correct. There is a clear distinction between a domestic homeowner with a mortgage and a domestic home investor with a mortgage. The domestic homeowner has no rental income to deduct any mortgage interest against. This is a purely domestic situation. The domestic home investor however, is receiving rental income. Hence, one situation is completely domestic in nature, whilst the other should be seen as a 'business'. Therefore, as has been the case throughout my career, the interest incurred on a mortgage secured over a domestic rental property and used as a domestic rental property should be able to be deduct the mortgage interest as an expense against the rents received from the property's tenant.

Interest is tax-deductible from all types of business income. Investing in a domestic rental home is no different than investing in a business. There is an income stream from which the expenses incurred in the earning of that income are deductible against that income.

Factually, we have loss-limitation in place now; the ring-fencing of rental losses which prohibits a loss being deducted against the rental income in the year in which the loss is incurred.

Conclusion
I'm sure that many many individuals and organisations will have written a submission about this matter and proposal.

My submission strongly supports the status quo. There should be *no* change to the current interest deductibility on residential property income.

Thank you for taking the time to read this.

Kind regards,

s 9(2)(a)

**From:** s 9(2)(a)
**To:** Policy Webmaster
**Subject:** [SUSPECT SPAM]Design of the interest limitation rule and additional bright-line rules
**Date:** Monday, 12 July 2021 12:32:47 PM

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Why is a new build defined as having code of compliance issued after March 21? 5 years ago we purchased a new build property. We have been the sole owners of the rental property over that time. Under the proposal we would meet the definition of being an early owner, but not the exemption criteria as our code of compliance was pre March 21. What makes our new build purchase any less valuable to the country tham a new build that has a code of compliance post march this year? Purchases such as our should also be included in the exemption criteria for however long the agreed period is.

**From:** s 9(2)(a) [redacted]
**To:** Policy Webmaster
**Subject:** Design of the interest limitation rule and additional bright-line rules
**Date:** Monday, 12 July 2021 12:43:32 PM
**Attachments:** Submission on Chapter 8 New build exemption from interest limitation .pdf

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Hi

Please see the submission attached.

Thank you.

Best Regards, Stay Safe and Well.

s 9(2)(a) [redacted]

新投投资集团（新西兰）有限公司
Luxury Infinity Investment Group Limited

s 9(2)(a) [redacted]

**Submission on**
**Chapter 8 New build exemption from interest limitation**
**Of**
**Design of the interest limitation rule and additional bright-line rules**

Hon David Parker
Minister of Revenue

We, As group of company listed blow, we would like to make a submission on Chapter 8,

**Clause 8.8** of the discussion document regarding Transitional rule .

We believe the Transitional rule is necessary. However, should not limited to "acquired on or after 27 March 2021" . The reason been:

1. This will create a unique unfair situation where certain new builds that received their CCCs before 27 March 2021 and after 27 March 2020, may not be able to be exempted by the new build.

   *A example attach: Person A enter a off plan sale contact with Developer for Apartment 210 of "City Living" Apartment on 1st of Jan 2021, The CCC was issued for "City Living" Apartment on 1st of March 2021, Person A under current discussion rules will not be able to get Apartment 210 of "City Living" Apartment exempted by the new build. However, Person B enter a sale contact with Developer for Apartment 310 of same"City Living" Apartment on 1st of May 2021, The CCC also issued same time as apartment 210 at 1st of March 2021. Under current discussion rules, Person B will be able to get Apartment 310 of "City Living" Apartment exempted by the new build.*

2. It is particular unfair to large Apartment project off-plan buyer who been punished for buying early than buyer in the same building who bought after 27 March 2021 who can get exempted by the new build.

3. The New Build exception rule should only deemed by the age of the building. The currently exemption will create situation that newer building could be excluded from New Build Exception, and older building might be included.

We would suggest Transitional rule apply to any building that received CCC within 12 months before 27 March 2021. Early owners, should be any person acquired excepted new builds before or within a year of issue CCC for that building. The New Build exception period should start at issue of Building CCC.

The End of Submission.

List of company support of the Submission:

Lead by:
LUXURY INFINITY INVESTMENT GROUP LIMITED (4692482)

KINGSMAN DEVELOPMENT LIMITED (5669727)
KINGSMAN DEVELOPMENT NO.2 LIMITED (7180674)
GREENVIEW HOMES LIMITED (4386457)
SPRING CONSTRUCTION LIMITED (8179450)
J Y K LIMITED (1904165)
JYK TRADING LIMITED (3639991)
KING OAK PROPERTY HOLDING LIMITED (5981647)
KINGSLAND ALBANY LIMITED (8183947)

**From:** s 9(2)(a) [redacted]
**To:** Policy Webmaster
**Subject:** Design of the interest limitation rule and additional bright- line rules
**Date:** Monday, 12 July 2021 12:46:23 PM

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To whom it may concern,

My name s 9(2)(a) [redacted] and I am a property investor who would like to make a submission and to express that I am not in favour of the proposed interest limitation rules.

I will be adversely affected by the new rules and what I find most unfair is that the rules have changed post my property purchase. When I purchased my property investment in 2020, I took into consideration all the known factors including tax rules at the time. To change the rules drastically post a recent purchase, puts in place a large burden.

The property I own does not fall into the “First home buyer” property pool, no first home buyer is likely to want to buy my property which caters for student accommodation and the price would be out of reach. Student renters needs somewhere to rent and the surrounding area of properties that house students, in my opinion would be undesirable for a first homebuyer or family environment.

When I purchased the investment property, I was pleased to be able to provide accommodation to students. However with the removal of the interest deductions this will greatly impact my financial situation.

If the new interest rated deductibility rules come into effect, I would like to see that the start date be moved to 28th of march, 2021, when purchases going forward knew what to expect.

I disagree with the proposed interest limitation rules.

- Capital account property investors who pay for a taxable sale should be able to deduct interest for the whole period of ownership in the year of sale.

- Date of commencement for a new build should be the earliest date possible for the process of developing and suggest from date the existing tenant moves out.

- Rollover relief should be included and should be broadened to include LTC elections and all related party transfers, including share transfers. This should also be back dated to 29/3/18

OVERALL – I disagree with the proposed interest limitation rules. It doesn't help with the supply of housing and does nothing to achieve one of the governments key housing objectives, which is to ensure "affordable home to call their own". I believe however that rents will increase over time as more existing rentals are sold onto personal house owners.

CAPITAL ACCOUNT PROPERTY HOLDERS – If a long term hold rental property is sold and falls under the Brightline rules or other taxing provisions, then interest should be fully deductible in the year of sale. The long term hold investor is already paying a large amount of tax if the sale is taxable, and if interest was not an allowable deduction, tax would then be at an unreasonable level and would severely penalise the property investor. If interest was not deductible for a taxable sale, it could see an investor paying more tax than the gain they make.

DATE OF COMMENCEMENT FOR NEW BUILDS– Interest deductions should be allowed from when the tenant moves out from the old property. This should be the first stage in an older rental property becoming a new build. Or the interest should be allowable from when the older property is demolished.

ROLLOVER RELIEF I agree that there needs to be rollover relief now that Brightline has been extended to 5 and then 10 years. This should cover all related party transactions and the following should receive rollover relief:
- Becoming an LTC should also be excluded from a Brightline sale, as becoming an LTC can simplify ownership for a Company and reduce unnecessary compliance costs.
- Sole trader or partnership to LTC, Trust, Company or LP
- LTC share changes, between related parties, including to

Trusts and between individuals
Roll over relief should also be back dated to 29/3/18 as there are a lot of rental property owners who unintentionally have been penalised by these rules.

MAKE IT SIMPLE – 143 page of discussion document, shows that these rules are already too complicated and will be an unfair burden on taxpayers to comply with the rules. The new rules need to be simple and easy for all to follow.

Yours sincerely

s 9(2)(a)

[redacted]

| | |
|---|---|
| **From:** | s 9(2)(a) [redacted] |
| **To:** | Policy Webmaster |
| **Subject:** | BusinessNZ submission on the design of the interest limitation rule and additional bright-line rules |
| **Date:** | Monday, 12 July 2021 12:48:27 PM |
| **Attachments:** | 210712 BusinessNZ Submission on the Design of the Interest Limitation Rule.doc |

Dear Sir/Madam

Please find attached BusinessNZ's submission on the *Design of the Interest Limitation Rule and Additional Bright-Line Rules* Discussion Document.

Kind regards
Steve

s 9(2)(a) [redacted] www.businessnz.org.nz

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13 July 2021

Design of the interest limitation rule and additional bright-line tests
C/-Deputy Commissioner, Policy and Regulatory Stewardship
Inland Revenue Department
PO Box 2198
Wellington 6140

Dear Sir/Madam

**Re: Design of the Interest Limitation Rule and Additional Bright-Line Tests**

I am writing to you regarding the issues paper, *'Design of the interest limitation rule and additional bright-line tests'* (referred to as "the Discussion Document"). While the Discussion Document canvasses a wide variety of related issues, BusinessNZ wishes to offer our broad thoughts on the proposed rules relating to interest deductibility and to comment on a few specific matters also of interest to this organisation.

Background
It would be fair to say the Government's announcement on 23 March 2021 regarding limiting the deductibility of interest on residential investment property, as part of its housing policy package, was a surprise to taxpayers, including the business community.

Deductibility of interest payments for business expenditure is a long-held principle of the New Zealand tax system. It is standard and accepted practice across the countries New Zealand typically compares itself to.

Consequently, any moves away from this accepted norm will automatically create a range of problems that will have to be addressed before any such limitation is implemented.

Supply, not demand
Overall, we agree that New Zealand has a long-standing housing affordability problem. Such problems can have far reaching consequences for many sectors of society. As an example, from a business perspective, being unable to buy a home,

combined with increasing rents, can have a significant impact on many businesses' ability to recruit/retain staff.

Therefore, we welcome the Government's examination of the regulatory tools and levers that can be used to address the housing affordability problem. However, what was announced in March principally involves measures to try to blunt demand rather than an attempt to deal seriously with supply-side issues.

Although, on balance, some of the Discussion Document's proposals are likely to be helpful, including those relating to greater investment, there is a significant difficulty over the lack of clarity when it comes to limits on interest deductibility. Any changes should be undertaken with a considerable degree of caution given their potential to increase the tax system's complexity while at the same time, failing to address the fundamental problem they are intended to solve.

Signal to investors

The legislation moves New Zealand away from standard tax policy practice, raising BusinessNZ's concerns about the signal being sent both to domestic and overseas investors. New Zealand's broad-based low-rate tax system has for many years been seen as predictable, something which in many quarters is viewed as an asset to the country's economic prosperity, particularly when it comes to future investment. Limiting interest deducibility challenges these views.

On balance, domestic investors typically have a good day-to-day understanding of the current state of the country, including its likely political path and economic shifts. However, the current Government's swift and unexpected change in policy means domestic investors are now likely to factor in other potential and/or unexpected adverse changes to investment rules in deciding whether to invest. Such a change in approach typically leads to a chilling of investment decisions.

Such chilling of investor behaviour will often be exacerbated for overseas investors, who do not have intimate knowledge of either New Zealand's political, or its economic, circumstances.

In previous tax submissions, BusinessNZ has highlighted the fact that the company tax rate is often seen as a headline global indicator when competing for overseas investors. In a similar vein, that New Zealand will now be an outlier in limiting the deductibility of interest payments for certain business expenditure does not send overseas investors the right initial signal. Instead, it raises the risk profile of New Zealand as a place to do business.

Therefore, BusinessNZ does not support limiting the deductibility of interest on residential investment property.

*Primary recommendation: That the Government does not proceed with its proposal to limit the deductibility of interest on residential investment property.*

Notwithstanding our primary view and recommendation above, BusinessNZ is concerned to ensure that if interest deductibility rules are to change, what replaces them should be as workable as possible.

Complexity of the topic

The Government's initial announcement came on 23 March 2021 with a period of just over six months to the proposed implementation date of 1 October 2021. For such a significant change to New Zealand's tax landscape, we believe that period to be woefully inadequate if the numerous and complex problems arising from the change are to be properly worked through by both the public and private sectors.

BusinessNZ notes that since the announcement, the Government has sought advice from private sector tax experts on several issues relating to the design of the interest limitation rules. While such steps are supported, the fact that the Discussion Document is 143 pages in length illustrates how complex the new rules remain. Other submitters will provide an in-depth view on a range of topics discussed in the Discussion Document but from BusinessNZ's perspective, getting to a point where a set of clear and concise set of rules can be put in place still seems a long way off.

Ongoing remedial work

In relation to the point above, one of our biggest concerns with such a short time-frame for consultation is that once the legislation applies, there will likely be significant and ongoing remedial work to be undertaken to address uncertainties and/or rules that seem in conflict both within the new legislation and with other tax legislation.

In turn, considerable Inland Revenue resources will likely be needed to work through such issues, as well as further consultative work undertaken that experts and private sector representatives will have to assist with/submit on. There will also be a cost for the many investors who will have to seek professional tax advice if they are unsure of certain aspects of the rules and this, over time, will represent a sizeable deadweight loss to the economy. Also, there will be opportunity costs associated with tax policy development that could otherwise have addressed different tax policy issues.

At the very least, we believe pushing out the consultation and implementation date for at least another six months would improve the chance of minimising ongoing remedial work.

***Recommendation: That the Government delays the implementation date of the changes so that the various details of the scheme can be properly worked through as part of the standard consultation process.***

Specific Comments
In addition to the broad comments above, BusinessNZ would also like to address three specific issues raised in the Discussion Document:

Business premises and dual-purpose buildings on the same title
Paragraphs 2.64-2.69 of the Discussion Document ask submitters whether an apportionment calculation allowing for interest deductions in relation to the business premises of a dual-purpose building may be preferable over an all-or-nothing approach. BusinessNZ agrees that a more nuanced apportionment approach is indeed preferable.

***Recommendation: That an apportionment calculation allowing for interest deductions in relation to the business premises of a dual-purpose building is preferred to an all-or-nothing approach.***

Employee accommodation
While we understand other submitters will provide detailed views on how employee accommodation is best handled within the structure of the interest limitation rules, overall, BusinessNZ agrees with the views expressed in paragraphs 2.70-2.74 of the Discussion Document that there should be some form of carveout for all employee accommodation.

***Recommendation: That within the context of interest limitation rules, some form of carveout for all employee accommodation should proceed.***

Exclusion for non-close companies
As outlined in paragraphs 3.1-3.9 of the Discussion Document, BusinessNZ supports the exclusion of certain non-close companies. There will be many companies that hold small amounts of residential investment property but are unlikely to contribute significantly to high house prices.

Paragraph 3.7 outlines a formula to ascertain whether a company would be classified as 'residential investment property-rich', namely comparing a company's residential investment property with its total assets. Any company that crossed the 50 percent threshold would be caught within the interest limitation deduction rules. However, we believe the formula is impractical because it will often be difficult to distinguish assets in the form of residential property from other business assets. Therefore, it is likely the formula will be taken to cover companies that would otherwise be excluded from its reach.

Instead, we would support the more practical options which other submitters will likely provide.

*Recommendation: That a more practical rule to establish whether a non-close company is 'residential investment property rich' is introduced.*

Thank you for your time, and we look forward to further developments.

Kind regards,

s 9(2)(a)

[redacted]

| | |
|---|---|
| **From:** | s 9(2)(a) [redacted] |
| **To:** | Policy Webmaster |
| **Subject:** | Design of the interest limitation rule and additional bright-line rules |
| **Date:** | Monday, 12 July 2021 1:00:21 PM |
| **Attachments:** | REAL iQ - The Government Housing Policy 2021.pdf |

In our submission, we would also like to include a survey we did of the Residential Property Management industry with regards to what the industry felt about the proposed changes in regards to the Bright-line test as well as the interest deductibility rule.

Firstly about me s 9(2)(a) [redacted]

I have worked in the Property Management industry for 16 years, s 9(2)(a) [redacted] also work with a number of social and community housing providers as well.

I have become very passionate about the industry and about what I believe needs to be done in regards to help improve renting in New Zealand. Tenants need to have protection but also landlords need to be able to make a return.

Much of what this Government has done in recent times I am supportive of. Tenants do deserve great protection under the Residential Tenancies Act and improvements have to be made to the rental stock of New Zealand.

The main focus of my submission is with regard to the rule around interest deductibility.

Firstly, I believe the proposal to tax income rather than profit is the wrong thing to do. It will likely lead to more aggressive rent increases and owners will be less inclined to spend on maintenance right at a time when we are needing them to invest more. It will also have a detrimental effect on the Property Management industry with more landlords choosing to self-manage which will lead to a reduction in the level of service that tenants will receive as many landlords fail to understand their responsibilities under the Residential Tenancies Act due to a lack of knowledge as well as time constraints.

However, I am realistic enough to realise that the chances of a Government changing its mind are pretty much close to zero.

The aim of the Government is to have safe, warm, dry and affordable homes that people can call their own regardless of whether they rent or own. Many families will be forced to rent for life so we have to reinvent renting.

With that in mind, we have to think differently in a way that we can develop a renting system that can support long term investors as well as giving tenants greater security. I have covered off my thoughts within this article that I have written on my website.

https://realiq.nz/reinventing-renting-the-need-for-long-term-tenancies/

**Landlords who offer long fixed-term tenancies to be exempt from interest rule.**

In Germany, the average length of a tenancy is 11 years and nearly 50% of the population are tenants. In New Zealand, the average length of a tenancy is extending but it is still roughly less than 2 and half years with one-third of the population renting. If the Government's aim is to have stability and security for tenants, then we have to think differently.

Our idea is to incentivize landlords to offer long term contracts to tenants whilst giving tenants the flexibility to give notice when their circumstances change, and they decide it is time to leave. If a landlord provides a tenant with, for example, a fixed-term tenancy for 10 years then they can be exempt from the interest deductibility rule. This is a choice that a landlord can take and by doing so they are showing that they are in fact long term investors and not speculators. If they have to sell the property then the purchaser is buying the tenancy so the tenant has security.

Tenants will have a place that they can call home and establish roots in communities whilst their children will remain in the same schools with the same friends. This benefits New Zealand as a whole. The agreements will be written in a way that allows a tenant to give notice meaning that they do not have to pay break lease fees when they decide to leave.

Tenants are now already able to make minor changes to the property and with healthy homes standards being implemented, technically, there should be no issues with regards to tenants living in unhealthy conditions. These agreements will allow tenants to have pets and landlords will not be penalized with regards to interest deductibility meaning that there will be less pressure with regards to increasing rents and no need for cutting costs on maintenance.

Bonds can be replaced with tenants paying specialised tenant insurance which can protect them from accidental damage or temporarily support them if they find themselves in financial hardship due to losing their job or income. There will be no need to undertake intrusive three-monthly inspections which, in my opinion, are invasive and unnecessary, particularly if you have long term tenants who have a great record.

The purpose of this is to ensure that landlords are motivated to provide long term rental accommodation that fits the needs of both tenants and investors. The tenants can establish roots and, if their circumstances change, they have flexibility.

**Exclude purpose-built rental accommodation from interest limitation rule**

The current laws around interest deductibility are simply unfair as it particularly penalizes landlords who own multi-unit dwellings or student accommodation. These types of properties are not going to sell to first home buyers and essentially if you own these you are stuck with them as whoever purchases them will have to allocate roughly 30% of the rental income to tax from day one. Investors who own such properties should be exempt from the interest rule

**Allow interest deductibility on renovations**

The Government's policy hurts tenants in other ways. Landlords will simply have no incentive to do extensive renovations on their properties since any extension on their mortgages that they establish will automatically not be allowed to be offset against rental income. Therefore, more and more rental property will simply be let go and will not be maintained. This makes no sense at all when there is a huge push to get landlords to improve the quality of their stock.

I thank you for taking time to read my submission.

s 9(2)(a)
[redacted]

Striving for a better industry

# The Government's Housing Policy 2021 Report

s 9(2)(a) [redacted]

May 2021

# TABLE OF CONTENTS

Real-iQ

s9(2)(a)

[redacted]

# Somethings got to give

Industry survey slams 'out of touch' Government with regards to their handling of the housing crisis

Nearly three-quarters of those surveyed express concern about their situation following the Government announcement. The comments from one person surveyed summed up the feeling of the Property Management industry following the Government's radical housing policy announcement on the 23rd of March. 'Short-sighted. There will be no winners, more owners will sell and there will be fewer houses to rent.'

There is no doubt that the Government's attack on landlords is bad news for our industry. Small businesses in particular could really struggle as the pool of investors begins to dry up. We have already seen emails from landlords to Property Management companies saying that they would rather leave their properties empty.

This prompted us to carry out a survey on the Property Management industry. We wanted to gauge the feelings and thoughts of the people who work at the coalface of our housing crisis. Their opinions were made loud and clear with many people condemning the Government's handling of the crisis and nearly three-quarters of the 140 individuals surveyed expressing concerns that their situations will be negatively affected by the Government's announcement.

Many expressed concerns in regards to the Government's inability to listen and consult with industry stakeholders with others calling the policies 'populist and idealistic'. The overall opinion was that this Government is making the situation worse rather than better. This was expressed in one of the questions when we asked if people agreed with the statement that the Government understood what was required in regards to the housing crisis. Over 57% of respondents strongly disagreed with this statement and in total 92.7% disapproved of the Government's handling of the crisis.

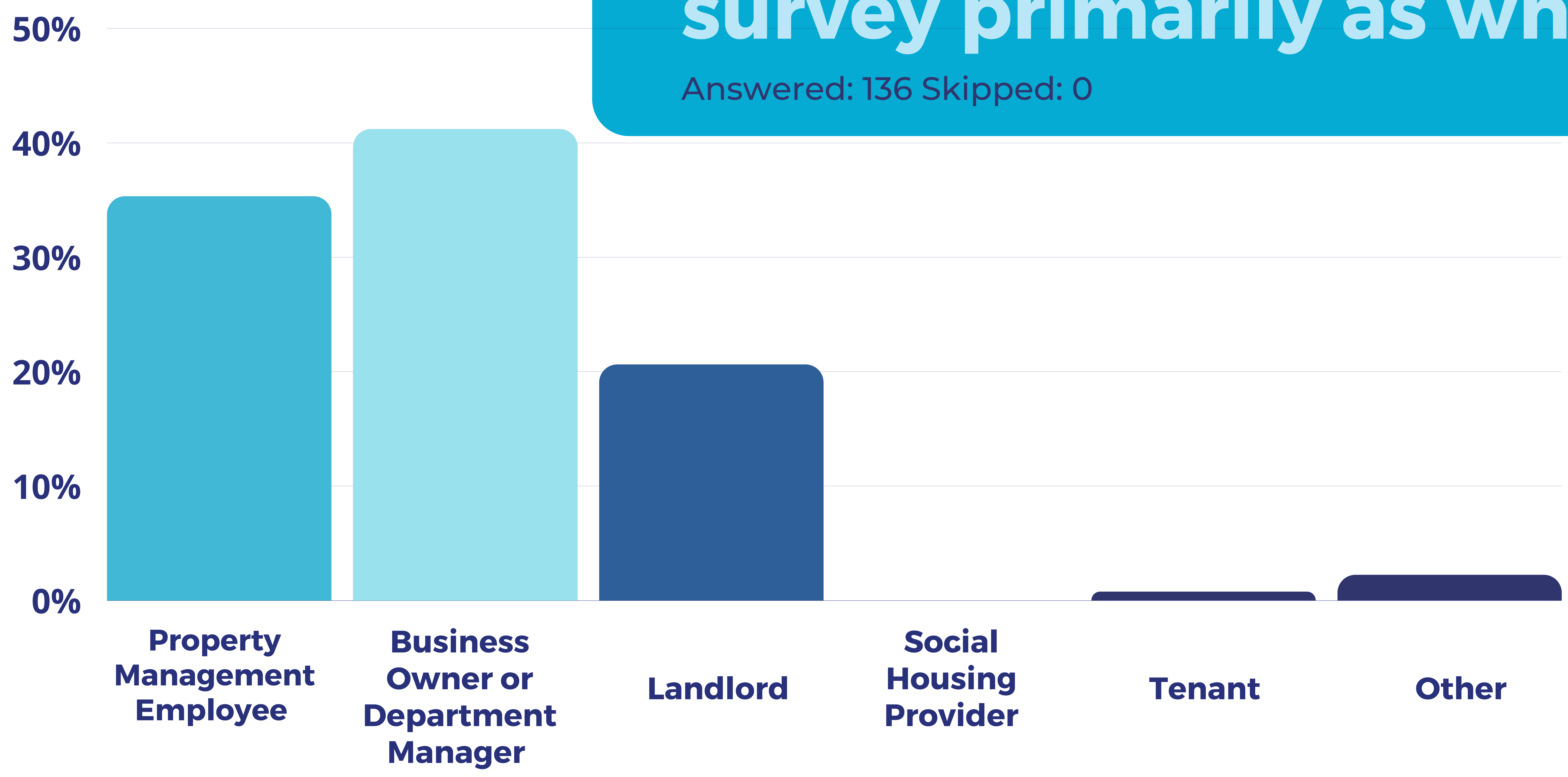
We hope you enjoy the survey!

s 9(2)(a)

[redacted]

## You are answering this survey primarily as what?

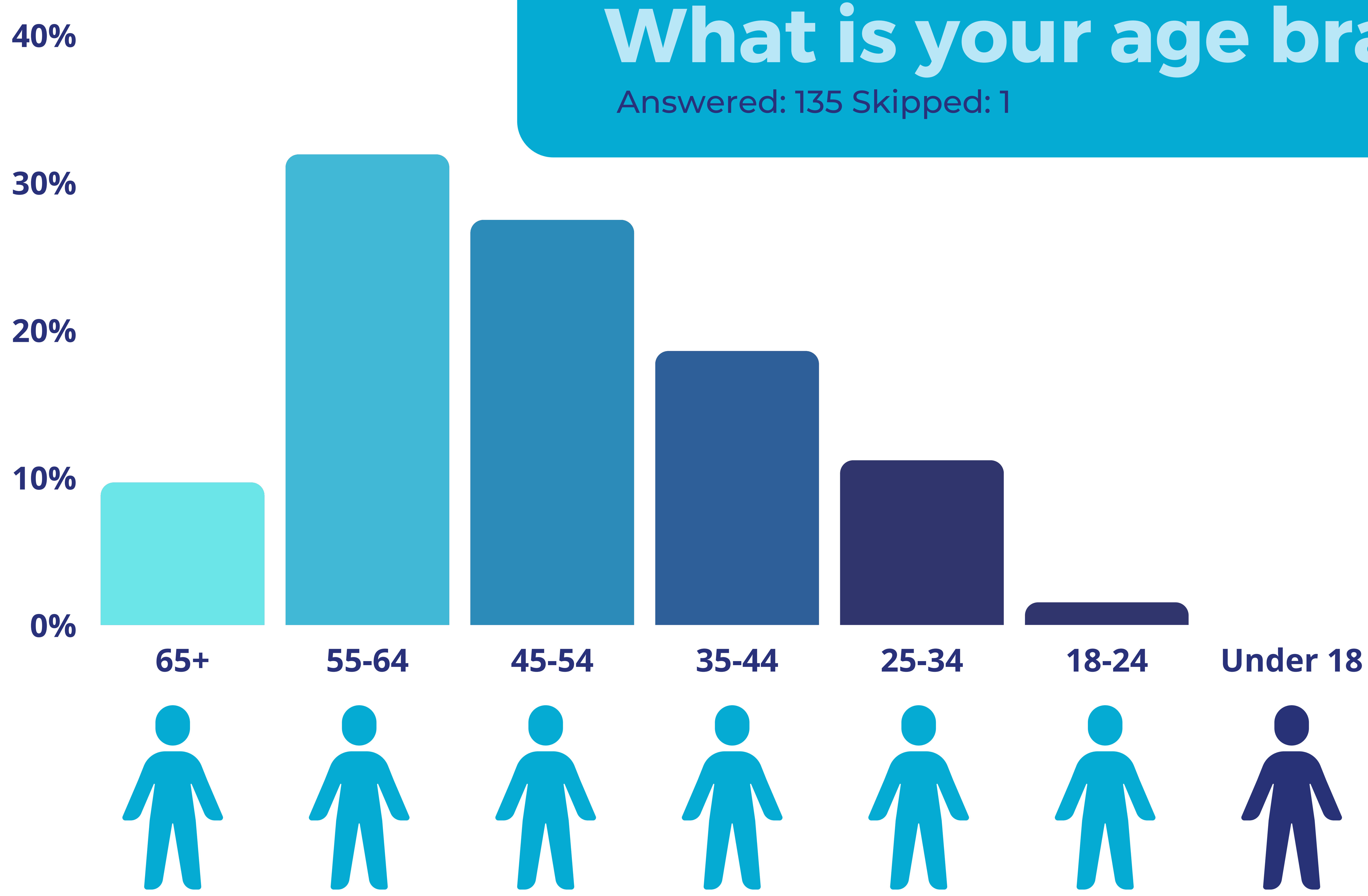
Answered: 136 Skipped: 0




This data shows us who our responses have come from

## What is your age bracket?

Answered: 135 Skipped: 1

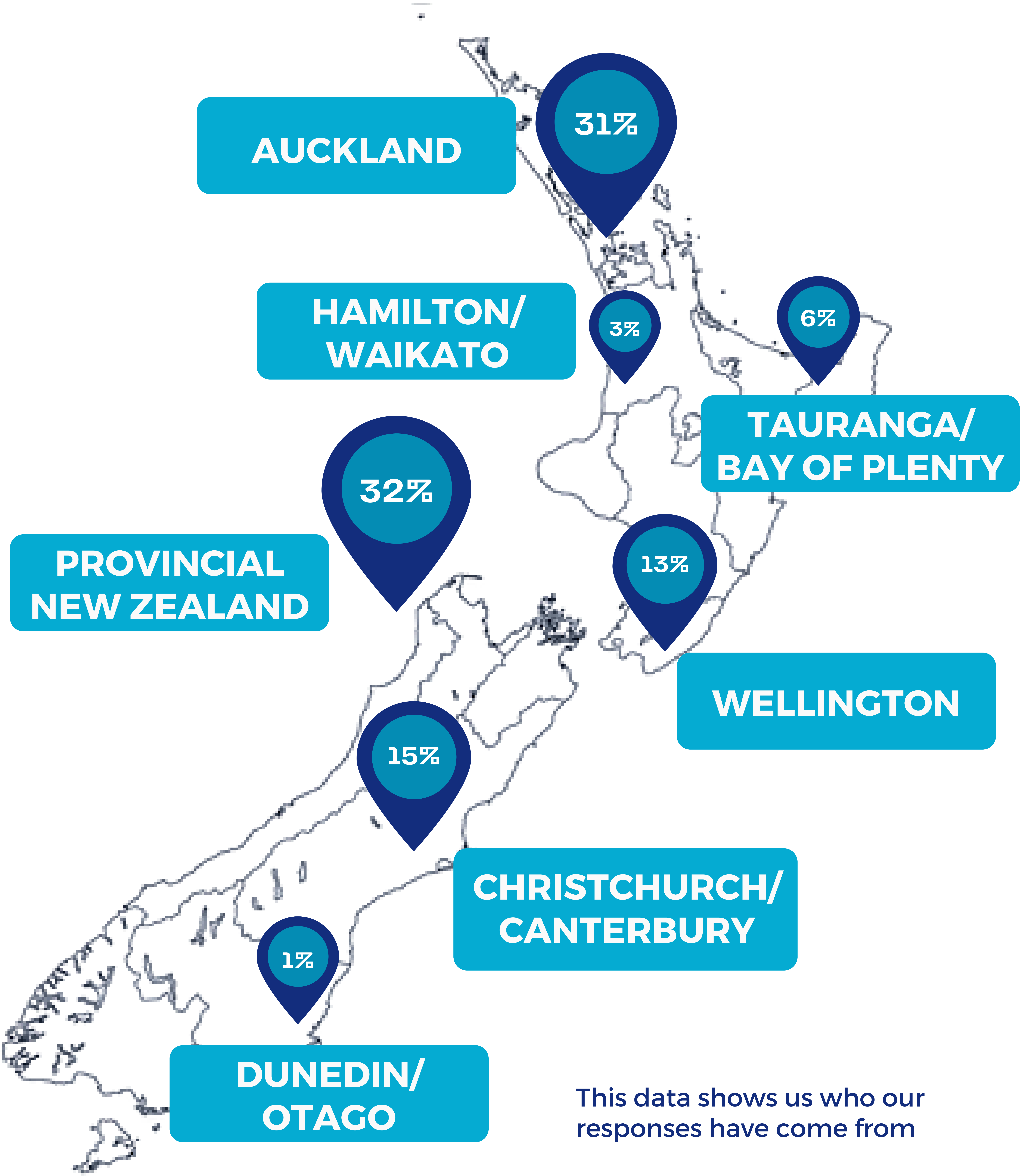




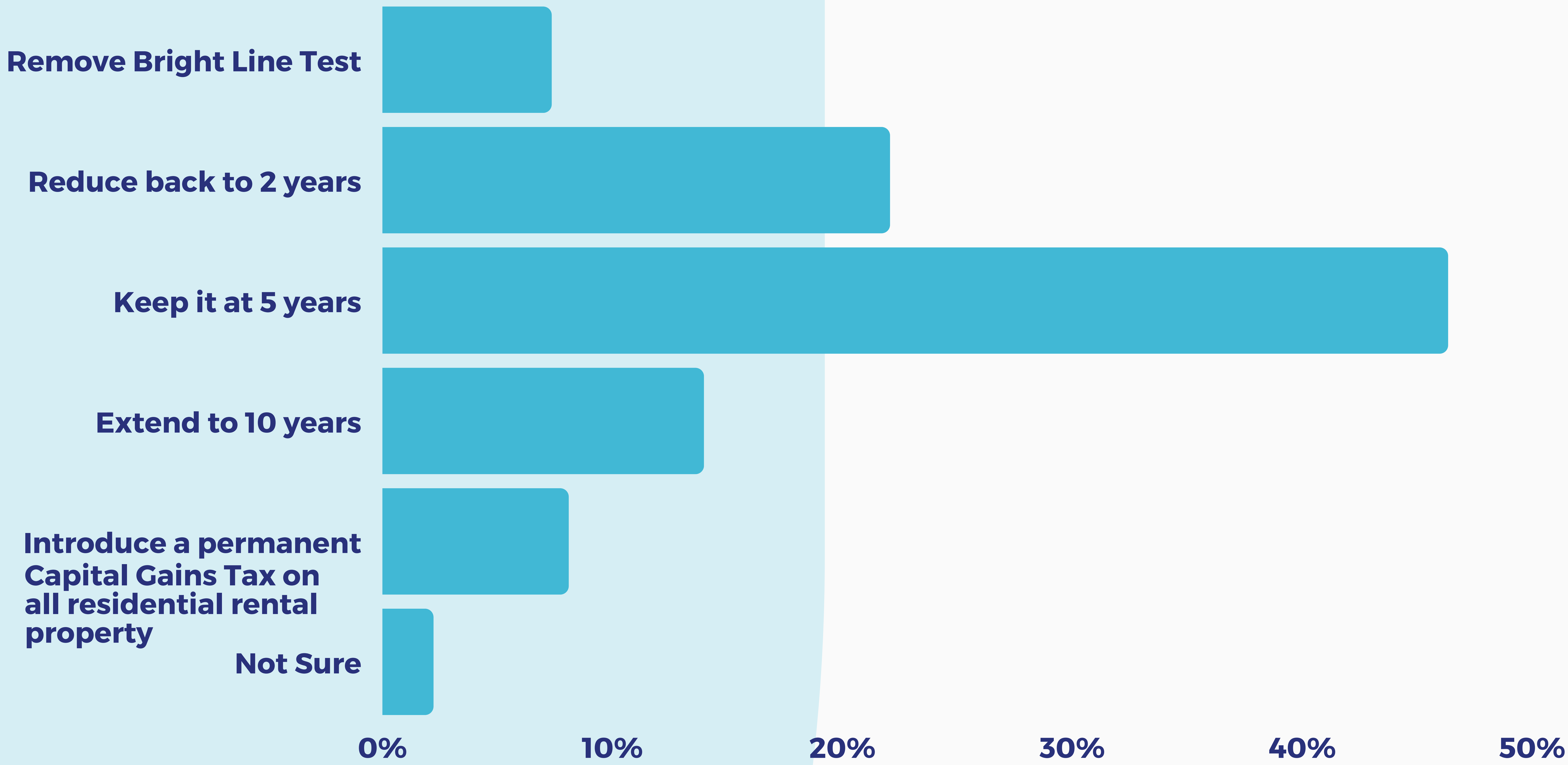

Real-iQ

# What is your location?

Answered: 136 Skipped: 0




This data shows us who our responses have come from




# The Government announced extending the Bright Line Test from 5 years to 10 years for existing rental properties. What do you think should happen?

The majority of people (47%) believe that the status quo should remain and keep it at five years. 14% believe that the Government is right to extend it to 10 years whilst just under 8% believe a permanent Capital Gains Tax should be introduced to residential rental properties.

Answered: 136 Skipped: 0

| ANSWER CHOICES | RESPONSES | |
|---|---|---|
| Remove Bright Line Test | 7.35% | 10 |
| Reduce back to 2 years | 22.06% | 30 |
| Keep it at 5 years | 46.32% | 63 |
| Extend to 10 years | 13.97% | 19 |
| Introduce a permanent Capital Gains Tax on all residential rental property | 8.09% | 11 |
| Not sure | 2.21% | 3 |



Real-iQ