Tax Working Group Public Submissions Information Release

Release Document

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Inner City Wellington's Submission to the Tax Working Group on the Interim Report

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Introduction

1. Inner City Wellington (ICW) submitted during the previous round of submissions. We were pleased to see that seismic strengthening costs are informing the discussion leading to the recommendation to reinstate depreciation for commercial, industrial and multi-unit residential buildings.
2. ICW's understanding of this recommendation is that it will not apply to residential owner-occupiers in multi-unit residential buildings. It will only benefit investor-landlords in residential multi-unit residential buildings.
3. ICW submits that there must be equity of treatment for all owners facing costs due to mandatory seismic strengthening requirements.
4. Commercial property owners and many investor residential landlords will be GST registered, and able to recover 15% off the costs imposed on them. Residential owner-occupiers, in general, cannot do this.

Who benefits from the investment in mandatory seismic strengthening?

5. Mandatory seismic strengthening of earthquake-prone buildings is primarily driven by public safety. While private residential owner-occupiers may benefit from the increased protection of strengthened buildings, their property rights have been removed.
6. There is a significant public benefit gained from private owners undertaking mandatory seismic strengthening on earthquake-prone buildings. Mayor Lester's recent letter of 15 October 2018 to the Minister for Building and Construction acknowledges this: '… the responsibility for strengthening earthquake-prone buildings sits in the first instance with the building owner. However, there are significant public benefits in assisting owners to strengthen, including the protection of human life and infrastructure, making the city resilient so there are minimal interruptions to critical economic activity, and the protection of important public buildings and heritage'.
7. The public safety and economic resilience drivers are the common theme in the media and from central and local government politicians.
8. Owners of commercial property gain an immediate private benefit on completion from being able to increase the rental and lease costs for property as tenants want buildings with a high seismic rating. To a lesser extent, investor residential landlords may see a similar private benefit through increased rentals, though landlords of earthquake-prone buildings are still getting market rental.
9. More importantly, the benefit is only realised once the owner-occupier sells their home. With the latest re-valuations in Wellington due to be released imminently, data will increasingly be available to assess the private benefit, or not, of strengthened buildings that have been sold.

10. Residential owner-occupiers do not see an immediate private benefit from the funds invested in their property. The property valuation may recover the discounted value following the removal of the earthquake-prone status, but there is no guarantee that owners will see an increase that reflects the investment made. The interest paid on increased loans or loss of interest from savings used for the strengthening further depletes any capital gain.
11. ICW's submission is that residential owner-occupiers are, in most cases, unable to claim GST refunds and are excluded from the possible re-instatement of depreciation on buildings, and there should be some tax relief to recognise the public benefit that is gained from their investment.

Contribution to tax revenue by residential owner-occupiers

12. The following table provides costs and taxes paid for completed seismic strengthening projects in wholly or predominantly residential owner-occupier apartment buildings, and two buildings where planning and cost scoping is well underway. The calculation on the amount of profit and the PAYE are conservative.
13. For Buildings D and E, there would be between 1 and 3 years where residential owner-occupiers would have to find and pay for alternative accommodation; these costs are not included

	Bldg A	**Bldg B**	**Bldg C#**	**Bldg D***	**Bldg E***
Construction costs	$1,565,319	$534,817	$1,528,400	$7,906,050	$25,000,000
Professional fees	$313,064	$156,532	$384,725	$1,976,829	$6,250,000
Added value	$173,924	$178,272	$319,021		
Other costs			$68,004		
Contingency					$5,000,000
Estimated total cost of project	**$2,052,307**	**$869,621**	**$2,300,150**	**$9,882,879**	**$36,250,000**
Estimated breakdown of costs:					
Profit @ 5%	$102,615	$43,481	$115,008	$494,144	$1,812,500
Materials @ 55%	$1,128,769	$478,292	$1,265,083	$5,435,583	$19,937,500
Wages @ 40%	$820,923	$347,848	$920,060	$3,953,152	$14,500,000
Income tax on profit of contractors @ 28%	$28,732	$12,175	$32,202	$138,360	$507,500
PAYE on wages paid @ 17.5%	$143,661	$60,873	$161,011	$691,802	$2,537,500
GST on project (only # GST reg Body Corp)	$169,315	$71,744	$189,762	$815,338	$2,990,625
Tax Paid/Due* to Government	**$341,709**	**$144,792**	**$382,975**	**$1,645,499**	**$6,035,625**
Building Levy; Building Research Levy 1.45%	$22,697	$7,755	$22,162	$114,638	$362,500

*Project is in planning stages, costs are based on quantity surveyor estimates. Building B and C had a 28% and 16% increase in the tender prices. Strengthening work has not begun.

14. There is a significant contribution from residential owner-occupiers to Crown revenue for what is predominantly a public benefit. From only three buildings there is nearly $900,000 in taxes. Building D covers three physical buildings (3-4 levels in height) that have a Wellington City Council heritage status, with just over $1.6m in taxes to be paid by the owners in two body corporates.

Forced into poor economic decisions by a one-size-fits-all policy

15. In Building E, the owners are very unlikely to complete the work as it is uneconomic. The owners are private home owners, not developers. Their only remaining options are to sell at

bargain-basement prices or do nothing and wait for the Council to initiate the legal processes, which includes the potential imposition of fines.

16. Both options force the owners out of their homes recovering little or no money, and in many instances leaving them with no home.
17. Some residential owner-occupiers may not make these investments if they had a choice about risks and their own safety in an earthquake – as residential owners in single household buildings do. The policy development has focused on public safety of commercial buildings occupied by tenants and people in public spaces around them – not the home-owners.

Conclusion

18. Residential owner-occupiers are contributing 17% of the total cost in the Crown's general fund to be used as the Government determines.
19. The mandatory seismic strengthening programme should be tax neutral for all owners.
20. Residential owner-occupiers are seeking financial recognition of the fact that they do not receive all the benefits 'gained' from an 'investment' imposed by legislation. The majority of the benefits are for public safety and the city and country's economic resilience.
21. ICW seeks tax relief that recognises this contribution by residential owner-occupiers for a public benefit so there is equity for the tax relief available to GST-registered owners and those able to depreciate their buildings.
22. ICW would welcome an opportunity to meet with the Tax Working Group.

For further information, please contact:

Geraldine Murphy, Deputy Chair

Inner City Wellington

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