IPTI Xtracts

Property Tax and Assessment News from Around the World

NEW ZEALAND – JUNE 2018

Tax could prick property bubbles

New Zealand property prices soared by 71 per cent from 2010 to 2017.

Over the past seven years, New Zealand has experienced one of the fastest rates of house price inflation in the developed world.

According to the Bank for International Settlements (the central banks' bank) residential prices in New Zealand ended last year 71 per cent higher than their level in 2010, a compound annual growth rate of 8 per cent. That compares with a cumulative rise of 43 per cent in Australia and an average 27 per cent across all advanced economies.

Among advanced economies, only Hong Kong and Iceland saw faster rises in residential prices. Indeed, after adjusting for consumer price inflation only Hong Kong outstripped New Zealand's 54 per cent real rise.

As a general rule, when we are an outlier in some economic measure it is not a good sign.

These arguments get very arcane. But they tend to ignore the crucial influence of leverage. An investment largely bought with borrowed money in a rising market will see the buyer's equity grow much more rapidly than the asset value. If the capital gain is untaxed, so much the better.

Conversely, leverage will amplify the investor's losses in a falling market.

It is the interaction between the tax system and the banking system which tips the scales in favour of housing over other investments.

Good luck, for example, going to a bank and saying: "I reckon Fletcher Building is oversold. I want to buy 100,000 of their shares and I would like the bank to put up 80 per cent of the money, please. I'll happily give you a mortgage over the shares."

The response is liable to be: "Never mind that. What about a mortgage over your house? You can do what you like with the money."

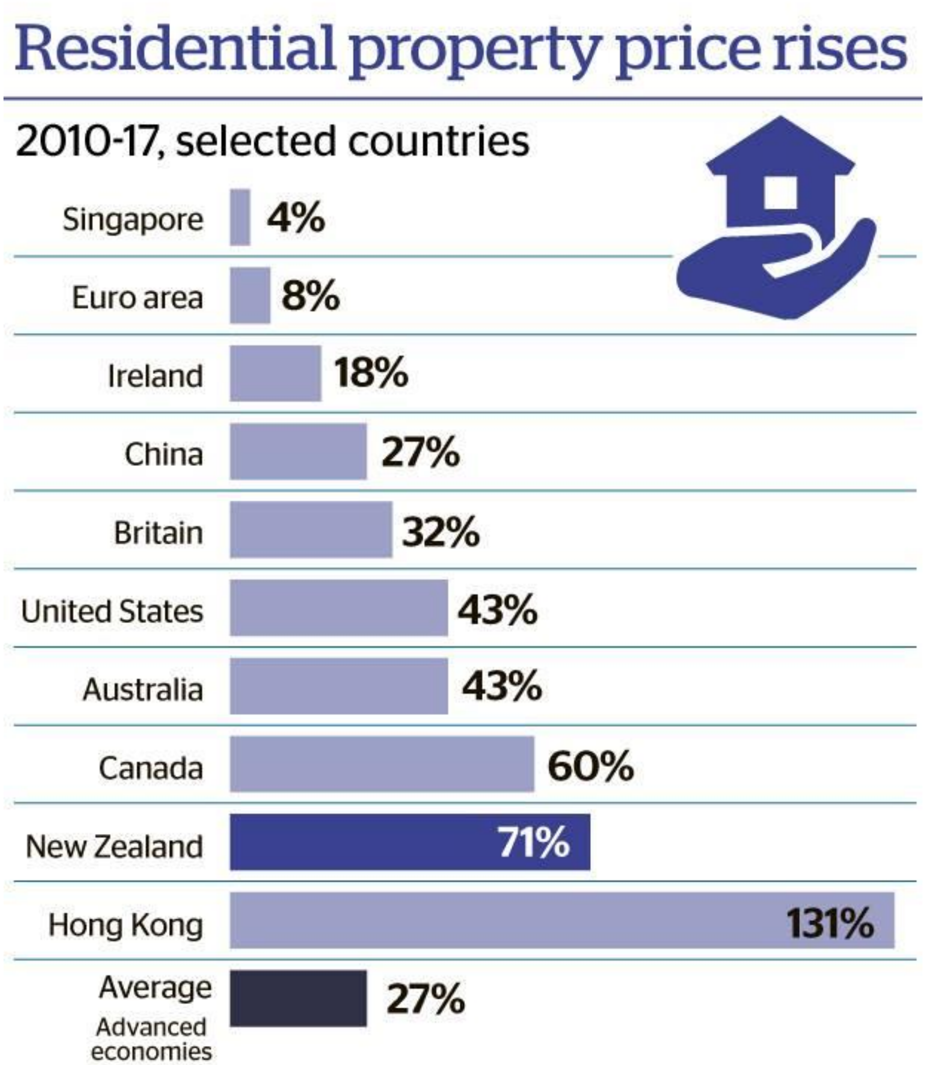
A simple way of looking at the issue would be to compare the tax paid by landlords with the value of the rental housing stock.

The Property Investors Federation, citing Inland Revenue data, says landlords paid $1.3-$1.5 billion a year in tax over the five years to 2016. Assuming, conservatively, that they own a quarter of the housing stock by value, and taking the Reserve Bank's estimates of the value of the national housing stock over that period, that would represent a tax yield of about 1 per cent a year.

Not exactly onerous, especially in times of rampant house price inflation.

Westpac's chief economist Dominick Stephens has used a model he developed some years ago to calculate the impact various tax changes would have on house prices and rents.

The model estimates the value of an average New Zealand house to a rational investor, based on the net present value of the rent that the property could generate, less the expenses. It is sensitive to inflation, interest rates and the tax system, and gives excellent signals as to what might happen to house prices when one of these factors changes, Stephens says.



For example, from 2014 to 2017 mortgage rates fell sharply and the model correctly predicted that this was a period of strong house price growth.

The reason for looking at what it is rational for investors to pay is that they tend to be the marginal buyers who set the prices would-be owner-occupiers have to outbid.

Westpac's model predicts that a capital gains tax at a rate of 10 per cent, which would exempt the family home, would reduce house prices by 10.9 per cent, all else being equal, but push up rents 5.5 per cent. It does not predict how long it would take for those effects to work through.

A capital gains tax is not the only option. A property tax of 0.5 per cent on the value of the property (house and land), again exempting the family home, would have a similar impact. By reducing the price an investor would be willing to pay, it would increase home ownership rates, reduce house prices by 10.5 per cent and put rents up 5.2 per cent.

A land tax of 1 per cent on the unimproved value of the land on which a dwelling sits, again exempting the family home as per the terms of reference, would reduce house prices, all else being equal, by 9.5 per cent, the model predicts, but push up rents by 4.8 per cent.

Properties for which land makes up a greater proportion of the value, such as houses with large sections, would experience a greater percentage decline in price, while apartments would experience a smaller percentage decline, Stephens says. "Auckland prices would probably fall further than prices elsewhere in New Zealand. This is because land makes up a greater proportion of the value of Auckland properties than in other regions."

The model assumes that one-third of the adjustment to a tax change would come through higher rents and two-thirds through lower house prices.

That is the assumption Stephens has least confidence in, he says, in that it is based on observations when the model was developed in 2007. But if rents rose less, house prices would fall more.

Councils need to rein in runaway rates

As councils around New Zealand consider next year's spending plans, families are bracing themselves to be socked with rising rates at a time when the cost of living is starting to increase, National's Local Government spokesperson Jacqui Dean says.

"Homeowners nationwide are concerned at the plans of councils to increase rates without any reassurance that they are delivering value for money or improving local economic growth.

"Excessively high rates bills hurt ratepayers and their families.

"Christchurch City Council, for example, is meeting today to consider plans to increase rates by 17 per cent over the next few years. Such a large increase during a period of very low inflation is unjustified.

"This 17 per cent rate increase could be in addition to higher petrol prices thanks to the Government's new regional fuel tax of 11.5 cents per litre that the council is also saying it wants to impose on ratepayers – one of 14 councils saying it wants the new tax.

"While Christchurch faces additional expenditure due to the ongoing earthquake recovery it has options other than major rates increases and it needs to seriously consider those and the impacts of any new costs on ratepayers.

"Local councils, like central government, need to show restraint before imposing additional costs and taxes on hard working New Zealanders.

"People are already hurting from the rising cost of living. Families will be over $100 per week worse off under this Government's policies pushing up the price of petrol, rent, and groceries - combined with their stubborn refusal to provide tax relief.

"Communities understand that efficient public services and resilient infrastructure needs to be balanced by councils' strong financial management and care for ratepayers' back pockets."

Rates increase of 9.7 per cent for Hamilton ratepayers

Hamilton ratepayers will be hit by a 9.7 per cent rates increase in year one of the 10-year plan, along with a three-year transition to a full capital value rating and UAGC of $500.

From year two there will be a 3.8 per cent annual rates increase.

The council is now updating its online rates information so ratepayers can see what the changes mean to their properties.

The search tool on the council's website will be offline until this update takes place — planned for the end of this week.

Under capital value rates are calculated on what is built on the land rather than just the land itself, while the UAGC is a flat fee to reflect base costs which apply to all residents and ratepayers. It would form part of a property's rates bill and is not additional.

It draws an end to a saga that started early last year when the mayor proposed a 12.5 per cent rates increase to balance the city's books.

That suggestion was knocked back by councillors at the time. Before the final rates discussion took place last Friday, Mayor Andrew King declared a conflict of interest and withdrew from the council chambers.

"To clarify in respect of the decision to move to capital value or not, I do not believe I have a closed mind on this topic, however what is clear is that due to the portfolio of properties I own or influence, or I have interest in I have a pecuniary interest to relation to any decision in respect of the move to capital value," Mayor King said.

"This interest is greater than the public's in general. Due to this conflict of interest I am going to vacate the chair now and leave the meeting."

Deputy Mayor Martin Gallagher took over the meeting.

After a series of amendments, heated debate and a bit of confusion, the council settled on the 9.7 per cent rise in one year, however some councillors were still unhappy.

After Mayor King returned to the meeting , councillor Angela O'Leary took aim at him.

"I made a plan with our residents in 2015 and that plan was agreed with them — that they could rely on us to keep rates at 3.8 per cent for the next 10 years and that meant something to me," Cr O'Leary said.

Councillor James Casson said he preferred the 3.8 per cent option and that the new rates rise is not perfect, but that they may as well get it done quickly.

Councillor Rob Pascoe said he favoured a short and sharp rise.

"I think the 9.7 is a compromise of sorts. I think delaying the increase over two years is fraught with a number of risks."

He said the property revaluation due at the end of 2018 would be one of those problems.

Councillors Paula Southgate, Siggi Henry and O'Leary voted against the rates increase.

Mayor King, Deputy Mayor Gallagher and councillors Ryan Hamilton, Leo Tooman, Dave Macpherson, Garry Mallett, Geoff Taylor, Mark Bunting, Pascoe and Casson voted in favour.

House prices still on the rise in Dunedin

Dunedin has bucked the trend of several other main centres and maintained residential property value gains of 4% during the past quarter.

Similarly, Queenstown Lakes still heads off wider Auckland with the higher $1.15 million value, but its year-on-year value gain was 9.6% against Auckland’s 1%, Quotable Value data for May shows.

QV general manager David Nagel said the QV house price index showed nationwide residential property values for May increased 6.9% over the year, while values rose 0.8% during the past quarter.

"As anticipated, nationwide sales volumes are down as we enter the usual winter slowdown, although value levels are holding," he said in a statement.

Values remained "relatively high" as low interest rates, the loosening of the Reserve Bank’s loan-to-value ratio restrictions, and the government kick-start packages, such as the KiwiSaver HomeStart grant and savings withdrawal, continued to fuel demand.

However quarterly value growth had come "virtually to a standstill" across the Auckland and Wellington regions, and was "flat" in Hamilton, Tauranga and Christchurch.

"Dunedin is the only main centre to buck the trend, where entry-level prices remain comparatively low and well-located properties continue to demand high prices," Mr Nagel said.

QV Dunedin property consultant Aidan Young said Dunedin values had continued their upward trend, rising 9.4% during the year to May and 4% over the past three months.

"Multi-offer scenarios are common-place, which gives us an indication of how busy the market is," Mr Young said of Dunedin.

The city’s average value is $408,827, while Dunedin South saw the strongest growth with values up 10.3% year on year and 4.5% over the last quarter to $390,162, he said.

He described the Dunedin market as "robust", with both entry-level properties and premium properties selling "reasonably quickly", provided they were priced right.

"The city’s premium suburbs within close proximity to the CBD or the beach, such as Maori Hill or St Clair, continue to attract demand and high values," he said.

Mr Young reported entry-level properties, below $300,000, had continued to sell quickly, particularly in suburbs such as Caversham and South Dunedin, and also Waikouaiti settlement, north of Dunedin.

He said Dunedin values should still steadily grow — or at least hold their value — over winter, given the usual winter slowdown period meant listing numbers declined, but demand was showing no signs of dropping significantly.

Mr Nagel said Queenstown Lakes district and Invercargill continued their steady value growth, respectively up 3.5% and 1.8% for the past quarter.