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Experts in property care and return
Welcome to your monthly update from Quinovic Merivale on property investment news and opportunities. *17 April 2019*

A stronger market has continued over the past month. We have had several opportunities to offer our services to new clients and interest from potential tenants has also been high. May this continue a little longer!

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When I bought this business 11 years ago I recall being told 'Don't forget your potential business. Stay in touch even if you don't get the new business immediately'. During this month I was offered the management of several properties – 8 years after first being in contact with the owner. We stayed in touch over all of this time, he received our monthly newletters over all of this time and finally the situation changed and he asked us to take the properties over. I am obviously delighted to get this business so thank you John.

Those of you who know how we operate will be aware that every week we scan the newspapers and TradeMe and make contact with all the private landlords who are advertising. Time consuming but rewarding and this has been the second major stream of new business after personal referrals from existing owners. Things that we have noticed over recent months when doing this:

- The number of To Let advertisements in The Press has fallen away to virtually nothing. Some weeks lately there have been no To Let ads and other weeks just 2 or 3 and most of those have been for room x room rentals. Compare this to when we started and newspaper To Let ads took more than 1 full page in the paper.
- Replaced by ads on TradeMe you would think. Initially this was so but now even this avenue is falling. A full report in next month's newsletter.
- The time ads are on TradeMe has grown as well. Generally speaking properties are sitting longer. But look a little closer and there are common reasons. Properties do not offer what tenants are looking for. Properties are not presented well.
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- Properties are remote from schools, bus routes, shopping centres and the like. Properties are over-priced for today's market.
- The key message here stays the same as always. Present well – be competitive. Provide what the market is seeking. Price it correctly. Such properties will always rent well.

Commentators are predicting that the Government may make an announcement on Capital Gains Tax this week. They have said April but it is suggested that they may 'hide' behind the Easter holidays to issue their decision.

The common thread behind nearly all of the commenters is that whatever we get will be a 'highly watered down' version of what the tax group proposed. More in line with the minority report as submitted by some on the panel.

It is suggested by some that it may in fact be restricted to a capital gains tax on rental properties only at this stage. This has led some leading commentators to predict that to do so will be very costly politically to the Government.

Shamubeel Eaqub states that the introduction of CGT in any form by the Government will see this out of office at the next election.

Cameron Bagrey slates the Government for not having the courage to introduce CGT in its entirety including having CGT on the family home.

However it is looked at it is an emotional issue which looks like being focussed on landlords as they are a soft target and such a move will be popular with many other sectors of the community.

Robin Oliver, former Deputy Commissioner of the IRD says' that the recommendation of the Tax Working Group are quite different to the capital gains tax that the Labour Party campaigned on for two elections. Much tougher and much purer".

"Pure and tough" was how one former member of the Tax Working Group described the group's capital gains tax recommendations to a Bell Gully event.

That description may do little to allay concerns about the results of the working group's 12 months of deliberation, which saw the majority (with an 8:3 split) recommend a broad extension of the taxation of capital gains in New Zealand.

"It's tougher and purer than the capital gains tax the Labour Party campaigned on for two elections and lost. Much tougher and purer," former Deputy Commissioner of the IRD Robin Oliver said at the event. At pains to point out that they no longer speak on behalf of the Tax Working Group, Oliver and former Bell Gully tax partner Joanne Hodge gave some insight into its recommended outcome, which many already anticipate will not result in a tax as pure or as tough once the Government responds to lobby groups and selects from among the group's recommended reform packages.

The capital gains tax recommended by the working group would become effective on April 1, 2021. It would apply only to gains made on assets after that implementation date (with a valuation of assets required as at the implementation date), apply at ordinary marginal tax rates on the full amount of the gain, and operate under a traditional realisation-based model.

Although international comparisons are difficult, New Zealand's lack of a comprehensive capital gains tax makes it stand out. But we will continue to stand out on the international scene should the recommendations be adopted in full. "It's hard to see any other capital gains tax in the world that taxes at full (marginal) tax rates – it makes sense in theory, but it's a tough result," said Oliver.

He said the group faced very little political constraint beyond the exclusion of the family home and any kind of "death tax". That resulted in relatively "pure" and comprehensive proposals by the standards of international regimes. In contrast, other countries have implemented capital gains taxes that are more politically driven – and subsequently not as tough. They tax capital gains at much lower rates than for labour and with many exemptions. "So when you say all these other countries around the world have a capital gains tax you are not talking about the same thing," he said.

Politics may yet play a part. There is every indication the Government is keeping its options open. It has signalled a measured approach will be adopted, with options to pick and choose aspects of the Tax Working Group's recommendations. Ministers have indicated it is highly unlikely all recommendations would need to be implemented.

But if the tax is watered down significantly, a different question arises: Is it worth it?Hodge said the "minority report", from the three members of the working group who did not support a comprehensive approach to extending the taxation of capital gains, reflected a number of concerns. They included a negative effect on productivity, a lock-in effect where people hold on to assets in order not to pay tax, the potential for double taxation from taxing business asset gains and share gains, the significant complexity added to the tax system, and the "immense, mind-bogglingly difficult" proposition of valuing all the affected assets in the economy. "A lot of the CGT litigation in Australia relates to disputes over valuations," she pointed out.

The forecast revenue over five years, from the CGT rules as proposed, amounted to less than would be raised by adding one percent to GST, she said. If the Government decided to water down these rules by imposing a lower CGT rate, introducing more exemptions and broader rollover, then a half a percent increase to GST would be a more relevant comparison. Under both scenarios the increased complexity of the rules would have a huge impact on New Zealand's 'simple tax system' operating neutrally in the background.

Meanwhile there are risks around the timeframe: a government response to the recommendations this month, detailed design to be consulted on and completed by August, a bill introduced between October and December, then legislation passed and enacted by July 2020 ahead of implementation in 2021.

“The timeline is completely infeasible,” said Hodge. “If faulty legislation is enacted it will lead to lack of confidence in the tax system and taxpayers will take full advantage of any loopholes. Subsequent amendments will be needed and these just add to already heavy compliance costs.” All five of the tax experts were of the view the proposed timeframe for enactment would produce risk to the tax base and a later implementation date was required.

The extent to which the tax experts in the group weighed such concerns differently to the broader group is revealing.

While the broader group had an 8:3 majority for a capital gains tax, only five of the 11 members of the group are tax experts. Of the “tax five”, while there was still a majority in favour of a capital gains tax, it is by a narrow margin.

Oliver and Hodge, with Kirk Hope of BusinessNZ, produced the minority view paper and did not recommend the introduction of the proposed CGT rules

While Hodge said extending the taxation of capital gains had perceived advantages, which included improving the fairness and integrity of the tax system and levelling the playing field between different types of investments, in the end the minority could not support a comprehensive capital gains tax approach. Ultimately, the case for taxing more gains from residential rental property was the clearest, and that was where they favoured action.

“The minority view is: keep plugging the gaps, as we have been doing over time, and enforce our existing rules better,” she said

From the New Zealand Property Investors Federation:

In the Friday, 29 March Herald, Dominick Stephens said "property is more lightly taxed than other forms of investment". He quoted a Treasury and Inland Revenue report to back up his claim.
That report was also used by the Tax Working Group. However economist Bevan Wallace found serious errors in the report and showed that the conclusion that rental property is undertaxed was wrong.
To their credit, the TWG accepted that there was an error in the report and agreed that rental property was not undertaxed compared to other forms of investment.
The TWG have said that a comprehensive CGT would not affect house prices, but it would increase rental prices. We already have a rental property crisis in NZ. Tenants do not want their situation made worse.
Rental property owners are ordinary New Zealanders providing for their retirement. They provide accommodation to a third of New Zealanders which is an incredibly important part of our productive economy. They pay tax on over $1.5 billion dollars of rental income each year.
If a CGT is introduced it shouldn't apply to some assets and not others. Excluding the family home is already creating a distortion. Applying a CGT just on rental property would be more than unfair, it would be unprincipled and unjust.
Andrew King

Time will tell. Any move we are told would not become law until after the 2020 elections.

KiwiBuild continues to get considerable negative coverage despite several attempts by the Government to project a more positive image around the program. I saw a quote the other day that referred to the 'Minister of 30 Houses' a dig at the small number of homes that have actually been completed to date.

The Government appears to be working hard with the building sector to get the program back on track but that in turn draws the ire of others. Bringing properties into KiwiBuild that have already been on the market and not sold does not add any additional properties into what we are told is an under-stocked market. If they haven't sold then there has to be an underlying reason – not what people are looking for, over-priced, in the wrong areas. Many suggestions have been tabled.

But we understand that there is another aspect to this which people seem to just be realising. If a property bought in under the KiwiBuild program does not sell within a set period of time then the Government will buy that property off the developer. No risk to the developer. Total risk to the people of New Zealand. We will try and confirm if this is in fact correct.

Transferring such properties to the portfolio of Housing New Zealand may also not be a viable solution. Treasury has issues a warning to the Government that allowing HNZ to borrow more against its own name posed a 'significant risk' in that ratings agencies would count such debt as belonging to the core Crown balance sheet. This could pose problems for the Government in the upcoming budget. The Governments self-imposed budget responsibility rules require that Crown debt comes down to 20% of GDP by the 2021/22 budget. By allowing HNZ to borrow in its own name effectively circumvents this rule.

However the three large ratings agencies say that they already look at non-core debt as a contingent liability. "If contingent liability becomes too large we can lower our overall debt assessment" says Andrew Walker of Standards and Poors.

From NewsHub:

Many property owners wouldn't improve their homes and rentals even if they knew they weren't up to scratch, according to a new study.
University of Otago researchers had warrant-of-fitness (WOF) checks carried out on 83 homes in Taranaki, 92 percent of which failed.
The most common reasons were failing to have functional spouting and stormwater functions, missing ground vapour barriers, decks and other surfaces being slippery and covered in moss, missing window security stays and wet underfloors.
They later interviewed 40 of the owners – four of them landlords – and found a quarter of them had not made any plans to fix anything at all, largely because of cost.
"This study indicates that people provided with a WOF assessment on their residential properties are often unwilling to ameliorate identified health and safety problems," the study's authors wrote in the *Australian and New Zealand Journal of Public Health*, suggesting subsidies might be needed to sort the problem out.
"Providing funding support to make improvements, as well as additional information to explain how improvements are likely to boost the health and safety of occupants and of visitors, could encourage owners to make improvements that have demonstrated health and safety benefits."
Another approach could be to toughen the law.
"The extant evidence on how rental regulation encourages owners to make improvements to their property suggests that a rental WOF needs to be mandatory to induce important improvements in housing and consequent health and safety outcomes."
Some owners weren't even aware their properties had problems. About a third of owners whose homes had issues said they thought there wasn't anything wrong.
"Our study supports research showing that one of the barriers to making housing improvements is a lack of knowledge about the home's defects, or believing the property is in better condition than it objectively is."
One of the most common issues was a failure to have secure storage in the kitchen out of children's

reach. Fewer than half of homes passed this requirement, and only two of the 19 owners whose homes failed said they'd remedy it.
As for a ground vapour barrier – which would cost about $200 to fix – only two of the 22 owners whose properties failed said they'd get one installed. Some admitted to not knowing what a ground vapour barrier even was, or thought it would make dampness worse.
Renters United says the results of the study raise "serious questions".
The tenants' advocacy group says there is only one way Healthy Home Standards can be "meaningfully implemented and enforced" – and that's through a WOF scheme.
"Such a scheme already exists for commercial rental properties," it told Newshub.
"Like that scheme, private landlords should hire a trained assessor to determine whether their property complies with the Healthy Homes Standards.
"The cost of such inspections would be reasonable, around $250, and last multiple years. That is a small price to pay for healthy homes."
The study's authors noted that as the vast majority of those interviewed were owner-occupiers, it was difficult to draw conclusions on whether landlords would be less willing to upgrade their rentals than their own homes.
They also note that just because a property owner said they were planning to make improvements after the WOF, that doesn't mean they actually did.
Tenancy Services told Newshub that the $15.14 million it was allocated last year would go towards both education and enforcement of the Government's Healthy Homes Standards.
"Education will help landlords know what they need to do, and there will be enforcement measures to encourage them to comply so all tenants benefit from warm, dry homes," it said.
It also vowed to "help landlords know what they need to do to comply with the standards".
"[An information and education campaign] will provide information about landlords' responsibilities and tools to help them comply, and encourage them to act before the compliance deadlines."

We circulated this to many owners earlier in the month. Just to get the message out to the others:

You may be aware that under their stated procedures with regards to rental properties and tenancies the Ministry of Business, Innovation and Employment has undertaken to audit property management companies around New Zealand to ensure compliance with their rules and regulations.

We have just been audited.

As daunting as this may sound I feel grateful for the experience. We have always believed that we operate fully within the expected standards but had the audit found that we didn't then I wanted to know this.

What did the process entail? We had a site visit from an MBIE compliance team member. There were a number of quick-fire questions regarding our processes in relation to tenancy applications, bond collection and payment practices, owner maintenance plans, our inspection frequency and process and the like. The auditor then selected a number of our property files at random and went through the relevant paperwork ensuring accuracy, compliance and that the correct insulation documentation was included. Whilst our agreements contained a couple of clauses that MBIE feel may not stand up in Tribunal they had no issue with our retaining those clauses in our agreement as they clearly outline our expectations of our tenants. The auditor also contacted a number of our tenants to confirm our processes were as we had outlined.

The outcome – 'No further action required". In other words Quinovic Merivale was deemed to be fully compliant with our obligations under the Residential Tenancies Act.

I am extremely proud of our result.

As always many thanks for your loyalty and support. If you know of anyone who may need our services please have them contact us or let us know.

Best wishes to you all
Sharon, Lexi, Carolyn, Andrea and Tracy