Tax Working Group Public Submissions Information Release

Release Document

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[1] 9(2)(a) - to protect the privacy of natural persons, including deceased people;

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In preparing this Information Release, the Treasury has considered the public interest considerations in section 9(1) of the Official Information Act.

[1]

From: john Paynter [1]
Sent: Friday, 11 May 2018 11:44 PM
To: TWG Secretariat
Subject: Submission re ring fencing of losses for residential property investors

Dear Sir.
I seem to have been going in (internet) circles to find where to send a submission (e.g. I sent it to the TWG address but told the Future of Taxation one was closed). Please accept this one on ring fencing.
PS: I have been away from Internet access these past two days while conducting remedial work at a property following abandonment and damage of a property (one of the many unbudgeted calamities that might befall an investor).

I have been a property investor (i.e. landlord) for 30 years. For many years my properties were cashflow negative. I did not deliberately set our for this to happen, as to me running a property at a loss makes little sense. However in the late 1980s and early 1990s (following the share market crash, in which I lost money I had hoped to use to refinance my properties), interest rates rose. property prices dropped, rents dropped alarmingly and as it was a renter's market the tenants could demand concessions such as new drapes to match their furniture). In addition costs such as insurance and rates and water went up (they never go down). I made substantial losses. Unfortunately, these (unexpected) losses were ring fenced then with only $10,000 per annum being allowed. Within two years the legislation around this was reversed, as the (un)expected consequences included loss of rental properties. Even though ring fencing was reversed the rules re the previous losses stayed in place and I had to spread the loss over the next six years. This precluded me from making rational decisions about new investments.

Since this time my properties have been cashflow positive, although I seem to have an unexpected large cost (and/or loss of income) on each property about once every ten years. i.e. I have around 10 investment properties with a 10% of a problem (these have included landslips, failure of a re-roof, replacement of a bathroom due to a hidden leak, a septic tank failure - it had to be replaced). I also have at times had a dud tenant who caused damage and/or failed to pay rent. As it takes a while to get a Tenancy Tribunal Hearing and more time to get it actioned (e.g. an eviction), there is often no income for several months, while the standard costs (insurance, rates, mortgage, body corporate fees etc) continue, then thousands may be spent remediating damage (which the current rules deem to be at the landlord's cost, not the tenant's), while the place still remains empty (I am facing this very predicament at present).

So a stream of positive cashflow years may be followed by one with a loss, so it hardly seems fair to prevent this being claimed in a given year.

Many expenses and cashflows are also predicted to be lumpy. e.g. my daughter is considering investing in a rental property and is looking at three different scenarios presented by a property consulting firm. In these, years of profits may be followed by a loss due to fixed interest rates going up at the end of the fixed term and increased maintenance being scheduled every few years.

I also prepare Long Term Maintenance Plans for several body corporates (as required by law). Even though I try to spread the maintenance costs evenly over the years, this is impossible due to several costs being relatively high (e.g. a complete exterior repaint, replacing a shared driveway, renewing services). It makes economic sense to do some of these at the same time. e.g. replace stormwater, sewerage, phone, gas and power lines and then relay the driveway. So all the costs tend to be lumped. Other costs also arise for which the investor has little control. For instance, we are faced with putting in or upgrading insulation and smoke alarms with the former not being deductible. We do not yet know what will be required under the Healthy Homes Guarantee Bill recently passed. For instance if we have to provide heat pumps we bear costs of several thousand per property.
If an individual investor had been making profits for some years and paying tax of these, then was faced with high body corporate fees for a given year, then it is hardly fair to ring fence this loss. If other costs are then deemed non-deductible on top of this, then landlords may be driven out of the business. The state would end up having to provide more accommodation (as occurred in the early 1990s, leading to the abandonment of ring fencing then).

Such situations are not good for investors, tenants or the State. So think very carefully of the consequences and inequalities of ring fencing being applied to residential property investments (particularly as they are not applied to other forms of business).

John Paynter MSc, BCom, JP

I am happy to meet the Working Group to discuss this issue and provide documentation of practical examples where legitimate losses have occurred in the past or may occur in the future.