Interest deductibility proposals at a glance

The Government intends to limit the ability to deduct interest to make residential properties a less attractive investment option and to help level the playing field for first home buyers.

The proposal is that, from 1 October 2021, interest will not be deductible for residential property acquired on or after 27 March 2021. For properties acquired before 27 March 2021, generally investors' ability to deduct interest will be phased out between 1 October 2021 and 31 March 2025. Some properties are excluded from these rules and some exemptions are proposed.

This information sheet provides a quick overview of the proposals. These proposals will be considered by Parliament and may change.

Phasing out interest deductions for properties acquired before 27 March 2021

Date interest incurred	Percentage of the interest that can be claimed
1 April 2020 to 31 March 2021	100%
1 April 2021 to 30 September 2021	100%
1 October 2021 to 31 March 2022	75%
1 April 2022 to 31 March 2023	75%
1 April 2023 to 31 March 2024	50%
1 April 2024 to 31 March 2025	25%

Acquired date for tax purposes

For tax purposes, a property is generally acquired on the date a binding sale and purchase agreement is entered into (even if some conditions still need to be met).

An investment could also qualify for phased-out deductions even if they acquired the property on or after 27 March 2021 provided they did so as a result of an irrevocable offer made on or before 23 March 2021.

Full information on when a property is acquired can be found in QB 17/02 available on taxtechnical.ird.govt.nz

Generally, any residential investment property in New Zealand that is suitable for people to live in long-term will be affected by these proposed changes. Typically, this would mean a house or an apartment, whether it is used for providing short-term or long-term accommodation.

Exemptions

To minimise any impact on housing supply, property development and new builds will be exempt from the proposed rules.

For more information on this, see information sheet 4 – Exemptions for property development and new builds.

Types of property to be excluded from the changes

The main home is not affected by these proposals.

Commercial property unrelated to the provision of accommodation is not affected by the interest limitation proposal.

The following types of residential property are proposed to be excluded from the rules:

- Main home – the interest limitation proposal would not apply to interest related to any income-earning use of an owner-occupier's main home, such as a flatting situation.
- Farmland.
- Certain Māori land, papakāinga and kaumātua housing, and land transferred as part of a settlement under te Tiriti o Waitangi/Treaty of Waitangi.
- Emergency, transitional, social, and council housing.
- Commercial accommodation such as hotels, motels, and hostels (but not short-stay accommodation provided in a residential dwelling).
- Care facilities: hospitals, nursing homes, hospices, and convalescent homes.
- Retirement villages and rest homes.
- Employee accommodation.
- Student accommodation.
- Land outside New Zealand.

For more information on this, see information sheet 2 – Properties not affected by the interest deductibility proposals.

Exclusions for certain organisations

To reduce compliance costs, it is proposed that the interest limitation rules will not apply to most companies where their core business does not involve residential land. These are companies where residential property (including new builds) makes up less than half their total assets.

Companies where five or fewer individuals or trustees own 50% or more of the company (referred to as close companies) will generally have to apply the rules even if their core business does not involve residential land. An exception is proposed for close companies that are Māori authorities or wholly-owned by a Māori authority. Such companies are distinct from other close companies, as they are accountable to a larger member group.

Kāinga Ora and its wholly-owned subsidiaries are proposed to be excluded from the interest deductibility changes because they provide emergency, transitional and social housing.

For more information on this, see information sheet 3 – How the rules work for certain entities.

Will interest deductions be permanently denied in all cases?

Previously denied interest deductions may be available when residential property is sold if the sale is taxable, although the deduction may be limited to the gain on sale.

What is the process from here?

The proposals discussed here will need to be considered by the Finance and Expenditure Committee (a parliamentary select committee). As part of its process, the Committee will usually call for public submissions on the proposals. Typically there is a six-week submission period. The Committee will then usually make its recommendations to Parliament. The proposals presented in these information sheets may change as a result of the select committee and parliamentary processes.

To make a submission to the Committee, see www.parliament.nz/en/pb/sc/how-to-make-a-submission

Other information sheets on the proposals are available on Inland Revenue's tax policy website. Detailed commentary on the draft legislation will also be published shortly to help inform public submissions on the proposals.

This information sheet provides a brief description of the Government's proposals. It does not attempt to provide comprehensive coverage. For full details of the proposals refer to the Supplementary Order Paper.

Properties not affected by the interest deductibility proposals

This information sheet provides general information on the way that proposals the Government is introducing are likely to work.

Under existing rules, a person who owns a residential investment property is allowed to deduct the interest costs they incur from acquiring that property. This means that they can reduce the amount of tax they are required to pay. The Government intends to limit that ability to deduct interest to make residential properties a less attractive investment option and thus level the playing field for first home buyers.

Some properties, because of their physical structure or purpose, would not be affected by the proposed rules. This information sheet provides a quick overview of the types of properties **not** affected by the rules (so you will be able to deduct interest expenses for them where applicable).

These proposals will be considered by Parliament and may change.

The proposal

In general, any house, apartment, or other such building in New Zealand that a person could live in would be affected by these changes. Bare land that could be used for residential property will also be affected. It does not matter whether the property is rented out long-term, used for short-stay accommodation, or even left vacant.

You'll still be able to deduct interest for some properties

Certain properties will be unaffected by these rules. This means that if you satisfy the other requirements for claiming deductions, you will still be able to deduct interest for these properties.

Main homes are not affected by these changes. You generally can't claim interest deductions for private use, but if you use your main home to earn income (such as from a flatmate or boarder), you will be able to deduct some interest against that income.

Provided you meet the other requirements for claiming deductions, you will still be able to deduct interest against income from these unaffected properties:

- A portion of the main home if it is used to earn income (for example, from flatmates or boarders).
- Properties used as business premises (except for an accommodation business), like offices and shops. This includes residential properties to the extent they are used as business premises (for example, a house converted into a doctor's surgery).
- Hospitals, hospices, nursing homes, and convalescent homes.
- Retirement villages and rest homes.
- Hotels, motels, hostels, inns, campgrounds.
- Houses on farmland.
- Bed and breakfasts where the owner lives on the property.
- Employee accommodation.
- Student accommodation.
- Land outside New Zealand.

In addition, the proposals also include a land "business" exemption and a "development" exemption. For more information on this, see information sheet 4 – Exemptions for property development and new builds.

Māori collectively owned land and housing

The Government is proposing that land would not be affected by the proposals if it is collectively owned by a Māori authority (or entity eligible to be one) and used to provide housing to a member of the relevant iwi or hapū (papakāinga and kaumātua housing). Also unaffected would be land transferred as part of a Treaty settlement and certain types of Māori land title.

Emergency, transition, social, and council housing

If your property is used for emergency, transitional or social housing when you leased it to the Crown (for example, the Ministry of Housing and Urban Development or Kāinga Ora) or to a registered community housing provider then you can still claim interest deductions.

What if part of my property is affected and part is excluded?

If you own a piece of land which has both a residential property and excluded property on the same legal title such as a two-storey building with a shop on the ground floor and a flat on the top floor, you will still be able to deduct interest for the portion of the property which is excluded. You'll need to use a reasonable method to apportion the interest between the two.

This information sheet provides a brief description of the Government's proposals. It does not attempt to provide comprehensive coverage. For full details of the proposals refer to the Supplementary Order Paper.

How the rules work for certain entities

The Government intends to limit the ability to deduct interest to make residential properties a less attractive investment option to help level the playing field for first home buyers. The proposed changes are generally intended to apply to all property owners. However, specific proposals deal with how **companies, developers and social housing providers** will interact with the rules. This information sheet provides a quick overview of the rules relating to those property owners.

These proposals will be considered by Parliament and may change.

Companies

It is proposed that the rules will not apply to most companies whose core business does not involve residential land. This is intended to reduce compliance costs for such companies, as allocating interest costs may be difficult and costly for companies with many different types of assets and sources of funds.

Companies that do not have a core business involving residential property are unlikely to be adding to house price pressures. These are companies where residential property (including new builds) makes up less than half of their total assets.

However, companies where five or fewer individuals or trustees own more than 50% of the company (referred to as close companies) will generally have to apply the rules even if their core business does not involve residential property. This won't apply to close companies that are Māori authorities or wholly owned by a Māori authority (or entities eligible to be Māori authorities). Such companies are different from other close companies, as they are accountable to a larger member group (even if they are technically close companies because they are owned by a single trust).

Developers

Property developers will not be specifically exempted from the rules, but it is proposed that their development activity will be so that interest incurred on property developments will continue to be deductible. See information sheet 4 – Exemptions for property development and new builds.

Social housing providers

Registered community housing providers will generally not be affected by the rules. Many are charities and have an income tax exemption.

Community housing providers that are not tax exempt will also be unaffected by the rules to the extent they would apply to interest on properties used for emergency, transitional, social, and council housing.

Kāinga Ora also provides social housing but is not tax exempt. It is therefore proposed that Kāinga Ora and its wholly owned subsidiaries be excluded from the interest deductibility changes.

This information sheet provides a brief description of the Government's proposals. It does not attempt to provide comprehensive coverage. For full details of the proposals refer to the Supplementary Order Paper.

Exemptions for property development and new builds

The Government intends to limit the ability to deduct interest to make residential properties a less attractive investment option and thus level the playing field for first home buyers. To encourage the supply of new housing, the Government is proposing exemptions from the rules denying interest deductions.

This information sheet provides information on the land business exemption, the development exemption, and the new build exemption.

These proposals will be considered by Parliament and may change.

Exemption for business developing land

The **land business exemption** will apply for interest relating to land if you hold that land as part of a developing, subdividing, or land-dealing business, or a business of erecting buildings on land.

Interest relating to remediation work and other expenses from ownership and development of the land will also qualify if this exemption applies.

Exemption for other property development

If you do not qualify for the land business exemption, the **development exemption** will apply for interest relating to land that you develop, subdivide, or build on to create a new build. You can only deduct interest if existing tax rules allow you to, even if you qualify for the exemption.

The exemption will apply from the time you start developing the land and end when you sell the land or receive a Code Compliance Certificate (CCC) for your new build. Once your new build receives its CCC, the new build exemption will apply instead.

Interest relating to remediation work done to an existing property that is not significant enough to create a new build will not qualify for this exemption.

Exemption for new builds

What is a new build?

A new build will generally be defined as a self-contained residence that receives a CCC confirming the residence was added to the land on or after **27 March 2020.** It will also include a self-contained residence acquired off the plans that will receive its CCC on or after **27 March 2020** confirming it has been added to the land.

A new build will not have to be made of new material or constructed onsite, so it can include modular and relocated homes.

If you convert an existing dwelling into multiple new dwellings, this can qualify as a new build. So too can converting a commercial building into residential dwellings.

When does the new build exemption begin?

The new build exemption will apply to allow you to deduct interest (provided it is deductible under existing tax law) from the dates:

- you acquire your new build – if it already has a CCC or you acquire it "off the plans", or
- your new build receives its CCC.

Expiry of exemption for new builds

The exemption will expire 20 years after a new build receives its CCC or when the new build ceases to be on the land (for example, it is demolished or removed), whichever is earlier.

Where a new build is acquired off the plans and before its CCC is issued, the 20-year fixed period will still run from the date of the CCC. Special rules also apply for hotel/motel conversions, and for new builds that receive their CCC after a significant delay.

The exemption will apply to anyone who owns the new build within this 20-year fixed period, and the timing of the exemption will not reset when the property is sold.

This information sheet provides a brief description of the Government's proposals. It does not attempt to provide comprehensive coverage. For full details of the proposals refer to the Supplementary Order Paper.

How interest deductions are affected

This information sheet provides general information on the way that proposals the Government is introducing are likely to work.

The Government intends to limit the ability to deduct interest to make residential properties a less attractive investment option and thus level the playing field for first home buyers.

For property investors who borrowed to acquire residential property before 27 March 2021, interest deductions will be phased out between 1 October 2021 and 31 March 2025 as shown in the table. Residential property investors who borrow to acquire residential property on or after 27 March 2021 will not be allowed to deduct interest incurred after 1 October 2021 (unless an exception applies). Certain exemptions apply and certain property types are excluded.

This information sheet provides general information on what interest is proposed to be either phased out or become immediately non-deductible from 1 October 2021.

These proposals will be considered by Parliament and may change.

Phasing out interest deductions for properties acquired before 27 March 2021

Date interest incurred	Percentage of the interest that can be claimed
1 April 2020 to 31 March 2021	100%
1 April 2021 to 30 September 2021	100%
1 October 2021 to 31 March 2022	75%
1 April 2022 to 31 March 2023	75%
1 April 2023 to 31 March 2024	50%
1 April 2024 to 31 March 2025	25%

Date property acquired

For tax purposes, a property is generally acquired on the date a binding sale and purchase agreement is entered into (even if some conditions still need to be met). Full information on when a property is acquired can be found in QB 17/02 on taxtechnical.ird.govt.nz

Funds borrowed on or after 27 March 2021

If you borrowed funds on or after 27 March 2021 for your property, interest deductions will no longer be allowed from 1 October 2021 except if you used those funds to purchase property acquired:

- before 27 March 2021 (for example, you entered into an agreement but settlement was in May 2021), or
- as a result of an offer you made before 24 March 2021 that you weren't permitted to withdraw before 27 March 2021 (for example, as part of the contractual terms and conditions in a tender process).

If either of these exceptions applies, your ability to deduct interest will be phased out according to the table above.

Note: If one of the exemptions for property development or new builds applies your interest deductions will not be limited under the proposed rules. For more information on this, see information sheet 4 – Exemptions for property development and new builds.

Refinancing on or after 27 March 2021

Refinancing up to the level of the original loan will not affect the deductibility of your interest. If the original loan qualified for phasing out, then that treatment remains the same.

Variable loans, such as a revolving credit or overdraft

Deductions for interest on a variable loan will also be phased out as per the table above. This is provided the amount outstanding (after subtracting any expenditure on deductible or private activities) is the same or lower than the amount that was outstanding on 27 March 2021.

If the amount outstanding is higher than the amount outstanding on 27 March 2021, only interest on the amount outstanding on 27 March 2021 will be deductible under the phased approach. Interest on the remainder of the amount outstanding will be non-deductible.

Borrowing used for other purposes

The interest limitation rules will not affect borrowings for non-residential property purposes. For example, if you borrow against a residential property to buy a truck for a transport business, your interest deductions will not be affected.

If you took out a loan before 27 March 2021 and cannot work out how much of the loan was used for residential property and how much was used for other business property, a special transition rule will apply. Under that transition rule, the loan will be treated as being used to acquire your other business property first (based on the market value of that business property) and then the balance will be applied to the residential property.

Property rented out and also used privately

The interest limitation rules will apply to interest relating to residential property that is rented out some of the time and used privately some of the time. This is the case with many holiday homes. Interest expenses for such properties will be entirely non-deductible from 1 October 2021 unless the interest qualifies for the phased approach because the loan is a pre-27 March 2021 loan (as discussed above).

The interest limitation rules will not apply if the interest relates to income you earn in your main home, for example, from a flatting or boarding situation. You will still be able to deduct some interest against that income.

Changes in how property is held

Proposed rollover relief will allow you to change how you hold the property after 27 March 2021 but still allow you to deduct a portion of your interest expense during the interest phase-out period.

Relief will be provided for some transfers to family trusts and for transfers to or from look-through companies and partnerships. This is consistent with the relief proposed for the bright-line test. Specific relief is proposed for transfers of land subject to the Te Ture Whenua Māori Act 1993 and transfers to trusts as part of settling Treaty claims.

Relief will also be provided for relationship property settlements and transfers on death. This is in line with existing rollover relief provided under the bright-line test.

This information sheet provides a brief description of the Government's proposals. It does not attempt to provide comprehensive coverage. For full details of the proposals refer to the Supplementary Order Paper.

Changes to the bright-line property rule

This information sheet provides general information on the way that proposals the Government is introducing are likely to work.

Along with proposals to limit the deductibility of interest, the Government has also proposed the following changes to the bright-line property rule:

- a 5-year bright-line property rule for new builds acquired on or after 27 March 2021
- changes to the main home exclusion to ensure the main home is not taxed
- changes to how technical transfers of ownership are handled

This information sheet provides a quick overview of these proposals. These proposals will be considered by Parliament and may change.

The bright-line property rule means that if you sell a residential property you have owned for less than a specified period, you may have to pay income tax on any gain. The bright-line period that applies depends on when the property was acquired:

When the property was acquired	The bright-line period that applies
On or after 27 March 2021	10 years
Between 29 March 2018 and 26 March 2021 inclusive	5 years
Between 1 October 2015 and 28 March 2018 inclusive	2 years

For more information see the property section on Inland Revenue's website at ird.govt.nz/property

New build bright-line property rule

If you acquire a "new build" on or after 27 March 2021, then a new 5-year bright-line property rule will apply (instead of the 10-year bright-line property rule). You must meet these requirements:

- You must acquire the new build no later than 12 months after it receives its code compliance certificate (CCC).
- Your new build must have its CCC by the time you sell it.

Generally, residential property will be considered a new build where a self-contained residence has been added to land, and it has received a CCC confirming this on or after 27 March 2020. Apart from the difference in length, the same rules that apply for the 10-year bright-line property rule will also apply for the bright-line property rule for new builds.

Changes to the main home exclusion

The main home exclusion currently ensures the bright-line property rule does not apply to residential land if you use more than half the land for a main home.

However, the exclusion doesn't apply if you use less than half the land for a main home. This means that if you use most of the land for a residential rental property and only have a small main home portion, and then you sell your land during the bright-line period, any gain on sale will be taxed. This happens even though you have a main home on the land.

The Government proposes to change the treatment where the main home portion is smaller than the rental property, so that any gain on sale will be apportioned. The gain that relates to the periods the property is used as a main home will not be taxed under the bright-line property rule. The portion of the gain that relates to the rental property would be taxed. This change will apply to all property acquired on or after 27 March 2021. This means it would apply to both the 5-year new build and 10-year bright-line property rules.

Technical changes of ownership will not affect the bright-line property rule

Proposed rollover relief will allow you to change how you hold a property without triggering the bright-line property rule. When the legal ownership of a property changes but the effective ownership is the same, the transfer will be ignored if it is in one of the prescribed situations. This means the original owner will not be taxed on the realised gain on the property, and the new owner will be treated as having acquired the land when it was acquired by the original owner.

Relief will be provided for some transfers to family trusts and for transfers to or from look-through companies and partnerships. Specific relief is proposed for transfers of land subject to the Te Ture Whenua Māori Act 1993 and transfers to trusts as part of settling Treaty claims. This is consistent with the relief proposed for interest limitation purposes.

Rollover relief will only be provided if the amount received on transfer is equal to or less than the original owner's acquisition cost. No relief will be provided if the amount received is more, but the original owner will be taxed based on that amount if it is different to the market value of the property.

The rollover relief will apply to disposals of residential land occurring on or after 1 April 2022, even if the original date you acquired the property was before the introduction of the bright-line property rule.

This information sheet provides a brief description of the Government's proposals. It does not attempt to provide comprehensive coverage. For full details of the proposals refer to the Supplementary Order Paper.