

# The Treasury

## Budget 2015 Information Release

### Release Document July 2015

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- [1] 6(a) - to prevent prejudice to the security or defence of New Zealand or the international relations of the government
- [2] 6(c) - to prevent prejudice to the maintenance of the law, including the prevention, investigation, and detection of offences, and the right to a fair trial
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- [9] 9(2)(g)(i) - to maintain the effective conduct of public affairs through the free and frank expression of opinions
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- [12] 9(2)(j) - to enable the Crown to negotiate without disadvantage or prejudice
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- [14] Not in scope

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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.

Reference: T2015/981

SH-13

Date: 8 May 2015

To: Minister of Finance  
(Hon Bill English)

Deadline: 8 May 2015  
(if any)

## **Aide Memoire: Application of new RBNZ asset classification and new IRD bright-line test**

Ministers have asked whether the definitions of dwelling use that will be applied by the RBNZ for asset class treatment of residential loans and the IRD for the brightline test will be the same or at least broadly aligned.

The RBNZ definition separates loans to **owner-occupiers** from other residential property investment loans. The distinction is designed to identify non-owner occupiers for capital purposes as they are seen as being worse credit risks in downturns. The definition is forward looking and is applied at the time of the application of the loan based on the stated use by the applicant. The LVR restriction would apply to the non-owner occupier loans in Auckland.

The IRD brightline test is proposed to tax all gains on residential property that is sold within two years of purchase unless the property was mainly used as the **principal residence** of the taxpayer. Any other residential property owned by the taxpayer would be subject to the brightline test. It will be backward looking and consider the actual use of the property over the time the taxpayer has owned it. It would apply irrespective of whether there was a mortgage on the property or was owned mortgage-free.

RBNZ, Treasury and IRD have discussed the definitions. They are not completely identical, for two key reasons:

- they need to be measured at different stages (before purchase or refinancing for the RBNZ test, after sale for the IRD test). The key RBNZ test will be borrower intention, while IRD can look backward at actual use.
- the RBNZ test needs to apply to all the mortgage borrowing a customer has at a bank, while the IRD test applies to individual properties.

For the majority of households, the definitions will align:

- It is likely that owner-occupiers with a mortgage under the RBNZ definition will be living in their primary residence for the purposes of the IRD's brightline test.
- It is likely that residential rental properties with a mortgage would be classed as investor (non-owner occupier) loans under the RBNZ definition and if the property was sold within two years, it would be deemed to be not the principal residence of the taxpayer for the purposes of the brightline test.

There will be some differences in application for more complicated cases:

- Unrented city apartments and baches – these are likely to be treated as being owner-occupied for the purposes of the RBNZ asset classification but would not be the primary residence of the taxpayer for the purposes of the brightline test.
- Dwellings where the use has changed – if an owner-occupier decides to rent out their house and live elsewhere, the bank may not record the change of use and continue to classify the mortgage as owner-occupied. However, the IRD would consider the actual use when assessing whether the dwelling was the taxpayer's principal residence if it was sold within 2 years.
- If an owner-occupier uses their house as collateral for the mortgage on a rental property, the loans on both properties would be treated as being investor loans by the RBNZ test. For the purposes of the brightline test, the principal residence would be excluded but the rental property would not.

If Ministers are wanting some simple communication messages to explain the differences we suggest the following:

- For the majority of people, the two tests are aligned.
- In a handful of more complicated cases, such as unrented baches and city apartments, or where collateral is spread over more than one property, transactions may meet one of the definitions of an "investor" but not the other.
- These differences are entirely appropriate given the purposes of the tests.

## **Consultation**

Inland Revenue and the Reserve Bank have been consulted and agree with the contents of this Aide Memoire.

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