The Treasury

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TE TAI ŌHANGA
THE TREASURY

Date: 12 February 2021

To: Minister of Finance (Hon Grant Robertson)

Deadline: None

Taxation of vacant land and vacant dwellings

Executive summary

1. You asked for a summary of the case for and against implementing taxes on vacant land and dwellings. Given time constraints, this paper provides a summary of work that was previously undertaken, drawing primarily on work prepared for the Tax Working Group (TWG) and a Productivity Commission report.[1]

2. Taxes on vacant land or dwellings are typically proposed as a means of increasing housing supply. A tax on vacant dwellings would increase the holding cost to the owner, helping to incentivise them to either rent out their house or sell it to someone who does rent it out, increasing the supply of available housing. Similarly, a tax on vacant land would incentivise the owner of underutilised or vacant land to either develop that land or sell it to someone who will. This could lead to vacant land being used in more intensively in the near-term, potentially leading to more housing developments.

3. As described below, both vacant land and vacant dwelling taxes are reasonably complicated to design. Their implementation requires difficult judgements about the meaning of vacancy and the scope of exemptions. The outcome of those decisions could impact the tax's effectiveness, as well as the ease with which it could be avoided. Limited data on the scale of the problem makes it difficult to quantify the impact these taxes would have on housing supply.

4. Should the Government wish to implement such a tax, the rate would need to be high enough to prompt behavioural change. Implementation and enforcement of a vacant land or dwelling tax is likely to be administratively costly and to increase compliance costs.

5. Moreover, the Productivity Commission concluded that a vacant land tax could reduce housing supply in the longer-term. There are reasons to think vacant land taxes may not be an effective tool for encouraging intensification, although thinking in this area is preliminary and ongoing.

6. The TWG noted that a few countries do tax vacant land or vacant dwellings, but that there is relatively little evidence to suggest that those taxes have increased housing supply. The TWG observed that this may be because the tax rates are too low. There is, however, some evidence (for instance, from Vancouver) that

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1 Taxing vacant property: Position paper for Session 23 of the Tax Working Group, 22–23 November 2018, available at https://taxworkinggroup.govt.nz/sites/default/files/2019-02/twg-bg-4037441-taxing-vacant-property.pdf; and New Zealand Productivity Commission. (2019). Local government funding and financing: Final Report. Available from www.productivity.govt.nz.

vacant dwelling taxes can reduce vacancy rates. **Annex 1** contains a summary table with examples of vacant land and dwelling taxes from around the world.

Taxes on vacant land

It is difficult to assess the impact of a vacant land tax given limited data

7. There is little official nation-wide data on the scale of vacant land in New Zealand. Measuring vacant land is challenging, partly because it involves value judgements about how to define what land is 'vacant' for the purpose of the tax. One mechanism is to identify only vacant land that has already been zoned for residential use. An Auckland City Council report in September 2014 identified a pool of over 5,000 vacant residentially zoned sections within the built-up area of Auckland, approximately 65% of which had been vacant since before 2007.[2]

8. In addition to data on the number of vacant properties, it is also important to understand the reasons why land is vacant. Without this information, it can be difficult to estimate the potential impact of taxing vacant land. Data on the reasons for vacancy would also inform design decisions on the need for (and impact of) exemptions. Yet there is limited data at present to explain why land in New Zealand is vacant.[3]

A tax on vacant land would be reasonably complicated to design

9. A tax on vacant land is intended to raise the cost for landowners, discouraging land banking and incentivising owners to either sell or develop vacant land. Designing such a tax involves several important design decisions, the outcome of which may impact the tax's effectiveness in increasing supply.

10. Should the Government wish to implement a vacant land tax, decisions would be needed on the following design matters:

    a. **Defining vacant land**. This requires identification of current land uses (for instance, public green spaces or carparking) that are less valuable than the provision of dwellings. It is likely to be difficult to strike the right balance: the Productivity Commission noted a narrow definition would enable speculators to easily switch to un-taxed types of land; a broad definition, while better constraining speculative investment, could increase risks and costs for developers and negatively impact the land development process. There may be opportunities, however, to rely on pre-existing zoning.

    b. **Scope of exemptions**. It would be necessary to define exemptions (which is likely to include land for sale or subject to development) and to define the period for which the land must have been subject to its current use. Exemptions are necessary but they risk resulting in suboptimal outcomes, including token uses of land to avoid the tax.

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2 Long-term Vacant Residentially Zoned Land in Auckland: Reasons for Prolonged Land Vacancy and Development Potential, September 2014, Technical report 2014/022.

3 There appears to be little systematic information, both domestically or internationally, that might assist New Zealand policy makers to clearly understand the reasons behind long-term vacant property. Auckland Council conducted interviews with 29 owners of long-term vacant residential land and found various reasons for the lack of development, including inadequate offers for sale, compliance and development costs, and owners considering they were better off speculating on capital gains.

c. **Value judgements about land use**. In the past, vacant land taxes were premised on certain cultural assumptions about 'appropriate' uses of land. Historically such taxes were used to justify the taking of Māori land.

11. A vacant land tax may be costly to implement due to the following requirements:

a. **Establishing and maintaining a register of vacant land**. Implementing a vacant land tax requires up-to-date information on land use and occupancy. Currently there is no single source of information on residential property ownership, land use, land zoning and local housing market conditions. Maintaining a register would likely involve compliance and administrative costs, especially in dynamic property markets.

b. **Monitoring and compliance** are likely to be challenging and costly, particularly given the number of exemptions that tend to apply. A vacant land tax will potentially reach many landowners who will need to consider their tax liability, even if they are not ultimately liable to pay the tax.

12. Should the Government wish to proceed with a vacant land tax, the tax rate would need to be sufficient to incentivise owners to change from their existing use of land. A common criticism of vacant land taxes is that their rate is too low. The Productivity Commission considered the rate would probably need to exceed 5% of the land's value (one jurisdiction has adopted a 30% rate). Historically, a 5% rate is very high: 10 to 20 times higher than typical property rates in New Zealand.

There are reasons to think a vacant land tax may not increase housing supply, particularly in areas that seek greater intensification

13. As noted above, a tax on vacant land is intended to raise the holding cost for landowners, discouraging land banking and incentivising owners to either sell or develop vacant land. It carries some risk, however, because the tax incentivises landowners to construct dwellings earlier in time than they otherwise would have. A landowner that is uncertain about the net return of a development may be more inclined to opt for lower cost projects (for instance, construction of one standalone dwelling) over a more intensive and more costly development. Accordingly, a tax on vacant land – which attempts to bring forward the construction of dwellings – may preclude the opportunity for more intensive development later in time

14. The Productivity Commission also highlighted the risk that vacant land taxes could reduce housing supply longer-term. Although a vacant land tax could help reduce land banking and increase housing supply in the near term, the Commission considered these effects were likely to be "small and transitory".[4] Vacant land sits in an intermediate stage in the property development process and helps to deal with uncertain and fluctuating demand. The Commission took the view that a vacant land tax would impede the development process and "would likely reduce housing-supply responsiveness by reducing developer flexibility and risk-taking".

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4 Work commissioned by the Productivity Commission estimated that 70–90% of vacant residential land in Auckland could be excluded from the tax. It found the first-round impact is likely to be transitory because increases in land supply would largely occur only for the period that stocks of vacant land are being reduced to their new (after-tax) chosen levels.

15. That said, it may be possible to mitigate this risk through design of the tax. There may be opportunities to design the tax (potentially through the inclusion of tax rebates) to mitigate potential negative impacts on supply.

Taxes on vacant dwellings

Data on the scale of the problem is limited

16. It is challenging to quantify the number of unoccupied dwellings. 2018 census data suggests that there were 191,646 unoccupied homes nationally. The proportion of unoccupied homes decreased across most major centres between 2013 and 2018, although the proportion in Auckland increased from 6.6% to 7.3%.

17. The census data, which includes property subject to repair and holiday homes, may overstate the number of empty homes. An alternative MBIE/Vector study that quantified the number of vacant dwellings using electricity connections classified 8,000 Auckland homes as vacant in 2015.[5] This represented around 1.6% of all dwellings in the Auckland Region, well below the figure from either of the 2013 or 2018 census. Further work on quantifying the number of vacant dwellings is ongoing by both the Ministry of Housing and Urban Development and Ministry of Business, Innovation and Employment.

18. In addition to the number of vacant dwellings, it is important to understand the reasons dwellings are vacant. Advocates for vacant dwelling taxes have an implicit rationale that the dwellings are vacant for a specific reason (that land bankers have decided not to tenant the dwelling). But if a large proportion of dwellings are vacant because they are holiday homes, or are scheduled for demolition and intensification, the number of houses subject to the tax may be limited. Without data on the reasons for vacancy rates, it is difficult to assess the impact such a tax would have on housing supply.

19. There is, at present, limited data on the reasons for vacant dwellings in New Zealand. Studies from Italy, Australia and Ireland suggest there are a wide range of reasons, cultural, economic and other, that explain why dwellings are left vacant.[6] It is also important to note that in housing markets there will always be some level of vacant property. A three percent vacancy rate is generally considered to represent a market in equilibrium, where nominal rent growth follows the rate of inflation.[7]

A tax on vacant dwellings would be reasonably complicated to design

20. Much like a tax on vacant land, a tax on vacant dwellings would also entail complex design decisions, including the following:

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5 Vector classified a dwelling as 'unoccupied' on any given day if it used less that 400W per day. From this base, Vector classified a property as vacant when it is unoccupied for at least 100 consecutive days.

6 From Italy: Houses without people and people without houses: a cultural and institutional exploration of an Italian paradox, March 2018, Gentili, M, and Hoekstra, J., Housing Studies; from Australia: Why no one was home on Census night, SGS Economics and Planning, Article July 2017; from Ireland: Indecon Report on the Taxation of Vacant Residential Property, September 2018, prepared for the Minister of Finance.

7 Speculative Vacancies 8 *The Empty Properties Ignored by Statistics* (2014), Cashmore, C., Prosper Australia at 37.

a. **Defining "vacant" property**. The general approach to taxing vacant dwellings is a time-based test to define vacant property, to ensure property owners could not avoid the tax by renting their otherwise vacant property for short periods. For example, the tax applies if a property is vacant for more than six months in a twelve-month period. There remain questions at the boundary, for instance, whether there should be an exemption for holiday homes, or whether a second home, intended to be a future principal residence after retiring, would be within scope. Some exemptions are likely to be necessary, but risk creating opportunities for avoidance.

b. **Establishing and maintaining a register of vacant dwellings**. There seems to be a range of different approaches to create registers of vacant property, but all involve some sort of monitoring and audit activity. Doing this would likely involve high administrative costs and challenges, particularly in a dynamic local property market.

c. **High administration and compliance costs**. Experience overseas suggests that vacant dwelling taxes have a high cost per dollar of revenue raised.[8]

21. If the Government wished to proceed with a vacant dwelling tax, the tax rate would need to be sufficiently high to incentivise owners to change from their existing use of land (which may be a particular challenge where an owner has made the decision to forgo rental income by leaving a dwelling untenanted).

A vacant dwelling tax could have longer-term impacts on supply

22. As noted above, the Productivity Commission concluded that a vacant land tax could have negative impacts on housing supply longer-term. A similar argument could be made against a vacant dwelling tax. Properties may be vacant for sound reasons related to development (e.g. prior to demolition and intensification); as above, it may be possible to mitigate this risk through the tax's design.

23. It would also be necessary to consider the interaction between vacant dwelling and vacant land taxes. Taxing vacant dwellings only could incentivise owners to demolish dwellings that may have otherwise been tenanted, if owners risked facing tax liability for the periods where the dwelling was untenanted.

24. The evidence above on the number of vacant dwellings (particularly the Vector/MBIE study) suggests a vacant dwelling tax is unlikely, at least on its own, to substantially increase housing supply. Should evidence emerge of a substantial increase in the vacant dwelling numbers, the case for such a tax may strengthen.

Juliet Bull, Analyst, Tax Strategy, [39]
Felicity Barker, Team Leader, Tax Strategy, [39]

8 The Productivity Commission referred at 191 to Vancouver's vacant-dwelling tax. In 2017 it spent C$2.5m administering the regime, which amounted to 12% of the C$20.6m revenue collected. In addition, it spent C$7.5m implementing the new regime. By comparison, the cost of administering the overall New Zealand tax system is less than 1% of revenue collected.

ANNEX 1:

Tax Working Group's summary of overseas examples and experiences

25. In many countries housing shortages have emerged, particularly in key cities. A World Bank review of vacant land taxes around the world shows that various governments have different ways of defining, identifying, and prioritising vacant land; of structuring vacant land fees; of choosing an implementation mechanism; and of deciding who benefits from the fee and how, as well as the various penalties to be imposed in the absence of required payment. There are also differences in prioritising how to apply the taxation—whether by location, time left vacant, or degree of development.

26. While most countries do not appear to have vacant property taxes, a few countries or cities do. The following table summarises examples of a vacant land tax and vacant dwelling taxes from some jurisdictions broadly comparable to New Zealand. The table briefly describes the tax, the relevant definition of vacant property and whether the measure is working in terms of encouraging the supply of housing.

	Measure	**Definition of "vacant"**	**Effect of the measure**
Ireland	In 2018 the levy rate was increased to 7% (from 3%) of the market value of the vacant land. Responsibility for identifying land to put on the vacant land register is delegated to the local planning authorities.	The levy applies to vacant or idle land, suitable for the provision of housing and situated in an area where there is a need for housing. The site must exceed 0.05 hectares (excluding a home and its associated garden) in order for the levy to apply. The levy only applied to land zoned solely or primarily for residential purposes ("Residential Land") and land designated with the objective of development and renewal of areas in need of regeneration ("Regeneration Land"), regardless of who owns it. In 2018 a change was made to exclude property that was sold during the year.	Legislation was passed in 2015, but the levy was not applied until 2018. As at 1 January 2019, 140 properties were subject to the charge. The main reasons for this small number were: • administrative difficulties in local planning authorities implementing the legislation • in many counties it is not clear which land, if any, could be deemed suitable for development for residential and regeneration purposes As the levy has not been in effect for long, there is no evidence of the effect on housing supply.
Melbourne; Australia	1% tax on the capital improved value of a vacant dwellings from January 2018. This tax is administered by Victoria's State Revenue Office.	A dwelling, within Melbourne's inner and middle suburbs, that is occupied for less than 6 months in a calendar year and is not an individual's principal private residence. Exemptions from tax include: • Death of owner • Construction or renovation • Change of ownership	We could not find any evidence of how much tax has been charged or paid in 2018. It is also not currently possible to say what effect this tax had on the Melbourne housing market.

		Properties occupied for at least 140 days for the purpose of working in Melbourne.	
Vancouver; Canada	1% tax on the value of the empty home from 2017. Increased to 3% for 2021. Enacted and administered by the City of Vancouver.	Home not used as a principal private residence; and or has not been rented out for a minimum of six months in a given year. A number of exemptions apply, including: • Home sold during the year • Renovation or redevelopment • Strata restrictions on renting property • Death of owner	The property status in Vancouver for the 2017 tax year (as at November 2018) was: Occupied – 178,120 Exempt – 5,385 Vacant – 2,538 Note that census 2016 recorded over 25,000 homes were vacant. Data released by the city Government showed a 25% reduction in the number of vacant dwellings between 2017 and 2019.
France	Surcharge on second homes in areas in France that face a housing shortage, which has applied from 2014 on the notional rental value for the property. Local councils can charge a rate of between 5% and 60%	The tax applies to secondary homes which are not registered as owner or occupier's principal private residence. Those who hold a second home for business or professional reasons are exempt, as are landlords who ordinarily let out a property on an annual basis.	There has been limited evidence of the impact of the vacant homes tax in France. The fact that the original tax, which was capped at a 20% surcharge, was reformed in 2017 to allow for a surcharge of up to 60% indicates that the initial tax was not having the desired impact on vacancy rates in the areas of the greatest degree of housing market pressure in France.