4 April 2019

Steven Bailey
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By Email: steven.bailey@productivity.govt.nz

Dear Steven

LOCAL GOVERNMENT FUNDING AND FINANCING – ISSUES PAPER (NOV 2018)
TOURISM INDUSTRY AOTEAROA SUBMISSION #2

Introduction

Tourism Industry Aotearoa (TIA) appreciates the opportunity to provide further information in response to your Issues Paper on local government funding and financing. This letter follows our first submission to the Commission on 15 February 2019 which provided detailed commentary responding to the issues identified by the Commission.

We concur that there are regions under pressure from tourism growth and the current funding systems are inadequate to manage that growth. Other regions want to attract more visitors but have limited financial ability to do so. To support a solution-driven approach we have since February undertaken a programme of work to identify a preferred regional funding model. This letter details the outcomes of that work and we are grateful to the Commission for agreeing to receive our findings for consideration into their Draft Report due for release in June 2019.

Process

At its 29 November 2018 meeting, the TIA Board agreed to undertake a project to identify a preferred regional funding model to support long-term local government funding and investment. After considering different ways to undertake this work a Design Sprint approach was adopted, which ran in Wellington over the week 11-15 March 2019, facilitated by CreativeHQ. A core group of eight industry leaders representing tourism operators and local government came together for the week to develop and test regional funding prototypes. The process included interviews with 20 experts across industry, local government and central government. The Design Sprint process was not guaranteed to identify a preferred regional funding model. What was more assured is that we would be better informed about regional funding options.

The Design Sprint team decided a national solution was needed and that for it to be of a size that could have meaningful impact, a funding stream of more than $200m p.a. was needed. In comparison the new International Visitor Conservation and Tourism Levy, to be introduced in July 2019, will raise $80m p.a. The government's current Tourism Infrastructure Fund provides $25m p.a.

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The Design Sprint process allows for all ideas to be considered. The team identified more than 30 possible models for directing funding to local government for regional tourism initiatives. These models were tested and rejected if they were unfair, insufficient, unworkable or the technology did not yet exist to make them possible.

Agreement was reached on a distribution system, which would effectively allocate any available funds (see further below). In terms of a collection system, several options were shortlisted and vigorously tested. One option was selected for socialising with five selected stakeholders. Further analysis and comment was sought immediately following the Design Sprint to inform a discussion by the TIA Board.

TIA Preferred Funding Model

The TIA Board met on 20 March to consider the prototypes developed through the Design Sprint. The Board concluded that the investigation had been extremely useful, but had reinforced its view that the cleanest and fairest method for collecting a contribution from visitors is the GST system. To commit a small portion of the GST take from international visitors to be redistributed to local government to address local issues, remains the most logical approach.

International visitors currently pay $1.7 billion p.a. in GST, collected by central government as part of the overall GST-take. While it might be argued the government already returns a portion of this to the industry via current tourism-related funds such as the Tourism Infrastructure Fund and Provincial Growth Fund, both are short-term solutions.

It is the recommendation of the TIA Board that central government annually sets aside 20% of the GST collection from international visitors and redistributes this to local government in accordance with the tourism burden borne by each TLA. The distribution could be via a Trust, with funds allocated in direct proportion to visitor impact.

Regional funding model options

While the Board did not endorse any of the shortlisted collection systems developed in the Design Sprint, it is worthwhile providing a summary for the Productivity Commission. The options are listed in order of preference of the Design Sprint team.

<u>Collection system</u>

1. A Tourism Tax of 2.5% collected from international visitors through the GST system. This would effectively create a two-tier GST system – 15% for New Zealanders (no change) and 17.5% for international visitors. Based on the current annual GST collection from international visitors of $1.7b, this would raise an additional $280m a year. The advice received was that while the GST differential of 2.5% is technically achievable there would be significant push-back from IRD on any proposals to change the GST system. In addition there was concern from industry operators about the continual reminder international visitors would get at each purchase that they were paying a tax differential while in New Zealand, negatively impacting on their experience.

2. A Foreign Exchange transaction tax on all purchases in New Zealand by overseas visitors (and possibly on all pre-visit purchases of New Zealand travel products). Based on an annual in-country visitor spend of $11.2b, a 2% tax would raise $220m. This

option was the 'invisible tax' – most visitors would not notice they were paying it. A serious flaw in this model was the ability to enforce the charge. The advice received was that credit card companies can move where they perform the currency exchange and there is no way for the receiving New Zealand bank to enforce a "fee" onto the payer's side of the transaction.

3. A Departure Tax on all international visitors based on the number of days spent in New Zealand. Based on 73 million stay days pa, a $3 per day tax would raise $220m pa (if Australian visitors are included). A departure tax is a common form of tax around the world. However there was concern about having more taxes at the border. There is the existing Border Clearance Levy (BCL), the incoming International Visitor Levy (IVL) and other charges which already make our border one of the most heavily taxed in the world. If the IVL was used as the mechanism, it would have to increase to more than $100 because it excludes Australians and Pacific Islanders, which would cause brand damage and deter significant numbers of visitors from coming to New Zealand.

4. An accommodation levy or 'bed tax' was investigated. Levying a tax on commercial accommodation is relatively easy, and technology may now allow this to be extended to some peer to peer accommodation like Airbnb. Queenstown District Council are currently in the process of undertaking a community referendum to gauge support for introducing a bed tax of between 5% - 10%. However, a bed tax unfairly targets one sector, who host only a proportion of total visitors. Only 30% of international visitors stay in commercial accommodation, and even including Airbnb that number would be less than 40%. A bed tax misses those who stay with friends and family or freedom camp. A bed tax is also paid by more New Zealanders than international visitors (23 million bed nights pa compared to 17 million bed nights for international visitors) and many New Zealanders feel they are already paying through existing taxes and rates.

The short-listed options all have pros and cons. Other than the bed tax, they all avoid imposing additional taxes on New Zealanders. They all raise considerable funds. All would undoubtedly put some people off from coming to New Zealand, so there would be some revenue leakage. To different degrees they are open to avoidance. On further investigation there may be fatal flaws (e.g. an inability for New Zealand to place a tax on Australians that New Zealanders are not required to pay). And all would require commitment by Government and Parliament to a unique solution.

<u>Distribution system</u>
The Design Sprint team identified a distribution system that it believes would work effectively with whatever funding source is made available. The basic features of the system are:

- At least $200m per year is collected by the Government (most likely by IRD).
- The funds as they are collected are immediately passed through to a Trust.
- The Trust has four members all appointed by the Government; an independent Chair, one trustee nominated by LGNZ, one trustee nominated by TIA and one government nominee.
- The Trust has 3-4 staff, including a Finance and Investment Manager.
- The Trust invests the funds as they are received and adds the interest and other earnings to the funds.
- The overhead costs for the Trust are intended to be less than 1%. 99% of its funds will be distributed.

- The Trust adopts an algorithm for allocating the funds based on the impact of visitors. Initially, this could be the Commercial Accommodation Monitor, which indicates where visitors, domestic and international, spend the night. It may be possible to complement this with a measure of peer-to-peer accommodation like Airbnb. A more accurate measure of visitor impact could be developed by using mobile phone data to create 'heats maps' showing where visitors spend their time.
- The recipients of the funds would be the 67 territorial local authorities. The TLAs would be encouraged to form regional groupings to receive the funding, but the entitlement would remain with the TLA.
- The TLAs would be expected to have committed to a Regional Destination Plan; if no Plan is in place, funding could be withheld. The TLAs would have to spend the funds to achieve the aims of the Regional Destination Plan but otherwise would be unrestricted.
- The TLAs would receive an estimation by 1 February each year of the annual funds they are likely to be allocated, so that they can build it into their planning processes.
- The funds would be paid out annually on 1 July.
- The Trust would issue an Annual Report detailing how the funds had been distributed and spent.

Conclusion
TIA has explored a wide range of options on how tourism can help address local government funding needs. Providing local government with a share of the GST paid by international visitors is seen by TIA as the most effective, efficient and fairest approach. Distributing these funds through a Trust and aligning the spend to Regional Destination Plans are suggested features of any funding model.

Should you require any further information please do not hesitate to contact me.

Yours sincerely

Chris Roberts
Chief Executive

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