



tourism
INDUSTRY

ASSOCIATION NEW ZEALAND

**The case against 'bed taxes': a tourism
industry perspective**

July 2005

About Our Association and Industry

The Tourism Industry Association New Zealand (TIA) represents the interests of over 2,000 businesses in the tourism or visitor industry.

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Tourism is a \$17.2 billion industry and generates 18.5% of New Zealand's exports. It employs 1 in 10 New Zealanders in a diverse range of businesses – the vast majority of which are small and medium sized enterprises. Not only is tourism important because of its size. As well as being 9.4% of New Zealand's GDP, it is also:

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- Highly employment intensive
- Regionally dispersed;
- Has the flexibility to change its target markets quickly as conditions change;

The tourism industry in New Zealand consists of more than 8,000 small and medium sized businesses. Of these businesses, most employ less than five people.

New Zealand welcomes almost two million overseas visitors to its shores every year. This is projected to increase to 3 million by 2010. The domestic visitor industry continues to drive the well being of the visitor industry overall and is much under estimated in terms its contribution to the economic well being of our regions. TIA estimates that over 75 million visitor nights are spent away from home by New Zealanders every year. *(Statistics are sourced from the Tourism Satellite Account, June 2005 and refer to the year ended March 2004)*

Purpose

The purpose of this report is to provide a discussion on tourism taxes, especially accommodation or 'bed taxes'. This document builds on and updates previous TIA analysis prepared between 2002 and 2003.

The report contains:

- Background on the recent history of bed taxes discussions in New Zealand
- A discussion about the nature of bed taxes and why they are proposed
- A discussion on the impacts of bed taxes drawing on overseas experience
- The approach that TIA recommends to local authorities seeking to fund necessary infrastructure and the facilities that tourism benefits from.

This report specifically focuses its discussion on 'bed taxes', and the issue of specifically targeting one particular sector within an industry such as accommodation businesses. 'Bed taxes' target a much smaller group of residents than tourism targeted rates and rating differentials which are already used in districts such as Wellington City, Queenstown and the Hurunui. 'Bed taxes' raise particular issues such as whether it is fair that services from which the wider community also benefits from should be paid by a narrow group of users, namely New Zealanders and other who

visit the region for business, conventions, events, to visit friends and relatives and, lastly, to holiday.

Background

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Tourism, international and domestic, is a significant source of economic activity and employment across regional New Zealand

The Local Government Rating Act provides the framework for local government funding powers in New Zealand. It provides local authorities with the ability to rate all ratepayers using a general rate, and it also enables councils to target particular rate payers for rates based on a range of criteria including the annual value of a property, the area of land it occupies and the area of floor space.

In 2002, when the Rating Act was still at the Bill stage, there was an attempt to include provision for a visitor stay rate (basically a bed tax) in to this piece of legislation. This was firmly opposed by the tourism industry as this sort-of rate specifically targeted a narrow area of tourism activity and would have captured only some visitors on overnight stays. This view was shared by the Labour Party as a coalition partner in the previous government, which rejected the ‘bed tax’ proposals.

Accordingly, a Supplementary Order Paper was prepared containing recommendations to remove this proposal. These recommendations were subsequently passed by Parliament.

Even though the visitor stay unit criterion was removed from the Bill, councils still have the ability to rate entire sectors under the Act. Councils such as Taupo, Wellington and Queenstown impose targeted rates and levies across the business community to cover the costs of marketing and promotion. This spreads the costs of these services over a larger number of ratepayers than narrowly targeted rates such as “bed taxes’ do.

However, there are still periodic calls from within local government for the Rating Act to be amended to provide for rates that specifically target the accommodation sector. This reflects the funding pressures that many local authorities are under to pay for high capital value infrastructure such as water and wastewater services.

Double taxing international visitors is not sustainable. The government already gains more than \$500m pa from international tourists because tourism is the only export sector to attract gst.

High levels of deferred maintenance motivate calls for ‘bed taxes’

The TIA report “Creaking Local Infrastructure” produced in September 2002 quoted the report of the Parliamentary Commissioner for the Environment titled “Ageing

Pipes and Murky Waters” which identified that there was \$5 billion¹ in deferred maintenance in the water and wastewater sector alone.

The Commissioner identified several issues behind this high level of deferred maintenance including:

- “consumers and ratepayers have increasing expectations about the provision and quality of water services but there is often a negative reaction to large rate increases or increased charges to fund required infrastructure”; and
- “lack of investment and deferred maintenance, in part through incomplete pricing and inadequate financial contributions from new developments”.

In essence, demands for high levels of service but a reluctance to pay for them lead to councils struggling to fund quality infrastructure. This, coupled with user charges (including water pricing and metering) being unpopular with local government politicians, lead councils to search for new opportunities to generate funding including tourism-targeted rates. Tourism is a visible and growing industry and frequent public statements by local politicians suggest some councils would support new provisions that would enable them to use mechanisms such as bed taxes.

This can create tensions between local government and tourism operators, despite the fact that TIA and the tourism industry overall has supported local government and has recognised the strong role it plays in facilitating sustainable tourism business activity.

The role of local government in tourism

Overall, there is a symbiotic relationship between tourism and local authorities and the communities they represent. Supportive communities enable tourism to flourish in local areas. Tourism provides significant employment and business activity and enhances the local rating base of local communities. Visitor growth potential can also be a catalyst for the development (and funding) of amenities and enhanced public spaces in local areas.

Overall, there are wide public benefits that accrue to local areas that support tourism. Councils exert considerable influence on the tourism industry by virtue of their funding powers and expenditure, the provision of infrastructure, their support of Regional Tourism Organisations and visitor information centres and their role in district planning and resource management.

TIA believes that local authorities can add value to the tourism industry where they:

- engage in fair and equitable rating practices and ensure that funding decisions lead to productive outcomes for all sectors of the community, including the business community

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- undertake activities that lead to high public good outcomes, while refraining from new activities that compete with private sector activities
- have well-developed, business-friendly regulatory practices that facilitate sustainable business development in the tourism industry
- ensure that core infrastructure in their areas such as water/wastewater, local roads, public toilets, parks and community amenities are of a high standard and can support both the community and a vibrant visitor industry
- recognise the importance of early and frequent consultation with the business community.
- work with the tourism sector to promote and market local areas effectively.

In summary, TIA believes that local authorities have a role in providing and funding infrastructure that serves as the foundation for its community and a vibrant industry servicing domestic and international visitors.

Perspectives on 'bed taxes'

“Bed taxes” on accommodation businesses have not yet been used in New Zealand but are used overseas in many jurisdictions, however they have generated mixed results and are widely unpopular. The overseas experience provides an insight into the issues that surround tourism rates and taxes.

Michael McMahon, a scholar at the University of Dublin has observed that “...governments are always looking for new tax bases and new industries, such as tourism, offer attractive possibilities for them.”² He notes that governments have imposed a range of charges and taxes on tourists including (but not limited to): exit taxes; hotel taxes and levies; taxes on transport; and visitor attraction taxes.³ Reasons for the popularity of tourism taxes include: being able to raise additional revenues from people who are not local voters; and tourists generally have above average incomes⁴.

McMahon suggests that it is fair for tourists to make a contribution to local infrastructure (such as maintaining roads, airport facilities and immigration officers), however, “...objections do arise if tourists feel they are expected to pay an undue proportion of the taxation.”⁵ He reveals some major shortcoming with any taxes that isolate the tourism industry for revenue collection, including:⁶

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⁶ IbidPP3-6

- A significant proportion of revenues collected from defined sources such as hotels are spent on non-tourism related services (e.g. in the U.S only 57% of taxes paid by hoteliers are being used for hotel or tourism-related purposes)
- Existing contractual arrangements may make it hard for tourism operators to pass on the costs of extra taxes to customers, meaning they must bear these costs themselves. In many cases, competitive markets may preclude operators from passing these costs on under any circumstances.
- Higher taxes on activities such as accommodation can lead to businesses closing their doors. This occurred in Ireland during the early 1980's when, following the Irish Government's decision to increase the VAT on accommodation to 23%, more than 10% of hotels closed their doors.⁷ In 1985, the Irish Government reduced the VAT on accommodation to 12.5% and since that time growth in the Irish tourism industry has increased dramatically, with 1990-96 tourism receipts increasing by 107%. While it is difficult to establish a clear, causal link between this tax reduction and the recent high growth, the performance of the Irish industry following the reduction in VAT contrasts strongly with the stagnation it experienced following the VAT increases in the early 1980's.

Governments in other parts of the world have also been removing or reducing taxes on tourism operators. For example:

- An unpopular hotel tax of 10% in New South Wales and 5% in the Northern Territories was removed following the introduction of GST to Australia in 2000
- In 1998, Hong Kong sought to provide a fillip to its tourism industry by halving the departure tax from its international airport, reducing the hotel room tax from 5% to 3%, and reducing ferry terminal fees⁸.

Based on these experiences overseas with accommodation taxes and other tourism-related taxes, we can conclude that:

- Tourism is often seen as a 'cash cow' by governments as it is visible and those paying the costs of tourism-related taxes often do not vote in local elections
- There can be significant economic consequences of tax policies that target tourism without understanding the impacts such policies might have on tourism activity
- Although tourism taxes have been extensively used overseas, governments are recognising that there is a fine line between raising rating or taxing tourism and negatively impacting on tourism. This has been reflected in decisions to introduce taxes, and then to backtrack on these decisions later.

⁷ Ibid P6

⁸ Hong Kong cuts its tourism taxes, Travel Trade Gazette Europa, 6 August 1998

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Local issues raised by 'bed taxes

As bed taxes are not used in New Zealand, the issues raised by their use overseas are expected to be relevant to New Zealand.

Other issues of concern about bed taxes to our industry include the following:

- The tax would be yet another form of compliance with which tourism SMEs are required to comply requiring expensive and time consuming amendments to computer programmes, and business processes and procedures
- Many visitors staying overnight in an area would not be subject to bed taxes as they stay in camp grounds, camper vans, private homes, or camp on road sides. Research undertaken by TIA in 2002 (based on an analysis of the 1999 Domestic Travel Survey) showed that proportions of visitors staying in accommodation that would generally be subjected to bed taxes would have ranged from 92.7% in one region to only 50.9% in another. This means that many visitors would end up not contributing to paying the rate.
- A shortcoming of bed taxes is that they do not cover day visitors to a district. This further narrows the rating 'base' that would be captured by bed taxes, to those who stay in commercial accommodation regardless of purpose of visit.
- Depending on the way that they are applied, there is a risk that bed taxes will not take into account changes in business activity and turnover. This is an issue if such rates apply whether a room is full or not.
- Tourism has large direct and indirect benefits that flow through local economies. In employment terms, the Tourism Satellite Accounts 2000-2003 identified that tourism employed 99,000 direct Full-Time Employees with a further 65,000 people indirectly employed in tourism. This demonstrates the powerful indirect benefits of tourism. Rates such as 'bed taxes' that seek to target a narrow range of ratepayers do not reflect that many different industry sectors receive downstream benefits from tourism (business services, transport, food and construction), and also benefit from activities funded from bed taxes including marketing and promotion, and infrastructure development. This leads to the conclusion that 'bed taxes' are unfair and inequitable and target a very narrow group of residents in an area.

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Tourism is already paying its way

Central government research has demonstrated that the visitor industry is paying its fair share of the costs of water and sewage systems.⁹ This same research has also concluded that there are existing funding tools available to local authorities to raise the capital required for investment in facilities.

The report noted that smaller communities faced particular problems with funding essential infrastructure due to their limited rating bases. This has been recognised with the introduction of three new subsidy schemes for water and wastewater over the last four years.¹⁰ Such schemes are a practical way of assisting smaller communities with particular funding issues to provide infrastructure to support their economic development.

Alternatives to bed taxes

TIA is aware that there are a number of viable alternatives to the use of bed taxes including:

- The greater use of pay-for-use mechanisms for services such as water and wastewater. Such mechanisms fairly target users and raise revenue as the use of such services increases.
- The use of pricing options such as seasonal pricing and peak pricing. Such mechanisms can be an extension of pay-for use pricing.
- The use of financial contributions mechanisms to raise funds for future capital investment from ratepayers and users that are likely to impose increased infrastructure burdens through their activities.
- The use of targeted rates available within Schedule Three of the Local Government Rating Act. These rating criteria already enable local authorities to rate defined groups of ratepayers where it is clear they benefit from specific services.
- The use of subsidies that are now available to local authorities and other water/wastewater providers. These include the Sanitary Wastewater Subsidy Scheme, the Tourism Demand Subsidy Scheme and the new recently announced Drinking Water subsidy scheme. TIA invites councils to work with the tourism industry and other business groups to advocate for even higher levels of central government resourcing for these subsidy schemes in the future.

Overall, TIA recommends that local authorities take full advantage of the rating mechanisms in the Rating Act (including those above), and central government

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funding assistance rather than advocating for additional mechanisms such as bed taxes.

Conclusions

‘Bed taxes’ are frequently raised as an option to increase revenue for local government.

Our conclusion is that bed taxes are a narrowly focused rating mechanism that fails to capture the full range of beneficiaries from services as marketing and infrastructure provision, services to which that some local politicians believe tourism should be making a greater contribution.

Other alternatives exist within the current legislative and policy framework, providing councils have the will to use them.

TIA is happy to work with local authorities to provide assistance and support for the development of destination marketing strategies.

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