Tax Working Group Information Release

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The advice represents the preliminary views of the member/s who prepared the paper and does not necessarily represent the views of the whole Group or the Government.

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EXTENDING THE TAXATION OF CAPITAL GAINS

For: Tax Working Group

From: Robin Oliver, Joanne Hodge
Kirk Hope

Date: 18 December 2018

Re: **Minority View**

The tax system should not impede experimentation and innovation

Despite varying policy views, submissions to the Tax Working Group (the **Group**) agreed that New Zealand needs to move towards a more productive and environmentally sustainable economy. We need to respond to demographic, technological and global economic change. In our mixed economy change cannot be led by the Government alone. Successful adaptation requires a private sector that embraces change. Business must take risks and be encouraged to experiment with new ideas and methods. Inevitably many ideas will not work. Entrepreneurship and experimentation should be encouraged and not penalised and New Zealand's tax system should not impede this.

We agree with the statement in our Terms of Reference that:

> The New Zealand Tax System has been justifiably commended internationally for being a simple and efficient system. The Government's starting position is that the guiding principle for the New Zealand Tax System – namely, that tax should operate neutrally and as much in the background as possible – is sound.

It is within this context that we have considered the extent to which New Zealand should extend the taxation of capital gains by implementing what is essentially a comprehensive capital gains tax system, as set out in Volume II of the Final Report of the Group. We agree that there is a strong case for extending the extent to which New Zealand taxes what are now untaxed capital gains. However, we consider that the costs of extending the tax rules in a comprehensive manner, as proposed in the Group's Final Report, would outweigh the benefits. This is a judgment call and we recognise that it is possible to reach differing views when trading off revenue, fairness, integrity, efficiency, and compliance and administrative costs impacts. In our view a comprehensive approach would impose efficiency, compliance and administrative costs that would not be outweighed by the increased revenue, fairness perceptions, and possible integrity benefits of the broader approach.

Instead we support a more moderate approach of extending current rules taxing gains, to property categories, only to the extent that benefits clearly exceed costs. This seems to be the case with residential rental property. These rules could be extended to holiday homes but doing this requires boundaries to be drawn between taxing holiday homes and other land (such as farmland) and will also impose added compliance costs on holiday home owners. The tax base could be extended to all land (and possibly buildings) but land and buildings can be inextricably integrated with business activities on which they are conducted. Taxing gains on business assets and shares raises issues about goodwill being taxed and impacts on capital markets.

At this point we believe that the costs of extending the tax base clearly exceed the benefits. Extending the tax base could stop at any of these asset classes but in our view the incremental approach of extending the tax base carefully over time is preferred. It has served New Zealand well over many of years of tax reform.

Finally, a number of submissions raised concerns about the announced timetable and process for implementation of reform. While the timetable and process for reform are not within our Terms of Reference we sympathise with those concerns. A more moderate reform programme would be easier to manage and provide a better outcome.

We outline our views in more detail below.

Residential rental housing

In our view the case for taxing more gains from residential rental property is clearest. This is based on advice from officials that the taxable income from such properties is low when compared with total economic returns. Comparing taxable income returned from this asset class with a rate representing a risk-free return applied to the same asset class indicates owners are relying on tax-free gains to complement their taxable returns from that investment. However, even if capital gains on residential rental property are more fully taxed, we accept the view from officials that there is a possibility that part of the incidence of this additional tax could flow through to higher rental costs. Given constrained supply of housing (through land supply, regulation and inadequate infrastructure) it is possible that this could lead to a reduction in the value of houses and higher rental costs. However, the impact of imposing additional tax on housing will be only one aspect to be considered by Government in its policies aimed at rectifying housing unaffordability.

If gains from residential property are to be more fully taxed, then this could be done with some modifications by extending current rules, including the bright-line tests. The proposed rules contained in Volume II that deal with housing could be used as a basis to amend the current bright line tests. Alternatively, we consider that a simpler option could be to apply the risk-free return method, or something similar, to residential housing. This method taxes net equity in an asset at a fixed rate each year.

Extending the tax base in this more limited way would generate much of the revenue expected from the comprehensive capital gains tax contained in Volume II. Officials estimate that some 39% of the total revenue from a capital gains tax would be from residential houses over a 10 year time period time[1].

Other asset classes complex

As additional asset classes are included in the capital gains tax system, the issues become more complex and there is an increasing need for exemptions and exceptions which are intended to reduce lock-in impacts and compliance costs, but can cause the reverse. Including business assets (such as goodwill and other intangible assets) and shares leads to complexity, high compliance costs and inconsistent rules characteristic of many overseas capital gains tax systems.

The need to value business assets such as goodwill on introduction date is one illustration. Valuing such property is likely to impose high compliance costs on businesses. It could also impose an unacceptable fiscal risk to the government (even with the proposed median rule). The response is to ring fence capital losses following from the valuation day cost base of these assets coming into the regime and this imposes a tax penalty on the experimental activity New Zealand needs to encourage. These particular rules are necessary to protect the tax base but they would directly impede this activity.

Taxing share gains

The Group's Interim Report acknowledges that taxing both business asset gains and share gains could create double taxation and potentially double deductions. Complex rules are required to counter the latter and the former would create a comparative tax penalty on New Zealanders owning shares in New Zealand companies, as compared to the proposed tax treatment of foreign shares (under the fair dividend rate method).

The Group has also concluded that a comprehensive tax on capital gains requires a redesign of current tax rules applying to KiwiSaver and other Portfolio Investment Entities (**PIEs**). This will change the current relatively consistent tax treatment of investors

[1] \$0.18b out of a total of \$0.59b in year 1 (30.5% of total CGT forecast) through to \$2.4b out of a total of \$6.2b in year 10 (39% of total CGT forecast in that year)

irrespective of the entity through which investments are made. As submitters have noted (including the NZX) such inconsistency risks damage to New Zealand's capital markets. Taxing KiwiSaver and PIEs on Australasian share gains on an accrual basis, as proposed, also requires the government to cash out accrued losses. We believe this will also create a significant fiscal risk to the government but not to do so would impose a tax penalty on KiwiSaver and other PIE investors.

The overall result of the proposed capital gains tax system on shares would be to increase the tax on New Zealand owners of shares in New Zealand companies. In most cases foreigners owning New Zealand shares would have no tax increase and the same would apply to New Zealanders owning foreign shares. While the reasons for these as explained in Volume II are valid, the outcome is clearly adverse. While there is evidence that residential rental properties are under-taxed there seems little to suggest that, overall, New Zealand companies or shareholders, with the possible exception of land rich companies, are taxed at less than full economic income in the same way that residential rental properties are undertaxed.

On balance

The Group was asked to consider a system for taxing capital gains that would improve the tax system. In order to evaluate whether such a system would be an improvement or cause damage to New Zealand's current tax system, the rules needed to be devised and then evaluated within the time available.

We agree that the taxation of capital gains could be expanded, on an asset class by asset class basis, until the costs of doing so exceed the benefits. However, in our view, and having regard to the significance of many of the outstanding issues, we do not believe that the costs of such an extension will exceed the benefits for asset classes other than residential rental property.

The risks involved in extending capital gains tax beyond residential properties include:

- Fiscal risks to the government
- Compliance costs
- Damage to equity markets
- Inconsistency in the tax treatment of investors

We are concerned that a greater level of tax on entrepreneurship and experimentation (and the domestic capital which supports that activity) will have a negative impact on New Zealand's productivity at the very time when we need to be taking active steps to improve productivity.

The extra revenue from the more comprehensive approach seems relatively low. Much of the estimated extra revenue seems merely to reflect the additional fiscal risks the government would assume. In taxing gains from business assets and shares the government would assume a proportion of what had been private sector risk. Arguably the government simply assumes a proportion of investor risk and in return receives as tax revenue a proportion of investor gains. The government could assume the same risk and extra revenue by investing directly in the share market. The fairness benefits seem easy to overstate especially given the exclusion of the family home set by our Terms of Reference.

Our current tax system is relatively simple and efficient. It does not overly stand in the way of the type of experimental behaviour we shall need to see more of in the future. In our view we would be better off amending some current rules (residential rental homes) and enforcing existing rules better. A study received by the Group[2] estimated that the hidden (untaxed)

[2] Cabral, A. C., & Gemmell, N. (2018). Estimating self-employment income-gaps from register and survey data: Evidence for New Zealand. Wellington: Victoria University Press.

economy from underreporting of income by self-employed (on average, 20% of their gross income) could raise approximately $850 million per annum. Countering tax evasion and properly enforcing rules already in place relating to property gains seems more sensible than experimenting with a new comprehensive capital gains tax system with high revenue risks and relatively moderate additional tax revenue over the forecast period.

For the reasons contained above it is our judgment that the disadvantages of the comprehensive capital gains taxing system we have worked on with the Group to date outweigh the advantages and it should not be implemented.

This summary represents the common views of the three authors. Additional views (not necessarily commonly held) are contained in the attached Appendix 1

A summary for inclusion in the Final Report is attached at Appendix 2.

Appendix 1

ADDITIONAL VIEWS

Background and Process

> New Zealand enjoys an enviable reputation for the range and quality of many aspects of its tax policy process, legislative provisions and administrative systems. Much of the innovation is based upon its status as a "first mover" in tax (and other) matters. Ironically, it is a "last mover" so far as CGT is concerned, but that may not be such a bad thing. It certainly enables New Zealand to seek out world's best practice and also to learn from other countries' mistakes.[3]

Other countries introduced their capital gains taxing regimes many years ago (United Kingdom 1965, Australia 1985, South Africa 2001). New Zealand has taxed many specific capital gains through targeted measures introduced consistently since the 1980s.

As compared with these other countries, the New Zealand tax system has some distinctive features:

- The top tax rate in New Zealand for trusts and individuals is 33% and 28% for companies
- New Zealand has no tax-free threshold for income tax for individuals
- We have a dividend imputation credit system similar to Australia's but our imputation credits are not refundable
- Family trusts are widely used as repositories for assets including the family home, rental properties and family businesses
- There are no concessions provided through the tax system for retirement savings, except that the top rate of tax on investment through managed funds is capped at 28% (and even this has more to do with the corporate tax rate being set at 28% than a desire to give a tax benefit to individuals on the higher marginal rates)
- New Zealand individuals earning only New Zealand source salary, dividends and interest and less than $200 of foreign source income (i.e. most of them) are generally not required to, and do not, file tax returns and the Government believes there are significant benefits to this approach
- Because we have no general capital gains tax, we already have explicit rules to tax as ordinary income a wide range of receipts that would be capital under common law. These include our financial arrangements regime, rules taxing lease inducement and surrender payments, restrictive covenants for employees, residential land sold within 5 years of purchase (other than a family home), and property sold that was purchased with an intention of resale
- Portfolio holdings of foreign shares are generally taxed based on a deemed return equal to 5% of opening value for the year instead of dividends and gains. There is an exception for Australian listed shares which are taxed on dividends only under current rules
- Dividends paid between members of 100% commonly owned corporate groups are tax exempt. Such members may but are not required to consolidate for tax purposes. Consolidation is not uniformly adopted by any means. It allows intra-group transactions to be ignored, rather than taxing the group as a single economic entity. A company can offset its taxable income against the loss of a company with 66% or greater common ownership, either by way of election or subvention payment.

The Government announced that it intended enacting any capital gains taxing legislation with effect from 2021. Having a greater appreciation for the complexities in the proposed rules and the number of unsolved issues, we do not consider that this timeframe is feasible and in fact will itself lead to risks to the tax base from incomplete legislation, higher

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[3] "New Zealand The Compliance Costs of Taxing Capital Gains" A report prepared by Professor Chris Evans (UNSW Sydney and University of Pretoria) 13 November 2018, para 121

compliance costs following from subsequent amendment and a general reduction in faith in the tax system by those taxpayers affected.

One of the beneficial features of the New Zealand tax system is a generic tax policy process that is followed by Inland Revenue with the introduction of all new tax legislation. This process seeks input from taxpayers (through representative groups) in the course of finalising that legislation, attempting to iron out significant problems, so that once legislation is enacted, it is robust. Robust legislation provides certainty for taxpayers, leads to more accurate self-assessment and reduces the need for subsequent taxpayer audit by Inland Revenue. We understand that Australia took two years to prepare a White Paper which set out their early proposals for their capital gains tax which was enacted in 1985. Between 1985 and 1997 the rules were essentially rewritten, between 1997 and 2010 they were subject to regular amendment, but from 2010 the rules have been considered stable and workable. Because of the differences in our two tax systems, it is not possible for New Zealand to merely take these now stable Australian provisions and easily adapt them for our purposes (and the same applies to capital gains taxing rules in other countries).

Systematic Gains and Returns to Risk

As mentioned, New Zealand has previously adopted a targeted approach to taxing as ordinary income a wide range of receipts that would otherwise be capital and not income, under common law. These existing rules aim to tax systematic gains from assets.

Appendix A to Volume II contains an explanation of the Fair Rate of Return Method and includes an explanation of the challenges of imposing taxes on returns to risk (as distinct from returns to time). To the extent that our remaining untaxed capital gains largely comprise the risk premium part of returns, this tax base has low to no market value. It follows that taxing a base with a low market value will in turn produce a trajectory of tax revenue with a low market value. The tax economic analysis of a risk-free return method has relatively recently been applied in New Zealand tax policy (refer the Fair Rate of Return Method for taxing foreign shares). However, the framework on which it is based is mature and well settled in the field of corporate finance and its principles are consistent with the Capital Asset Pricing Model.

If the Government alters is share of risk in the economy by taxing a return to risk and subsidising a loss to risk, the private sector will adjust its capital allocation decisions towards reinstating their "pre-tax change" positions, which can be shown to offset the expected tax revenue from taxing returns to risk. Whilst the forecasts are based on assumptions of existing asset allocations within the economy these allocations will alter in response to the tax, further reducing the amount forecast to be collected.

Like taxpayers, the Government can also adjust its portfolio of investments. It can achieve equivalent exposure to the risky return through taxation, by direct investment in risky assets (for example via the Accident Compensation Corporation's investments or through the New Zealand Superannuation Fund). The economic outcome for Government would be the same in revenue base terms but the negative outcomes we identify in this note from complicating the tax system would be avoided (compliance costs, impediments to growth as mentioned above, as well as the specific business concerns below).

Specific Concerns for Business

The following are specific concerns raised by Business New Zealand[4] and we believe these to be valid.

- *Negative impact on productivity of the New Zealand business sector*. Levying further taxes on business will have negative impacts on productivity; New Zealand needs to lift productivity. These include:
  - An increase in the hurdle rate required for business to make new investments.
  - Constraints being placed on traditional pathways into businesses ownership for family owned businesses. Businesses will not be able to be passed onto the next generation without a tax cost unless the transfer takes place on a death event.
  - Additional taxes could remove an incentive for the next generation of entrepreneurs to take risks and create the next great New Zealand businesses.
  - The lock in effect. Unless there are generous roll-over relief provisions, businesses may be penalised for trading up to new/different assets. The taxation of capital gains will effectively be a stamp duty, acting as a brake on market transactions potentially preventing transactions occurring because of that tax cost with a consequential lost opportunity for growth.
  - There could be cases of double taxation where business earnings are taxed and undistributed and shares in the business are then sold. There does not appear to be an easy solution to this.
  - The existing corporate tax rate is already higher than the OECD average. New Zealand does not currently have any issue with collecting over 30% of GDP in tax revenue; existing taxes collect more than jurisdictions which already have capital gains tax regimes[5].
- *Constraining capital needed to grow business.* Investors will have less funds available to them to invest into businesses and/or the New Zealand capital markets. When investments are evaluated there will be a higher hurdle rate for that investment to proceed. Different investment entities will face different taxing regimes and this will create distortions. There has been insufficient analysis undertaken on the potential impacts on New Zealand's capital markets to address these concerns. The impact on productivity and capital markets could be significant (for example, a wholesale adjustment downwards of all asset values) and these issues need to be properly researched and considered.
- *Impact on New Zealand as a business location.* New Zealand ranks highly internationally on indices measuring the ease of doing business. One factor considered is the relative simplicity of our tax regime. The introduction of complex tax legislation will not encourage non-residents to invest here or talented (high net worth) individuals to choose to base themselves or remain here. The New Zealand tax system should operate to encourage and not discourage innovators to base themselves here and create jobs.

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[4] Business New Zealand's mandate is to support government initiatives that encourage capital to be invested in New Zealand and to lobby constructively for policy settings that allow this capital to be used for the benefit of business and therefore, New Zealand. It represents the views of the four regional associations, being the Employers' and Manufacturers' Association, Business Central, Canterbury Employers' Chamber of Commerce and Otago Southland Employers' Association, as well as the Major Companies Group and the Affiliated Industries Group. The Business New Zealand family also includes ExportNZ, ManufacturingNZ, Sustainable Business Council, BusinessNZ Energy Council and the Buy NZ Made Campaign.

[5] https://taxworkinggroup.govt.nz/resources/charts-and-data-future-tax-submissions-background-paper, Figure 2

New Zealand's tech sector is the fastest growing part of the economy and imposing complex tax rules on what is a very mobile sector more is likely to influence decisions on where those businesses base themselves.

- *Asset values*. There are two aspects to valuations. The first is that a proposed valuation day approach will impose immense deadweight costs on the economy in valuing single assets, and in valuing businesses. The valuation of a business is not a straight forward exercise and for complex businesses two professional valuers may arrive at two materially different values. The second aspect is the impact of the proposed capital gains taxing system on increasing rents and the potential to lower house prices (although refer the next paragraph) with potential for a flow-on impact on the banking sector and interest rates.
- *Distortions.* Owner-occupied housing already receives preferential tax treatment and this will become even more so under the capital gains tax system. A rational investor could choose to relocate investments in liquid assets into owner-occupied housing, creating the so-called "mansion effect" and compounding the existing issues with housing supply and increasing house prices.
- *Compliance costs*. The main beneficiaries of a capital gains tax will be accountants, lawyers and valuers. The losers will be businesses of all sizes who will need to comply with very complex legislation; with small businesses bearing the highest compliance cost burden. Exemptions and rollovers aimed at reducing such costs add to the complexity of the legislation and influence taxpayer behaviour to ensure they fall within a particular concession. Compliance costs could increase by 30%on the basis of anecdotal evidence from professional firms and businesses in Australia.
- *Target the problem areas.* If unaffordable housing is the problem, the capital gains tax proposals are unlikely to provide the solution. Whilst tax rules can be used to encourage the supply of housing and to tax those who are profiting from the residential property market, there are other more targeted options available to Government: freeing up the supply of land, fast-tracking related and necessary infrastructure, reducing delays caused by regulation and co-ordinating policy issues as between Central and Local Government. If the problem is about labour income being re-characterised as capital gains, then better targeted avoidance rules can be introduced.

Reservations regarding extended taxation of housing

Holiday Homes

Taxing residential rental properties but allowing holiday homes (or second homes in another city for example) to remain untaxed will cause further distortions, encouraging houses that might otherwise be rented for all or part of the year to remain empty. For this reason, there is a view amongst some but not all of us that these houses should also be taxed if residential rentals are to be taxed.

Appendix 2

MINORITY VIEW INSERT INTO CHAPTER 5

This condenses our paper into the main points for inclusion in the appropriate place in Chapter 5 (after the summary for the majority).

Minority Views

The Group was asked to consider a system for taxing capital gains that would improve the tax system. In order to evaluate whether such a system would be an improvement or cause damage to New Zealand's current tax system, the rules needed to be devised and then evaluated within the time available. *[These opening sentences could go elsewhere in Chapter 5 as they are generic.]*

It is the view of three of the Group (Robin Oliver, Joanne Hodge and Kirk Hope) that the comprehensive approach to taxing remaining untaxed capital gains in New Zealand would impose efficiency, compliance and administrative costs that would not be outweighed by increased revenue, fairness perceptions, and possible integrity benefits. Our specific concerns follow.

Tax system should not impede experimentation and innovation

New Zealand needs to respond to demographic, technological and global economic change. Businesses must take risks and be encouraged to experiment with new ideas and methods; entrepreneurship and experimentation should be encouraged and not penalised. New Zealand's tax system should not impede this. In our Terms of Reference the Government confirmed its view that our tax system should operate neutrally and as much in the background as possible and we agree with this. It can be seen from the circumstances noted below that the proposed capital gains taxing system will impose new impediments to innovation and is likely to distort investment decisions in more instances than at present.

Residential rental housing

We agree that there is a case for taxing more gains from residential rental property, based on advice from officials that the taxable income from such properties is low when compared with total economic returns. Comparing taxable income returned from this asset class with a rate representing a risk-free return applied to the same asset class indicates owners are relying on tax-free gains to complement their taxable returns from that investment.

We accept the view from officials that there is a possibility that part of the incidence of any additional tax could flow through to higher rental costs. Given constrained supply of housing (through land supply, regulation and inadequate infrastructure) it is possible that this could lead to a reduction in the value of houses as well. However, the impact of imposing additional tax on housing will be only one aspect to be considered by Government in its policies aimed at rectifying housing unaffordability.

If gains from residential property are to be more fully taxed, then this could be done with some modifications by extending current rules, including the bright-line tests (and the proposed rules contained in Volume II that deal with housing could be used as a basis to amend the current bright line tests). Alternatively, we consider that a simpler option could be to apply the risk-free return method, or something similar, to residential housing. This method taxes net equity in an asset at a fixed rate each year.

Extending the tax base in this more limited way would generate much of the revenue expected from the comprehensive capital gains tax contained in Volume II. Officials estimate that some 39% of the total revenue from a capital gains tax would be from residential houses over a 10 year time period[6].

Other asset classes

The incremental approach of extending the tax base carefully over time has served New Zealand well over many of years of tax reform. However, extending the taxation of capital gains to the additional asset classes referred to below in accordance with our proposed capital gains tax system (having regard also to the proposed timeframe for enactment of the legislation) is problematic.

Other land and buildings, businesses and goodwill

Land and buildings (other than residential rental) can be inextricably integrated with business activities conducted on or within them. Taxing gains on business assets, including goodwill, gives rise to an increasing need for roll-over reliefs and exceptions which are intended to reduce lock-in impacts and compliance costs, but can cause the reverse. It can be seen from the rules we have designed that there will be complexity, high compliance costs and inconsistent rules and these are characteristic of many overseas capital gains tax systems.

The need to value business assets such as goodwill and other intangible assets on introduction date is one illustration. Valuing such property is likely to impose high compliance costs on businesses. It could also impose an unacceptable fiscal risk to the government (even with the proposed median rule). The response is to ring fence capital losses following from the valuation day cost base of these assets coming into the regime and this imposes a tax penalty on the experimental activity New Zealand needs to encourage. These particular rules are necessary to protect the tax base but they would directly impede experimentation and innovation.

Taxing share gains

Taxing both business asset gains and share gains could create double taxation and potentially double deductions. Complex rules are required to counter the latter and the former would create a comparative tax penalty on New Zealanders owning shares in New Zealand companies, as compared to the proposed tax treatment of foreign shares (under the fair dividend rate method).

A comprehensive tax on capital gains requires a redesign of current tax rules applying to KiwiSaver and other Portfolio Investment Entities (**PIEs**), changing the current relatively consistent tax treatment of investors irrespective of the entity through which investments are made. Such inconsistency risks damage to New Zealand's capital markets. Additionally, taxing KiwiSaver and PIEs on Australasian share gains on an accrual basis and requiring the government to cash out accrued losses will create a significant fiscal risk to the government. Not to do so would impose a tax penalty on KiwiSaver and other PIE investors.

The proposed capital gains tax system on shares increases the tax on New Zealand owners of shares in New Zealand companies while, because of our double tax agreement obligations, foreigners owning New Zealand shares would mostly have no tax increase. The same would apply to New Zealanders owning foreign shares. While the reasons for these as explained in Volume II are valid, the outcome is clearly adverse.

While there is evidence that residential rental properties are under-taxed there seems little to suggest that overall, New Zealand companies or shareholders, with the possible exception of land rich companies, are taxed at less than full economic income in the same way that residential rental properties are undertaxed.

Revenue to be raised

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[6] $0.18b out of a total of $0.59b in year 1 (30.5% of total CGT forecast) through to $2.4b out of a total of $6.2b in year 10 (39% of total CGT forecast in that year)

The extra revenue forecast to be raised from the more comprehensive approach to taxing remaining gains seems relatively low, reflecting the additional fiscal risks the Government would assume. In taxing gains from business assets and shares the Government would assume a proportion of what has been private sector risk; the Government simply assumes a proportion of investor risk and in return receives as tax revenue a proportion of investor gains. The Government could assume the same risk and extra revenue by investing directly in the share market.

Conclusion

We agree that gains from residential rental property could be more fully taxed. Existing rules can be amended or more targeted rules introduced to achieve this.

The fairness benefits from extending the proposed capital gains taxing system to other assets are likely to be overstated, especially given the exclusion of the family home set by our Terms of Reference. Our current tax system is relatively simple and efficient. It does not overly impede the type of experimental behaviour to be encouraged in the future. In our view it would be preferable to amend some current rules (residential rental homes) and to better enforce existing rules. For example, a study received by the Group[7] estimated that the hidden (untaxed) economy from underreporting of income by self-employed (on average, 20% of their gross income) could raise approximately $850 million per annum. Countering tax evasion and properly enforcing rules already in place relating to property gains seems more sensible than introducing a new comprehensive capital gains tax system with high revenue risks and relatively moderate additional tax revenue to be collected over the forecast period.

For the reasons above it is our judgment that the disadvantages of the comprehensive capital gains taxing system we have worked on with the Group outweigh the advantages and it should not be implemented.

[7] Cabral, A. C., & Gemmell, N. (2018). Estimating self-employment income-gaps from register and survey data: Evidence for New Zealand. Wellington: Victoria University Press.