Tax Working Group Information Release

Release Document

September 2018

taxworkinggroup.govt.nz/key-documents

This paper contains advice that has been prepared by the Tax Working Group Secretariat for consideration by the Tax Working Group.

The advice represents the preliminary views of the Secretariat and does not necessarily represent the views of the Group or the Government.

Appendix H – Reducing taxes on future generations

Further information on specific revenue-negative proposals

July 2018

Prepared by the Inland Revenue Department and the New Zealand Treasury

Reducing taxes on future generations

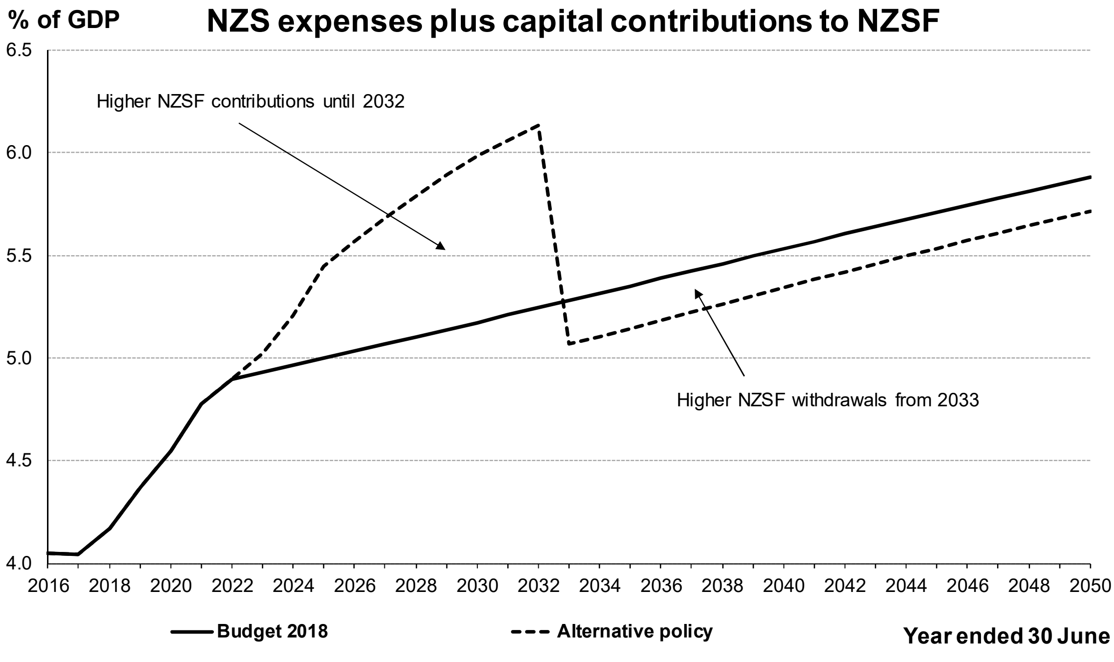
Proposal

1. The Government could save additional tax revenues for a period (eg, ten years) to permanently reduce taxes on future generations. This could be implemented through additional contributions to the New Zealand Superannuation Fund (NZSF).

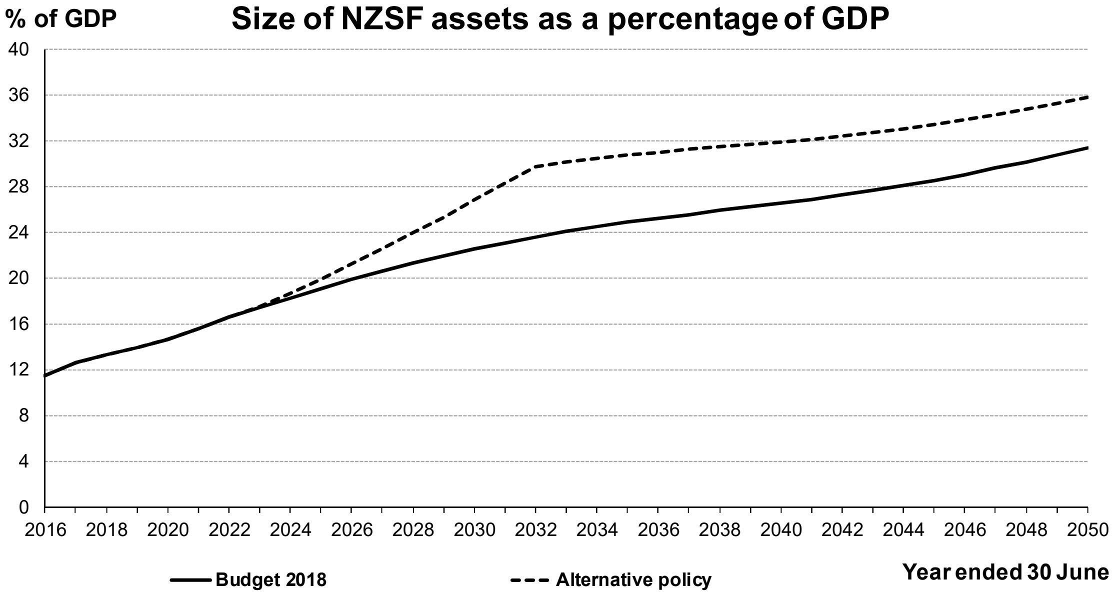
2. An illustrative scenario is modelled below where contributions to the NZSF are increased by the amount of projected CGT revenue for ten years (2022/23 to 2031/32). These contributions are in excess of contributions determined by the formula in legislation. Compared to the Budget 2018 projections (based on current policy), additional contributions for ten years would mean that the NZSF's assets are higher and capital withdrawals are higher from 2032/33. Higher capital withdrawals from 2032/33 mean that taxes can be lower than otherwise, so it would benefit future taxpayers. This reduction in future taxes is equivalent to about 0.2% of GDP or 1.5% of personal income tax revenue.

Problem

3. Population aging is projected to lead to increased New Zealand Superannuation (NZS) expenses over the next forty years. Unless future NZS entitlements are reduced, this will lead to rising taxes on future generations to fund higher NZS expenses under a pay-as-you-go model. The NZSF exists to smooth costs across generations via partial pre-funding of future NZS expenses. Additional tax revenues from a capital gains tax could be saved to increase the level of pre-funding and therefore enable lower taxes than on future generations than otherwise.



Source: The Treasury



Efficiency

4. The measure would enable lower tax rates than otherwise in the long term. In the illustrative scenario, this occurs permanently starting in 2032. There could be efficiency benefits associated with lower tax rates, although these would likely be small owing the small reduction in future taxes. There would be an efficiency cost from taxes being higher than otherwise for ten years.

5. The policy would also increase public saving. This is likely to increase national saving (unless fully offset by lower private saving), with possible broader economic benefits for the economy.

Distributional impact

6. Distributional impacts have not been quantified. The policy would entail increased taxes on those paying capital gains taxes (although the economic incidence may fall elsewhere) and reduce taxes on those paying general taxes from 2032. This would have inter-generational impacts with older cohorts likely to be worse off than younger (and future) cohorts who get a benefit from lower future taxes.

Fiscal impact

7. The fiscal impact of this option would depend on the amount of revenue raised that was saved by the Government. There would be an impact on the Government's balance sheet as assets were accumulated in the NZSF (or, equivalently, debt reduced) and then drawn down over time.

Conclusion

8. Whether to reduce taxes on future generations, and increase taxes for current taxpayers, requires a value judgement and comparing this option with other potential measures.