Tax Working Group Public Submissions Information Release

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Submission to Tax Working Group (TWG)

The purpose of any tax system should be to collect, in the most efficient way possible, the minimum amount of revenue necessary for government to undertake its essential functions. It should *not* be used for social engineering purposes, since any attempts to do so inevitably have unintended adverse consequences on efficiency and equity.

With these core principles in mind, I have some brief comments on a few worrying ideas that have been floated. My comments can be summarised as follows:

I. A capital gains tax would increase compliance costs, tax evasion and bureaucracy, and would fail to pass any conceivable cost-benefit test.
II. A broad-based land tax could well be a good idea, but exempting the family home makes it, at best, pointless.
III. Allowing for varying rates of GST would be the economic equivalent of an own goal.
IV. "Public health" taxes (e.g., sugar tax) typically do not work, have unintended consequences, and open up ethical cans of worms.

I am happy to discuss these points further should the TWG consider it necessary to do so.

1. Capital Gains Tax

Proponents of a capital gains tax (in addition to the one that already exists) frequently justify their position on the basis that many other countries already have such a tax. Yet, as the socialist economist Joan Robinson famously remarked in another context: "Just because other countries are stupid enough to put rocks in their harbours doesn't mean we should put rocks in ours."

The three certain consequences of a capital gains tax are:

- a massive increase in compliance costs for honest taxpayers;
- a significant increase in tax evasion activity by dishonest taxpayers;
- the creation of a major new bureaucracy for helping honest taxpayers and fighting dishonest taxpayers.

In return, the government will receive a relatively small, pro-cyclical, amount of additional revenue, while any possible (but doubtful) impact on the tangential goal of improved housing affordability will be eliminated by the requirement that the family home is exempt.

In short, a capital gains tax could not pass any conceivable cost-benefit test.

2. Land Tax

A broad-based land tax would not suffer from the disadvantages of a capital gains tax noted above: additional compliance costs would be low and evasion would be difficult. So, if introduced in conjunction with a reduction in income tax rates, a land tax could well be a sensible initiative.

However, the benefits of doing so are completely eliminated by the requirement that the family home be exempt. With such an exemption in place, all that will happen is a large increase in the number of "families" and, consequently, "family homes". Worse still, exempting the family home beds in a system that taxes land used for relatively high-productivity purposes (business and enterprise) while not taxing land used for lower-productivity activities (owner-occupied housing). This makes no sense at all.

In short, a land tax could be a good idea, but exempting the family home makes it a pointless exercise.

3. Variable GST rates

There are two certain consequences of offering lower GST rates on so-called "merit" goods:
• endless arguments about what should be on the list of merit goods;
• endless disputes about whether a particular good meets the definition of an already-agreed merit good.

Messing around with NZ's beautifully simple GST system would be the economic equivalent of an own goal.

4. "Public Health" taxes

A prominent example of this sort of thing is a sugar tax. Yes, too much sugar is bad for us, and undoubtedly contributes to the so-called obesity crisis. But economics and tax experts have repeatedly concluded that sugar taxes do not result in lower incidences of obesity (that would require a tax on obesity). So introducing a sugar tax would penalise responsible sugar users while having no effect on public health outcomes (it would also, incidentally, almost certainly be regressive).

Taxes of this kind are also a slippery slope. If sugar, then why not, say, meat? Excessive consumption of the latter is just as bad as sugar for public health, and it has significantly more adverse environmental consequences (not to mention its animal welfare implications). So the case for a meat tax would seem to be considerably stronger than for a sugar tax. But the political fallout would be such that it would be an extraordinarily brave TWG that recommended a meat tax. At the same time, it would be an extraordinarily hypocritical TWG that recommended a sugar tax and not a meat tax.

To avoid getting bogged down in such moral quagmires, I suggest the TWG avoid these kinds of taxes altogether.

Conclusion

No tax system is perfect, but the current NZ system is simple, easy to navigate, and relatively efficient. As they say in Texas, if it ain't broke, don't fix it. While there may be improvements that could be made at the margin, major reform is simply unnecessary.

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