Tax Working Group Public Submissions Information Release

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Future of Tax – submission 29 April 2018
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[1]

Prioritisation of government spending relative to tax income

For years politicians have used the tax system for left or right wing political gain purposes. The left wing usually increasing benefits and the number that qualify for free (state) money and the right for reducing taxes and in some equal measure reducing some services and the amount of free money available.

Fundamentally though any government needs a vibrant and growing economy to be able to generate incomes that can be taxed and provide excellent services to its citizens

Maintaining current tax levels and economic growth with increasing GDP actually increases government tax income.

Increasing taxes reduces motives for work and for inward investment thus reducing the GDP and essentially maintaining a same level of income while making people poorer and eating up more of the pot in additional unemployment costs

In order to improve the effects of the wealth gap that exists in any economy one should look at effect on quality of life and look at bringing a better balance to that

<u>Comment on spending</u>

- In New Zealand despite having one of the lowest unemployment rates in the world we spend fully 33% of the government's budget on social welfare.

  A good part of the spending goes on working for families and similar financial aid packages for working families whose income is deemed too low. This has effectively been subsidising employers for more than 15 years since its inception – but comes from the left wing of political thinking of creating dependant voters.

  Instead the right thing to do would have been at the time, and since is to force employers to actually pay a sensible wage or an additional employment cost similar to ACC or other compulsory charges, rather than substituting taxpayer money. The simplest new tax you can introduce is one on employers that is a compulsory cost before profits based on their employee payment profile – the lower the average hourly rate the higher the employer's employee contribution is which would fund the working for families. This is already workable from the existing PAYE documentation and is simple data analysis and invoicing – and can be monthly.

This alone would be a fairly targeted tax aimed at reducing the wealth gap and improving quality of life for all.

- Student loans and funding. The tertiary education system has a poor and inefficient funding model – many institutions work on bums on seats mentality and the quality aspect of teaching goes out the window. Many institutions take a full fee even after the student has dropped out having a negative effect on the person and creating inefficiencies in the system. Throwing money at education does not work this has been demonstrated time and again and shows in New Zealand self-deluded methods of calculating successful outcomes with devalued qualifications. Looking at ways of improving the outcomes for students into meaningful employment is the key – in other countries educational institutions have to follow through on their teaching by ensuring graduates are employed within three months of graduating – they have to have a job finding and placing facility – a target of 90% success is a normal target. Change the way these institutions are funded

  Change the way student loans are allocated – reduce the amount of the loan available – in other words lower fees to tie in with changing the institution funding model - but allow a real level of accommodation and living expense allowance for free, based on student performance at the institution – measurable and merit based but effective. This will have the effect of having a much higher graduation ration but students leaving institutions with much lower debt levels – immediately allowing the to achieve better quality of life outcomes rather than paying off massive debts for the most productive time of their lives.

- Taxation levels – this is always a thorny issue – what is fair? After all hard work at becoming a specialist on one's field and working hard should not be penalised with higher taxes than for people who do not do that – but there are medians that need to apply for systems to function

Taxable income	Tax on this income	Effective tax rate
$0 - $10,000	Nil	0%
$10,001 - $35,000	19c for each dollar over $10,000	0% to 13.57%
$35,001 – $60,000	$4750 + 25c for each dollar over $35,000	13.57% to 18.33%
$60,001 - $90,000	$11000 + 31c for each dollar over $60,000	18.33% to 22.56%
$90,001 - $180,000	$20300 + 36c for each dollar over $90,000	22.56% to 29.28%
Above $180,000	$52700 + 39c for each dollar over $180,000	29.28% to 39%

The above would result in an overall higher tax income for the government but still be relatively fair to most ordinary Kiwis. The real benefit comes from the people below an income of $35,000 benefitting much more with dramatically lowered taxes, whilst the middle-income earners largely standing still with curve stretching out to $90,000 from $70,000 but being more than made up for by the 36c and 39c rates above these.

The fundamental benefit is a lower level of government subsidy for the lowest earners but with a slightly higher tax income overall – whilst still maintaining New Zealand as a competitive labour market.

Essentially the above steps would fundamentally reduce the need for safety net type of spending whilst maintaining the same levels of tax income – freeing up the excess several billion to be spent on more healthcare, public defence, fighting the drug war threatening to break society and on genuine environmental improvement options.

Some fundamental truths about the effects of taxation:

- Raising tax on a product or service has never in the history of taxation reduced its price – it has always increased its price
- Raising the price of a product or service has a tendency to reduce the demand for it – e.g cigarettes
- Reducing the demand for a product or service through artificial methods of price increase such as taxation does not work so well when it comes to absolutely must have necessities such as housing and fuel – it results in homelessness and reducing travel and increased product prices.

One cannot argue for the sake of convenience that increasing taxes will create a larger tax income while simultaneously arguing that increasing taxes will successfully reduce demand – these are not mutually exclusive effects. For example:

- Putting tax on petrol will cause a reduction in the volume by 4% to 5% of petrol bought - this will cause a net reduction or at best no change in the overall duties received not an increase. This is because a rather large chunk of the petrol price is tax – but the worse side effect is a reduction of economic activity coupled with an accompanying increase in the cost of goods and services – a double negative whammy for no real change in tax income

- Creating a capital gains tax where it does not exist has several effects.
    - Firstly, the CGT on property is designed to raise taxes for the sake of increasing tax income – no other reason
    - However, the argument being used to justify it is that it will reduce house prices by reducing house trader activity and therefore leave a bigger pool of houses for people to buy.
    - This whole argument pre-supposes there is a balanced supply/demand equation at work and the reduction in demand from investors will leave excess supply which will lead to lowering of prices and more opportunities for home buyers to acquire. The problem with this logic is:
        - 35% of properties listed are investors selling to upgrade – this level of listings would reduce dramatically so the supply would decrease
        - 35% of new houses built are built by investors – this would also reduce thus reducing stocks further
        - The stock levels between supply and demand are already not in balance – there is currently a shortage of stock which would be exacerbated by a CGT
        - House prices would increase. In order to make up for the loss of a portion of the capital gain to taxes the investors would look to increase the selling price of the houses in compensation. This means rent increases by a suitable percentage to make the investment equation work – this

would occur naturally due to the initial shortage the CGT will create

  - It has been demonstrated in every jurisdiction that capital gains taxes is not effective at changing investment habits – typically it flattens for a year and then carries on catching up with where it should have been without it over the next three years. It is not effective at creating lower priced more affordable houses – if anything it has the opposite effect for would be renters trying to save for a deposit by increasing rents
  - It is a myth that rents only increase at the rate of wage inflation – when a major re-alignment occurs in all business costs these are passed on – there is no competition. This has been proven by the 40% rent increases of the last four to five years relative to an overall 10% to 15% wage rise – it is the same as increasing the OCR, universally applied.

- Personal tax rates - Making misleading claims in the Submission background notes around the higher tax rates. Figure 7 on page 28 tries to paint a picture that the top tax rate on personal income is much lower that in many other countries. But the level at which the top rate is charged in New Zealand is almost the lowest in the world – in Australia for instance its 45%, but this applies to taxable incomes above $180,000 with the effective rate being 30% for amounts below this level and dropping. See table

Taxable income	Tax on this income	Effective tax rate
$1 – $18,200	Nil	0%
$18,201 – $37,000	19c for each $1 over $18,200	0 – 9.65%
$37,001 – $87,000	$3,572 plus 32.5c for each $1 over $37,000	9.65 – 22.78%
$87,001 – $180,000	$19,822 plus 37c for each $1 over $87,000	22.78 – 30.13%
$180,001 and over	$54,232 plus 45c for each $1 over $180,000	30.13 – less than 45%

New Zealand also has the fifth highest tax on personal income as percentage of GDP – this is as a result of the average wage being almost at the level where the highest tax rates kick in

There is nothing like increasing taxes in order to reduce investments both personal and economy growing. Why would any business think of increasing investments if the returns, both personal and business are going to be penalised more – the sensible big and medium money investors will invest offshore as will the pension funds

Taxation and its purpose

The purpose of a taxation system is to raise funds in order for the state to provide governance and other services. The typical services a modern western socially responsible state would provide includes:

- National defence system and services
- Legal system – Courts
Prosecution service
Public defence service
Police force
Prison system
- Financial and commerce regulation systems and services
- Health care system and services - Hospitals
Emergency and ambulance
GP and community health care
- Education system and Services - Primary
Secondary
Tertiary
- Infrastructure management and development – Energy
Roads
Rail
Ports
Environment
- Social welfare system and services – Benefit system
Pensions
Poverty eradication
Social housing
- Fire fighting and rescue services
- Secondary Services – Heritage, Culture and recreation