Tax Working Group Public Submissions Information Release

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Submission on the future of tax in New Zealand

The Institute of Directors (IoD) appreciates the opportunity to comment on the Future of Tax paper (the paper) published by the Tax Working Group (the Group). We support the review of New Zealand's tax system to ensure it is fit for purpose and sustainable going forward. Notwithstanding our comments here, the IoD may make further and broader comment as the review progresses.

About the Institute of Directors

The IoD is a non-partisan voluntary membership organisation committed to driving excellence in governance. We represent a diverse membership of over 8,600 members drawn from listed issuers, large private organisations, small and medium enterprises, state sector organisations, not-for-profits and charities.

Our Chartered Membership pathway aims to raise the bar for director professionalism in New Zealand, including through continuing professional development to support good corporate governance.

Background

The last tax review in New Zealand took place in 2009/2010 (see A Tax System For New Zealand's Future published by the Victoria University of Wellington Tax Working Group). A lot has happened since then and it is timely for the tax system to be re-examined.

The Tax Working Group, established by the Government, has been tasked in its Terms of Reference with considering further improvements to the structure, fairness and balance of the tax system.

Currently, the tax system supports Government spending of approximately 30 per cent of GDP and a key focus of the review is to maintain this level of revenue.

IoD Commentary

New Zealand has a highly regarded tax system with many strengths including its relative simplicity. However, we recognise that New Zealand can't rest on its laurels in this time of rapid change and uncertainty. It is an appropriate time to stand back and consider what is working well and what can be improved to future proof the tax system. We appreciate the complexity of the review for the Group and the challenges around achieving consensus among different stakeholders.

What makes a good tax system was well summarised by the previous Tax Working Group:

> "A good tax system should minimise the harm it does to growth; minimise impediments to people working, saving, investing and innovating; minimise distortions to investment allocation decisions; and maximise the integrity and fairness of the taxation system so that there is widespread trust in it and that taxes paid reflect ability to pay and not opportunity to avoid. A good tax system should also be flexible enough to meet future government

funding needs and respond to changing international developments." (A Tax System For New Zealand's Future, the Victoria University of Wellington Tax Working Group at p 59)

A good tax system should also support business in New Zealand and aid our global competitiveness (eg it is important for organisations to be able to make business decisions with certainty of the tax implications). Tax is also a governance issue and it is critical for boards to be clear about their role in tax governance, understand potential risk areas, and ensure their organisations have a tax management strategy that sets expectations about policies and practices including disclosure to shareholders and stakeholders.

Challenges, risks and opportunities
The Group is exploring major challenges, risks, and opportunities facing the tax system including:

- changing demographics, particularly the aging population and the fiscal pressures that will bring
- te ao Māori and the role of the Māori economy in lifting New Zealand's overall living standards
- the changing nature of work
- technological change and the different business models that will bring
- falling company tax rates around the world
- environmental challenges
- growing concern about inequality and
- the impacts of globalisation and changes in its patterns.

Businesses and organisations are facing many of the same challenges. It is essential to take a long term approach to navigate the uncertainty and change on the horizon, and to achieve better business and societal outcomes.

Review criteria
New Zealand (and other developed countries) tax reviews have used the following criteria in analysing the costs and benefits of various reforms:

- *efficiency*: minimise impediments to economic growth and avoid distortions (biases) to the use of resources
- *equity and fairness*: achieve fairness including through 'horizontal equity' (the same treatment for people in the same circumstances) and 'vertical equity' (higher tax obligations on those with greater economic capacity to pay). Procedural fairness is also important for a tax system
- *revenue* integrity: minimise opportunities for tax avoidance and arbitrage
- *fiscal adequacy*: raise sufficient revenue for the Government's requirements
- *compliance and administration costs*: minimise the costs of compliance and administration, and give taxpayers as much certainty as possible
- *coherence*: ensure that individual reform options make sense in the context of the entire tax system.

These are well recognised principles and objectives and we support them in the context of this review.

The Government's new Living Standards Framework which consists of four capitals (physical/financial, human, social and natural capital) is referred to in the paper as a potential framework for thinking about taxes and wellbeing. This has the potential to bring about a more holistic review than previous reviews.

Broad-base and low-rate system
New Zealand has a *broad-based, low-rate* tax system. It is described as broad base because GST, company and personal income tax account for more than 90 per cent of all tax revenue and there are very few exemptions. The broad-base, low-rate approach has many benefits including administrative simplicity. We believe that this should continue to be an underlying framework for New Zealand's tax system.

Company tax
New Zealand's company tax rate is relatively high (compared with OECD countries), and the proportion of company tax revenue to GDP is high. We welcome the Government's initiative to explore the rate of company tax. It is essential that New Zealand remains a competitive place to do business (including in relation to Australia) and the company tax rate is an integral consideration in this examination.

Goods and services tax
New Zealand's GST regime is world leading and we believe GST should continue to apply broadly with no new exemptions. Introducing exemptions would add complexity and undermine the strength of the current regime.

Other observations
Many parts of New Zealand's tax system are working well and these should be preserved as much as possible.

The Group is exploring the case for introducing new taxes (such as land and wealth taxes). New Zealand has had previous experience with such taxes and we encourage the Group to consider this experience where relevant. New taxes should *not* be introduced without comprehensive analysis and justification (eg examining the cost of implementation, collection and monitoring against the expected revenue), and consultation. This includes consideration of a capital gains tax (CGT). The costs and benefits of a CGT have been thoroughly examined in previous tax reviews. The last review raised "significant concerns over the practical challenges arising from a comprehensive CGT and the potential distortions and other efficiency implications that may arise from a partial CGT".

We acknowledge that there is work underway outside of the review and this should also enhance New Zealand's tax system in the future. Specifically, Inland Revenue's Business Transformation Programme, Base Erosion and Business Profits measures, and the consultation on introducing a research and development tax incentive.

We look forward to the Group's interim report to the Minister of Revenue in September and appreciate the opportunity to comment on behalf of our members.

Yours sincerely
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