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Release Document

September 2018

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3 May 2018

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In the funding of NZ government public services, tax is unnecessary

The NZ Government can always fund all of its public services by borrowing from its own bank, the Reserve Bank of New Zealand Limited, without raising any money in tax whatsoever. As is the case in any bank lending[1], the Reserve Bank of New Zealand creates an 'asset/ liability' against itself called a deposit, and sells the 'asset/liability' to the Government for a promise by the Government to pay the Reserve Bank, in future, the amount of the deposit plus interest. As the Government then draws down the deposit it has purchased from the Reserve Bank, (spending the amount of the deposit on public services, by cheque or electronic funds transfer or bank notes) it no longer has the deposited funds that were created as an asset in its account by the Reserve Bank (it has instead the goods, services or other abstract rights it purchased), but it has the liability to pay the Reserve Bank, in future, the amount drawn down.

However, while the Government becomes increasingly indebted to its own bank (the Reserve Bank) on the one hand, that growing debt is always matched on the other hand by the government's 100% ownership interest in the Reserve Bank, which asset grows at the same rate as the future debt – the liability of the Government and the asset of the Government being equal, the net effect (for example, on consolidation of the Government's assets and liabilities) is zero. The Government's liability and its asset cancel each other out. The Government spending on providing public services and public assets has not relied on taxation at all. Further, it has released currency into circulation in the economy, which currency the private sector is able to use to discharge private sector credit obligations.

The important difference between the Reserve Bank and other commercial banks is that one customer of the other banks does not own those banks, 100%, as the Government owns the Reserve Bank, (and, as the ultimate fall back position, only the Government has

[1] For example, see Henry D MacLeod, The Theory of Credit, vol 2, part 1, pp 349-350 & 359 - 364 (London, Longman Green & Co, 1890), extracts in appendix; and generally see MacLeod's other texts on The Theory & Practice of Banking (London, Longmans Green Reader & Dyer, 1886) and on The History of Economics (London, Bliss, Sands & Co, 1896). MacLeod was a London Barrister-at-Law, expert in commercial law.

the legal power to acquire all assets within its jurisdiction, normally exercised through taxation, to meet its liabilities[2]). There can be no in substance set-off, consolidation or merger of asset and liability for other commercial banks, as is the in substance position for the Government and its Reserve Bank. Borrowing by customers of the other commercial banks (like credit sales from any supplier to the supplier's customers) has to be paid off by the customer concerned in the future. Failure to pay most often leads to bankruptcy of those unable to meet their liabilities in currency (ie by paying over bank notes or transferring bank deposit amounts) – you can attend at the local High Court on bankruptcy /insolvency morning each week, and see the financial demise of citizens (including companies) who have been unable to secure 'circulating money' to pay off debt that has fallen due – to IRD, to commercial banks, and to other suppliers of credit. Only a foolish government borrows currency from a domestic lender other than its own central bank, and only a stupid government incurs financial obligations to a foreign creditor in a foreign currency (as NZ realized in 1984).

So, where the Government chooses to use NZ currency (in bank notes and in assigned NZ currency bank deposit amounts) that it has collected as tax to pay interest on its Reserve Bank debt or to pay off the loan principal, that is an entirely voluntary act on the part of Government, and an act that is not necessary for the provision of public services, including benefits and of public goods. In fact, tax is entirely unnecessary when it comes to funding government public services and benefits and public goods in New Zealand.

The purpose of taxation is simply to take currency out of circulation, and to make circulating currency somewhat scarce, and therefore valuable, as an exchangeable abstract right. Tax sits alongside the requirements for commercial bank reserves (deposits at the Reserve Bank), and the setting of the official cash rate by the Reserve Bank, as the mechanisms or tools for taking currency out of circulation. The tools are used to protect against an unwarranted fear of inflation and a misunderstanding of hyper-inflation (there can be no inflation without the printing of currency, and inflation can always be controlled by making currency scarce so that maturing credit obligations cannot be met). Inflation is, in fact, a necessary incident and benefit that enables private enterprise vendors to make profits in selling goods, services and other abstract rights. Without inflation, in a completely free and unfettered market, a seller cannot make a profit – because the costs of the thing sold becomes the exchange value for that thing when sold.

By taking currency out of circulation, and making it scarce after citizens have entered into their own credit arrangements that have been funded by the currency released into circulation, citizens are left 'on the hook' and have, in future, to scramble to find currency to discharge their credit obligations as they mature. In the initial creation of the credit, however, the government and banks have had ready access to currency created out of nothing by the Reserve Bank (ie creating a liability against itself, that it has sold as a deposit amount) that is then made available to citizens (by government spending and by commercial bank lending). Citizens in turn use the currency borrowed from banks to discharge their credit obligations incurred with other citizens. The currency is in circulation, and properly in circulation, and the citizen borrowers should

[2] The Roosevelt government decision to seize nearly all gold in the US by executive order 6102 on 15 April 1933 is an example – abstract rights were issued in exchange to the compelled vendors. The French government did something similar to pay off the 5 billion gold franc indemnity imposed on it by Germany at the end of the Franco Prussian war in and after 1871 and get German occupying troops off French soil. The clearest example of wholesale confiscation by government followed the Norman Conquest of Britain in 1066.

have a legitimate expectation that it will remain in circulation so it can be available for use to pay off their borrowing. However, that is not the case – currency is deliberately taken out of circulation, mainly by taxation, to create a currency scarcity.

When tax is seen for what it really is, simply a tool for controlling the amount of currency that is in circulation at any particular time (and that is available to discharge the tax and the credit obligations entered into by citizens), and that it is entirely unnecessary to fund the provision of public goods, services and transfers (the euphemism for benefits) by government, it becomes clear that a proper and valid reason for persuading citizens to pay tax is required. A proper valuable exchange is required. Citizens need to have personal abstract rights accruing to them from the government in exchange for the currency they pay to the government, by way of tax, to enable the government to take such currency or a portion of it out of circulation in the interests of controlling inflation.

Abstract rights to Government provided pensions, in properly large amounts for living in dignity for old age, and for poor health, and for other individual circumstances, should be accruing to citizens in return for their carrying the obligation of paying tax. To discharge the obligations in the accrued abstract rights, the government simply borrows from its Reserve Bank and makes the pension payments. The debt to the Reserve Bank is matched by the increasing value of the Reserve Bank as an asset of government and nets to zero. There are no intergenerational issues, because the government debt from its Reserve Bank never needs to be repaid – it is always matched by the value of the Bank to the government that owns it. [3] Citizens will be prepared to pay taxes in return for abstract rights accruing to them for these personal pension benefits.

I have endeavoured to put this submission succinctly, without elaboration on its points (which would require a book). However, I believe that on close examination, you will find each of the points set out above, which may appear surprising at first, to be correct, and indeed that no changes are required to parts 1 and 2 of the Public Finance Act 1989, as amended. I am in the process of putting them into a book – but consider it is important to make the points here and now, given the errors that litter the Background Paper.

Yours sincerely
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Appendix: two extracts from H D MacLeod, The Theory of Credit, pp 349 – 350 & pp 359 – 364 (see footnote 1 earlier)

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[3] This is what Justice Holmes meant by the words '... for civilized society' in his much misrepresented quote 'Taxes are what we pay for civilized society' – that is, taxes are not what we should pay for an increasingly uncivilized society based on increasing wealth disparity, with governments wrongly claiming they do not have the money to do anything about it.

The Theory of Credit by Henry Dunning MacLeod 1890 Pages 349-364

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