

## **Tax Working Group Public Submissions Information Release**

### **Release Document**

**February 2019**

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## **Submission on the Tax Working Group's Interim Report**

Dear Sir Michael

Thank you for providing me with the opportunity to make a submission on the Tax Working Group's interim report.

I also wish to thank your colleague Marjan van den Belt and the Tax Working Group secretariat for inviting my staff to the October 11 meeting on the Environmental and Ecological Outcomes chapter. I hope their insights at that meeting proved useful.

### **General comments**

I am pleased that the Tax Working Group (TWG) supports the case for broadening the base of the tax system and making greater use of environmental taxes.

The case for taxes that incentivize businesses and households to reduce their environmental impact is a well-established one.

However, taxes are rarely the only policy option available and should be considered in the context of any other complementary measures that may be necessary. A well-designed package of taxes and complementary measures can enable a lower explicit tax rate than would otherwise be needed.

Notwithstanding a broad mandate to explore "[w]hat role the tax system can play in delivering positive environmental and ecological outcomes, especially over the longer term" the TWG appears to have adopted a narrow approach focusing uniquely on environmental and resource taxes.

I would like to reiterate my previous submission to the TWG that a subject of equal, if not greater interest than environmental taxes, is the impact of other tax instruments within the broader tax system on environmental incentives or disincentives. I have read the Ministry for the Environment's submission, which appears to share this view.

While I was at the OECD, an important piece of work I led investigated the alignment of policies with climate objectives. As we know, addressing climate change requires urgent policy action. However, even ambitious goals can be defeated if broad regulatory, tax and fiscal settings are misaligned with climate objectives.

It would be useful for the TWG to undertake a diagnostic analysis to determine whether other taxes – or their absence – are consistent with the need for New Zealand to transition to a low-emissions economy.

### **Draft framework used to assess environmental taxes**

I note that while economic efficiency and administrative complexity were deemed relevant principles for assessing resource taxes, they do not appear for environmental taxes. Perhaps the ‘sufficient scale’ principle, for example, captures administrative complexity, but this is rather vague. I also disagree with the assertion that taxes are inherently more costly in administrative terms than equivalent regulations.

I recommend that the framework explicitly includes administrative complexity and economic efficiency in an amended framework.

A key objective for the framework should be to assess whether to implement an environmental tax or to continue to apply regulations. A key differentiation between taxes and regulations is frequently their relative economic efficiency.

Regulatory approaches often prescribe who should mitigate an externality and how it should be achieved. Unless particular care is taken, prescriptive regulations can end up picking winners – commercially and technically.

Taxes, by contrast, leave businesses considerable flexibility to decide how they might change their behaviour and reduce environmentally harmful activities at least cost.

The high cost-effectiveness of taxes over regulations is not just found in textbooks. There is real evidence that supports it. For example, the OECD found that trading schemes and taxes reduce emissions at very low cost in comparison with policy instruments such as feed-in tariffs<sup>1</sup>.

### **Analysis of key short-term environmental tax recommendations**

The TWG’s recommendations for priority attention would benefit from additional development and supporting analysis. For example, the chapter contained no or limited analysis of the extent to which tax reform could improve environmental outcomes. This would require more substantive analysis potentially including modelling work.

In addition, the Environmental and Ecological Outcomes chapter states that “... tax should not be considered in isolation when dealing with the environment; instead, the merits of tax as a policy instrument should be assessed together with the merits of other tools and approaches”. I agree with the sentiment, but the chapter does not contain a critical evaluation of alternative policy instruments.

It is important that taxes are seen in the context of a broad suite of policy instruments available to policy makers to improve environmental outcomes.

As short-term priorities, the TWG’s nomination of waste, congestion and climate change have merit. However, I consider water pollution and abstraction are more medium-term

issues especially given the existence of complex existing allocation regimes and the contentious issue of iwi rights and interests in the freshwater area.

### ***Waste***

I support the TWG's recommendations for the waste disposal levy including that: the coverage of the levy be expanded, the levy rate be reconsidered based on a reassessment of the negative externalities from waste, and the current approach to hypothecation of the levy be revisited.

A reassessment of the externalities should consider the different types of waste, which could allow for a more nuanced waste disposal levy. For example the United Kingdom's landfill tax uses a differential tax rate based on estimates of the externalities associated with waste disposal<sup>ii</sup>. The standard rate is currently set at £88.95 per tonne, while a lower rate is set at £2.90 per tonne and applies to less polluting waste.

The policy of applying the totality of the levy revenue to a waste minimization fund, which hands out grants to projects should be reviewed. While some hypothecation may be justifiable, funds could be reallocated directly to businesses according to defined outcome measures (e.g. level of recycled material embodied in a product).

### ***Congestion***

I am also supportive of the TWG's recommendation regarding congestion charging. However, the recommendation relating to road transport and congestion charging is currently underdeveloped and requires more substantive analysis.

The analysis should include the adoption of a whole-of-system perspective encompassing the multiple externalities associated with road transport and infrastructure provision. Within this context, consideration should also be given to the role of taxation in facilitating the adoption of low emission vehicle technologies including electric vehicles.

Road transport generates a range of externalities including greenhouse gas emissions, air pollution, congestion and vehicle accidents. In addition, these externalities are highly context specific and vary according to time, location, distance and vehicle class.

It is important to recognise that congestion is only a subset of the total external costs resulting from road transportation. Most of these external costs are closely aligned with driving activity as opposed to other factors such as fuel consumption. This suggests that driving activity may well be an appropriate tax base for the purpose of correcting many road transport externalities including congestion.

I am aware that Singapore has implemented a charge that accounts for time, distance, location and vehicle class. While this charge has been applied only to congestion, it demonstrates that charging for all road transport externalities is possible, especially with the increasing availability of digital technologies to measure driving activity.

## *Climate change*

While I agree with the priority the TWG attaches to climate change, I don't consider that it should pursue recommendations in this area. The Interim Climate Change Committee is currently progressing work in this area and, given the resources and expertise it has, is best-placed to advise on any emissions taxes or reforms to the NZ ETS.

A reformed NZ ETS which includes agriculture is only one approach for addressing methane and nitrous oxide. I will be addressing how biological emissions from agriculture could be addressed in a report due for release early next year.

## **Final comments**

Once again, thank you for inviting further comment. Given the time that remains available I would encourage the TWG to consider focusing its available resources on the waste issue it has identified since this has the potential to yield significant progress in the relatively near future.

Beyond that, a road map for a genuinely in-depth investigation of both environmental taxation and the broader issues I have referred to would be a genuinely useful way of ensuring that this topic does not succumb to the sort of ad hoc tinkering that has characterized its development in New Zealand to date.

With kind regards

[1]

Rt Hon Simon Upton  
Parliamentary Commissioner for the Environment

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<sup>i</sup> OECD, 2013. Effective carbon rates. OECD Publishing: Paris.

<sup>ii</sup> HM Treasury, 2013. Landfill tax rates from 1 April 2013. HM Treasury: London.