# Tax Working Group Public Submissions Information Release

## Release Document

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# Submission to the 2018 Tax Working Group 2018-03-06

**Simon Louisson (individual)**

A good portion of TWG terms of reference relate to the concept of whether the NZ tax system is fair and I submit that it is fundamentally unfair as there is little to no tax on the increase in the value of assets while all income from wages and salaries attracts tax.

For example, my family trust makes hundreds of thousands of dollars most years and attracts almost no tax because the vast bulk of that wealth increase (effectively income) comes from the rise in the value of shares, which is not taxable. This is just completely unfair from a societal viewpoint.

Household A earns $200k from income and pays around 25% of that in tax while Household B earns the same from selling shares that have risen in value, legally pays no tax.

Just as important as fixing the unfairness of the system is that if those who are currently not contributing their fair share, via their legal tax avoidance through capital gains, are brought into the tax system, then the vast majority of people (~80%) would be better off.

The latter point is crucial, in selling tax reform and countering the hysteria (they want to put a tax on your car/boat) that would inevitably be promoted by those with a vested interest in preserving the tax-free status of assets.

The side-effect of our unfair system is that NZ has low productivity because of misdirected investment. Most of NZ's available assets are directed towards the most obvious method of avoiding tax, which happens to be the property market because the tax system is also unfairly skewed in favour of property investment.

There has also been over-investment in farming, where people invest very large sums into farms that make very poor returns over the medium-to-long term but they achieve very high non-taxable gains when they sell their farms. This contravenes the concept in your terms of reference relating to finding the right balance between supporting the productive economy and the speculative economy.

Another obvious side-effect of our unfair and skewed tax system has been the spiralling property market bubble that is both dangerous to the integrity of the financial system and has meant that owning a house has shifted beyond the reach of someone on the average wage. A house-price-to-income ratio of 9x in Auckland is undesirable from a social point of view, unproductive from an economic point of view and dangerous from a banking point of view.

New Zealand is one of the few countries in the developed world not to have a wealth or proper capital gains tax. The so called "Bright Line" test is a joke, even when extended to five years. Firstly the name is confusing (deliberately so, as the previous government did not wish to be seen to be introducing a weak form of CGT). Secondly, most investors are quite happy to wait even five years when house prices keeps heading north. Then they pay no tax on their gain. The test should have no time limit – it should apply no matter when a second house is sold.

The clear solution to the problem of unfairness and widening the tax base is a comprehensive wealth tax on all assets (including the family home or at least on the value above the median house price). All assets should attract tax equivalent to a 5-year government bond.

So for example, if you owned a $100,000 section, that would be deemed to have earned $5000 (assuming a government bond rate of 5%) and the tax on that would be at your marginal tax rate of say 33%, which means your tax bill for the asset would be $1650.

It is relatively straight-forward process to value your assets – most people do an assessment every time they take out insurance.

The beauty of a wealth tax is double pronged – firstly it eliminates the unfairness of the current regime. Secondly, it will change investment behaviour so that investment will be directed towards productive assets that achieve a better rate of return that government bonds. This will discourage over-investment in the property market (where rents are nowhere near an adequate return on capital) and will likely see investment in unproductive farms retreat.

The most important part about introducing a comprehensive wealth tax is that there should be an offsetting reduction in either income tax or the rate of GST. **It has to be shown that the majority of people will be better off.** The only ones who will be worse off will be people like myself who are currently able to get away with not paying their fair share.

It is **absolutely crucial** in selling the concept to the public that people should be totally clear that there will be **no net increase** in the government's tax take.

As the effects of the wealth tax kick in, there must be a process set in concrete whereby either income tax or GST would be cut by the amount collected in the wealth tax.

Communications and selling the concept in terms of its fairness would be vital to the introduction of such a system. Recent polls show the majority of New Zealanders support a tax on assets. https://www.tvnz.co.nz/one-news/new-zealand/over-half-new-zealanders-support-capital-gains-tax-properties-other-than-family-home-poll This poll shows that most people understand the current system is unfair and so long as the new system is shown to be fair and not seen as a tax grab (ie that there is an inbuilt system for offsetting the government's gain from the wealth tax by offsetting tax cuts) they will welcome a comprehensive wealth tax, particularly if it is shown that most will be better off.

Other points:

- Progressive tax system
  I think that as a general principle the tax system should encourage progressiveness. New Zealand as a society has in the past thrived on being an equal society where the disadvantaged have had similar opportunities to the advantaged thanks in the main to having a progressive tax system where the better off pay more for public facilities than the less well off.

Equality has diminished in the post Rogernomics era. Introducing a comprehensive wealth tax would mitigate the necessity of increasing the progressiveness from the current set-up.

- Gift tax

  The abolition of the Gift Tax was simply another way for the wealthy to avoid playing tax or for them to pass on their wealth to their children. It should be restored and the old $27,000 allowance should be inflation adjusted.
- Trusts

  Most trusts are used as a vehicle for avoiding or minimising tax. They are almost exclusively used by the well off to shield assets from Inland Revenue. The TWG should assess how much tax is lost to the system through people using trusts and should make recommendations about a comprehensive review of trust law to minimise this activity
- Base erosion and profit shifting

  The failure of large foreign companies to pay their fair share of tax in this country (and others) undermines the tax system and unfairly disadvantages local firms paying their fair share.

  I believe it is quite simple to bring the likes of Google and Amazon into the NZ tax system. Basically, after say a two-year set-up period, any foreign company should be taxed at the NZ company tax rate, based on its NZ sales and taking into account the profit to sales ratio of the parent company. The onus should be on the company to show why it should not pay the full rate of tax due based on an assumed rate of profit/sales in line with the parent company. If the company can show it is making fresh investment in New Zealand that is legitimately tax-deductible, then well and good.

  For example in the case of Google, its parent company, Alphabet, in the last quarter had gross income of $32.3 billion and net profit of $6.b billion – a 20% profit ratio to sales. In 2016 it is estimated Google had $12.2m sales in New Zealand but paid only $356,000 in tax. http://www.nzherald.co.nz/business/news/article.cfm?c_id=3&objectid=11999548 Under my proposal, it would have had to pay $683,000 (assuming a profit ratio of 20% on sales and a 28% tax rate on those sales) unless it could show it had offsetting new investment in New Zealand that should reduce that amount.

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