

Tax Working Group Public Submissions Information Release

Release Document

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A submission to the Tax Working group. April 2018.

From Toby Heale.^[1]

[1]

Challenges, risks and Opportunities

When Indirect taxes were introduced in Europe it was claimed that they would herald the shift from direct to indirect taxation.

Universally we now have both and at high rates.

All government is addicted to spending. Some have a worse addiction than others but it remains a truth. There will never be enough tax income.

I regret that I must step outside your terms of reference so soon, but it is necessary to strike a balance between raising tax and government waste. Naturally, one man's spending is another man's policy, but waste exists. I cite NZTA funding ECan to run busses that are contracted from a Christchurch City Council owned company. The busses lose so much money (and are not patronized) that ECan must subsidize them further.

The willingness to pay tax evaporates when such pluralism and waste is exposed as it always is, but always at the last possible moment. By that I mean there is a posture to protect the status quo rather than to reform. That's human, but it is not supportable with taxpayer money.

New Zealand does not deserve to earn the reputation of being profligate, but New Zealand is not taking proper steps to root out waste, so it risks earning that reputation.

All tax revenue will be harder to raise once that reputation has been awarded.

Changing Demographics. A great deal is being written about the increase in older people as a percentage of the population and you can see observers extrapolate their conclusions. That has to be wrong. The growth in older people in the population is a one-off. It is a shift that is all, there can be no comfort in the notion that old people will go on growing in percentage. Only increases in lifespan will do that. Once the average age reflects the increased lifespan the one-off effect will have been absorbed and, like inflation, it will pass out of the statistics. When that happens, wealth will flow from the old to the young as it used to, and houses will be released in the same percentage as they were. Naturally there are intermediate steps, like retirement homes, that alter the figures somewhat, but they will not alter the proposition.

Immigration is the other driver of demographic change, but immigration can only progress at the speed of assimilation. Multi-culturalism does not work according to Angela Merkle. It produces ghettos. While no one will tolerate forced integration, it must be accepted that immigrants have come to New Zealand because they want to be here. Promoting diversity is to promote schism in society when there is every reason to hope for homogeneity. Current policy can be seen as hostile to efficient government use of taxpayer interests.

Maori interests have particular place in New Zealand history and life, but it is difficult to 'see' a Maori economy as a separate entity from New Zealand's. It is certainly not tolerable to grant any part of the community special rights or tax breaks. However, to correct any imbalance in wealth creation or retention, emphasis could be placed on education and that could be dealt with efficiently (see below).

Government revenue will collapse from existing sources, principally fuel duty and revenue from electric power. The law of diminishing returns will certainly apply to fuel if the government increases duty, because there will be a surge in electric car purchase. Yes, they are expensive, but in time, more will enter the second-hand chain, and as the product goes up the 'S' curve new car prices will reduce. The

balance of payments will be beneficially impacted by lower fuel imports and that will be critical because, as interest rates rise in the near future, it will be necessary to repay foreign debt. The responsibility to repay debt will be a great drag on government's ability to spend. Income from power-stations will also reduce as consumers switch to solar-panels. These prices will collapse in the coming years as perovskite panels are printed on a roll. It will serve as a tax break to consumers, and government would be ill-advised to take it back. Therefore, government must, first watch every penny, and second it must contain its appetites.

Containing its appetite means that government must face its Bottomless Pits and see them for what they are. (see below). Reforms are essential in this area because the current situation will run into an uncontrollable behemoth. When considering the cost of health care, it is worth bearing in mind that the British National Health is Europe's largest employer.

Climate Change is arguably not caused by man-made carbon dioxide emissions, unless you consider the big change, which is that in the 1800s there were approximately 1.7bn people on the planet and now there are approximately 7.1bn. But you would have to include woman-made carbon dioxide emissions, however much that might offend political correctness, for which I have no time. However, global warming does exist and it is likely to continue for another one hundred years or so if you believe (as I do) in the cyclical argument. You do not 'fight' it. That is like fighting night and day or high and low tide. It is a childish attitude to a severe problem. Disease control will be an important dimension as New Zealand is faced with importing diseases and pests previously unknown here. These will threaten agriculture and humans alike. There is an answer that will prove to be the cheapest and it is to use New Zealand's isolation to advantage. New Zealand should ensure that its neighbours in the Pacific are disease free. It must be clear that if they are not neither will New Zealand be. But if they are, New Zealand has an opportunity to use notifications nearby as an early warning system.

The changes in weather are just as likely to be more benign as less benign. There can be no assurance that the weather will necessarily be worse. There will be more water available from the hydro dams (because power will come from the sun) for irrigation and that may be necessary. Regardless of environmental concerns there can be no tolerance of any policy that risks farmland becoming a dust-bowl. So far as pollution is concerned, New Zealand has an old stink-pot vehicle population. That will erode in time and if fuel prices are increased that erosion will be faster.

Financial Capital is weak. Capital formation is poor with a weak presence by the New Zealand Stock Exchange. There is far too much reliance on funds from (foreign-owned) banks and when interest rates rise, as they will in the fullness of time, the pain suffered by New Zealand business, and particularly agriculture, will be severe to back-breaking. Because government is also funded on the short-term there will be little ability of central government to help domestic business. Local government finances risk becoming a shambles. A domestic bond market is urgently required and borrowers be brought to understand the advantage (especially at these rates) of locking in finance for twenty years or so. Because this is urgent it will almost certainly require tax concessions on coupon payment to increase acceptance. Therefore, withholding tax has no future.

Human Capital has been debased by a politically motivated emphasis on Human Rights rather than on Human Duties, Obligations and Responsibilities. In other words, the subjugation of the population rather than protection of its citizenship. This is a world-wide shift started by President Carter and used by the American negotiating team to advantage at the Helsinki and Reykjavik disarmament talks. The emphasis on rights was not expected to leak into domestic American life. However, the English-speaking world has no immune system that protects against Americanisms. For instance, the word 'harassment' has been imported, when attached to the word 'sexual', complete with the American stressing.

It remains true that Citizens are cheaper to look after than Subjects. Citizens (who are led or, even misled, politically) are inclined to take control of their lives, to make their own decisions and to make the best of what they have. Subjects (who prefer to be ruled) require to be provided for and they know their rights. This observation is not politicized as far as I know, but it easily could be. If this proposition is accepted and progress to correct the perceived imbalance is seen as desirable, it is important that it is not politicized.

Social Capital stems from a lack of corruption. But I caution that the closer corruption is to you the more difficult it is to see. From 'The Old Pals Act' to hiring environmentalists to police the 'issue of concern' in a development, rather than to allow them to protest about it, demonstrates corruption. New Zealand is a small community and a great deal is accomplished on the old boy (and old girl) network. It represents social capital of a sort because it's how things get done. But it is dangerous today, because it tilts the playing field against those who are new to New Zealand and they will become an ever-increasing percentage of the population. Integration and not diversity is the key decision to make sure New Zealand business and society become homogenous.

The Design of the Current Tax System needs some review for changing circumstances. And the claim that it is a low-rate tax area should not go unchallenged. Adding all imposts together produces an expensive country to live in. The law of diminishing returns is probably closer to hand than politicians may admit.

Social Taxation like social engineering is a disaster. This is usually an avenue for partial activism and the suppression of tobacco use is a classic example. While no one claims smoking is in not harmful, it can be made less so. By prohibiting the addition of any chemicals to either the paper or the tobacco in a cigarette, the nature of smoking cigarettes changes, because after one puff the cigarette goes out. One cigarette would do the work of possibly ten. I asked if there had been

a study that found, or failed to find, any relationship between the suppression of tobacco use and the rise of Meth-Amphetamine use. I did not get an answer. But the cost of Meth-Amphetamine use must be added to the cost of tobacco and the name changed to the cost of smoking. Further, if the person driving towards me was on any drug, including sedatives, I would prefer it was tobacco. There is every reason to reduce duty on a chemical free cigarette. It is worth emphasising also that smoking and drinking are reaction, usually to induced stress. The activists are treating the symptom, not the cause. Maybe the activists themselves are the cause.

Capital Gains Tax was introduced into the UK by Harold Wilson as a sop to the Unions who wanted to 'get the bosses'. It is regarded as revenue neutral by everyone involved except the accountants who can be relied upon to be avid supporters. It is so complicated to levy and calculate that even the revenue (in the UK) does not challenge the numbers. Instead, it selects an accountant and raids it *pour encourager les autres*. As a result, no one trusts the tax authorities and that is territory the tax authorities in New Zealand have been in before and have escaped from. I am convinced they have no desire or intention to return there. Capital Gains taxes are a light-weight sop to activism. They are a heavy-weight burden to those who have to comply and given that accountants fees are tax deductible it will be the revenue that winds up paying for it. Also, very careful study of the allowance for capital losses may change the appetite for such a tax. Other countries have made this mistake. There is no need to follow them, especially while the political will and ability to repeal bad legislation is so weak.

Distributional Outcomes touches on what government cannot do. If it is accepted that when demand is put in the private sector wealth is generated, while if the same demand is put into the state sector wealth is drained, there needs to be more caution about de-distributing tax money. It is clear from the charts on pages 31 & 32 that the current policy is massively wasteful. Deciles 1-3 don't have disposable income but they are taxed. Money is then transferred back to them. It

is necessary and urgent that these deciles are given a chance of standing on their own feet and able to make a success of their lives. There should be a personal allowance and I don't believe that would be questioned. The basic rate should be reduced to one percent to prevent the audit trail from going cold (back-dating that would be a vote-winner, but we are not discussing that -yet), and it would be accepted that the cost of collection exceeded the revenue generated. But the downstream information would be used to set to the parameters necessary for an equitable outcome. The basic pay-rate is now \$15.60 an hour making \$624 for a basic forty-hour week. That translates to \$31,200.00 gross per annum on a 50-working-week year. It is a political decision where the one per cent rate ends, but it would seem sensible that it did not end below \$31,200.00. It must be borne in mind that Deciles 4 & 5 only break-even (Fig 11) and still require support (Fig10). The golden rule must be that taxation is affordable. Usually it is 'the rich' who complain, but in the current situation it is the poorest who are being hurt the most.

Rich and poor. Although not appropriate in this section it is necessary to consider that a lack of taxable allowance on domestic staff is hindering employment in a group unable to find it elsewhere. There are many people who could find employment in domestic service and discharge their duties with diligence, pride and a sense of purpose. They may be able to achieve little else in life. But because of political prejudice they cannot find employment in domestic service because the employer cannot offset the cost of domestic full-time staff against their personal taxation. It is an example of political bigotry getting in the way of safe and reliable employment for people it is otherwise proving difficult to employ.

Thinking outside the current system with a few alteration New Zealand has an admirable situation to start from. The American adage, 'if it ain't broke don't fix it' applies. Complication in taxes is to be avoided and New Zealand has some taxes to get rid of. The pie chart on page 24 (Fig 4) demonstrates that four taxes yield 5%. There is every justification to assert they cost more to collect then they yield

and they should be abandoned. Simplicity is key. If there is any concern, ‘where will the money come from?’ see Bottomless Pits below. FIF is nonsense, as is any capital tax. New Zealand is short of domestic capital. The country is inventive and its entrepreneurs and inventors must seek their investment finance in the USA and elsewhere. That is truly sad and it a true betrayal of all the country stands for because ownership is transferred for the investment. It is imperative to leave capital alone and help it grow. If the revenue could go without domestic withholding taxes then do so. Perhaps withholding tax-free bonds for domestic borrowers would be an avenue to study. All the councils are bust or nearly so. Rising interest rates might do it for some of them. They need to fund long-term and domestically. New Zealand must, as in must, develop its quoted, trading, domestic capital market.

There is so much nonsense in the attitude that state owned assets are crown jewels. You can hear it. Investments are like leeks. You plant them, grow them and harvest them. There is no magic about it. These assets will degrade in time and ratepayers will be left with the residue. And the residue will be debt, not compost. Local authorities must be led to divest and spare their ratepayers from unnecessary rate rises or unnecessary gearing. Although this is not directly taxation it will have a huge and positive impact on the nation’s finances. And in that sense it is relevant to taxation because it generates wealth in the private sector and reduces the need for taxation because it reduces state (including local government) involvement in business. There is no evidence that local authorities can run assets better than the private sector and there is ample evidence that it cannot.

Thinking outside the Current System – Bottomless Pits. Fig 6 (on page 25) demonstrates clearly that government will never, like ever, be able to satisfy the demands for money for three customers. Education, Health and Social security and welfare are each Bottomless Pits.

I have made two suggestions that might, should, reduce the burden of social welfare costs. Domestic service and a 1% basic tax rate. It

would be prudent to see if those generate the desired result before going further. Health and Education are both different manifestations of the same problem. They are local services and they serve local needs. 'User pays' is the concept that can be applied, but only in part. I would propose a new corporate category, a 'Not for profit corporation'. I appreciate that some not for profit companies are viewed with suspicion because they pay themselves too much, but the structure does have a valid use here and both teachers and nurses could do with some wage inflation. The state would cap spending on both education and health in light of budget availability and need. The balance would be raised locally through donations, subscriptions and a change in the way ACC works. There is no need for ACC to pay for the cost of car accidents. It takes only a little downstream activity to identify the insurer of a car (number plate) and to identify the cost of victim's treatment (internal accounts). Adding a margin to that and sending the bill to an insurance company would sort out a great deal of bad driving. There would have to be a change to the law, and there would be complaints from insurers. There would also be threats of higher premiums. But there would be a desirable result for the hospitals. Schools need to understand that standards have been falling for years. This is because of a lack of leadership and a drift towards consensus policy forming. Consensus policy forming is a drift to lower standards. Schools should run their own classes in the evenings for adults in all the subjects they find it difficult to fund. That would have the effect of 'sharpening up' the standard of teaching and could bring substantial revenue to a school by using its assets more effectively. There could be objection from teachers. That might lessen when they discover that they were to be paid.

While on Fig 6, please watch Finance costs. They will balloon unless attention is given to growing the domestic capital market for long-term bonds.

Overseas Suppliers. Satisfactory agreements must be made about transfer pricing. But, where a foreign company trading and selling

into New Zealand and is thought to be washing its tax liability out of New Zealand a sum can be derived.

GST on sales =15% of turnover in NZ(i)

(i)divided into parent company's total turnover = percentage of total turnover garnered from NZ business. (ii)

Divide (ii) into gross profit of parent company to calculate liability to NZ tax. There will be protests but they will come to the table to talk and you are back to a transfer pricing agreement.

Overseas Supply -Bottled Water A flat tax of two cents a litre on all water for export, bottled in New Zealand or not. It would be outrageous to increase any impost on New Zealand citizens while allowing foreign (or local) companies to export natural resources without making any contribution to the country.

Toby Heale

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