Tax Working Group Public Submissions Information Release

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[1] 9(2)(a) - to protect the privacy of natural persons, including deceased people;

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In preparing this Information Release, the Treasury has considered the public interest considerations in section 9(1) of the Official Information Act.

Taxing times

Tax and taxation are as old as civilization

From ancient manuscripts and books such as the Bible we learn of rulers and governments levying citizens to maintain power, defend against enemies, foreign and home grown, and to fund the building of infrastructure and monuments, useful and otherwise, that we now take for granted.

There has always been discussion, dissention, protest and sometimes revolution over the imposition of taxes. The Boston Tea Party that began as a protest against ‘taxation without representation’ was to become the trigger that set off the American Revolution.

Taxation can be used to promote social change, by increasing the price of goods deemed to be undesirable or of a “luxury” type, thereby guiding spending and investment into areas deemed to be more socially or economically desirable.

This can be fraught with difficulty, however, as many examples, old and new show.

The classic story beloved by generations of children of “The Scarecrow of Romney Marsh” was based on the exploits of smugglers “providing ‘brandy for the Vicar, baccy for the clerk’ at cut prices by dodging the King’s Revenue Men.

In the same way in modern New Zealand, robberies to obtain alcohol and cigarettes, both subject to steeply rising taxes, show that such a policy can lead to an even greater evil than the one supposedly being cured.

Economists pontificate about the “distortions to the market” caused by this or that tax, as though a perfect, untaxed market is some sort of holy grail, instead of being rightly dismissed as a fantastic pipe dream.

Income tax, our most common form of raising revenue over more than 2 centuries, taxes work, a highly desirable activity.

It was originally a temporary measure introduced by William Pitt the Younger in England to finance the Napoleonic Wars and is complex and expensive to collect, with high compliance costs for taxpayers.

In its current form it has no place in a modern economy.

So in the 21st century who or what should we tax, how, and how much should different people pay? Should it depend on age, wealth, income, occupation, star sign or random chance?

Reason would suggest that we should be favouring taxes that efficiently promote desirable activity, and discourage anti-social or otherwise undesirable activities that impose avoidable costs on society either in monetary terms e.g. more spending on health, or that curtail freedoms such as levies and charges on access to information, and these policies can be at odds with each other depending on the definitions of cost and freedom.

In New Zealand we currently tax personal income, transfers of goods and services (GST) which is a value-added tax, i.e. it is only levied on the increase (or rebated on the decrease of each transaction and while NZ has one of the most broadly based such taxes in the OECD, there are large sections of economic activity that are exempt, such as financial fees and charges, including interest.

Initially levied at 10% (ten cents in the dollar) it has since been raised to 12.5 % and is currently at 15% and is seen as having the benefit of encouraging saving by adding costs to spending.

While it is levied at a flat rate it is in its effect a regressive tax, with poorer people who must spend a higher proportion of their income each week paying proportionately more of their income in a tax that puts up the cost of the essentials of living at the same rate as luxury goods which are discretionary for those with surplus income.

We also tax company profits, with a range of exceptions and a complex set of rules around expenses, fringe benefits and Loss Attributing Companies as well as other ‘fine print’ provisions.

No wonder the IRD has some 2000 forms on its website!

There are also a raft of special levies, such as fuel tax, alcohol and gaming taxes and duties etc., etc. each one with its compliance costs and peculiarities.

These complexities ensure that Taxation advisers and lawyers are busy people.

They are also protected people. If their advice is wrong, the liability rests with the taxpayer, not the adviser. Compare this to the requirements placed on a Real Estate Agent for example, who is deemed to be culpable and liable to heavy sanctions if they pass on incorrect information to a prospective purchaser, even if the client has deliberately lied to and misled them.

Then there are other areas that escape the net. Capital Gains (the increase in value of an asset) are only taxed in some circumstances and the definitions and grey areas have tax lawyers laughing all the way to the bank.

Then there is the REAL BIGGIE!

Total transactions through banks, stock exchanges futures markets, etc. amount to at least Sixty (yes, 60) times the trade in goods and services that form the basis of Gross Domestic Product or GDP as it's commonly known.

None of this purely financial activity attracts tax unless declared as profit. Indeed much of it is aimed at avoiding tax by obscure and complex shuffling of money.

A large part of GDP is subject to GST at 15%, and while dealing in Millions of dollars by computer on the financial markets is seen by some as necessary and beneficial to the economy, it is not paying a cent.

When I was 16 (not yesterday) I watched a ship being loaded with frozen lamb carcasses at the Port of Timaru. In the days before containerisation each carcass was unloaded by hand from a rail wagon placed on a greased wooden chute and pushed down the chute onto a sling placed on the wharf, to be hoisted into the hold and stacked. I the length of the 5 metre chute there were 4 wharfies each giving the lamb a gentle push to speed it on its short downhill journey. Given the nature and incline of the chute one would have been ample.

This sort of 'featherbedding' cost the producers money and in the end cost the wharfies the sympathy and support of their fellow workers when technology and containers became the new normal.

The point of this story is that, if we need to shift each dollar 60 times to generate $1 worth of GDP then the financial markets are worse than those wharf workers by far. It is inefficiency writ large, and tax free into the bargain.

There is no penalty, and indeed current tax law and mechanisms encourage such behaviour.

It is fair to assume that a good proportion of the 2008/9 income tax cuts which favoured those on higher incomes found their way into speculation in the property (Auckland housing) market or financial markets where returns could successfully avoid tax with little risk.

Let's debate these questions:

Are these such desirable activities that they should pay no tax?

Is shifting large sums of money by computer doing anything to assist the health of our society or the environment of our planet?

If not, should and can they be taxed*?*

My conclusion is that not only can they be and should they be, but it would be beneficial for the markets themselves and the whole economy.

A small levy of less than 1 cent in the dollar on every financial transfer would raise enough money to enable us to remove some of our more regressive taxes, such as GST, that have a disproportionate effect on the 80 plus per cent of us who live on less than the average wage.

We could set the personal income tax threshold much higher at say $50,000

We could get rid of some or all of the compliance heavy company taxes, and let companies put that effort into the productive part of their business.

All this can be done by using the existing Computer System, doing the

Transfers to take a small levy on Every Financial Transaction just as the

Banks do now on a daily basis with their Fees and chargers.

No forms, no exemptions so no avoidance - LETS DO IT!

N.B. This form of taxation was originally proposed by Nobel Prize winning economist James Tobin who wanted it as an international tax to fund the United Nations and "to throw sand in the gears of the markets".

All this in the days before markets were computerised and shifted vast sums at the speeds now achieved.

This tax is currently being seriously considered in Britain and Europe.

The tax is low rate and flat in imposition, but progressive in application (he/she who moves the most money pays the most tax.

The only unknown factor is the amount that would be raised given that the degree to which it will influence behaviour is untested.

If initially levied at a very low rate of about 0.3% say as a potential replacement for GST, it could be phased in in a balanced way, and prove no more disruptive to the economy than the now widely accepted practice of the Reserve Bank of altering interest rates. In fact small variations of the Transfer Tax rate could be a useful alternative tool for controlling inflation, by removing excess purchasing power without pushing up mortgage costs and cost of working capital for businesses.

Having a fiscal tool with a more direct impact than interest rates would be a better solution in the face of sudden major disruptions, but its use would need to be well controlled to avoid over-corrections and excess volatility.

Future Proofing.

In our rapidly changing world driven by technology and the global markets with which we now interact, traditional taxes will become harder to levy comprehensively. The current moves to try to impose GST on small private imports are a case in point.

How much simpler, and fairer to simply take a fraction of a cent in the dollar on the credit card transaction associated with the deal and have the onshore trader paying exactly the same.

Similarly with the rise of cyber payment methods such as “bit coin” and others the payment can be the same percentage.

In Conclusion:

It’s simple, cheap to operate, hard to avoid, not distortionary to the economy.

Can we possibly fund the requirements of a modern civilization for better infrastructure, health care and environmental improvement in a fairer way?

I don’t believe we can – let someone prove me wrong if they can.