

Tax Working Group Public Submissions Information Release

Release Document

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**INDEPENDENT SCHOOLS
OF NEW ZEALAND**

Representing the nation's leading private schools

Independent Schools of New Zealand – Submission to the “Future of Tax” review by the Tax Working Group

Introduction

Independent Schools of New Zealand (“ISNZ”) is the national body representing 46 independent schools in New Zealand which collectively educate around 88% of private school students in New Zealand.

The role of ISNZ is to promote choice in education in its widest sense. This includes representing the independent school view on education committees, advocating choice in education to Members of Parliament and government officials, providing services for schools, influencing educational thinking and policy, organising professional development programmes, liaising with other education groups nationally and internationally, and generally providing a forum for joint action by ISNZ Member Schools.

Independent schools spend approximately \$489 million annually, directly contributing around \$361 million to New Zealand’s economy with a total GDP impact (direct, indirect and induced impacts) of around \$697 million. In 2015, independent schools received \$42.2 million in government funding equating to \$1,580 per student. This equates to a quarter of the funding of an equivalent student in the state school environment. It is estimated that independent schools save the government around \$130 million per annum in salary and operational costs¹.

It is on behalf of our Member Schools that we make the following submission. Please note that our comments are limited to the tax issues with the provision of early childhood, primary and secondary education (i.e. education below a tertiary level), as these directly impact our members, their students and students’ families. This is not to say our proposed solution does not have wider application, but that it is not our area of expertise.

General comments and summary

ISNZ is grateful for the opportunity to provide input into the “Future of Tax” review by the Tax Working Group. We acknowledge the importance of this review and the challenges associated with ensuring that New Zealand has a fair, appropriate and sustainable system of taxation which meets the needs of New Zealanders by funding vital public services including healthcare, justice, welfare, infrastructure, and education.

We are pleased to note that the Four Capitals approach as per the Treasury Living Standards Framework is highlighted in the Tax Working Group background paper as being relevant to any

¹ Report on the Economic Contribution of Independent Schools in New Zealand, MartinJenkins 2016

analysis of the purpose and benefits of maintaining or amending the existing tax system. Human Capital, encompassing people's knowledge, physical and mental health is one of the four core elements impacting New Zealanders' wellbeing and contributing to our wider prosperity as a nation.

With respect to encouraging the development of Human Capital, through the education system, which is so crucial for fuelling the success of all New Zealanders, we consider that the Future of Tax review provides a timely opportunity to address unfairness in the tax system as it relates to participating in education provided by independent schools.

A focus on the taxation of education delivery is appropriate as part of the broader considerations being undertaken by the Tax Working Group, as the inconsistent application of the tax rules can adversely impact the availability of a parent's and/or student's choice of educational facility and accordingly, the wellbeing of New Zealanders.

Within the *Future of Tax: Submissions Background Paper* (the "Background Paper"), a series of specific questions are posed. ISNZ considers the question of whether the tax system should provide exemptions for certain goods and services from New Zealand's Goods and Services Tax ("GST") is directly relevant to the education sector.

While we acknowledge it is often a choice for parents to send their children to a private or independent school, rather than a state school, we believe this choice should be neutral viz-a-viz tax considerations such as the GST treatment of private school fees (discussed below), such that an independent school option is accessible to as many families that would like to choose it as possible.

We also note that a number of families who opt for a private education for their children do so because there is no viable alternative, for example for some children and families living in remote and rural areas. Further, private education institutions also provide alternatives for children of families whose beliefs, values or other specific needs cannot be met within the state school system. The population of students at independent schools is diverse as a result. It would be wrong to assume that only those parents with financial means can and choose to send their child(ren) to an independent school. The children attending independent schools are from a wide range of socio-economic backgrounds. Across the independent school network there are many parents who work multiple jobs and/or require financial support from extended family in order to pay for their child's/children's independent school education.

We consider that New Zealand's public policy needs to take into account the value of choice in education to achieve the aspirational goals of society as a whole. Specifically, recognising that the state school system does not suit all students and the increasing unaffordability of education alternatives, we request that the Tax Working Group consider remedying a disincentive to private school education by reducing the impact of GST on the cost of school fees, where a child attends an independent school.

New Zealand's GST is a broad-based value-added tax on general consumption, with very few exemptions. While this results in a relatively simple system that is easy to follow, ISNZ considers the application of GST to school fees promotes an inequitable system.

The current system charges GST on tuition fees charged to parents of students at independent schools. A 2016 report on the Economic Contribution of Independent Schools in New Zealand by MartinJenkins, (the "2016 MartinJenkins Report") found that in 2014 independent schools paid approximately \$64 million in GST on fees. ISNZ Member Schools accounted for around 95% of that figure. This tax is an additional contribution that must be funded by parents of students attending



independent schools as state and integrated schools do not charge tuition fees. At a family level, this can be a significant barrier to educational choice outside of the state school system (and as noted above, this is not always a choice available to parents).

ISNZ notes that state and state-integrated schools typically rely on the payment of donations to fund additional activities and expenditure. A tax rebate is available in relation to such payments. We support the availability of tax relief for contributions by parents to help fund a more holistic experience for their children. Independent schools provide a similar experience outside of the state education sector, catering for different educational needs. However, there is no tax relief for the cost of such an education (either through tax rebates or deductibility of school fees). The GST on school fees is an added disincentive.

Recommendation

The zero-rating of GST on tuition fees charged by independent schools would be a small but significant change to tax policy that would result in greater fairness for parents seeking choice, by educating their children outside of the state system.

ISNZ recommends that the GST rules be amended to provide for the zero-rating of the supply of education, specifically tuition at early childhood, primary and secondary schools.

Our detailed analysis, including consideration of the Tax Working Group's objectives, and the different analytical frameworks follow.

Tax Working Group objectives and framework

ISNZ notes that the education sector has a key role in preparing young New Zealanders to face some of the challenges identified in the Background Paper. These include:

- changing demographics – including an ageing population and an important role for the Maori and Pasifika communities, in particular, in fuelling NZ's future prosperity;
- the changing nature of work – with those growing up today expected to have “multi-stage” careers during their lifetimes, with various educational interludes in between as they retrain – partly, because of intensifying technological change.
- environmental challenges and concerns about inequality – with our younger generation increasingly concerned about the state of the planet and societal structures they will inherit.

Applying an educational lens to the challenges identified, the availability of a viable alternative to state schools is increasingly important to many New Zealanders. The role of independent schools is not to replace the state sector in the provision of education, but rather about providing greater choice for parents, who may wish to pursue different academic and other objectives for their children, with this challenging future environment in mind.

Technological disruption, the changing nature of work and changing demographics all have an impact on the demand for different types of education solutions. Variance in school ethos, location, religious affiliation, academic and sporting focus, and underlying principles ensure that different schools are able to cater to an increasingly diverse population with differing requirements.

While universal education is important so that all children have an equal opportunity for education and ultimately, contribution to society, the ability to select an educational facility based on desired outcomes or needs for a child is equally important. The availability of such choice also recognises



that Government does not have the ability to provide all New Zealanders' educational needs itself and should not attempt to do so.

Applying the Living Standards Framework

ISNZ also strongly supports tools like the New Zealand Treasury's Living Standards Framework in helping to analyse the trade-offs from different Government policies. In particular, the acknowledgement that all public policy, including education and the tax system, is ultimately aimed at improving the "wellbeing" of New Zealanders, which is wider than outcomes that can be measured financially, such as a person's income or New Zealand's Gross Domestic Product. (That said, positive policies are more likely than not to also lead to positive financial outcomes.)

ISNZ further acknowledges that wellbeing can be difficult to measure quantitatively, but agree that their impact should be considered qualitatively. We have attempted to do this below.

In ISNZ's view, the application of the Living Standards Framework strongly supports the availability of quality educational alternatives to New Zealand children.

While education touches on all elements of the Living Standards Framework, it is most closely aligned to the Human and Social capitals, of the Four Capitals:

- *Human capital* – school plays a key role in developing an individual's skills, competencies and knowledge at an early age, which in turn benefits society as a whole. Further, the school environment is important for supporting students' physical and mental health and preparing them for their role in society.

One of the potential measures of human capital development is students leaving school with NCEA (or similar) level qualifications. New Zealand academic results show that, on average, private schools outperform state schools of the equivalent decile level.

According to the 2016 MartinJenkins Report commissioned by ISNZ, students from independent schools in New Zealand scored higher than state school students in international PISA tests across maths, reading and science literacy. That report also estimates that \$110 million of New Zealand's GDP growth can be attributed to the level of educational attainment at independent schools.

- *Social capital* – in addition to promoting high educational standards, independent schools act as a community hub, providing facilities for various community groups to come together, they instil values in students which are beneficial to wider society, and provide opportunities for students from disadvantaged backgrounds to receive a high-quality education. All independent schools offer financial hardship scholarships to students to the extent they are able.

Application of the Living Standards framework suggests that educational choice is a desired public policy outcome. This in turn supports the removal of financial barriers, including through the tax system, that make it difficult for those parents who would like to exercise their choice to educate their children outside the state school system (for whatever reason) to do so.

Our concern is with the current inequitable treatment of fees paid by parents of children attending independent schools, which are not only not tax deductible (which compares with school donation tax rebates for state school contributions by parents) but are subject to tax (15 percent GST).



It is that latter feature of the current tax system that ISNZ's submission is focussed on. The current GST treatment contrasts with positions taken in most other countries with a GST or Value Added Tax type, including Australia which does not apply its GST to education services (public or private).

The Background Paper recognises that removing GST from some goods and services is often discussed in public debate as a way to ensure that people can afford more of these goods and services. We believe there is a clear public policy objective for encouraging greater choice in New Zealand early childhood, primary and secondary education, through the removal of GST on the cost of New Zealanders' education, if they choose to attend an independent school.

Applying the traditional tax policy evaluation framework

We believe the argument for removing GST on school fees is also supported applying the traditional tax policy evaluation criteria:

- *Efficiency*: An efficient tax will minimise the impact on economic decision making. The New Zealand GST is considered efficient, or at least more efficient than taxing capital or labour income directly. While we acknowledge that the GST's broad base is seen as a key feature of its simplicity and, accordingly, its efficiency (i.e. if all goods and services are subject to the GST, then it does not distort behaviour in favour of certain goods and services), we do not believe that efficiency argument will be adversely impacted by removing GST (i.e. zero-rating) on the provision of education below a tertiary level. We note that there are precedents with provision of "financial services" and long-term rental accommodation currently outside of the GST net. Notwithstanding the exclusion of these activities, which will be much larger in scale than private education, New Zealand's GST base is still considered far more comprehensive than any other country's GST or VAT. In contrast, the net GST contribution from private/independent schools at around \$64m per annum would not have any significant impact on the GST base (but will have a material impact for those parents who must pay an additional 15 percent on the cost of their child's education).
- *Equity and fairness*: we believe this presents the strongest argument for removal of GST on education costs.

Taxpayers who choose to send their children to an independent school are effectively funding education twice. Firstly, through the payment of general taxes which fund and maintain the state school system, and secondly through the payment of private school fees through their after-tax income. ISNZ acknowledges that this is often a choice, but it does mean that from a 'horizontal' equity perspective a family that chooses to send their children to an independent school, by not participating in the state school system which their taxes fund, will face an additional cost that a parent of a state school child will not.

While it could be argued that this additional cost is justified from a 'vertical equity' perspective for higher income parents and families, that have choices that may not be available to those from lower socio-economic backgrounds, not all children attending independent schools are from privileged backgrounds in the same way that not all children attending state schools are from lower income backgrounds.

Our concern, from a tax fairness perspective, is that the application of GST to school fees creates an additional financial barrier to families (of whatever background) who are contemplating the benefits of independent schools for any number of reasons. Tax should not be a reason for limiting choice.



We note that Australia considered this issue and concluded that education services should broadly be GST-free, for equity reasons.

A background policy document that drew on the Australian Labour Government's 1985 Draft White Paper ("the Reform of the Australian Taxation System"), noted that:

*"Education services are provided by both government and private organisations; government-provided services are essentially free while private organisations charge fees (and are frequently in receipt of a government subsidy). It is not possible to apply a [Goods and Services Tax] directly to publicly-provided education services as there is no direct charge. **Private education services could be included in the [Goods and Services Tax] base but to do so would no doubt be considered highly arbitrary and discriminatory.**"*

Compliance and administration costs: ISNZ understands that one of the key concerns with excluding items from the New Zealand GST base is the potential compliance costs for providers and consumers, and the administrative costs for Inland Revenue.

ISNZ believes the introduction of GST zero-rating for primary and secondary education services would be administratively straightforward. There is already a zero-rating regime, and a definition of services, to which the following education services could be added:

tuition provided by a private school that is registered with the Ministry of Education, and accommodation provided at a boarding facility operated by a registered private school.

Fiscal adequacy: The annual contribution of approximately \$64 million to New Zealand's GST revenue is immaterial in the context of the approximately \$18 billion collected in 2017². Therefore, excluding private education services from the scope of New Zealand's GST will not adversely affect the future revenue sustainability of that base in any material way.

Discount on school fees for staff members' children

We note that another taxation issue of concern is the treatment of the discount on school fees to staff where their children attend the school at which they teach. The value of the discount is typically subject to Fringe Benefit Tax ("FBT").

The rationale for this treatment is that discounted school fees represent an employment benefit provided to the teacher by their employer, the school. While we acknowledge that there is a "private (economic) benefit" to the teacher, through reduced education costs, we believe that there are wider public policy benefits from treating such discounts as exempt from FBT.

Often, a teacher will choose to teach at a particular school because it aligns with their personal values, beliefs and ethos and will generally wish their child to also attend that school for that reasons. ISNZ considers that there are strong non-tax reasons for not discouraging this via the tax system.

ISNZ notes that there are number of benefits provided by employers "on premises" which are exempted from the FBT rules, for various reasons. This includes substantial benefits such as car parks. The provision of discounted school fees, in our view, is fitting of being included in the list of "on premises" benefits.

² Source: Schedule of non-departmental revenue, For the year ended 30 June 2017, IR Annual Report 2017, pp144-145



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