

Tax Working Group Public Submissions Information Release

Release Document

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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.

Tax and the Environment Submission: Ministry for the Environment

Key points

- Environmental and resources taxes and other pricing tools can play an increasing role in making Aotearoa New Zealand the most liveable place in the world
- Environmental and resource taxes and other pricing tools can be used as effective policy instruments, in concert with other tools, to change behaviour to achieve environmental outcomes and improve economic efficiency
- Environmental and resource taxes may not meet all traditional tax criteria but should be considered on a case-by-case basis
- We would appreciate the Tax Working Group's views on the framework (or frameworks) for designing environmental and resource taxes and prerequisites for successfully implementing them
- We strongly promote the continued development of the New Zealand emissions trading scheme (NZ ETS) as the principal tool to reduce greenhouse gas emissions and support our transition to a low emissions economy
- Where taxes are designed to change behaviour (e.g. to reduce pollution), we consider the outcomes sought can be further incentivised to reach efficient levels by hypothecating the revenue back to projects that aim to achieve the same outcomes
- We welcome the Group investigating the nature of the entire tax system to support a transition to a more circular economy.

Terms of Reference

The Group's terms of reference asks, amongst other things, "what role the taxation system can play in delivering positive environmental and ecological outcomes, especially over the longer term." In 2017, the OECD¹ reviewed Aotearoa New Zealand's environmental performance and recommended the Government expand the use of environmental and resource taxes, potentially within an overall reform of the taxation system. As such, the decision to investigate the role of taxes to deliver environmental benefits is timely.

The Ministry considers this term of reference opens multiple issues for investigation by the Group, including:

- environmental taxes that aim to change and correct behaviour that result in negative environmental externalities (e.g. nutrient runoff resulting in water pollution)
- resource taxes (or resource rentals) that aim to provide a fair return from a public or community asset that is used for private benefit (e.g. mineral royalties)
- tax concessions that aim to reinforce and support positive environmental externalities (e.g. conservation of native habitat on private land)
- uses of tax revenue received from environmental and resource taxes, and the potential to recycle or earmark tax revenues for specific purposes (e.g. environmentally-related research and development, remediation projects, or addressing iwi and hapū rights and interests).
- wider tax system impacts on environmental and ecological outcomes (e.g. the incentives or disincentives on consumption provided by GST and income taxes, and improving

¹ OECD, 2017. *OECD Environmental Performance Review: New Zealand 2017*. OECD Publishing: Paris.

income/wealth equality, which correlates with positive environmental outcomes, through changes to income and other taxes).

The Ministry encourages the Group to consider the environmental, social, cultural and economic impacts of each of these issues. Iwi and hapū rights and interests need to be appropriately considered as part of any analysis of environmental and resource taxes.

The Ministry also notes that there are environmental trends, such as climate change, which will place increasing burden on the Government's finances. For example, managed retreat from natural hazards and the maintenance of critical infrastructure.

View of the Ministry

Aotearoa New Zealand faces considerable environmental challenges and the Ministry believes taxes and other pricing tools should be part of the Government's response to these challenges.

Environmental and resource taxes should be seen as complementary to a suite of other potential tools including regulation, trading schemes, direct investment and education.

Advantages of environmental and resource taxes

The Ministry views environmental and resources taxes as powerful tools as they can potentially:

- improve the efficiency of natural resource use between competing users and across generations
- ensure environmental damages and pollution are included in the cost of goods and services, which encourages changes in behaviour as people respond to prices
- provide a fair return of a public asset that is used for private benefit
- provide flexibility and clarity to allow people to choose the lowest-cost combination of methods of reducing their environmental footprint
- provide an ongoing incentive for polluters to reduce pollution (rather than just reducing to an allocated discharge level)
- incentivise innovation to increase resource efficiency, and reduce environmental and ecological impacts
- raise revenue that can be used for environmental projects or reduce more-distorting taxes.

Overall, the Ministry believes that environmental and resources taxes and other pricing tools can play an increasing role in addressing some of Aotearoa New Zealand's environmental challenges and to make this country the most liveable place in the world.

We see environmental and resource taxes and other pricing tools, when appropriately complemented with other tools, as particularly useful to support meaningful transitions in our economy. For example, the Ministry considers a meaningful emissions price through the NZ ETS as critical to transitioning Aotearoa New Zealand to a low emissions economy and achieving our 2050 emissions target.

Environmental and resource taxes may not meet all traditional tax criteria but should be considered on a case-by-case basis

Critics of environmental and resource taxes have raised a number of issues associated with their implementation, such as instability of revenue, regressivity, inaccuracy of tools to measure environmental units, difficulty in determining an efficient price (that represents the cost of the externality), public acceptance, reducing industry competitiveness, and administrative complexity. We agree that some or all of these can be issues for certain environmental and resource taxes, however these criticisms do not apply to all of them. Some critics have suggested that environmental taxes should be nationally uniform. However, we do not consider this is necessary and if the tax is attempting to correct for externalities, differentiated taxes might be more appropriate. For example, charging a higher rate for nutrients to reduce the impacts on an iconic lake.

The Ministry considers that environmental and resource taxes should be analysed on a case-by-case basis, and considered against the alternative tool or tools available. For instance a tax could reduce industry competitiveness by applying additional costs to an industry; however the alternative may be a regulation which imposes even higher costs on the industry.

We note that with improvements in technology and increased focus and investment, the measurability of pollution levels or environmental harm has improved significantly. For example, improvements in telemetering of water abstractions provide a much more accurate picture of how much water is being taken out of our rivers, lakes and groundwater sources. Similarly, there has also been improvements to the OVERSEER model, which is being used to allocate nutrient discharge allowances to individual properties and used to estimate greenhouse gas emissions. But there is room to do more and this will require investment from both the private and public sectors.

The Ministry considers hypothecation of environmental tax revenues back to environmental projects is appropriate, especially where such taxes are set well below their efficient rate. In these cases, hypothecation can improve environmental and economic outcomes through both the incentive effects of the tax and the earmarked funding supporting further mitigation including fostering research and development in new low pollution technologies. We also see hypothecation as useful to improve the public acceptability of introducing such taxes. Where environmental and resource taxes are not hypothecated, they can reduce more distorting taxes in the economy. We would welcome the Group's views on the prerequisites to successfully implement environmental taxes.

The Ministry welcomes input on environmental and resources taxes and other pricing tools, especially for climate and fresh water

Currently, the Ministry administers a number of tax and similar pricing tools, including the Waste Disposal Levy and the NZ ETS. The ongoing water allocation (including allocation of discharges to water) work programme will also consider tax and other pricing tools within the scope of its work.

We strongly promote the continued development of the NZ ETS as the principal tool to reduce greenhouse gas emissions and support our transition to a low emissions economy. The NZ ETS will soon be analysed by the Interim Climate Change Committee, as part of its deliberations on the role of agriculture in climate change policy, and the transition to 100 per cent renewable electricity. We believe it is unnecessary for the Group to consider these issues given that a separate expert body has been developed specifically to do so. However, other aspects regarding the ongoing development of NZ ETS are welcomed including the use of auction revenue and the use of price controls, amongst other things.

How to allocate uses of, and discharges to, fresh water is a complex policy question. If tax and other pricing tools were used, they would likely be just one of many tools that would be woven together to address the issues of freshwater allocation. The Ministry would welcome the Group's analysis on how taxes could improve freshwater environments and ecosystems, as well as increase the social and economic benefits from the use of fresh water.

The Ministry welcomes input on how the entire tax system can support environmental and economic outcomes and make Aotearoa New Zealand the most liveable place in the world

The Ministry considers that environmental and resource taxes can support a transition towards a more circular economy. For example, we consider that using environmental taxes (including improvements to the waste disposal levy) and resource taxes can reduce waste, pollution, environmental degradation and resource depletion to a more efficient level and create more sustainable, resilient, long-lasting value in the economy. We note that the OECD² has recently found that "... a transition to a circular economy – with the associated reductions in resource extraction and waste generation – could take place with potentially significant positive (or at least without negative) consequences for economic growth or overall employment." We see changes to the tax system through an increase in environmental and resource taxes and a reduction in more economically distorting taxes as important, as it could provide significant environmental and economic benefits to Aotearoa New Zealand. We welcome the Group investigating the nature of the entire tax system to support such a transition to a more circular economy.

The Ministry recognises that the Resource Management Act (RMA) 1991 is a critical piece of legislation and it enables development to reflect and adhere to the values of the community. As such, we consider the RMA does not unnecessarily restrict the development of land. The Ministry welcomes the Group investigating the potential impacts on development and resource use that capital gains and land taxes could have. For example, we see land taxes could provide incentives to increase the efficiency of land use and disincentivise land banking.

Role of Tax Working Group

We look forward to the Tax Working Group raising public awareness of how taxes and other pricing tools can be used to deliver positive environmental and ecological outcomes. We hope that this will encourage further public discussion and highlight the priorities and concerns the public has about environmental and resource taxes.

Given the scope and timeframes for the Group we do not anticipate that it will be able to address such matters as detailed design of environmental or resource taxes, or how to address iwi and hapū rights and interest in relation to these taxes and pricing tools. We would appreciate the Group's views on the framework (or frameworks) for designing environmental and resource taxes and prerequisites for implementing them. We expect that this framework will need to be developed further to design taxes, and woven together with a wider package of tools.

² OECD, 2017. The macroeconomics of the circular economy transition. Working paper, OECD: Paris.