# Tax Working Group Public Submissions Information Release

## Release Document

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# FUTURE OF TAX

## Submission and Proposal

Submitted by Josh Hubbard

[1]

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# The Future of Tax in New Zealand

## Introduction

I want to begin this submission by expressing my gratitude for the tax working group for not only facilitating such an important discussion, but also for allowing the people of NZ to have their say on the matter too.

New Zealand's current tax system is fit for purpose in today's world. Should the world continue to develop as it has in the past, then it is capable of remaining relevant with mere tweaking at the fringes. However it is highly unlikely that things will continue as they have in the past.

With the advent of emerging digital financial technologies such as crypto-currencies, we run the risk of becoming fatally out-dated. The Banks understand this and are frantically buying up every crypto-currency patent that they can get their hands on, in an attempt to stay relevant.

If state institutions are unwilling to adapt, there is the potential for them to lose all relevancy in what some have described as the 4th industrial revolution. Crypto-currencies are already moving quickly beyond the decentralised payment block-chain that is BitCoin. In fact, the block-chain is already dated technology as new alternatives emerge that are less costly to operate, but far more scalable than BitCoin.

This emerging technology brings with it the possibility of a commercialised 'Internet of Things'. Meaning billions of micro or even nano smart contracts happening every minute. These smart contracts could form the basis for new automated companies that operate on a decentralised currency with a transaction network so vast that it would be nearly impossible to regulate or police. The current system has to rely on the conversion of crypto-currency into fiat before taxation can be policed. If users are no longer required to transfer in and out of these new currencies, then the current system will become irrelevant in this field.

Further, with stabilised crypto-currencies, and more user friendly digital interfaces, there is the possibility for a large scale uptake in use of crypto-currencies as payment methods within our economy. This also brings about the possibility of a dramatic increase in non-disclosed income. The more widespread that this becomes, the further crown tax revenue will fall.

If we were ever to reach a point where crypto-currencies became the preferred method of payment, Inland Revenue would have to revert to a single land tax (or similar), as it would be highly likely that they would not have the resources to police a decentralised payment system.

Therefore, I submit that in order to retain a functioning national revenue gathering system, we need to get ahead of the curve regarding emerging financial technologies. Fortunately, the current structure of Reserve Bank payment clearance systems lends itself well for a near seamless shift to a comprehensive single tax that has effectively zero compliance costs and is practically unavoidable.

# Proposal

***That New Zealand remove all taxes (save for excise or behavioural based taxes) and adopt a single infrastructure tax, in the form of a flat rate transaction tax administered by the Reserve Bank of NZ.***

I submit that doing so, at a rate of 1%, will gather over 30% of GDP in revenue, and greatly reduce the cost of administration of the IRD, and compliance costs on individuals, companies and corporations alike.

# How Would Such a System Work?

The Reserve Bank of NZ operates the Exchange Settlement Account System, and High value clearance system NZClear. Together with SWIFT, Real Time Gross Settlement (RTGS) at the Reserve Bank clears on average $29 Billion a day. Multiplied by 250 business days per year, that would give us an annual clearance value of $7.25 Trillion. At 1% of just those clearance payments, NZ could raise $72.5 Billion in tax revenue.

To date I have been unable to get an estimate of the relative size of intra-bank transactions. However, conservatively estimating that intra-bank transactions would value around 25% of the value of total inter-bank transactions. This tax system levying 1% of the above mentioned transactions and intra-bank transactions via digital collection (Programed into the processing software and transferring the revenue gathered directly to the Crown Settlement Account), would raise over $90 Billion in revenue. Approximately 32% of GDP @ a GDP of $280 Billion.

Additionally, The Continuous Linked Settlement system works on the ESAS-SWIFT interface. Settling an average daily exchange of $60 Billion, there is the potential to gather up to $150 Billion per annum. However, this would need to be weighed in order to assess whether it would have any negative effects in international payments. It could, however, be a valuable tool in decreasing high frequency trading and speculation in the NZD, therefore increasing the stability of our currency and reducing the likelihood of a speculative attack.

If this tax were implemented, and the entire settlement amounts above were available to be taxed, then it would be possible to raise approximately 40% of GDP (GDP @ Approx. $280 Billion) with a tax of 0.5%.

This philosophy of this tax is to remove the focus from income, and place it on transactions. In other words: “In order for you to facilitate this transaction, you must use public infrastructure, therefore, you must pay a levy of 1% (for example) of the transaction to the State to maintain and improve that infrastructure.”

[1]

# The Future Environment

***What do you see as the main risks, challenges, and opportunities for the tax system over the medium- to long-term? Which of these are most important?***

As mentioned above, technology will usher in many difficulties. There is an on going shift in consumer behaviour that is only increasing. For example, traditional brick and mortar retail outlets have to compete with the likes of Amazon, Wish, and AliExpress. With international shipping becoming more and more effective, and the quality of cheep goods slowly closing the gap with more expensive alternatives, consumers are purchasing international goods with ever increasing ease.

Further, the increase in emerging alternative and decentralized payment methods such as crypto-currencies is creating a growing field of potential alternatives to traditional currencies. Though currently volatile, relatively un-scalable and at times costly to operate, this emerging tech is adapting quickly and overcoming many of the hurdles preventing it from becoming a preferred payment method. I submit that it is not a matter of if, but when, will these technologies displace sovereign fiat currency.

***What do you see as the main risks, challenges, and opportunities for the tax system over the medium- to long-term? Which of these are most important?***

# Purposes and Principles for a Good Tax System

## Principles for assessment

***What principles would you use to assess the performance of the tax system?***

A tax system must be fair, and raise enough revenue to maintain and expand the countries infrastructure to support sustainable growth. It is important for a tax system not to dis-incentivise earning more, and it should be simple enough, yet comprehensive to prevent taxpayers from avoiding or evading the payment of tax.

## Defining 'fairness'

***How would you define 'fairness' in the context of the tax system? What would a fair tax system look like?***

A fair tax system encompasses principles that enable it to levy taxes in relation to someone's ability to pay, while taking into account the level of benefit a taxpayer receives from the use of our collective infrastructure.

For example, The person who uses our roads, energy grid, education system and health services should have a lower tax burden than the person or company that requires vast infrastructure usage to facilitate large volumes of sales to generate profit.

By taxing transactions rather than incomes, and removing the ability to avoid payments based on overspending or using loopholes, we further widen our tax base and remove the ability to avoid paying. The larger a transaction, the larger the overall revenue gathered.

# The Current New Zealand Tax System

## Frameworks

***New Zealand's 'broad-based, low-rate' system, with few exemptions for GST and income tax, has been in place for over thirty years. Looking to the future, is it still the best approach for New Zealand? If not, what approach should replace it?***

As noted above, with the rapid development of emerging financial technologies, the current tax system may no longer be the best approach. It is important to shift to a simplified and non-invasive system to mitigate the incentives of a wide-scale adoption of alternative payment systems that will likely erode tax revenue.

## Taxes and behaviour

***Should there be a greater role in the tax system for taxes that intentionally modify behaviour? If so, which behaviours and/or what type of taxes?***

Taxes can be a valuable tool for effecting behaviour. However, such taxes should be used only to help the damage caused by the behaviour the government seeks to modify (i.e Hypothecated). The current regime of excise taxes is separated from the three primary tax revenue sources, and therefore could remain in place during a shift to the new tax system.

It should be used rarely, as the advantage of the above-proposed single tax is for simplicity and reduced/eliminated compliance cost. Adding more taxes for the purpose of behaviour modification will undermine its simplicity.

## Retirement savings

***Should the tax system encourage saving for retirement as a goal in its own right? If so, what changes would you suggest to achieve this goal?***

Any encouragement of retirement savings must be applauded, however, adding complexity to a tax system for the sake of encouraging savings is counter-productive. The above noted revenue gathering potential shows that there is the possibility to greatly increase government revenue. Therefore, rather than complicating a streamlined tax system, it would be better to invest part of that additional income for direct incentives such as dollar for dollar retirement saving incentive schemes.

# The Result of the Current Tax System

## Fairness and balance

***Does the tax system strike the right balance between supporting the productive economy and the speculative economy? If it does not, what would need to change to achieve a better balance?***

No, particularly around speculating with the NZ Dollar. Also we see the damage caused by speculation in the housing markets. Though lauded for its simplicity, New Zealand's tax system is still sufficiently complicated to allow individuals and companies to limit, avoid or outright evade tax liability through the use of various financial instruments.
Such evasion results in reduced tax revenue and deteriorations of the standards of infrastructure causing a detrimental affect to our supporting infrastructure, and therefore the productive economy.

Further, the average individual or small business does not have the same resources to limit or avoid tax liability, meaning that a large sector of our economy is disadvantaged. This disadvantage limits healthy free market competition that promotes progress by empowering an effective monopoly of large companies.

The above-proposed system is so comprehensive that settlement cannot occur without the attached tax liabilities being satisfied. There are no loopholes for transactions settled in NZ with the NZD.

## Tax and business

***Does the tax system do enough to minimise costs on business?***

No, the system outlined in this submission shows that compliance costs on business can be greatly reduced. Further, the lack of compliance and elimination of large seasonal outgoings would greatly assists many of the business start-ups that currently fail in NZ.

***Does the tax system do enough to maintain natural capital? Are there types of businesses benefiting from low effective tax rates because of excessive deductions, timing of deductions or non-taxation of certain types of income?***

No, the ability of some individuals and companies to avoid taxes does not necessarily mean retention of natural capital. In fact, there is very little to support that the use of trusts for example is used to reinvest into the growth of the company. Meanwhile, companies in early stages can struggle with the seasonal nature of outgoings. Provisional tax and lump sum tax payments can put undue stress on small businesses unnecessarily, leaving them with reduced working capital.

A transaction tax at the reserve bank level means that tax obligations are satisfied at the time of the transaction taking place. The result is zero compliance costs and a practically unavoidable/evadable tax system.

# Thinking Outside the Current System

***What are the main inconsistencies in the current tax system? Which of these inconsistencies are most important to address?***

Companies purposely running at losses or specifically spending in ways to avoid tax obligations are inconsistent with the concept of income tax. Companies with charitable trust shareholders have the ability to avoid paying tax even in situations where it may not be that all the income is directed towards charitable purposes.

By shifting the rational for the tax away from being based on income, and instead base it on use of infrastructure; transactions are taxed for the purpose of maintaining the underlying infrastructure, rather than levying a portion of income to support services.

This removes the ability to redefine income as something else to avoid the attached tax liability. Further, it means that charities will have to prove that funds were spent on charitable uses to obtain a cash tax rebate, rather than to claim that it was used for such purposes in the hope it will never be investigated.

***Is there a case to consider the introduction of any new taxes that are not currently levied? Should any taxes be reduced if new taxes are introduced?***

No, additional taxes mean additional compliance and administration costs. The more complicated a system is, the greater the opportunity to avoid obligations. Moreover, the more intrusive a tax system is, the greater the incentive is to avoid it. As repeatedly mentioned in this submission, if there is a strong incentive to avoid tax obligations, then there is a higher possibility of a large-scale uptake in emerging disruptive financial technology.

If anything, the tax system should be greatly simplified.

# Specific Challenges

## Housing affordability

*How, and to what extent, does the tax system affect housing affordability for owners and renters? Is there a case to change the tax system to promote greater housing affordability? If so, what changes would you recommend?*

Again, by complicating the tax system, the possibility of unintentional tax loopholes increases.  That being said, tax can be a valuable tool for affecting behaviour.

By implementing the proposed tax system in this submission, there arises a possibility to establish a tax rebate on the family home, as well as a percentage based rebate on tax liabilities arising as part of a new home build.

## Capital gains tax

*Should New Zealand introduce a capital gains tax (that excludes the family home)? If so, what features should it have?*

Capital gains taxes are another way of further complicating our tax system that is currently praised for its broad base and simplicity.

However, the proposed tax system acts in place of a capital gains tax. For example, if there is a capital gain in the value of property, and that capital gain is extracted and spent; the arising transaction subjugates the gain to the same flat rate tax applied elsewhere. Even though the system is simplified further than current, it also broadens the tax base.

## Land tax

*Should New Zealand introduce a land tax (that excludes the land under the family home)? If so, what features should it have?*

As mentioned above, introducing more taxes increases compliance and administration. Further, by levying taxes on a single group of people, there is an increase in risk of how those taxes will be mitigated by the landowners. There is little control over where the ultimate liability will lay. For example; a land tax on an investment property will likely end up being paid by the tenants.

Instead, we have the opportunity to simplify the tax system and place the liability on those who are using public infrastructure. Meaning that everyone that participates in a transaction will pay the same. Those who financially use the infrastructure more will pay more with zero compliance cost, and very little administrative cost.

## Environmental taxation

*What are the main opportunities for effective environmental taxation?*

Environmental taxes are one of the exceptions where I see a valid argument for hypothecated excise taxes. Particularly around importation of plastic, and plastic packaged products, and high pollution industries. Any such tax should be strictly hypothecated, with all revenue raised being invested in preventing further environmental damage and repairing previously damages ecosystems.

## Progressive company tax

*Should the tax system do more to support small businesses? In particular, is there a case for a progressive company tax?*

Any action to support small business is to be commended. There are also instances of provisional taxes hurting small business and the self-employed with varied incomes year to year.  Though a progressive company tax may go someway to supporting small business, compliance is also problematic, and some small start-ups can get themselves into trouble where they are unaware of their complete tax liabilities.

A flat rate transactional tax such as the one proposed in this submission removes all compliance costs on small businesses. Further, there is an element of progressivism in that the rates paid by larger businesses are proportionately higher given that more transactions tend to occur during typical business of a large company in comparison to a small company.

**GST exemptions for particular goods**

*Should the tax system exclude some goods and services from GST? If so, what should be excluded? What else should be taxed to make up for the lost revenue?*

The calculations used in establishing the viability of the proposed system in this submission took into account revenue raised via GST. The system proposed would remove GST altogether while increasing total tax revenue.

# Summary

As the world enters the next stage in financial technology, New Zealand has the opportunity to ride the waves of development and bring all of its people along for the ride.

We can do away with costly administration, and compliance costs, freeing up the resources of hard working New Zealanders to produce more, relax more, or spend more time with loved-ones.

We can be world leaders in embracing the change and investing in our people and our infrastructure. We can increase spending on education, transport, health, environmental issues, and research and development. We can do all of this while operating a relatively non-invasive tax system.

All with an automated flat rate transactional tax that is administered by systems that we already operate.

Please feel free to contact me if you require any further information or source material from which my calculations have been made.

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