Tax Working Group Public Submissions Information Release

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SUBMISSION TO TAX WORKING GROUP

From: Geoff Cole

Date: 22nd April 2018

"If it ain't broke, don't fix it."

The phrase is widely attributed to Gainesville, Georgia-born Thomas Bertram Lance, the Director of the Office of Management and Budget during Jimmy Carter's Presidency. Apparently Bert Lance believed he could save Uncle Sam billions if he could get the government to adopt the motto, "*If it ain't broken, don't fix it!*" He went on to explain, "That's the trouble with government: Fixing things that aren't broken and not fixing things that are broken."

In February 2018 it was reported that he New Zealand government's operating surplus was bigger than expected in the first six months of the 2018 financial year as low unemployment and upbeat consumer sentiment helped GST and income taxes continue to track ahead of forecast.

The above was not an isolated instance but another tick on this country's very good financial report card over a number of years.

Overall, the current level of tax revenue, including local government rates, is equivalent to 32% of gross domestic product (GDP), which is slightly below the OECD average of 34% of GDP. This more than it should be and the Tax Working Group should be looking at how to get this figure even lower.

This submission is about let us not fix things that aren't broken but let us fix things that are.

And there ain't many things either way.

Our Tax System

The NZ Treasury claim in their 'Tax policy Priorities' (March 2012) that:

To be internationally competitive, the tax system must...

- Raise enough revenue to meet government spending
- Support taxpayer decisions that direct effort and resources to where they are most valuable
- Contribute to wider government goals
- Tax income at relatively low rates, to help keep New Zealand an attractive place for people to work, save, invest and establish businesses
- Operate in a consistent manner that creates certainty for taxpayers
- Be fit for a small open economy with one of the most internationally mobile labour forces

- Be relatively cheap to comply with and administer

In short, our tax system must be fair, balanced, simple, cost effective and administered well.

This submission covers the following topics:

1. Income Distribution and Growing Inequality
2. Wealth Tax
3. Goods and Services Tax [GST]
4. Taxing Tourists
5. Taxing Foreign Investments – Australian Ones In Particular
6. Tax Relief For Research & Development (R & D)
7. Housing Affordability
8. Tax Relief for Health Insurance for the Elderly
9. Capital Gains Tax [CGT]

1. <u>*Income Distribution and Growing Inequality*</u>

The spiralling upwards in the size of remuneration packages for Chief Executive Officers (CEO) and senior management is a disgrace. The concentration of incomes at the top is not only bad governance but can result in stagnant and even falling wage rates at lower levels. This situation can impact on housing affordability, especially when housing supply is stretched, as well as engender feelings of discontent and anger by those who feel their position is becoming increasingly hopeless.

If those who determine and award these ludicrous remuneration packages will not act then other measures should be investigated. For example: Higher tax on 'super' sized salaries.

The 'Otago Daily Times' (1 November 2017) reported as follows:

> *Otago University Business School Accountancy and Finance researcher Dr Helen Roberts' longitudinal study, which adjusted for inflation, showed the proportion of CEOs paid over $500,000 per year had also increased approximately five-fold across three different compensation measures.*
>
> *It showed chief executives were now paid 30 to 50 times more than the average wage of $60,000.*
>
> *Almost half of New Zealand chief executives now earned at least $500,000 as the cash component of their compensation package in 2013, compared to only 10% of CEOs in 1997.*
>
> *However, cash only represented some of the picture and total compensation and real wealth had more than doubled since the research began, with considerable change recorded in the last decade.*
>
> *In real terms, mean total CEO compensation was up 114% in 17 years, while mean real worker income is up 26%, confirming there is a widening gap between the CEO's income and that of their workers.*
>
> *The ever-widening pay ratio is an international trend - the CEO pay ratio in the United States for instance is typically between 300 and 500, but in some cases exceeds 1000 times that of the average wage.*
>
> *The highest paid executive of a listed New Zealand company this year is Fonterra CEO Theo Spierings, who received an $8.32 million salary package.*
>
> *Mr Spierings' 2017 base salary was $2.463m, plus benefits of $170,036, short-term incentive pay of $1.832m and long-term incentive pay of $3.855m, which worked out to an annual increase of 78.5%.*
>
> *Dr Roberts also tracked the economic performance of the CEO's company alongside remuneration, to give an objective overview of the link between CEO performance bonuses and company's annual results.*
>
> *"This clearly demonstrates an overall trend of marked growth over time which is not on the same trajectory as the economic ups and downs of publicly listed companies in New Zealand, nor worker salaries."*
>
> *Income fluctuated from one year to the next, but while some downturns, like the Global Financial Crisis, for example, dampened the increases, they still rose.*

The remuneration of CEO's in the public sector situation is also a disgraceful. It should be remembered that it was not so long ago that local authority CEO's were called Town Clerks.

Nick Truebridge focussed on Christchurch in an item for 'Stuff' (9 December 2017) when he wrote the following. It would be a fair assumption to say that Christchurch would not be the only city in New Zealand to be so afflicted.

> **Christchurch's public sector CEO salaries revealed**
>
> *Enable chief executive Steve Fuller earned $808,000 last financial year – that's $338,000 more than Prime Minister Jacinda Ardern.*
>
> *Fuller, who heads the Christchurch City Council-owned fibre broadband company, took home a fixed salary of $441,000 and performance-based pay totalling $367,000.*
>
> *Lyttelton Port chief executive Peter Davie, Christchurch's highest paid public boss, took home $955,000 – a fixed salary of $597,000 and incentive payments of $209,000 and $149,000. He is forecast to earn $961,000 next year. Paying council employees a living wage of $20.20, which will benefit 470 staff, will cost the city $775,000 a year.*
>
> *At lines company Orion, Rob Jamieson made $628,000 in the last financial year, while his counterpart at Christchurch Airport, Malcolm Johns, got $721,000, including a base of $600,000, an "at-risk" salary of $100,000 and Kiwisaver contributions of $21,000.*
>
> *Lyttelton Port Company chief executive Peter Davie earned two incentive payments of $209,000 and $149,000 in addition to his fixed salary of $597,000 last financial year.*
>
> *British Prime Minister Theresa May is on just over NZ$296,600.*
>
> *City Care chief executive Onno Mulder raked in $710,000 – a $547,000 base topped with an incentive payment of $163,000.*
>
> *Fuller, Davie, Jamieson, Johns and Mulder are among Christchurch's most well-paid public sector leaders. The companies they work for are either wholly or partially-owned by Christchurch City Holdings Limited (CCHL).*
>
> *Councillor Yani Johanson wants an overhaul of the way public sector chief executive salaries are set.*
>
> *The Public Service Association (PSA) argues the public sector has been sucked into paying private sector wages, but the Canterbury Employers' Chamber of Commerce (CECC) says it is "absolutely" important to keep these pay packets competitive in the open market.*
>
> *PSA national secretary Glenn Barclay says the shift to private sector practices has happened for about 20 years. "We've been sucked into the private sector argument that . . . these are the salaries you've got to pay to attract the right kind of chief executives because it's a global market and that's what they're worth."*

Canterbury Employers' Chamber of Commerce chief executive Leeann Watson says public salaries need to remain competitive to attract top talent.

"We obviously think that there are problems with that," he says. There are "numerous examples" of private sector bosses securing bonuses even when their company's performance "isn't that great or is even going down the gurgler".

"But for the public sector to buy into it as well is completely wrong. The public service element is what should drive the setting of salaries.

"Our members, by and large, they come to work for public sector organisations because they want to help, they want to make a difference. "It's a well- established factor known as the public service contribution and we think that should apply to chief executives as well," Barclay says.

CECC chief executive Leeann Watson offers a different opinion. "We've got some big challenges ahead of us as a city, so we should absolutely be making sure that those salaries are competitive in the market to attract the very best people and the right talent for the job."

Barclay says the public and private sector "shouldn't necessarily be in the same market".
"Going back to the state sector reforms, and local government got caught up in a bit of this as well back [in] the 80s and 90s, there was the idea that we needed as much movement as possible between the private and public sectors. "I wouldn't dismiss that, but I do think that what's more important is the notion of the career public service – the people who are doing well in that get promoted over time and they're the ones who understand the public sector, who understand the concept of public service and the importance of the public service ethic," he says.

Watson, despite being supportive of offering competitive public salaries in the open market, believes there needs to be a balance. "They do need to strike a balance, but that's a hard role for any organisation to take when you are trying to make sure that you provide a competitive salary package when you are being compared to others in the market place. "Absolutely there is a difference between big corporate organisations and your state-owned enterprises, so I think there is a balance. "But that has to be also balanced with actually putting something competitive out there in the marketplace to attract the right people, so that we can actually get the job done that we need to get done across the city," Watson says.

She has views on another feature of the city's 12 highest-paid public professionals, just two of whom – Christchurch City Council boss Karleen Edwards (on $402,900 a year) and Christchurch NZ chief executive Joanna Norris (on $325,000 a year) – are women.
"We have to make sure that we've got the right people in the right roles with the right skill set, regardless of gender. "I think it's always a bit disappointing to see the lack of women in leadership positions. "But actually I think as a region we do pretty well and we're starting to see more women in leadership positions and that's something that I'm pretty passionate about," Watson says.

Yani Johanson and Aaron Keown were on opposite sides of post-earthquake Christchurch's most high profile chief executive salary debate. The public sector boss in question was Tony Marryatt. Councillors eventually approved his $68,129 pay rise in December, 2011, boosting his annual salary to $538,529. Marryatt was controversial. Christchurch business leaders raised concerns over his operating style and questioned his reappointment process.

He was criticised for his involvement in the Ellerslie International Flower Show purchase, the proposed Arts Centre music conservatorium and the $17 million purchase of five properties owned by developer David Henderson.

Johanson was firmly against the increase and continues to speak out against large public pay packets. "I have repeatedly requested, when I was on CCHL and also on council, for a complete overhaul of how CEO pay is set. "There needs to be a different way of doing CEO public sector pay." Johanson does not pull punches when assessing current remuneration levels, calling the system "unfair" and "out of touch".

"I think the issue for me is we've seen a huge rise in inequality in our society over the last few decades and that's been exacerbated by this sort of situation," Johanson says. He asks a fundamental question – how much is a person worth?

"When you start to see some of the figures that are being paid, it's absolutely extraordinary in my view to think that would be necessary for someone to do the job. "That's in no way a criticism or an attack on anyone that's doing the job. "I think as elected members and as boards there needs to be a degree of accountability back to the people who are setting these levels of remuneration," he says. Johanson wants to see a system of relativity between those at the bottom of an organisation and those at the top, rather than the current system, which he says compares those at the top with those at the top.

"Effectively, you compare the ease of [how] some of these salaries seem to be set, versus the struggle to get a living wage paid to those people at the bottom," he says.

Keown was on the other side of the Marryatt debate. He voted for the salary increase.
At one stage, he was almost barred from helping appoint the council's next chief executive when Christchurch investment adviser and businessman Tim Howe lodged an injunction after concerns over Keown's public support for the incumbent, Marryatt.

His support of Marryatt continues to be a bit of a noose around his neck, he says. "People bring it up all the time. "But for me at the time, Tony's [increase] was just pay parity – that's what other people in the same position as him were getting paid," Keown says. "The bit that I didn't enjoy about that whole experience was why don't we go after all CEOs? Why is one person getting singled out?"

Marryatt's increase was in line with other city chief executives, including then-Canterbury Earthquake Recovery Authority boss Roger Sutton, who was on $500,000.

However, Keown believes there should be a cap on what public sector bosses are paid. "There should really be a limit to what they get paid, because isn't there a level of public service involved?" he asks, pointing to current leaders who have taken pay cuts to enter the public sector.

"They've gone from being multi-millionaires to try and make their country a better place.
"Look at America at the moment, I'm sure Donald Trump made way more doing property," he says.
Stuff

Recent news media reports have indicated that senior Plunket managers are now embroiled in 'the toxic problem of excessive executive pay.' Showing that the matter has now spread from the corporate to the voluntary sector. Disgraceful.

Recommendation: This is 'broken'. Fix it!

2. ***Wealth Tax***

The purpose of tax is to raise revenue NOT pander to the politics of envy.

New Zealand already has a tax on wealth. It is called rates and is levied on almost all real property. The higher the value of your chunk of real estate the more rates (i.e. taxes) you pay plus you pay GST as well.

Other than real estate wealth can take on an almost infinite variety of forms. From fine art to vintage airplanes; from rare stamps to ingots of gold; bank deposits to celebrity autographs. Imagine the army of experts the IRD would need to employ to:

(a) find this wealth
(b) assess the value of it, and
(c) actually collect the tax.

On the other side of the fence would be an army of tax experts that would be employed to thwart the fiscal fiends. Just what this country really needs!

New Zealand used to have a wealth tax – it came in the guise of death duties. In the 1990 election campaign, National promised, among much else, to abolish estate duty, and in 1993 they fulfilled that promise. The justification offered by the Minister of Revenue, was that estate duty was easy to avoid and therefore capricious. Nothing has changed.

In the UK they have death duties but they are called an inheritance tax and it is paid if a person's estate (their property, money and possessions) is worth more than £325,000 when they die. It doubles to £650,000 for a married couple - as long as the first person to die leaves their entire estate to their partner. The current rate is an eye watering 40%.

There is also the possibility of double taxation. Suppose you win $5 million in a lottery and deposit the money into a bank term deposit carrying an interest rate of 3.5%. You will pay tax on the $175,000 of interest earned. Fair enough but then along comes a wealth tax and takes a whack off your $5 million. A real vote catcher this one.

New Zealand has a low wage economy with poor productivity. A wealth tax is unlikely to encourage savings and investment and so build prosperity for its people.

Recommendation: A wealth tax is a nonsense. Forget it. Move on.

3. ***Goods and Services Tax [GST]***

"New Zealand's GST is the most efficient Value Added Tax (VAT) in the world." {NZ Treasury 'Tax Policy Priorities' March 2012}.

This is largely due to its design, comprising a single rate with very few exemptions and being a low-cost tax.

This is a clever tax as it is simple, pretty much unavoidable, easy to understand and inexpensive to collect.

It is paid by everyone including the highly paid, high nett worth individuals. Data may well show that the wealthy not only earn more but also spend a lot more and so are good GST contributors.

Tourists pay GST. Approximately $1.5 billion a year according to Chris Roberts, Chief Executive, Tourism Industry Aotearoa. This is half a billion dollars more than Shane Jones's pork pie Provincial Growth Fund.

The Government is missing out on some GST revenue through overseas internet shopping. Although this is likely to change as the previous Government had already commenced work on such a proposal and significant progress has already been made with Customs, Inland Revenue and Treasury. It would be a shame if the current Government was to abandon this work on the flimsy pretext of being accused of 'copy-cat' or 'stealing' policy.
Australia are about to implement a so called 'Amazon Tax'. Observing their experience may well be useful.

If the Tax Working Group really want to have a fiddle and suggest something over and above the 'Amazon Tax' then they might like think about increasing the GST rate to say 20%.

Certainly do not consider complicating the system by exempting certain goods and services.

The anguish of a GST increase that may impact on the lower paid could be mitigated via suitable adjustments to the welfare benefit system.

Recommendations: (a) Consideration be given to the idea of introducing an 'Amazon' tax;
BUT
(b) Our GST system ain't broken so no need to fix it!

4. ***Taxing Tourists***

Throughout New Zealand the growth in tourism is pressuring local authorities to provide a scale and quality of facilities that surpasses the needs of the local population and their ability to pay. The key issue is that the costs and benefits of tourism are spread unevenly. An estimated $14.5 billion annually comes from tourists into central Government coffers via GST, income and company taxes. The costs however are borne locally and local authorities have to go begging to central Government for money. Yet another example of the socialisation of profits with losses carried by individuals.

Local authorities are seeking the ability to charge tourists to help pay for the local infrastructure that they use. Currently the only tool local authorities have is the blunt instrument of a special rate on accommodation and hospitality.

Some form of local mechanism is required. The question is "What?" In this regard the local authorities and local tourism operators are perhaps the best people to provide practical and sustainable solutions.

Passenger service and facility charges levied at the border are a much less complex matter. Travellers all around the world face an increasingly complex web of taxes and they have different names under different jurisdictions. In general the departure & arrival taxes have morphed into various passenger service or facility charges; Border Clearance Levy; Fuel Surcharges; Bio & other security charges, Air Passenger Duty; Passenger Movement Charge; etc. They now tend to be included in the air or cruise ship fare.

It is claimed, for example by UHY Hacker Young (31 October 2016), that 'the financial burden of such taxes stifles tourism, hampers economic competitiveness and puts regional airports at a considerable disadvantage.' This may well be so for countries that are not over 2,100 km from their nearest neighbour and have many more international ports and airports often in close proximity to each other. Choice is not a luxury New Zealanders enjoy in this regard.

International visitor arrivals in the year ended January 2018 were in excess of 3.7 million. This was up 5% on the previous year and is forecast by MBIE to reach 4.9 million by 2023. Hardly a good case for the stifling of tourism argument and/or the hampering of economic competitiveness.

It is understood that the Border Clearance Levy, when combined with existing charges, is about $NZ36 for a return flight - lower than Australia's A$55 (NZ$58) passenger charge and Britain's £71 (NZ $137) long-haul passenger charge. Clearly New Zealand's levy is substantially less than either of the two examples.

The levy is due for review and reset on 1st July 2018.

This tax is simple to understand, difficult to avoid, readily collected and imposes the burden where it should belong - on that of the traveller. An increase of say $10 (or $20 return) represents only a small percentage of the total travel cost of those s arriving and / or leaving New Zealand.

Recommendations: (a) Taxes on tourism while not broken need to be more focussed at the local level;

AND

(b) Consideration be given to a modest increase in border levies.

5. ***Taxing Foreign Investments – Australian Ones In Particular***

Mum and Dads who want to diversify their savings and invest in Australian company shares have many complex hurdles to jump and our Inland Revenue Department contributes significantly to this situation. The problem is even worse for investments outside Australia to the extent that many do not even bother as it is in the too hard basket.

The prime investment focus for many New Zealanders is residential property. Governments appear to want this to change but have so far been largely ineffective. Maybe the big stick ain't working and the carrot on a string trick may be worth a try. Investment gurus are forever encouraging investors to diversify into other vehicles such as company shares in a variety of activities in a spread of countries. The theory being to reduce the risk of significant loss.

Unfortunately achieving these objectives is proving very difficult. The problem, apart from our low level of financial literacy, is the Foreign Investment Fund (FIF) regime administered by the Inland Revenue Department. The rules are so extremely complex that even tax accountants baulk at undertaking this work for clients. The FIF tax rules that were introduced around April 2007 and were aimed to encourage savings by low and middle income earners. It hasn't worked.

There are currently 13 companies that are incorporated or have a main place of operations in New Zealand that listed on the Australian stock exchange but not the New Zealand stock exchange. All 13 companies do not qualify for exemption from the draconian FIF regime. New Zealanders wanting to invest in these 13 New Zealand based companies are effectively told to go and look elsewhere. That is just plain dumb.

If you want to invest a total of less than $NZ50, 000 in certain Australian company shares then the FIF regime is not an issue. Step away from this and the eyes mist over in total bewilderment. The reasons for this include:

De Minimus Threshold: The figure of $NZ50, 000 is now too low and needs to be raised immediately to say $250,000.

Certain Australian Companies: The IRD's website provides the following information:

> ***List of companies that qualify for the exemption***
>
> *To assist investors in determining whether or not an Australian company satisfies the exemption criteria we'll provide a Australian share exemption list (IR871) for the relevant year. This is a list of companies from the ASX All Ordinaries index which we consider qualify for the exemption from the FIF rules.*
>
> *Investors with the standard balance date will be able to rely on the list and treat the investment as subject to tax under the general rules. We'll treat any investor who relies on the list as having taken reasonable care in taking that tax position and will not be subject to any shortfall penalty if the shortfall arises from errors in our list.*
>
> ***When the list is available***
>
> *The Australian share exemption list (IR871) is issued as soon as possible following the end of the tax year on 31 March.*

The reality is that IR871 is not now available. No reason is given for this but an on line tool is provided by IRD that replaces the IR871 list. It is frankly almost useless and poorly designed. But it gets worse.

Investors wanting to spread their risk via Listed Investment Companies (LICs) are advised by IRD that:

> *"Due to copyright restrictions over the FTSE AFSA Australia Listed Investment Companies (LIC) Index, we can't include LIC information in this tool. Contact the investment company or the FTSE to confirm whether your investment is part of the LIC Index."*

There are over 90 LICs listed on the Australian stock exchange. Attempts by the submitter recently to obtain this information failed miserably. Only 3 out of 15 LIC's Company Secretaries contacted bothered to reply and one of those that replied didn't know what the FTSE AFSA Australia Listed Investment Companies (LIC) Index was. All in all not very encouraging.

If the owners of the copyright are not prepared to license the use of their product then either scrap it or find something else. If the latter then something simple, readily found and understandable.

Almost all of the LIC's listed on the Australian stock exchange pay a dividend. As a result tax would be paid by holders of those LIC's. So why bother with the FIF regime? It may in fact be possible that more tax would be collected on the dividend income than via the FIF regime without even taking all the bureaucratic paper work into account.

Investing in shares is towards the upper end of the risk spectrum. Having uncertainty about the possible tax consequences makes it even more hazardous. Hence the attraction of property. If the Government want to shift investment away from residential property then the alternatives need to be made more attractive.

New Zealanders wishing to invest in Exchange Traded Funds (ETF's) listed on the Australian stock exchange are discouraged as none of the 175 or so available are on the so called exempt list. By way of comparison there are only about 25 ETF's listed on the New Zealand stock exchange and the range to choose from is pretty much a waste of time.

For many investors Kiwisaver is the beginning, middle and end. A choice of one is no choice at all especially as concern is being expressed over the high fees being charged. Diversification needs and greater financial literacy mean additional and / or other avenues become attractive. ASX listed LIC's and ETF's offer that opportunity but our tax system discourages such investments. Further, it gives the NZ stock exchange a significant advantage by default.

The New Zealand stock exchange is minute and the variety of shares offered is miniscule. To obtain some semblance of diversification investing off shore is often recommended. The FIF regime makes achieving this not quite so easy. The value of all New Zealand shares on the main board is about $130 billion. This is about the market capitalisation of the big two Australian miners – BHP and Rio Tinto. Or about a 14% of Microsoft.

A future tend that the Tax Working group may wish to take cognizance of is the uptake of ETF's by 'millennials' in the USA and more recently in Australia. Tony Kaye in "InvestSmart" of 15 March 2018 wrote:

> *Australia's exchange-traded funds market is evolving rapidly, with the take-up of ETFs products by younger investors accelerating and more financial planners actively recommending them to clients.*
>
> *It's a trend that is being mirrored in the United States, where millennials (those born from the early 1980s through to the late 1990s) now account for more than 30 per cent of the $US4.8 trillion US ETFs market.*
>
> *What's the big attraction for millennials? It simply comes down to the fact that ETFs offer easy diversification across different shares and markets, their low-cost structure, and the ability to buy and sell them just like any other stock.*
>
> *Data from US stockbroker Charles Schwab shows that 63 per cent of US millennials believe ETFs will be their primary investment vehicle in the future, versus only 23 per cent of Baby Boomers.*
>
> *This week, in Australia, research firm Investment Trends and ETFs product issuer BetaShares released their own findings on the booming domestic ETFs sector, showing a similar gravitation towards these products by younger investors including millennials.*
>
> *Indeed, their BetaShares/Investment Trends Annual ETF Report 2017 found that currently just over one in four ETF investors are retired, with the typical investor aged 49.*

Some of the key findings of the research include:

- *ETF investors are getting younger, with the average age of those who started investing in ETFs in the last 12 months 42. That's well down on the average age of 56 among those who started investing in ETFs more than five years ago.*
- *The ETF market has significant potential for further growth with the number of "next wave" ETF investors reaching record highs. Almost one third of these investors are millennials (those born from the early 1980s through to the late 1990s).*
- *Diversification, cost-effectiveness and access to overseas markets are the top drivers of investing in ETFs.*

Recommendations: (a) Raise the $NZ50,000 De Minimus threshold to $NZ250,000;

AND

(b) Reinstate IR871 or find a replacement;

AND

(c) Include on the exempt list all ASX listed but New Zealand incorporated companies;

AND

(d) Include on the exempt list all ASX listed LIC's and ETF's.

This is broken. Fix it.

6. ***Tax Relief For Research & Development (R & D)***

Many New Zealanders were delighted to learn of the new coalition government's goal of boosting spending on research and development, (R & D), to two per cent of GDP by 2027.

According to the OECD (Organisation for Economic Co-operation and Development), New Zealand's level of gross spending on R&D is just 1.3% - about half that of the OECD average of 2.4%. A very dismal effort.

Good news is that according to a recent Statistics New Zealand's Business Operations Survey (Year ended August 2017), New Zealand businesses are investing more in their growth and research and development. The not so good news was that while the number of businesses carrying out R&D is at a 10-year high only 11 percent of firms are doing it. In terms of barriers to innovation, 18 percent claimed that the cost to develop or introduce innovation was an impediment and 17 percent cited a lack of management resources.

The Government's R&D policy is essentially a scrapping of the Callaghan Innovation Growth grants and replacing it from April 2019 with a 12.5% tax credit on companies' spending on research and development. Businesses would need to spend a minimum of $100,000 on eligible expenditure, within one year, to qualify.

Apparently all other Callaghan Innovation grants and services will remain in place. However one needs to read the fine print to discover that this will be the case. It could be argued that that is of no consequence as nobody knows about them anyway.

Five key difficulties are foreseen in implementing the new R & D tax incentive:

Firstly, the 12.5% tax credit may not be enough and could be supplemented perhaps by a re-introduction of some of the grant programmes, (see below), of about a decade ago, suitably updated to reflect today's environment and to remedy any perceived defects in the old grant system. Hindsight suggests that these grant / funding programmes were terminated prematurely and that whatever replaced them have been poorly directed and almost certainly not marketed with the consequence that they have been ineffectual in building R & D capability.

New Zealand Trade & Enterprise

<u>Growth Services Fund (GSF)</u>

Provides co-funding support to medium- to high-growth potential firms to purchase external advice and expertise, marketing intelligence, and development services.

<u>Enterprise Development Grants for Market Development (EDG-MD)</u>

Provided co-funding support to help businesses enter a new export market, or carry out market research, or a new activity in an existing export market. The aim was to encourage greater integration of more New Zealand businesses into global markets.

Technology New Zealand

<u>Grants for Private Sector Research and Development (GPSRD)</u>

This scheme provided assistance for small and medium-sized "technologically aware" firms to undertake research and development projects with potential to raise their technological capability.

Technology for Business Growth (TBG)
This programme aimed to promote research and development and innovation by part-funding projects that enhance the technological capabilities of firms.

Technology for Industry Fellowships (TIF)
This provided assistance for placing researchers or technologists in firms to build links and encourage technological innovation.

TechLink
Provided technology guidance, strategic planning, and promotional services to stimulate awareness of technological innovation in firms.

Secondly, there is doubt that we have enough researchers and that there will be a need for an increase in their number. Add to this the finding in a recent Statistics New Zealand's Business Operations Survey (Year ended August 2017), that 17 percent of those surveyed cited a lack of management resources as being a barrier to innovation.

The number or researchers required probably means that foreign scientists, engineers, technologists, etc. will need to be recruited. They will not come for the low DIY No 8 wire research budgets that New Zealand offers or our mediocre salaries.

In this regard the absence of a capital gains tax is important. It is one of our significant points of difference to other countries. Compensation by way of equity participation and/or employee shares can be offered in the event that the research results in marketable product(s). A capital gains tax is a deterrent against such 'windfall' remuneration or 'sweat equity' being devoted to riskier investments without the chance for reward. Few things are riskier than investing in a start-up company – and we need more investment in innovation.

Other than remuneration attracting appropriate researchers will mean a huge marketing pitch on lifestyle, being in a politically stable country, having academic freedom, being in a collegial research environment and away from military / terrorist / street & drug gang conflict zones, etc. will be no doubt be necessary. Accommodating these people and their families will add more pressure to the housing demand unless emigration fixes it first.

Thirdly, for most businesses cash flow is king. Many start-up innovative businesses do not make a profit for a number of years and so unless the R & D tax credit puts real money in the bank rather than a line or two on a balance sheet a tax credit is nigh on useless.

To offset this a temporary grant scheme will be implemented to provide support for Growth Grant recipients with insufficient tax liability to use the R&D credit immediately. However, the Growth Grant scheme will be closed to new applicants on March 31, 2019. After this date? Go whistle dixie.

Fourthly, New Zealand has very few businesses with large research budgets, and rebating what is really a small proportion, 12.5%, of an already small expenditure would do little to achieve the large-scale focused investment required to make a difference. For small to medium sized businesses 12.5% may prove, in dollar terms, to be so puny to be not worth the bother. In which case a well thought out grant programme to encourage innovation and entrepreneurship may be more successful. It will need to be marketed though.

Fifthly, In the Statistics New Zealand's Business Operations Survey (Year ended August 2017), 18% of businesses surveyed claimed that the cost to develop or introduce innovation was an impediment. Investing in R & D and producing your firm's amazing widget is one thing commercialising it another. Grant programmes need to be available to businesses to assist them to get their amazing widgets on their pathway to market.

One of the disappointing aspects of the Callaghan Innovative grants system is that New Zealand tax payer's money is used to fund the grants yet the recipients are, once their project or development is or close to commercialised, are free to give overseas investors a better chance to buy equity than the New Zealand tax payer who funded their enterprise initially.

For example: Volpara Health Technologies is listed on the ASX but not the NZX.
Volpara has received grant funding from Callaghan to develop its software products designed to improve clinical decision making and aid in the early detection of breast cancer. If a New Zealander wants to invest in Volpara shares they are subject to IRD's complex and convoluted FIF regime. Australians have no such restrictions.

This is broken and a few steps appear to be have been started to fix it. Will they be the right ones?

Recommendations:

a. Modify & update the existing Callaghan grant schemes and in the process include commercialisation aspects;

   AND

b. Implement a comprehensive marketing programme for the Callaghan grant schemes;

   AND

c. Retain the Callaghan Growth Grant scheme and supplement it by introducing the proposed 12.5% tax credit for research and development.

   AND

d. Introduce as a condition for a grant or tax credit the requirement that in any public equity raising that New Zealand investors be given first option and that New Zealand stock exchange listing be sought.

7. ***Housing Affordability***

The question of housing affordability has vexed politicians in many countries for many years. The issue has been and will continue to be because housing affordability is essentially a problem of supply. With the other side of the coin, demand, equally problematical.

The Valuation Department, (now non-existent), undertook some research a few decades ago into the determinants of house price inflation. Their finding was that the single most significant factor was the 'rate of household formation' and in this regard immigration flows were more often than not the major factor.

Numerous studies from around the world all contend that the size and direction of migration flows are strongly determined by differences in economic opportunities. This applies to both international migration and the movement from rural or small towns to the cities. In general 'the grass is always greener on the other side of the fence'.

Motivations for Migration

	Push factors	**Pull factors**
Economic and demographic	Poverty Unemployment Low wages High fertility rates Lack of basic health and education	Prospects of higher wages Potential for improved standard of living Personal or professional development
Political	Conflict, insecurity, violence Poor governance Corruption Human rights abuses	Safety and security Political freedom
Social and cultural	Discrimination based on ethnicity, gender, religion, and the like	Family reunification Ethnic (diaspora migration) homeland Freedom from discrimination

Source: World Bank

In New Zealand the early 1970's house prices increased by more than 50%. This more or less coincided with not only a special Samoa immigration quota that was introduced but also with a record inflow of immigrants in 1973 and 1974 when there was an assisted passage scheme and publicity to attract migrants due to labour shortages. More immigrants, more households, more demand so up went the prices.

Very different reasons in around 1981 - 83 contributed to the next period of high increases in house prices. This increases more or less corresponded with the flow on effects two pieces of legislation. (a) The Property (Relationships) Act 1976. This act was mainly about how the property of couples was to be divided up when they separate or one of them dies. (b) The Family Proceedings Act 1980. This act made 'no-fault' divorce possible. Irreconcilable breakdown of marriage became the only basis on which divorces were granted. No one was blamed. The result was that instead of mum, dad & the kids being under one roof two or more dwellings were now needed.

In more recent times New Zealanders returning home, many of whom arrived with plenty of cash, and others deciding to stay at home, perhaps to invest an inheritance in a rental property, has created much higher than normal housing demand. It would be interesting to see the political fallout should a Government decide to stop its citizens from leaving the country or returning home. Discouraging them from returning home, as opposed to stopping, is another issue. For example, Government may consider extending the qualifying residential / earnings period for ‘free’ health and education services, welfare benefits, National Superannuation, etc.

According to Statistics NZ net migration peaked at 72,400 in the July 2017 year. At 2.7 persons per household this was the equivalent of about 26,800 homes or about the size of New Plymouth. Building a city of this size in that timeframe stretched resources.

Negative net migration, (i.e. emigration), could diminish housing demand just as rapidly as it rose.

Land supply is core to unaffordability, but it is wrong to assume that more land being released and consented more cheaply and rapidly equals more housing more quickly. It is a good start but if there are people that have no money to buy a home or there are no builders or there are no building materials then a plentiful land supply means nothing. Prefabricated or factory built houses may help but they will still need to be paid for and sited on a piece of land. Be that as it may being a developer in the business of creating building sites either from bare paddocks or derelict warehouses is not for the faint hearted. The profit for the developer doesn’t come until the cash from last few building sites sold is in the bank. In the meantime the developer has to pay for the land, the infrastructure, the holding costs, etc.

If the Tax Working Group really want to fiddle with this they may wish to address taxation issues specific to those confronting property developers after all nobody builds houses in order to pay more tax.

Recommendation: This is not broken. Can be left alone and be viewed as being part and parcel of global economic cycles.

8. ***Tax Relief For Health Insurance For The Elderly***

Private health providers can take pressure off the public health system by those prepared to pay for health insurance. It is totally reasonable that those paying private health insurance premiums should receive a tax benefit as they are also paying for the public health system.

Those who have retired know what happens to medical insurance premiums. They go up and up and up. It is therefore no surprise that medical insurance is one of the first cost items that is shed or down-graded by those qualifying for New Zealand superannuation.

It doesn't have to be that way. Making private health insurance premiums tax deductible for the New Zealand superannuant may well slow down the 'grey hair flight' from private health insurance schemes.

With more of our elderly using health insurance, space on public waiting lists would be freed up for those without. It would mean that all New Zealanders would get treated sooner. It would help conditions to be treated before they become debilitating and additional time in hospital may not be required. Add in the reduction in the use of expensive pharmaceuticals as well as medical staff and carer time and attention that could be devoted to other tasks.

With an ageing workforce and population coupled with advances in medical treatments and technology we need to take a big picture approach to health. Anything that assists with the fiscal problem facing healthcare especially for the elderly, reduces waiting lists, promotes good health and quality of life seems like a no-brainer.

Making private medical cover tax deductible for those receiving New Zealand superannuation may well reduce the burden on that bottomless pit called the public health system.

Recommendation: The public health system is broken. Consider making private health insurance premiums tax deductible for the New Zealand superannuant.

9. Capital Gains Tax [CGT]

A capital gains tax is a tax on the increased value of an asset. It is a tax that New Zealand does not need. The election results of 2011 and 2014 indicate that it is not wanted by the public either. There are strong reasons for it being not needed or wanted.

The Manawatu Standard, 12 Sept. 2017, published the following item written by Liam Hehir, "Capital Gains Not Worth The Hassle".

> *The fact that we are one of the few countries without a capital gains tax is not, in itself, good reason to adopt one. Compared to most other countries, our system of taxation is simple and elegant. Tax simplicity is one of our few competitive advantages. This is sometimes under-appreciated by those who only pay PAYE and GST, but is not something New Zealanders should take for granted.*
>
> *It is also no coincidence that, compared to other countries, we also have a very high rate of tax compliance. Tax simplicity is wonderful.*
>
> *Taxing capital gains is an invariably complicated exercise. Before implementing the tax, you need to determine the types of assets to be taxed and when it will be payable. Will art be captured? What about shares? Kiwisaver portfolios? What if it's jointly owned and one person dies? What if it's left to you in a will? What if it's in a family trust? All these things require complex rules for implementation, administration and compliance.*
>
> *In return, you don't actually raise a lot of revenue.*

[For the full article: https://www.stuff.co.nz/manawatu-standard/opinion/96699833/capital-gains-tax-not-worth-the-hassle]

Despite there being many questions that need to be answered before a CGT is even thought about being introduced the Government has gone ahead and introduced a CGT anyway via the 'bright line test.'

The 'bright line test' requires tax to be paid on any gains made from a residential property sold within two years of purchase. It was introduced and applies to residential properties for which an agreement to purchase was entered into on or after 1 October 2015. Property gains that are subject to the rules are taxed at ordinary marginal tax rates.

In March 2018 the bright line test was foolishly extended to 5 years. The Inland Revenue Department (IRD) considers that two years is the better bright-line period and warned the Government that the high level of non-compliance so far seen with the bright-line test will continue if it is extended by another three years.

An impact statement by the Treasury and Inland Revenue said that "high-level analysis" of taxpayer compliance with the existing bright-line rules suggests that voluntary compliance is less than 50%. It is no surprise that property investors have been managing their affairs to avoid the bright-line test. To ensure greater compliance a bigger bureaucracy will surely follow. What a mess of potage. Despite all this sound advice the Government pressed on and argued that extending the test to five years will help deter property speculators and “**may**” have of a dampening effect on the housing market. This is ‘suck it and see’ legislation and a CGT by surreption to appease the envy sector.

This fool hardiness is being exasperated because the housing market is already showing signs of quietening down. Five examples follow:

1. *Auckland house prices weaken in February as volumes increase. House prices in New Zealand's largest city of Auckland are likely to remain stable over the remainder of the summer and autumn sales season according to Barfoot & Thompson, the city's largest realtor.*
   The average sale price fell to $919,454 in February, down 1.6 percent from January and 2.7 percent below February last year. The median price of $820,000 is 1.2 percent below January and unchanged from February last year. (March 2018)

2. *Powered by CoreLogic data, the February 2018 QV House Price Index shows the late values resurgence witnessed in Auckland post-election subsided in February, dropping by 0.5%. Simultaneously, Wellington capital city values tracked sideways after previously experiencing more sustained growth throughout the second half of 2017 and into 2018.*

3. *Parts of the country are suffering sharp house price falls of more than 10 per cent, and the downturn could spread. The Real Estate Institute data for January 2018 reveals that although the number of properties sold across the country was up 2.7 per cent compared to January 2017 but compared to December, national house prices dropped 5.5 per cent to a median $520,000.*

4. *Property asking prices fell in five regions of New Zealand last month, creating opportunities for house-hunters.*
   Realestate.co.nz has released its data for March (2018), which shows weakness in some of the country's main centres.
   Auckland's average asking price was down 1.3 per cent from February to $949,538. Central Otago/Lakes dropped 5.2 per cent to $879,325. Southland was down 4.1 per cent to $289,796, Canterbury down 2.8 per cent to $488,157 and Otago down 1.3 per cent to $386,793.

5. *According to the NZ Property Institute’s housing predictions for 2018 their CEO, Ashley Church, (31 Jan 2018), says that the cost of renting will replace the price of housing as the #1 housing issue in 2018 – and the housing polices of the new Government, combined with uncertainty around housing investment over the next few years, will ‘scare’ some property investors out of the market - creating a growing crisis in the number of dwellings available for rental. people will choose to desert the market rather than stay in for three to four years, house prices are flat, that means no capital gain, add in rising compliance costs like insulation and some properties won't pay their way. Plus a review of tenancy laws is also making some nervous and won't fix the problem.*

   The full list of the NZ Property Institute’s predictions can be seen via the link below. Their predictions for 2017 had a 100% ‘hit rate’.

{ http://www.scoop.co.nz/stories/BU1801/S00485/property-institute-housing-predictions-for-2018.htm }

Questions To Be Answered BEFORE implementing a CGT.

- ? What assets will be liable?
- ? Who owns the assets?
- ? Will the costs of owning the asset be deductible?
- ? How will capital losses be treated?
- ? How efficient is a CGT?
- ? Will the double tax issue be fixed?
- ? What adjustments will be permitted to compensate for inflation?

What assets will be liable?

Family home: How many days each year does it need to be lived in?
What if it is partly used for a business?
What if you inherit an additional home from a recently deceased family member?
Holiday home: Define this. What if close family members live in it for some months?
Company Shares:
Gambling & Lottery winnings:
Retirement portfolios such as Kiwisaver
Maori Land
Crown Land

Are things like the following going to be liable for CGT? If not, why not?

art	gem stones and jewellery	precious metals
rare stamps	coins & bank notes	vintage cars
fine wine	collectibles such as dolls & toys	militaria
autographs	sport memorabilia	old cameras
antiques furniture	china & porcelain	books & comics

The list is almost endless.

Who owns the assets?

Joint ownership: How will splitting the CGT liability be handled? Can mum, dad, children, siblings, uncles, aunts, cousins, grand-parents all now become joint owners and so share the tax burden?
Family Trust: What about rights to occupy?
Maori Land: How will CGT on Maori land be dealt with? Could the Maori Land Court quickly, fairly and effectively sort out Maori CGT liabilities?

Will the costs of owning the asset be deductible?

In the UK you can deduct certain costs of buying, selling or improving your personal possession from your gain. The costs you can deduct include:

- fees, e.g. for valuing or advertising; insurance, brokerage, storage, etc.,
- costs to improve your possession (but not repairs),
- VAT (unless you can reclaim it). (VAT is equivalent to our GST)

You can't deduct certain costs, such as the interest on a loan used to buy your asset.

If the above were to be adopted here what a delightful can of worms it would open. The raft of avoidance possibilities is almost infinite. Already compliance with the 'bright line test' is an issue. The trouble is that failure to allow such costs renders a CGT as a very unfair tax and is probably and rightfully political suicide.

How will capital losses be treated?

If gains are taxed then losses must be allowed to be used to offset against other tax liabilities. Or if there are no other liabilities then cash in the bank will do nicely thank you. In other words, a capital gains tax socialises profits while privatising losses.

Unfortunately, a CGT is a deterrent against riskier investments and an incentive for safer ones. E.g. The family home, (if it is to be exempt), as New Zealanders perceive residential property to be safe haven. Among the things that New Zealand needs is less money being poured into residential property as an investment and more angel and venture capital investors. A CGT inhibits such activity.

Presuming the tax is payable on the sale of an asset, it can be easily avoided by simply not selling it. Consequently freeing up capital to invest in something more promising becomes harder and more expensive. Productive opportunities fall by the wayside and effectively capital becomes locked away. The result innovation and entrepreneurship are stifled.

How efficient is a CGT?

The short answer is probably not very. The cost of collection is said to be very high and hard reliable data is needed to verify or discredit this claim. Perhaps there is a reason why data on the cost of CGT collection is nigh on impossible to find.

Not having a CGT is an important point of difference in marketing New Zealand to investors and entrepreneurs. Further, because other countries have a CGT is no reason why we should have one too.

A CGT will result in a whole new avoidance industry being created. CGT are for practical and political reasons invariably riddled with exemptions and exceptions making them devilishly complicated to administer and to comply with. Making it a veritable bonanza for tax lawyers, tax accountants, tax consultants and tax bureaucrats. But bad news for everyone else.

In July 2011 Labour's Phil Goff proposed a CGT of 15%. It would raise a miserable $17.5 million – about the cost of a flag referendum – in the first year. However this would rise to $3.7 billion by 2028. Sounds impressive but it ain't. At the time Treasury's Long-Term Fiscal Model estimated that the total tax in 2028 would be $120 billion. The CGT would therefore be only 2.83% of the total tax take. Why bother?

Will the double tax issue be fixed?

Many companies, perhaps the majority, that make a tax paid profit do not distribute all of their profit back to their shareholders usually by way of a dividend. The retained profit is reinvested back into the business. {Perhaps as increased R & D investment}. This retained profit usually and eventually gets reflected in a higher share price. A CGT will then steal some or all of the increased share price. This is double taxation and such a complete and utter rort that a CGT on shares should be abandoned forthwith.

There is a glimpse of an argument that claims that share prices reflect the expectation of future profits and that those expectations exceed the level of retained earnings. Not surprisingly sound evidence for this argument appears to have gone astray.

Companies can reinvest their retained earnings in many ways. One such way might be investing in developing products and processes which are expected to generate further profits over time. In such instances a CGT can be seen a tax on expectations rather than reality.

For small businesses that are not stock exchange listed the value of the business is usually a very close approximation of the net present value (npv) of its expected income stream. The income stream is taxed and so the value of the business is an after tax valuation.

Suppose a business makes $1000 a year and the npv discount rate is 10% then the value of the business is $10,000. Deduct tax at say 30% and the business is now worth $7,000.

The business owner get busy and doubles the earnings to $2,000 a year. Now the business is worth $20,000. Deduct tax at say 30% and the business in now worth $14,000.
The owner can sell the business and trouser a capital gain of $7,000.

However along comes a CGT of 15% and steals $1,050 of the capital gain leaving only $5,950.

So instead of paying $6,000 in tax, (30%) on the $20,000 the business now pays $7,050 in tax or 35.25%.

Thinking that a CGT is about imposing "fairness" – even if it results in everyone being worse off as a consequence – then it's got to be a terrific idea hasn't it?

What adjustments will be permitted to compensate for inflation?

Numerous researchers have examined the impact of inflation on the assessment of CGT and have concluded that it is nothing more than highway robbery.

Inflation distorts all aspects of the taxation of personal income but is particularly harsh on the taxation of capital gains. When company shares or any other asset is sold a capital gains tax be paid on the difference between the selling price and the original cost even though much of that gain was the result of a general rise in the prices of consumer goods and services. Taxing capital gains in this way very substantially increases the effective tax rate on '*real'* price adjusted capital gains.

> *Under the federal tax code, the increase in an asset's price is determined as the nominal amount (i.e., not adjusted for inflation). When an asset (often a stock) is sold above its purchase price, a gain is realized and is taxed. Any capital gain due to inflation is not accounted for, and the taxpayer is taxed on both their increase in income and on increases in prices economy-wide. As a result, the effective tax rate on the real (inflation indexed) capital gain has exceeded the statutory rate every year since 1950 and has averaged around 42 percent.*
>
> *In some instances, the practice of taxing the nominal gain can lead to an infinite effective rate on real capital gains when the increase in price is only due to inflation. In fact, if a taxpayer purchased an average stock in 1999, 2000, or 2007 and sold in 2013, they would be taxed entirely on inflation.*
>
> And there was more:
>
> *More specifically, in 1973 individuals paid capital gains tax on more than $4.5 billion of nominal capital gains on corporate stock. If the costs of these shares are adjusted for the increases in the consumer price level since they were purchased, the $4.5 billion nominal gain becomes a real capital loss of nearly $1 billion.*

["Inflation and the Excess Taxation of Capital Gains on Corporate Stock" by Joel Slemrod. 1983 National Bureau Of Economic Research and published by the University of Chicago Press]

The following item is from UK's 'The Telegraph' and somewhat scathing about failing to make allowances for inflation when assessing CGT.

> ## *Capital gains tax without inflation is 'highway robbery'*
>
> *Plans to increasing capital gains tax would be akin to "highway robbery" unless allowances are made for the effects on inflation, experts warned.*
>
> *By Harry Wallop, Consumer Affairs Editor, The Telegraph;* 21 May 2010
>
> *Without adjustments for natural increases in prices, many savers will be forced to pay tens of thousands extra in tax. Some will see their bills double.*
>
> *The new coalition government is planning to increase the tax savers and investors pay when they sell any assets from 18 per cent to 40 per cent or even 50 per cent. This move will hit hard second home owners, buy-to-let investors, or anyone with a decent portfolio of shares. Some accountants have suggested as many as a million people a year will be caught by the tax.*
>
> *However, leading tax experts have given warning that it would be "grossly unfair" to raise the tax without introducing indexation. This is the technical term for taking into account inflation.*
>
> *When people sell any asset, be it a picture they inherited or a second home they bought some years ago, they have to pay tax on the profit -- or capital gain -- they*

have made. But some of the profit could be down to inflation during the time they have owned it.

If someone bought a second home twenty years ago, for instance, the average price would have been £69,000, according to the Halifax. The average home is now £168,000. So, the person would be sitting on a near £100,000 profit.

But according to Government statistics, nearly £50,000 of that profit is down to simple inflation, as measured by the main cost of living index. Indexation strips out this effect, meaning consumers only have to pay tax on the real return. In this instance they would pay tax on £50,000 profit rather than £100,000 -- thus halving the tax bill.

Mike Warburton, leading tax partner at Grant Thornton, the accountancy firm, said: "I have had a lot of clients ringing up worried about this. They feel it is grossly unfair to pay tax on inflationary gains. And let's face it, inflation has not gone away. The dragon has not been slayed. Taxing people on any gains they make from inflation is a big disincentive to save."

Earlier this week, the Office for National Statistics said that inflation, as measured by the Retail Prices Index, had climbed to a 19-year high of 5.3 per cent.

Indexation has been part of capital gains tax ever since it was raised to 30 per cent in 1988. Only when Alistair Darling, as chancellor, moved capital gains tax down to 18 per cent two years ago did indexation get scrapped.

Bill Dodwell, head of tax policy at Deloitte, the accountancy firm, said: "There are plenty of arguments in favour of increasing capital gains tax. But it would be very unfair to do so without reintroducing indexation. That has to happen.

"The longer people hold assets, the more inflation affects the value of that asset."

Mark Dampier, head of research at the independent financial adviser Hargreaves Lansdown, said: "When CGT was 10 per cent, or even 18 per cent, people understood that you might not get inflation taken into account.

"But to put it up to 40 per cent without indexation is pure highway robbery. Over the long-term your asset could increase in value considerably, but only because of inflation.

"There is a real feeling from our clients that it is unbelievably unfair to put up the rate without indexation. It is unfair to be taxed on inflation."

A spokesman for the Treasury said: "There are a range of possible options on capital gains tax to fulfil this aim and no decision has yet been taken on one option. It will be important to take the time to get this right."

In addition to the above compelling arguments there is the question of what indexes would be used to measure inflation. For example:

Consumer Price Index	QV House Price Index
S&P NZX All Index Gross	Producer Price Index
Labour Cost Index	Trade Weighted Index

Using these indexes or a combination of them to determine the true capital gain net of inflation is quite complicated especially allowing for the cost of maintenance and other adjustments that will be made over a number of years of ownership. It's hard to do financially, witness the issues with the FIF regime, let alone in terms of writing and then administering tax law.

Then there is the issue of Government meddling with the activities of the Reserve Bank to influence the movement of inflation and so dictate the quantum of CGT assessed. It is just six months since there was a change in Government and already the Reserve Bank is being required to establish a committee, the members of which will be appointed by the Minister of Finance, to pay more attention to the state of the labour market and not just inflation when setting interest rates. Unlike the inflation target, there will be no hard number on employment. The employment goal will be dynamic and broad and impacted by many variables. Maybe one of those variables will be the quantum of CGT the Government wants to collect.

Unfortunately it doesn't look like it is going to end here as the new Government has asked Treasury to undertake a wide ranging review of the way the central bank operates and how it makes decisions.

Having a Government influenced inflation rate over which you the tax payer have no control could well determine your tax liability. It may well prove to be a step too far. Banana republic here we come.

Recommendation: A Capital Gains Tax is not needed or wanted. Forget it. Move on.

Conclusion

There is a section of the New Zealand population that are always up for taxing the rich and the successful. It's certainly does not appear to be about improving the well-being of the citizens or the economy. The Tax Working Group have been given an opportunity to be a catalyst to change this thinking for the betterment of all New Zealand citizens.

Finally, one can only hope that the Tax Working Group will take heed of Bert Lance's advice that the trouble with government is that they fix things that aren't broken and not fix things that are broken.

Contact Details

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