# Tax Working Group Public Submissions Information Release

## Release Document

## September 2018

**taxworkinggroup.govt.nz/key-documents**

Key to sections of the Official Information Act 1982 under which information has been withheld.

Certain information in this document has been withheld under one or more of the following sections of the Official Information Act, as applicable:

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

[2] 9(2)(k) - to prevent the disclosure of official information for improper gain or improper advantage.

Where information has been withheld, a numbered reference to the applicable section of the Official Information Act has been made, as listed above. For example, a [1] appearing where information has been withheld in a release document refers to section 9(2)(a).

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

# Submission by Ian Kuperus to the Tax Working Group

# Capital gains tax

## 1. Proposal for a Variable CGT rate

### Executive summary

This proposal is that the capital gains tax rate varies according to the length of time that the asset has been held. An asset held for one year would be subject to the “base CGT rate” while assets held for longer periods would be taxed at a proportionately higher rate. For example if the “base rate” is set at 25% an asset sold after 5 years may be taxed at 27%.

The benefits of a variable CGT rate are improved economic efficiency, fairness and increased revenue. Specifically -

1. It virtually eliminates the “lock- in” incentive of the typical realisation based CGT
2. It removes the pressure to put in place rollover relief provisions which in essence only exacerbate the lock-in effect and make the CGT more complicated
3. It makes the capital gains tax fairer when compared to other income types which pay tax on a regular basis.
4. It will facilitate **“capital gains tax deposits”** that are the subject of a second submission. **Capital gains tax deposits** will allow taxpayers to manage their CGT exposure on an accrual basis and will provide the government with significantly advanced revenue.

**Setting the Variable CGT Rate**

The intent of a variable CGT rate is to substantially eliminate the lock in incentive that is a drawback of a realisation based CGT regime. With a variable rate the benefit from deferring CGT under a realisation based scheme is offset by an increasing tax rate. Appendix 1 sets out a suggested tax rate structure based on an underlying 4% compounding interest rate and a starting base rate of 20% or 25%. Appendix 1 calculates the rates for 1 year to 40 years.

The table below summarises the CGT rates for 1, 5 10, 20 and 40 year holdings.

| Years Asset Held For | CGT Rate –( Base Rate 20%) | CGT Rate – (Base Rate 25%) |
|---|---|---|
| 1 | 20% | 25% |
| 5 | 22% | 27% |
| 10 | 24% | 30% |
| 20 | 30% | 37% |
| 40 | 48% | 59% |

There are a number of reasons to consider a CGT rate base rate less than the top marginal tax rate eg an allowance for inflation and the potential exposure to double taxation through company structures. Setting a base CGT rate at say 20% or 25% would make a variable rate easier to sell politically.

**Eliminating the Need for Rollover Relief**

The pressure for rollover relief comes from selling and buying similar assets and the argument that the imposition of capital gains tax is unfair when compared with someone that continues to hold the same asset. Rollover relief significantly complicates a CGT regime and there is significant benefit in removing the pressure for rollover relief.

**A variable CGT rate makes the regime fairer**
Being able to defer tax on economic gains is unfair when compared with taxpayers who pay on an annual basis. Salary and wage earners for instance would jump at the chance to defer their tax payments for 20 years and have those funds earn income in a KiwiSaver or similar scheme.

**Capital gains tax deposits**
The benefits of a capital gains tax deposit scheme depends upon a variable CGT rate. Full benefits of a CGT deposit scheme are outlined in a further submission.

**Issues That Warrant Further Consideration**

The following issues warrant further consideration.

- **Rate Setting-** both the base rate and the inherent interest rate. The higher the inherent interest rate the more Government revenue will be advanced – see CGT Deposits paper. On the flip side the higher the inherent interest rate the more difficult the political sell will be. Very long dated assets will pose a political sell problem but these will be rare. It may be that an outright cap in the rate at say 49% may be appropriate.
- **Changing the Inherent Interest rate with changes in market rates.**
- **Allowing voluntary assessments –** Taxpayers could elect to voluntarily assess and pay CGT on a valuation basis to “restart the number of years” calculation. This may be attractive if there is a sudden spike in value. There should be no problem with allowing a voluntary assessment to be retrospective for a year or so
- **Increased Calculation- requirement for Number of Years –** Each asset sold would require a number of years ownership to be allocated. Given that most will be business assets and a starting value will be required in any event I do not think that this should be a major problem.

I would be happy to engage with officials on these points if the TWG considered the proposal warranted further analysis.

**Appendix 1 – Calculation of Variable CGT Rates Based on 4% Implied Interest Rate**

| Variable CGT Rate- Base Rate 20% | | | Variable CGT Rate- Base Rate 25% | | |
|---|---|---|---|---|---|
| **Number of Years asset Owned** | **Marginal period compound Rate** | **Variable CGT Rate *** | **# of Years asset Owned** | **Marginal period compound Rate** | **Variable CGT Rate *** |
| 1 | 20.00% | **20.00%** | 1 | 25.00% | **25.00%** |
| 2 | 20.80% | **20.40%** | 2 | 26.00% | **25.50%** |
| 3 | 21.63% | **20.81%** | 3 | 27.04% | **26.01%** |
| 4 | 22.50% | **21.23%** | 4 | 28.12% | **26.54%** |
| 5 | 23.40% | **21.67%** | 5 | 29.25% | **27.08%** |
| 6 | 24.33% | **22.11%** | 6 | 30.42% | **27.64%** |
| 7 | 25.31% | **22.57%** | 7 | 31.63% | **28.21%** |
| 8 | 26.32% | **23.04%** | 8 | 32.90% | **28.79%** |
| 9 | 27.37% | **23.52%** | 9 | 34.21% | **29.40%** |
| 10 | 28.47% | **24.01%** | 10 | 35.58% | **30.02%** |
| 11 | 29.60% | **24.52%** | 11 | 37.01% | **30.65%** |
| 12 | 30.79% | **25.04%** | 12 | 38.49% | **31.30%** |
| 13 | 32.02% | **25.58%** | 13 | 40.03% | **31.97%** |
| 14 | 33.30% | **26.13%** | 14 | 41.63% | **32.66%** |
| 15 | 34.63% | **26.70%** | 15 | 43.29% | **33.37%** |
| 16 | 36.02% | **27.28%** | 16 | 45.02% | **34.10%** |
| 17 | 37.46% | **27.88%** | 17 | 46.82% | **34.85%** |
| 18 | 38.96% | **28.49%** | 18 | 48.70% | **35.62%** |
| 19 | 40.52% | **29.13%** | 19 | 50.65% | **36.41%** |
| 20 | 42.14% | **29.78%** | 20 | 52.67% | **37.22%** |
| 21 | 43.82% | **30.45%** | 21 | 54.78% | **38.06%** |
| 22 | 45.58% | **31.13%** | 22 | 56.97% | **38.92%** |
| 23 | 47.40% | **31.84%** | 23 | 59.25% | **39.80%** |
| 24 | 49.29% | **32.57%** | 24 | 61.62% | **40.71%** |
| 25 | 51.27% | **33.32%** | 25 | 64.08% | **41.65%** |
| 26 | 53.32% | **34.09%** | 26 | 66.65% | **42.61%** |
| 27 | 55.45% | **34.88%** | 27 | 69.31% | **43.60%** |
| 28 | 57.67% | **35.69%** | 28 | 72.08% | **44.61%** |
| 29 | 59.97% | **36.53%** | 29 | 74.97% | **45.66%** |
| 30 | 62.37% | **37.39%** | 30 | 77.97% | **46.74%** |
| 31 | 64.87% | **38.28%** | 31 | 81.08% | **47.85%** |
| 32 | 67.46% | **39.19%** | 32 | 84.33% | **48.99%** |
| 33 | 70.16% | **40.13%** | 33 | 87.70% | **50.16%** |
| 34 | 72.97% | **41.09%** | 34 | 91.21% | **51.37%** |
| 35 | 75.89% | **42.09%** | 35 | 94.86% | **52.61%** |
| 36 | 78.92% | **43.11%** | 36 | 98.65% | **53.89%** |
| 37 | 82.08% | **44.16%** | 37 | 102.60% | **55.20%** |
| 38 | 85.36% | **45.25%** | 38 | 106.70% | **56.56%** |
| 39 | 88.78% | **46.36%** | 39 | 110.97% | **57.95%** |
| 40 | 92.33% | **47.51%** | 40 | 115.41% | **59.39%** |

*The CGT Rate is an average of the Marginal Period Compound Rate