Tax Working Group
Te Awheawhe Tāke

Tax Working Group Public Submissions Information Release

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

[1]

2 October 2018

Dear Michael Cullen

I recently found an old PSA Journal amongst some old papers.
It seemed very topical, and the discussion of Capital Gains tax very cogent.
I forward it for your interest.

Yours sincerely

Rosemary Collier

TAXING CAPITAL GAINS

It won't be news to most workers that some of the wealthiest people and biggest companies have been making huge tax-free profits in recent years.

One reason for the number of new Mercedes, Porsches and BMWs in Auckland is that large profits have been made on the sharemarket, many of which were tax-free capital gains.

What is a capital gain?

It is the gain made when an asset (eg, property or shares) increases in value. Countries which tax this gain only ever do so when the gains are realised (that is when the asset is sold at a greater price than it was bought for).

In the case of shares, a capital gain is made when share prices have increased since they were bought. In New Zealand unlike most other countries, this capital gain can be received tax-free when the shares are sold.

Sharemarket capital gains also feature in many companies' profits announced recently eg, Watties has had tax-free gains of $195 million so far this year and NZ Forest Products had $77 million as part of last year's profit. It tends to be wealthier people and companies, who have the spare income to invest for capital gains in areas like the property market.

How can they do this?

Quite simply they are able to make these profits and pay no tax because New Zealand has no capital gains tax. We are one of the few Western countries not to have one.

Just before Australia introduced its recent capital gains tax, an overseas visitor told them they were the only civilised country in the world without one. Leaving aside either the oversight or slur on NZ, this shows that taxing capital gains is not a radical notion, and it shows how basic it is considered to any country's tax system. NZ is a virtual tax haven without one.

Who want a capital gains tax?

* Most other countries similar to New Zealand advocate and have this tax. Australia introduced legislation for this tax in 1986. International tax authorities such as Terry Shananhan from Touche Ross (a firm employing 2500 tax accountants in 87 countries), say this tax is inevitable.

* The unions called for a capital gains tax at the FOL/CSU National Taxation Seminar in 1986.

* Those who want a neutral climate for investment. On this basis Treasury should want this tax.

* The Institution of Policy studies have released two papers which advocate this tax – Andrew Alston's "The Taxation of Capital Gains in New Zealand", and "How Should Business Be Taxed" by Paul Bevin.

* Hugh Fletcher said recently that it is unarguable that capital gains should be taxed.

* The Reserve Bank favoured this tax in its annual report to Parliament.

Why should we have one?

* To stop a favourite method of tax avoidance – converting income into capital gains.

* Fairness. It tends to be the wealthier who have the spare income and knowledge of how to get tax-free capital gains.

* Efficiency. To stop people investing for tax-free income rather than in the most productive investment for the country. With a capital gains tax investment is discouraged from speculative areas.

What type should we have?

* A tax of gains only when sold (realised).

* At income tax rates.

* After exempting people's homes, small gains, superannuation benefits, and other items which the tax is not intended for.

* After deducting losses (limited to the amount of gain).

* After deducting expenses to do with the asset, such as the legal fees on selling.

* A tax on all gains accruing from commencement of tax, not just those on assets purchased after commencement date.

Inflation

* Usually some allowance is made for inflation with capital gains taxes. However, no allowance is made for low to middle income earners who suffer from the effects of inflation by being moved into higher tax brackets all the time (this is called fiscal drag). Companies and the wealthy do not suffer from fiscal drag.

* While other parts of the tax system are not protected from inflation, there should be no allowance for inflation with a capital gains tax. Note that many of the schemes to obtain capital gains involve borrowing, and when it is repaid there are gains from inflation. Therefore, this offsets the need for inflation-proofing a capital gains tax.

What are the arguments against one?

* It is said that it will not raise much revenue. However, raising revenue is not an argument used by people wanting the tax. Also, if people stop investing for capital gains because of the tax, then more revenue can be raised in other parts of the tax system, where they have swapped their investment to.

* It is said that there are too many practical problems with the tax. However, other countries obviously manage to decide what type and how to implement the tax.

* Roger Douglas says that investment will not move around as easily as it is at present. However, it is no good investment moving easily if it is being encouraged to the wrong places as at present, into speculative rather than more productive areas.

Conclusion

A capital gains tax is very much needed in New Zealand. When one is introduced it should not be adjusted for inflation, while the rest of the tax system is not.

Vivienne Nelson