# Tax Working Group Public Submissions Information Release

## Release Document

## February 2019

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**From:** David Whitburn <action@campaignnow.co>
**Sent:** Tuesday, 30 October 2018 11:49 AM
**To:** TWG Submissions
**Subject:** Reply submission to Tax Working Group's interim report and proposals

Dear members of the Tax Working Group,

This is a submission in response to the proposals and questions set out in the Tax Working Group's Interim Report. I am a former Tax Consultant with Deloitte, and Tax Solicitor with Russell McVeagh. I support much of the Tax Working Group's work, particularly on behavioural taxes like increasing tax on sugar and cigarettes and other anti-social products that cause huge costs to the health system, and salute the Group's dedication and diligence on their enormous task.

In my submission, I focus on Capital Taxation. Whilst I strongly disagree with the introduction of a capital gains tax, conversely I do support a capital income tax with an extension of the brightline test to 10 years and simplifying subpart CB on land taxation in the Income Tax Act 2007.

**Capital taxation - submission against a capital gains tax**

Currently New Zealand has one of the higher company tax rates in the OECD. This doesn't help businesses get money to reinvest for growth, resulting in a low-investment, low-productivity economy. We would like to see our Government commit to increasing New Zealand's productivity and allowing for greater growth in incomes through tax policy.

Tax is punitive by definition as it takes money from those who created it. The Tax Working Group has put forward two proposals for an even higher tax burden on capital and investment. New Zealand is far far more than just the Government, it is the people. He aha a te mea nui. He tangata. He tangata. He tangata. We, New Zealand people, will never become prosperous if we use an opportunity to review our tax system to simply punish entrepreneurship and investment.

Jason Clemens, Charles Lammam, and Matthew Lo for the independent Canadian research group the Fraser Institute note: "Capital gains taxes, of course, raise revenues for government but they do so with considerable economic costs. Capital gains taxes impose costs on the economy because they reduce returns on investment and thereby distort decision making by individuals and businesses. This can have a substantial impact on the reallocation of capital, the available stock of capital, and the level of entrepreneurship".

There are many reasons why the capital gains tax harms economic performance. Clemens, Lammam and Lo explain the "lock-in effect."

> "Capital gains are taxed on a realization basis. This means that the tax is only imposed when an investor opts to withdraw his or her investment from the market and realize the capital gain. One of the most significant economic effects is the incentive this creates for owners of capital to retain their current investments even if more profitable and productive opportunities are available. Economists refer to this result as the "lock-in" effect. Capital that is locked into suboptimal investments and not reallocated to more profitable opportunities hinders economic output. ...Peter Kugler and Carlos Lenz (2001)...examined the experience of regional governments ("cantons") in Switzerland that eliminated their capital gains taxes. The authors' statistical analysis showed that the elimination of capital gains taxes had a positive and economically significant effect on the long-term level of real income in seven of

> the eight cantons studied. Specifically, the increase in t he long-term level of real income ranged between 1.1 percent and 3.0 percent, meaning that the size of the economy was 1 percent to 3 percent larger due to the elimination of capital gains taxes."

Clemens, Lammam and Lo further analyse the impact of capital gains taxes on the "user cost" of capital investment.

> "Capital gains taxes make capital investments more expensive and therefore less investment occurs. ...Several studies have investigated the link between the supply and cost of venture capital financing and capital gains taxation, and found theoretical and empirical evidence suggesting a direct causality between a lower tax rate and a greater supply of venture capital. ...Kevin Milligan, Jack Mintz, and Thomas Wilson (1999) sought to estimate the sensitivity of investment to changes in the user cost of capital...and found that decreasing capital gains taxes by 4.0 percentage points leads to a 1.0 to 2.0 percent increase in investment".

Next, they investigate the impact on entrepreneurship.

> "Capital gains taxes reduce the return that entrepreneurs and investors receive from the sale of a business. This diminishes the reward for entrepreneurial risk-taking and reduces the number of entrepreneurs and the investors that support them. The result is lower levels of economic growth and job creation. ...Analysing the stock of venture capital and tax rates on capital gains from 1972 to 1994, Gompers and Lerner found that a one percentage point increase in the rate of the capital gains tax was associated with a 3.8 percent reduction in venture capital funding".

Last but not least, the authors also discuss the impact of capital gains taxation on compliance costs, administrative costs, and tax avoidance. They also look at the marginal efficiency cost of capital gains taxation and report on some of the research in that area.

> "Dale Jorgensen and Kun-Young Yun (1991)...estimate the marginal efficiency costs of select US taxes and find that capital-based taxes (such as capital gains taxes) impose a marginal cost of $0.92 for one additional dollar of revenue compared to $0.26 for consumption taxes. ...Baylor and Beausejour find that a $1 decrease in personal income taxes on capital (such as capital gains, dividends, and interest income) increases society's well-being by $1.30; by comparison, a similar decrease in consumption taxes only produces a $0.10 benefit. ...the Quebec government's Ministry of Finance...found that a reduction in capital gains taxes yields more economic benefits than a reduction in other types of taxes such as sales taxes. Reducing the capital gains tax by $1 would yield a $1.21 increase in the GDP".

Therefore I strongly submit against imposition of a Capital Gains Tax in New Zealand.

**Simplifying taxation of capital income from land sales**

Currently you are taxed for capital income from the sales of land (real property) if you:

- buy and sell a property within *five* years from 29 March 2018 and onwards;
- within *two* years if the property was purchased between 1 October 2015 through to 28 March 2018 inclusive;
- within *ten* years if you were a property dealer or developer at the time you bought the property. This is regardless of whether the purchase was part of your property business or not;
- within *ten* years if you sell a property that had building work being completed on the property, and you were a builder or in the building business at the time you bought the property. This is regardless of whether the purchase was part of your building business or not;

- *any* time from any properties you sell, which were bought as part of your property or building business; and
- If you're associated with someone in the property industry - you're an "associated person". This means you may have to pay tax on all or some of your property transactions, even if you're not personally a property dealer, developer or builder.

  These transactions include tax on the sale of a property if you had an association with:

  - a property dealer or developer when you brought the property,
  - a builder when significant improvements started on a property.

- *any* time when a property has been bought with the firm intention of resale you'll have to pay tax on any profit from the sale. The intention to sell does not need to be the main reason for buying the property - it could be one of a number of reasons for buying.

I submit that these rules are confusing and should be simplified. Sections CB6A to CB23B of the Income Tax Act 2007 should be altered to provide that any sale within a **ten (10) year period be subject to capital income tax on land** with the exception of home owners and business owners (irrespective of the entity they choose to own the land in), provided there are no more than two sales in any two year period and no more than five sales in any ten year period. This means the brightline test would be ten years, the builder/trader/developer and associated persons test go to be ten years, and the firm intention is difficult to prove, and negligible revenue is collected from land sales over ten years. The goal is to ensure speculators and traders are taxed, and to ensure a genuine creation of long term housing stock in New Zealand. Holding property for ten years is fantastic and lets New Zealanders provide for both their retirement and also New Zealande rs accommodation needs. Therefore the beauty is the simplicity. I submit that *every land sale is subject to capital income within 10 years*, with the sole exception being sales by home-owners and business owners, who may have no more than two sales in any two year period, and no more than five sales in any ten year period.

I wish the Tax Working Group all the best in their consideration of my submissions to have a ten year capital income tax on land sales, and not to implement any Capital Gains Tax.

Yours sincerely,

David Whitburn