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Retirement Policy and Research Centre

The Future of Tax in New Zealand
27th and 28th November 2018

Commentary
Tax and Inequality

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Overview

- Taxes, transfers, and inequality
  - Are TWG’s hands tied?
- How did we get into such a EMTR mess?
  - Thanks Rogernomics!
  - The mess gets worse
  - IWTC worth a TWG checkup.
- PIES are bad for us
  - Reinforce and promote inequality
- What is the real inequality elephant in the room?
  - Surprise, surprise, it is housing
- Boldness required
  - All power to the TWG’s final report

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1. Taxes and inequality

Goals of a good tax system

- Efficiency,
- Equity: horizontal ***and*** vertical
- Administrative simplicity

But

"What matters is the distribution of disposable income. We get into trouble when we think of them as separate"

Royal Commission Social Policy 1988

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Interim report

The following are outside the scope of the Working Group’s review:

- Increasing any income tax rate or the rate of GST
- Inheritance tax
- Any other changes that would apply to the taxation of the family home or the land under it, and
- The adequacy of the personal tax system and its interaction with the transfer system **(this will be considered as part of a separate review of Working for Families).**

Taxes and transfers are opposite sides to the same coin

TWG...WEAG

Taxes ? Benefits

where do tax credits fit?

"The tax system is not particularly progressive. Instead, **progressivity is largely delivered through transfers, such as Working for Families**. Yet New Zealand's tax and transfer system reduces income inequality by less than the OECD average". TWG p 19.

Déjà vu (TWG 2010)

‘A key concern with the current tax system is the levels of effective marginal tax rates (EMTRs) that people can face due to the combination of higher statutory marginal rates of tax and abating social assistance. ….**implications of tax reform on the interface with the social assistance system** are not discussed in detail here, but **would need to be analysed as a part of developing any reform options**’

Whose job is it?

- TWG?
- WEAG?
- Echoes of TWG 2010 ?

Tax/transfer interface falls through the cracks yet again

2. How did we get into this EMTR mess?

We traded

Universal social provision and a progressive tax scale with high EMTRS at top	FOR	a broad-base, low, flattish tax scale, flat 15% GST and **targeted** social provision

High EMTRs have been shifted to low and middle incomes

The Mess has got worse

More use of targeted provision in delivering social goals

Family Tax Credit
In Work Tax Credit
Minimum Family Tax Credit
Best Start
Student loans
Child Support
KiwiSaver
Accommodation Supplement
Childcare subsidies

Tax/welfare interface has become more problematic since 2010 report

4. What is the real inequality elephant in the room?

TWG have been asked

- "to consider a package or packages of measures which **reduces inequality**, so that New Zealand better reflects the OECD average whilst increasing both **fairness across the tax system** and **housing affordability**".

https://taxworkinggroup.govt.nz/resources/tax-working-group-publishes-interim-report

Family one earner, 3 kids, Auckland rent, income of $48,00 earns an extra $10,000

- Tax
- Loss WFF
- Loss AS
- Student loan

- 3,000
- 2,500
- 2,500
- 1,200

- 92% EMTR

3 child family

- WFF abates for incomes between
- AS abates for incomes over
- Student loans

- $42,700- $104,00
- $30,000- 90,000
- $19, 200-

BUT all is not lost

Taxes to AFFECT BEHAVIOUR *are* part of TWG scope

- Savings incentives
- Should also consider the tax credit that is supposed to incentivise work
- IWTC costs $560 m pa
- Fails to achieve aims
- Does not match reality of 21st century work
- Intensifies child poverty
- **Adding it to other WFF is a logical and highly redistributive way for TWG to achieve revenue neutral outcomes**

3. Why PIES are bad for us

- Top tax rate is only 28% for the highest incomes
- Worsens inequality
- Means we have little idea of how much *income*, wealthy people actually have

Solutions?

- selectively lower the other PIE rates (TWG)
- **Raise top PIE to 33%**

or

- **Impute income**

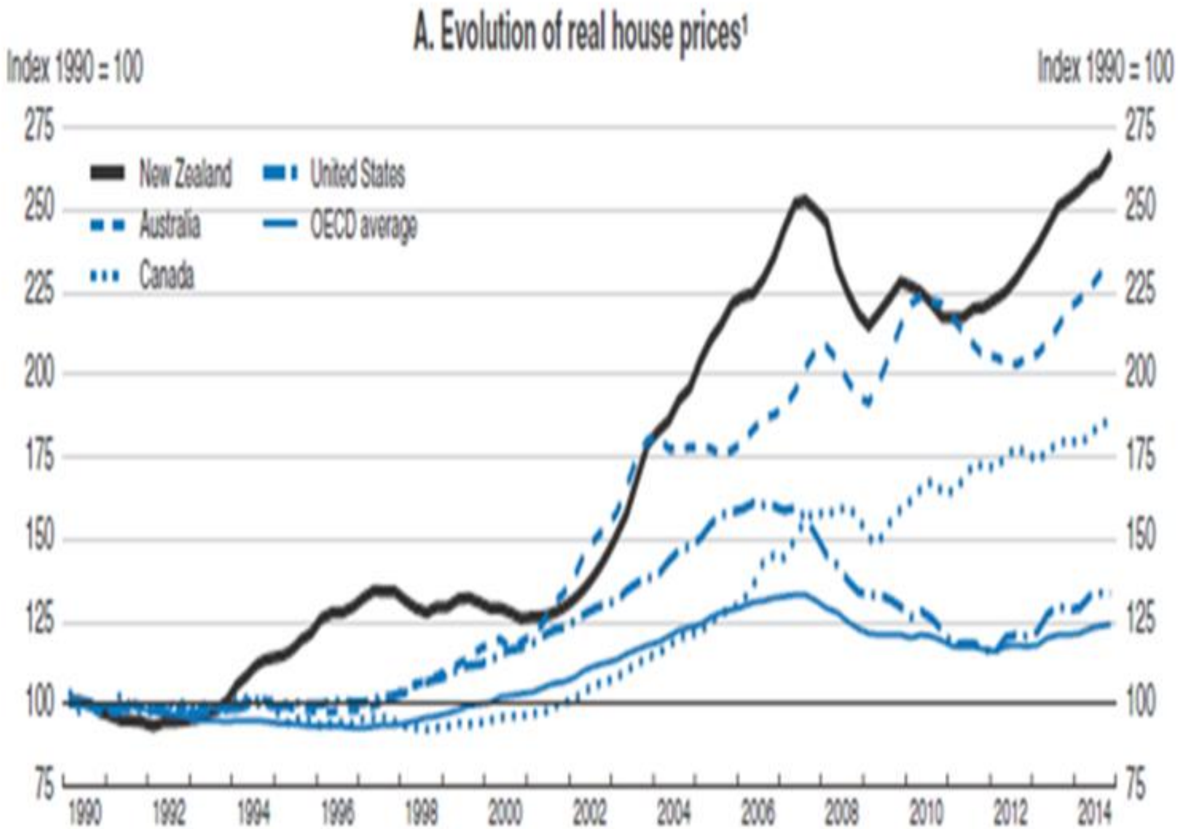
Wealth inequality compounds over time

:

"In New Zealand a very high level of capital assets are held by the top 10 or 20 per cent of the population and that is the main reason why our tax system is less 'redistributive' than most developed economies." Cullen TWG.

"It is also evident that New Zealanders are deeply concerned about the high cost of housing, and its impact on wealth inequality, social cohesion, and social capital" (TWG, p 6)

Up up and away



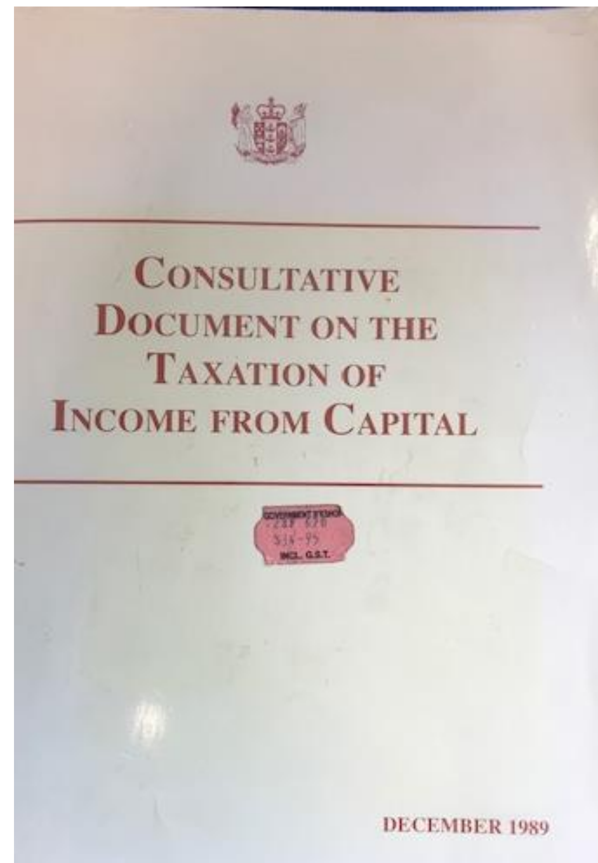
(OECD 2015)

Capital Gains Tax

- CGT (if perfect) *may* achieve *horizontal equity* for future capital gains
- No impact on wealth accumulated and compounded over years of neglect to date
- Capital losses can be carried forward
- Family home exempt
- Etc etc

Déjà vu

- 1967 Ross Committee
- 1982 McCaw Committee
- 1987 Brash Consultative Committee Accrual Tax
- 1988 Valabh Consultative Committee International Tax Reform
- 1989 Report of the Consultative Committee
  - Income from Capital
  - Abandoned 20th March 1990 by David Caygill



- 1988 Royal Commission Social Policy
- 1988 Brash Committee Superannuation
- 1988 Brash Committee Life insurance
- 2001 McLeod Tax Review
- 2010 Tax working group report
- 2019 TWG report?

If not capital gains tax then what?

RFRM or net equity approach is superior if meaningful reduction in housing inequality is to be achieved

All housing wealth aggregated and registered first mortgages deducted

Net equity treated as if on term deposit earning 3-4%

Net equity tax would

- Retain current bright line tests for short term gains
- Affect the top 20% of wealthiest property owners and absentee owners
  - Have an individual exemption on a family home of up to $1 m
- Do away with the need for landlords to feed tax accountants
  - No rental losses
  - No interest write offs
  - Capture capital gain in the equity base
  - Divert resources from luxury housing
  - Change the culture of housing as an investment commodity-better use of housing stock

5. Call for boldness

Government has asked for measures that reduce inequality, so…

- Government needs to know
  - TAX TRANFER INTERFACE must be considered
  - Design of Working for families as a major tax redistributive tool must be included
  - A full analysis of the RFRM or net equity approach is needed as a serious alternative to CGT
  - The family home cannot be taken off the table