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CEO Comment

Tax rebalance is essential for faster growth

The debate surrounding New Zealand's tax system has been reinvigorated by the Tax Working Group. There is a widespread consensus that the balance of taxes must change in order to reduce the load on personal and corporate taxes which are towards the top end of the OECD. The leadership and political will to make the changes have been less forthcoming.

The two major changes proposed by the Tax Working Group so far have been an increase in the rate of Goods and Services Tax (GST) and the introduction of a capital gains or land tax.

An increase in the GST rate would send the right messages in terms of incentives to the economy. It would encourage people to invest rather than consume, providing a long-term benefit to the economy. A higher GST rate would cause some problems for lower income earners but this could be easily offset.

A capital gains or land tax has been more contentious. The working group identified that the 200 billion dollar rental property sector essentially operates tax free and this hole should be plugged. They then came to the conclusion that a land tax would be more efficient in terms of collection as it would effectively just act as an addition to council rates. However, a tax on capital gains would align that source of revenue with other sources of income creating a fairer system.

The arguments against a land or capital gains tax fall into two camps:

- Those who argue that such a tax would be inefficient; and
- Those who argue that such a tax would not prevent housing bubbles.

Both arguments completely miss the point; we need a broad low tax base, and perhaps more importantly we need to send better messages to investors. If investment in assets continues to be tax-free then we must expect the same household debt situation and underinvestment in business to continue. Closing this hole is the most important thing; the method used to do it is secondary.

Coming out of the economic crisis, we need macroeconomic settings that support activity rather than assets and consumer spending. I hope that we will see the Government follow through on the Tax Working Group's proposals to get the incentives right. If we need a model on how to do it we need look no further than Australia:

- No PAYE deductions to property speculators (ring fence losses as Australia does);
- A Capital Gains Tax (CGT) on everything other than the family home (Australia);
- All current investment is exempt when the CGT is introduced so that the CGT is not retrospective (Australia); and
- Capital Gains Tax only applies on the difference between inflation and the realised value (Australia again).

The message is this is not hard, but it does need leadership.