TWG final recommendations – Capital gains

THE REPORT

The Tax Working Group has completed its final recommendations

- Capital and wealth
- Business tax
- Savings
- Personal income tax
- Environmental & ecological outcomes
- Other opportunities for improvement

See next page for summaries

A capital gains tax, not just black and white

MAJORITY AGREE

A clear majority of the TWG supports a comprehensive approach to the taxation of capital gains

NO CONSENSUS

Some group members have reached a different judgement

MATTERS OF JUDGEMENT

These members consider that the costs of extending the tax rules in a comprehensive manner, as proposed in the Group's Final Report, would outweigh the benefits

$8b

8 BILLION

The approximate amount a comprehensive capital gains tax could raise over 5 years (see next page for how TWG suggests this money could be spent)

NO SIMPLE SOLUTION

The Government does not face a binary choice regarding whether or not to tax capital gains. There is a spectrum of choice.

ISSUES TO CONSIDER

- What to include
- What to exclude
- Complicated issues
- Design choices

A SPECTRUM OF CHOICE

For this reason, the Government could choose to extend the taxation of capital gains to some asset classes only e.g. property, businesses, savings. The Government also has options around how to stage the timing of its introduction.

THE SPECTRUM

Included assets

- Land & improvements to land — *Excluding the family home*
- Shares
- Business assets
- Intangible property

Excluded assets

- The excluded home — *The place that a person owns, where they choose to make their home by reason of family or personal relations, or for other domestic or personal reasons*
- Personal use assets — *Jewellery*, *Fine art*, *Taonga and other collectibles*

Complicated issues

- Death
- Relationship breakdowns
- Selling an asset & buying a new one
- Double taxation

Design choices

WHEN

- Realisation basis in most cases
- Leaving New Zealand

HOW

- Marginal tax rates
- Gifts are treated as being disposed of for market value
- Capital losses generally deductable but some ring fencing

WHO

- Individuals
- Companies
- Partnerships
- Trusts
- Non-residents

What's next?

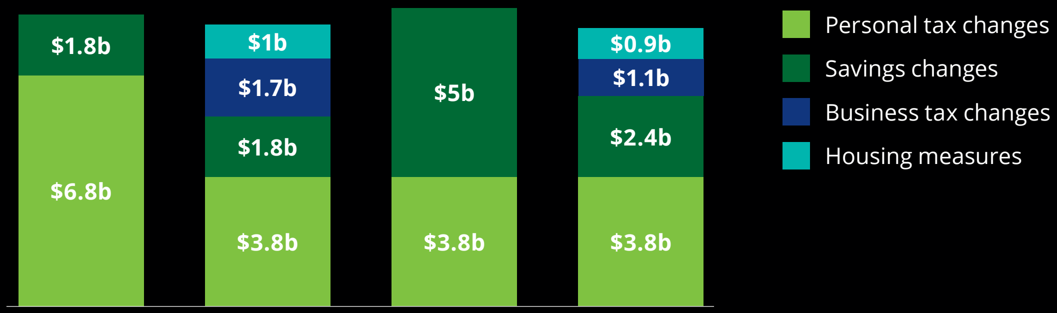
The Government will gauge feedback on the options and will announcements on decisions in April 2019. Any changes are expected to be legislated and enacted before the 2020 general election.

TWG final recommendations – At a glance

PACKAGES OF REFORM

The Tax Working Group has put forward 4 options of packages of how any capital gains tax revenue can be spent (estimated to be approximately $8 billion over five years).

Any overall tax reform is expected to be fiscally neutral, so the recommendations in areas (such as business tax, savings, personal taxes) are contingent on more tax revenue being raised to fund them.



OPTION 1
Reductions in personal income tax: Potential increases in the lowest two tax thresholds from 2022

OPTION 2
Business and housing focus: Personal tax increase to bottom tax threshold to $20,000 from $14,000 from 2023

OPTION 3
Savings focus: Personal tax increase to bottom tax threshold to $20,000 from $14,000 from 2023

OPTION 4
Diversified focus: Personal tax increase to bottom tax threshold to $20,000 from $14,000 from 2023

***Note:** Option 1 & 3 also include depreciation deductions for seismic strengthening [$70m]*

BUSINESS TAX

A range of options is given for further exploration to support the productive economy, boost investment, and reduce compliance costs. Further work would need to be undertaken by Inland Revenue, but options include:

- Changes to the loss continuity rules that will support the growth of innovative start-up firms
- Introduce a $10,000 safe harbour to allow upfront deductions for low levels of feasibility expenditure
- Reform to blackhole expenditure, allowing otherwise non-deductible expenditure in relation to assets to be spread over 5 years
- Reinstate building depreciation at a rate of 1%. Due to fiscal costs, some buildings may remain ineligible for depreciation
- Allow deductions for seismic strengthening costs
- Reviewing the treatment of non-resident employees
- Consider tax concessions that encourage building to higher environmental standards
- Develop a regime which encourages investment into nationally-significant infrastructure projects
- Reduce compliance costs in a range of ways including: reducing number of depreciation rate options, adjusting unexpired expenditure thresholds, increasing capitalisation threshold for small assets, simplifying fringe benefit tax, simplifying the entertainment adjustment, removing resident withholding tax from some payments, improving some record keeping requirements, IRD notification processes and tax application processes, increasing the 'cash basis person' threshold, increase the thresholds for GST adjustments
- Exempt small businesses and simple transactions from the hybrid mismatch rules

SAVINGS

The TWG concluded in the interim report that there was not a case to radically reform current savings tax rules. However the TWG believes that an increase in the tax benefits provided through KiwiSaver would encourage more people, particularly low-income earners, to save for their retirement. Options for further consideration are:

- Refunding Employer Superannuation Contribution Tax for KiwiSaver members earning up to $70,000pa, with only a partial refund for members earning more than $48,000pa
- Providing the maximum member tax credit to KiwiSaver members on parental leave, even if $1,024 of individual contributions are not made
- Increasing the member tax credit from $0.50 per $1 of contribution to $0.75 per $1 of contribution, with the overall contribution cap remaining at $1,024 (i.e. the member tax credit would increase from $512 to $768)
- Reduce the current 10.5% and 17.5% PIE rates for KiwiSaver funds to 5.5% and 12.5% respectively

PERSONAL INCOME TAX

The TWG's objective has been to enhance living standards for New Zealanders – particularly those on low incomes. The TWG specifically recommends against having a tax-free threshold and instead recommends options to changes to the existing bands and rates.

Status Quo		Option 1a		Option 1b		Option 2	
0 – $14,000	10.5%	0 – $22,500	10.5%	0 – $20,000	10.5%	0 – $30,000	10.5%
$14,001 – $48,000	17.5%	$22,501 – $48,000	17.5%	$20,001 – $48,000	17.5%	$30,001 – $48,000	21%
$48,001 – $70,000	30%	$48,001 – $70,000	30%	$48,001 – $70,000	30%	$48,001 – $70,000	30%
$70,001+	33%	$70,001+	33%	$70,001+	33%	$70,001+	33%

The TWG notes that these options are likely to have a minor impact on income inequality.

Increasing top personal tax rates would have a greater impact on income inequality.

Increases in tax rates were, however, outside the Terms of Reference of the TWG so could not be recommended.

ENVIRONMENTAL & ECOLOGICAL OUTCOMES

The TWG conclude that the tax system can play a greater role in delivering positive environmental and ecological outcomes in New Zealand. While noting that taxes are not well suited to all environment problems, and regulation may be a better approach for some issues, the TWG make some general recommendations:

- In the short term improve the waste disposal level, the emissions trading scheme and congestion charging
- In the long term, consider use of tax instruments to address challenges in water pollution and water abstraction, including tax on fertilises
- In the long term, consider tools like an environmental footprint tax or natural capital enhancement tax
- Review a number of existing industry-specific tax provisions and the introduction of targeted new concessions to ensure the tax system is supporting and not harming natural capital. For example farming, forestry and petroleum mining
- Use tax for promoting positive environmental and ecological outcomes
- Commission research on who will incur the costs of any new environmental taxes and design appropriate mitigation measures

OTHER OPPORTUNITIES TO IMPROVE THE TAX SYSTEM

A number of other recommendations were made in the TWG's Interim Report, these remain as recommendations. Refer to our interim report infographic for more information. The TWG identifies some issues which require attention from the Government:

- The future of work – review the tax rules applying to self-employed contractors
- The integrity of the tax system – review recent Australian initiatives to reduce the hidden economy; strength criminal sanctions and impose unpaid tax liabilities on some directors; strengthen enforcement of tax rules for closely-held companies; and consider whether rules to counter loss trading in trusts are needed
- The administration of the tax system – more statistical information should be collected by the Government on wealth (e.g. through a census question)

Other areas identified for more work by the Government include:

- Charities – The TWG's analysis of issues relevant to the charitable sector has been passed to the Department of Internal Affairs as part of the Charities Review
- Corrective taxes – a framework should be developed for deciding when to apply corrective taxes
- Housing – The TWG recommends the Productivity Commission looks at taxes as part of its review of Local Body Financing; with a view to considering a tax on vacant residential land to be collected at the local rather than national level