



Future of Tax: Submissions
background paper
PSA Submission

May 2018

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PSA submission to the Tax Working Group

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Background

1. The New Zealand Public Service Association Te Pūkenga Here Tikanga Mahi (the PSA) is the largest trade union in New Zealand with over 64,000 members. We are a democratic organisation representing members in the public service, the wider state sector (the district health boards, crown research institutes and other crown entities), state owned enterprises, local government, tertiary education institutions and non-governmental organisations working in the health, social services and community sectors.
2. The PSA has been advocating for strong, innovative and effective public and community services since our establishment in 1913. People join the PSA to negotiate their terms of employment collectively, to have a voice within their workplace and to have an independent public voice on the quality of public and community services and how they're delivered.
3. PSA members have a strong commitment to protecting the democratic integrity of our public institutions and our legislative framework - both at a local and a national level.
4. We are an organisation that is committed to the principles of the Treaty of Waitangi.
5. The PSA is affiliated to the NZCTU and endorses its submission to the Tax Working Group.

Key points and recommendations

6. Thank you for the opportunity to submit on the Future of Tax: Submissions Background Paper. The paper covers a useful range of topics in a thoughtful and accessible way.

7. Our submission focuses on the revenue and equality outcomes of the current tax system and recommends changes to improve outcomes in both these areas.
8. The key points of our submission are that:
 - a) tax settings need to change to increase the level of revenue available to the crown;
 - b) this additional revenue needs to come from currently un-taxed income and wealth; and
 - c) adjustments need to be made to current tax settings to improve progressivity.
9. We don't believe that the current crown revenue gathering and expenditure settings - at 30% of GDP - are sufficient to fund sustainable and quality public and community services, or to ensure decent employment conditions for the people who deliver these services. Our members in the core public service have faced an unofficial wage-freeze over the last nine years, while those members in the almost wholly-government funded community services sector experience low pay and insecure work.
10. We are concerned that current revenue and expenditure settings rely on the systemic and historic under-valuing of the work undertaken by women working in public and community services. Women workers have a legal right to receive wages that fully reflect the value of the work that they do; rectifying gender pay discrimination across the state sector will require significant government investment that may not be achievable within current fiscal settings.
11. There are many gender-related dimensions to tax policy which are generally overlooked by policy makers, including that women are greater users of public and community services, and have lower earnings. We urge the TWG to broaden the remainder of its discussions to include an analysis of the gender implications of its recommendations.
12. Many of our members on low to middle-incomes struggle to make ends meet, particularly after housing costs have been accounted for. While this is largely a problem of low and stagnating wages and the high cost of living, the tax system is currently inadequately structured to address income and wealth inequalities. Our key concerns relate to the high and uniform application of the regressive GST; the steep introduction of the lowest and middle tax rates at relatively low income levels and the absence of a capital gains tax. The sharp clawback of government transfers, such as Working for Families means that many of our members see little net benefit from wage increases.

13. We welcome the discussion in the background paper on the absence of a capital gains tax and hyper-inflation in the housing market. Addressing housing affordability is a key concern for our members, as is reducing inequalities.

Recommendations

14. The amount of revenue raised by current tax settings is insufficient to ensure that New Zealanders continue to have access to high quality public and community services and a decent social welfare system. In many instances public and community services have been subsidised by the low wages of a female dominated workforce. The PSA **recommends** that a key part of tax reform must entail increasing the overall tax revenue, and that the arbitrary tax collection rate of 30% of GDP be set aside.

15. Current tax settings entrench, rather than mitigate, income and wealth inequalities. The PSA **recommends that** radical changes should be made to the tax system to ensure that currently untaxed wealth and income is taxed, and to restore progressivity.

16. We **recommend** the following changes to the tax system. They aim to increase revenue and improve the equality outcomes of the tax system. These recommendations are high-level and principle-based only.

- a. the introduction of a comprehensive Capital Gains Tax excluding the family home and the land underneath it;
- b. the introduction of taxes and/or mechanisms designed to capture currently untaxed financial transactions and activities, such as a Financial Activities Tax on financial institutions; a Financial Transactions Tax on international transactions; and measures to ensure that large multi-nationals not based in NZ contribute their fair share of tax;
- c. a reduction in the rate of GST to increase the real disposable income of low to middle income people;
- d. changes to PAYE rates to improve progressivity, for example, increasing the threshold at which the current 30% rate applies, and introducing a new tax rate on incomes over \$100,000.

17. We recognise that income tax rates are outside the TWG terms of reference, however their centrality to a discussion on the fairness and balance of the tax system necessitates their inclusion.
18. While outside the scope of the TWG terms of reference, we **recommend** that the TWG note that urgent attention needs to be paid to the impact of Effective Marginal Tax Rates and the fairness and adequacy of transfer payments.

Detailed comment

The PSA and tax

19. In 2017 the PSA published a booklet on tax, [Progressive thinking: ten perspectives on tax](#)¹. One of the reasons we published the book was to try and shift public debate on tax away from seeing tax as a burden, but rather as something that supports a thriving society. We also wanted to encourage our members and the broader public to become active in discussions on tax, rather than seeing it as the domain of politicians and tax 'experts'.
20. This submission focuses on two functions of tax: revenue and redistribution. These are the areas where our members have common interest, and for which there is strong national and international evidence that change is required. There may also be support from within our membership for the introduction of taxes to mitigate environmental damage, including climate change. This is an area where the PSA needs to do more analysis.
21. Revenue from taxation funds the essential services that our members work in, and that we all depend upon. The level of revenue that the government collects from tax impacts directly on the quality and availability of these services: if revenue sinks too low (through tax cuts) and government spending is reduced, services decline and the jobs and working conditions of our members are compromised.
22. Our members who are delivering these essential services have the right to decent pay and conditions that reflect the value of the work they do. Too often public service and

¹ Available at: <https://www.psa.org.nz/media/news/progressive-thinking-ten-perspectives-on-tax/>

community workers bear the brunt of Government decisions to freeze or reduce revenue gathering and spending, through low and stagnant wages, insecure work and redundancies.

23. These public services, sometimes called the “social wage”, are vital to the health and wellbeing of individuals, families, communities, our society and our economy, and are part of the redistributive function of tax. The integrity, availability and quality of these services, and the important role that they play in ensuring the health and wellbeing of our communities being eroded, risk being eroded if they are not funded properly.
24. Tax is part of the everyday life of PSA members; it affects their disposable income and thus their ability to make ends meet, now and in the future. Student loan repayments and high effective marginal tax rates mean that many of our members are paying a sizeable portion of their income in tax, and are paying higher rates than others.
25. The absence of a capital gains tax has contributed to hyper-inflation in the housing market. This has placed home ownership out of the reach of many of our members, while those of our members who rent face rent increases that are well above wage increases. This is exacerbated by the high rate and blanket application of our highly regressive Goods and Services Tax which disproportionately impacts on the spending and saving power of low income people.

Gender

26. There is an important gender dimension to tax policy. At an individual and a collective level, women have more to lose and less to gain from tax cuts than do men.
27. Women both use public services more than men, and are more likely to work in public services than men². This means that there is a disproportionate impact on women of government decisions about revenue gathering and redistribution as tax cuts inevitably lead to the loss of services and jobs.
28. With the dominance of women in low paid occupations within the community and public sector – such as care workers, social workers and administration and clerical workers – there is a compelling argument to be made that female workers have long subsidised our public services through receipt of wages that don’t represent the value of their work. The PSA’s

² As at 30 June 2017 female workers made up 60.5% of the public service workforce. State Services Commission (2017), “Diversity and Inclusion: Workforce Diversity”, accessed 21 March 2018 at <http://www.scc.govt.nz/public-service-workforce-data/hrc-diversity>.

long-term commitment to equal pay for women workers is an attempt to rectify this long-term discrimination; achieving this goal will rely on government raising adequate revenue from taxation and being prepared to allocate sufficient government spending to close the gender pay gap.

29. In addition, because women are more likely to be in unpaid work than men, the personal gain from tax cuts - in terms of increases in disposable income - is lower for women than men.

The NZ Tax system

30. Contributors to the PSA booklet on taxation identified a number of problems with the current tax system, including the lack of a comprehensive Capital Gains Tax, the regressive nature of GST and the problem of major tax avoidance by multi-national companies.

Redistributive and revenue outcomes

31. Of interest to the PSA is the effectiveness of our tax system in **reducing inequalities** (its redistribution outcomes), and in raising sufficient **revenue**.
32. The redistributive aspect of taxation helps to limit income and wealth inequalities. The effectiveness of this depends on the design of the tax system. A fair tax system is characterised by *horizontal equity* (people in similar circumstances pay the same tax) and *vertical equity* (tax rates vary according to people's ability to pay). As the TWG background paper notes our system performs poorly in terms of reducing inequality.
33. Although Effective Marginal Tax Rates (EMTR) are outside the scope of the TWG they are a key factor in understanding the redistributive weakness of the NZ tax system. Our high EMTR mean that some low- and middle-income households pay higher rates of tax than high income households. Similarly, those people paying back student loans, are also essentially paying higher tax rates than non-borrowers. So-called 'bracket creep', where people move into higher tax rates because of annual wage adjustments is also worthy of attention by the Government.
34. The combined impact of GST, income tax, EMTR and student loan repayments on people's disposable income is significant, especially in the context of steeply-rising housing costs and stagnant wage growth. Our survey of PSA members last year on the impact of the housing crisis revealed that many members are struggling to make ends meet.

35. The absence of wealth and capital gains taxes undermine the fairness of the system, and has contributed to recent hyper-inflation in the housing market. Unlike labour, capital is not taxed in New Zealand, which contributes to growing wealth inequality.
36. The PSA is also concerned with the level of revenue raised by the tax system, and questions whether it is sufficient to meet the level of public infrastructure and service investment required now and into the future. The consequences of close to a decade of austerity-like funding of core public services are becoming obvious, as the recent crisis at Middlemore Hospital exemplifies.
37. Importantly, the Government needs to raise enough revenue to ensure decent working conditions for those delivering public and community services, including pay that is free of gender and ethnicity discrimination. People working in public and community services have faced nine years of stagnant wages, and workforce shortages that cause significant stress to workers. Many female workers in public and community services have essentially subsidised these services for decades, through receipt of wages that do not reflect the full value of the work that they do.
38. The Government has committed itself to limiting crown expenditure and tax revenue to 30% of GDP. This is below the OECD average. The PSA and a number of economists³ argue that this tight fiscal framework is an unnecessary restraint on funding needed to meet critical public service and infrastructure cost pressures.
39. These tight fiscal parameters will also make it very difficult for the Government to fund improved wages and working conditions in the public and community sectors, including full and fair equal pay settlements.

PSA Position on Tax

40. The following pages outline the PSA's formal position on tax. This outlines some overarching principles of progressive taxation as well as some high-level recommendations for change to address identified weaknesses in the current tax system.

³ See, for instance, Bernard Hickey (<https://pro.newsroom.co.nz/articles/2650-comment-the-case-to-borrow-and-invest>), and Shamubeel Eaqub (<https://www.newsroom.co.nz/2018/02/12/88442/the-case-to-throw-off-the-fiscal-straitjacket>).

Principles of progressive taxation

41. A well-functioning tax system that is fair, progressive and transparent should be the goal of government reform, underpinned by several key principles:

- A truly progressive tax system must apply proportionately. Those who gain the most from economic growth should contribute the most, considered summarily across all forms of earnings and taxes. A key objective of the tax system should be to reduce income and wealth inequalities.
- Public services are the shared resources made possible through taxation. They must be sufficiently funded and accessible to those who fund them – the public – and sufficient tax must be collected to ensure they operate efficiently and responsively, and that the people working in them receive decent wages and conditions;
- Taxes must be transparent (understandable and clear to those they apply to), stable and sustainable (not exclusively drawn from sources prone to excessive fluctuation or exhaustion), and instructive (responsively based on behaviour, with some attempt to correct market failure and other externalities).

Proposals for change

42. The table below summarises the changes in response to some identified weaknesses in the current tax system. The proposals are high-level and principle-based only.

43. The main thrust of these proposals is that changes need to be made to improve the **redistributive and revenue outcomes of the tax system**: more revenue needs to be raised, but from sources that are not currently taxed. Ideally, there would also be changes to income tax and GST to improve progressivity, and reduce the amount of tax being paid by people on low to middle incomes. The NZ tax system needs to do more to reduce income and wealth inequalities in New Zealand.

44. The PSA believes that additional revenue from tax needs to be raised, particularly if the Government is to make the investment in public and community services, infrastructure and working conditions that we believe are necessary. This includes paying women workers wages that reflect the full and fair value of their work.

45. There may also be support from within our membership for the introduction of taxes to mitigate environmental damage, including climate change. This is an area where the PSA needs to do more analysis.

Proposal	Objective(s)	Comment
1. The introduction of a comprehensive capital gains tax (CGT) , that exempts the family home and the land underneath it.	<ul style="list-style-type: none"> • Increase the fairness and balance of the NZ tax system by treating income from capital the same as income from labour; • Lessen growing wealth inequality; • Close loopholes which allow owners of capital to reduce tax liability; • Raise additional revenue; • Dampen the housing market by disincentivising property speculation, and encouraging investment in productive activities, 	New Zealand is unique in the OECD in not having a comprehensive CGT. The current absence of a CGT undermines the so-called 'broad' nature of the NZ tax system and is key contributor to the growing wealth inequality in New Zealand.
2. The introduction of new taxes on currently un-taxed financial activities and transactions.	<ul style="list-style-type: none"> • Increase fairness and balance by taxing activities that are currently un-taxed, and by closing loopholes which allow large multi-national companies to avoid tax; • Raise additional revenue; • Stabilise international financial movements and exchange rates. 	<p>These could include: a Financial Activities Tax (FAT) levied on the sum of profits and remuneration of financial institutions (as proposed by the IMF⁴⁴); a Financial Transactions Tax (FTT) on international financial transactions; and measures to ensure that multi-national companies like Facebook and Google that don't have a presence in NZ, pay their fair share of taxes.</p> <p>These taxes are sometimes called Tobin Tax, and/or the Robin Hood tax.</p>
Reduce the rate of GST	<ul style="list-style-type: none"> • Increase individuals' real disposable income; • Lessen the impact of this regressive tax on low to middle income people who are disproportionately affected. 	<p>This is proposed as an alternative to previous calls for GST to be removed from fresh food and essential items. There are valid administrative arguments against removing GST from selected items; this proposal lessens the impact of GST but maintains its current uniform application for simplicity and ease of administration.</p> <p>The key disadvantage of this proposal is that it would reduce crown revenue (the increase in GST from 12.5-15% resulted in approximately \$2 billion additional revenue to the crown). This decrease in revenue could be offset by the introduction of new taxes on capital and financial activities (see above)</p>

⁴⁴ See: <https://www.imf.org/external/np/seminars/eng/2010/paris/pdf/090110.pdf>

<p>Review of income tax rates, with the possibility of introducing a new tax rate on incomes over \$100,000 and increasing the threshold at which the 30% rate currently kicks in (\$48 000.). The PSA would also support the introduction of a mechanism to make regular adjustments to tax thresholds (for instance at the level of CPI) to mitigate the problem of 'bracket creep'.</p>	<ul style="list-style-type: none"> • Improve progressivity in our PAYE system, and hence the equality outcomes of the system. • Increase the disposable income of low to middle income earners, and increase the contribution of high income earners. 	<p>The Government has ruled out any changes to income tax rates. However, this is a key issue in discussions on tax fairness that should be addressed.</p> <p>The tax income rate of 30% rate applies at a relatively low level, and there are very few steps in rates. Someone on \$70,000 pays the same PAYE rate as someone on \$150,000.</p>
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