Abstract

Political commentators have long said that the enactment of a comprehensive capital gains tax (CGT) in New Zealand (NZ) would be “[a] sure-fire path to political suicide”. (Edlin, 2008) Recently, there has been a change in the mood in NZ with a number of commentators as well as business and political leaders supporting the introduction of a CGT.

This has been reflected in the political landscape. In the 2011 General Election the centre-left Labour Party unsuccessfully campaigned on inter alia introducing a comprehensive CGT levied at a rate of 15 per cent in New Zealand. Their policy has been retained for the 2014 election. On the basis that the Mixed Member Proportional (MMP) electoral system produces coalition-based governments and the Green Party of Aotearoa New Zealand (Greens) and Labour (at least) are likely coalition partners, it is possible that the 2014 General Election could see a Labour-Greens coalition elected to the front-benches and the introduction of a CGT. Should the centre-left be unsuccessful in 2014, as a CGT is now clearly part of the NZ political agenda of the left-of-centre parties it is arguably only a matter of time before it is introduced in NZ by a Labour-led coalition.

This paper, using Adam Smith’s criteria for a good income tax, considers the Labour Party CGT proposal and the United States (US) experience in dealing with capital gains. It notes that the NZ proposals are consistent with CGT regimes generally,
such as it being realisation-based and not permitting indexing, but may involve complexities and pitfalls that the US system has previously encountered or has avoided. For example, Labour’s proposal to exempt collectables is likely to influence behaviour in favour of these forms of investment compared with other investments subject to the CGT such as shares. The definition of collectables will therefore need to be clear and robust and for this reason in our view the US approach of taxing such gains (and at a higher CGT rate) is clearly preferred. Not only does the US approach assist keeping the income tax system progressive as many of these items are owned by more wealthy individuals, but from a policy perspective these are generally not the types of assets that a nation wants to incentify investing in.

The success of a CGT, or any tax, will inter alia depend on a clear policy rationale which informs the design, consultation and implementation phases. “A failure to clearly articulate its purpose and adhere to it will potentially lead to a poorly designed and functioning CGT.” (Maples, 2014) The paper concludes that, in the New Zealand context, when debating and evaluating the introduction of a CGT, it is important that politicians, policymakers and taxpayers are clear as to its purpose and heed the caution of Gammie (2000), “[a CGT] is a compromise, and, as is so often the case with a compromise, it functions badly and pleases no one.”

Does this paper relate to a PhD that you are currently enrolled in?

☒ No
☐ Yes [please advise current institution you are enrolled in]

If a PhD student are you planning to be attend the PhD Workshop activities on Monday 19 January 2015?

☐ Yes
☒ No

Tick whether you want this paper to be considered for any of the following prizes:

☐ Best PhD Student Paper
☐ Best Tax Teaching Paper
☒ Best Tax Research Paper

(Consideration for prizes requires the full paper being lodged by 13 December 2014).