

# A local view of capital gains tax

By PKF Francis Aickin Ltd

We didn't plan this topic, but it's unavoidable, and it doesn't look like this beast is going to go away. You're going to hear a lot about it over the next few months, and you may yet have to learn to live with it.

What is capital gains tax (CGT)? We know that income tax is one that taxes gains from everyday income-generating activities, but capital gains tax taxes gains on the sale of assets which are of a long-term nature, like houses, sections, farms and shares. The range is endless, and that's one of the problems. For example, would CGT be levied on the capital growth gains on KiwiSaver accounts? If not, why not?

At the outset, let's comment on two of the most popular and most suspect comments we've heard from politicians so far:

It's too complicated. No it's not. Numerous other countries do it, and if that were a good reason not to do it, then how about scrapping the many tax laws that are very complicated? The PKF International Tax Directory lists more than 40 countries with CGT.

It'll raise billions of dollars a year. We doubt that, and in the kind of years we've had recently capital losses are likely to have exceeded the gains.

Why should we adopt a CGT? We all know

that Labour governments like to tax those who are better off, and the next National government likes to undo what the last lot did. When it was last elected to power Labour raised the top income tax rate from 33 per cent to 39 per cent. When National was elected it put it back again.

Whilst Labour now seems to be seeing CGT as another way of getting at the better-off, we believe that CGT should be less about Robin Hood economics and more about doing things better for the nation.

The problem we have in New Zealand is that whereas many of us earn our living and our wealth through working, and therefore paying income tax, there are many who have created wealth through investing in assets which grow in value, and when sold are not subject to tax. That creates an incentive to invest capital in those sectors. The most popular example in New Zealand is investments in residential housing. The argument is that if capital gains were taxed, the incentive to invest in non-productive assets would be removed, and we will be more likely to invest our capital and savings in productive sectors such as business, shares, forests etc.

For most of us in the Far North, our long-term interests, and those of our children, will be best served by increasing investment in

the productive sectors of the economy.

We believe that CGT is inevitable, and the question is therefore not will it happen but what will it look like? Consider the following:

■ Will capital gains be inflation-adjusted? In Australia pre-1999 assets are, but post-1999 assets are not.

■ Will it be taxed as income, at income tax rates, or will it be a separate regime with special rates?

■ Will the rates be progressive, like our income tax rates, or will they be fixed? Britain has a separate tax, but it is progressive. The US has a combination of both.

■ What exemptions will there be? Britain, for example, has an annual £10,000 exemption. Germany exempts gains on property that has been owned for more than 10 years.

■ What range of share investments will be included? For example, will KiwiSaver gains be exempt?

■ Will there be relief for re-invested gains, like the British model? For example, where a farmer sells one farm to re-invest in another?

■ Will CGT become a death duty in disguise?

■ Will CGT replace or simplify our very complex land sale taxation regime?

■ Will CGT be a step towards a broader, flatter tax base, with more people paying less?

The debates will be lively and frequent.

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