

CGT AND COMPLIANCE COSTS ARE A DOUBLE TAX ON NZ BUSINESSES

- TWG didn't calculate the costs associated with CGT...administration, compliance and deadweight costs
- To double tax NZ businesses is to divert billions of dollars of capital away from investment in growth and productivity
- **BIG RISK:** CGT will lower net returns (IRR). Investors will not absorb this...the result will be lower asset prices
- A CGT will change the behaviour and decision making of thousands of investors / owners (Deadweight Effect)

FACTS YOU NEED TO KNOW

1 INDICATIVE COMPLIANCE COSTS OF \$1.6B OVER 5 YEARS

- Compliance costs are costs to the tax payer made up of Valuation Day costs and on-going compliance costs
- The compliance cost for assets included in the TWG calculation are estimated to be \$1.6b
 - For the assets included in TWG calculations, the valuation costs are estimated to be \$0.8b
 - Based on evidence from Australia, CGT compliance costs could be as high as 16% of tax revenue, we have assumed 10% on the basis that NZ's CGT is less complex (cost of \$0.8b)
- This excludes the valuation cost for private businesses (not included in TWG calculations), estimated to be up to \$5.5b

2 INDICATIVE ADMIN COSTS OF \$210M OVER 5 YEARS

- Administration costs are the IRD's costs of collecting CGT
- CGT admin costs are estimated to be 2% - 4%¹ of CGT revenue

“Compliance costs are high and significant; compliance costs are regressive [will hit small business harder than big business]; and compliance costs are not reducing over time”

PROFESSOR CHRIS EVANS,
TAX ADVISER TO TWG

3 INDICATIVE DEADWEIGHT LOSS OF \$1.5B - \$4.2B OVER 5 YEARS

- Increased taxation leads to deadweight loss (the value of lost output) by prompting people to switch from higher valued to lower valued economic activities.
- Studies estimate deadweight costs on all taxes at 18% – 50% of Tax Revenue
- Every dollar a business incurs in compliance costs results in a dollar less to invest in growth and productivity

COMMON SENSE

- ➔ We can't ignore the material cost and complexity of a CGT on businesses
- ➔ It does not make sense to examine the benefit of a Capital Gains Tax without also examining the significant costs
- ➔ It will be counter-productive to increase the cost burden of New Zealand businesses

A LOT OF PAIN FOR LITTLE GAIN

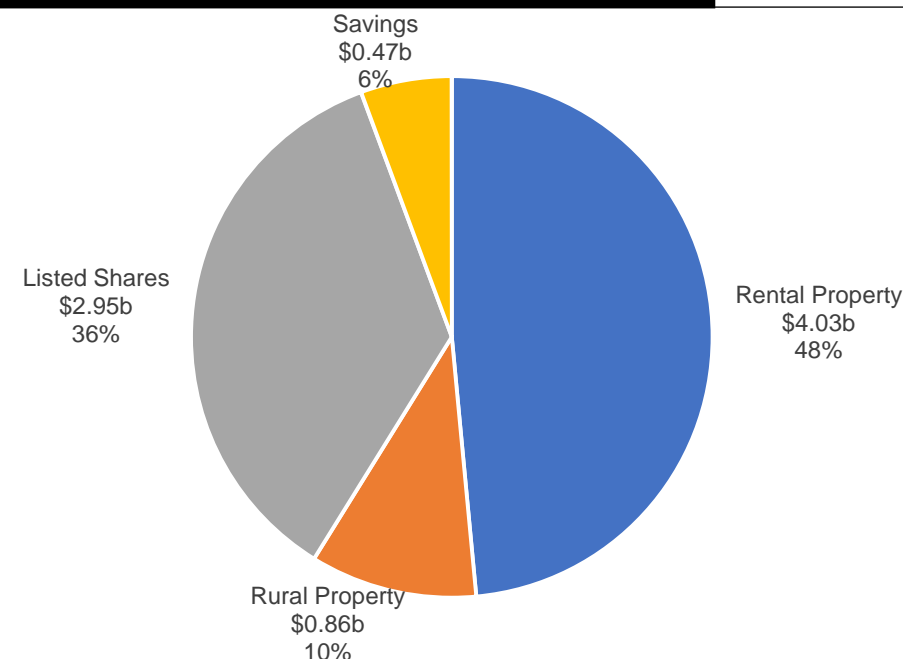
- Economic Drag over the first five years is estimated to be \$2.75b - \$6.81b
- If it is not revenue neutral (i.e NO revenue recycling) total economic drag over the first five years is estimated to be \$10.9b - \$14.8b
- Deadweight loss estimated to be \$1.5b – \$4.2b

WHAT YOU NEED TO KNOW

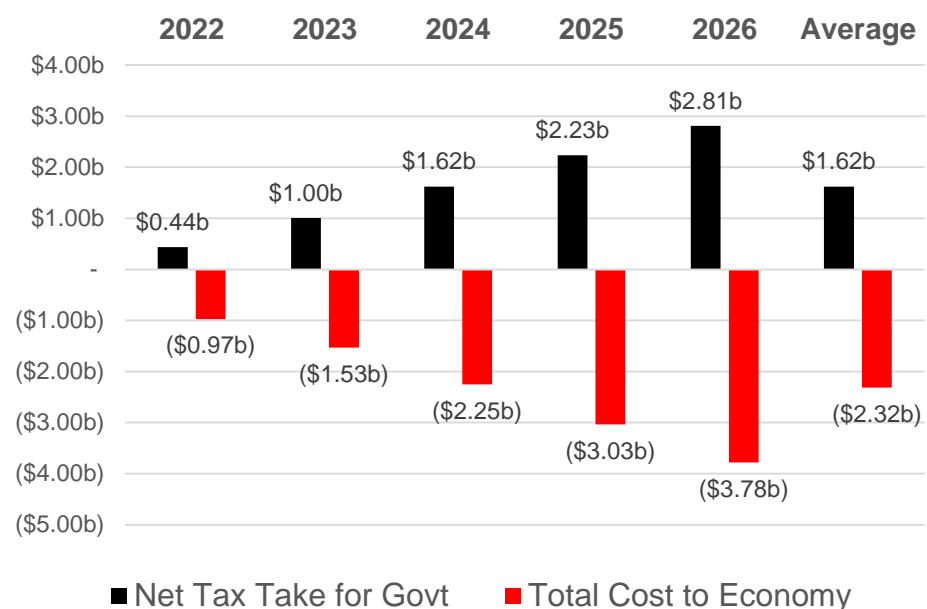
TWG 5 YEAR FORECAST OF CGT REVENUE (Adjusted for Estimated Admin and Compliance Costs)

	2022	2023	2024	2025	2026	Total	Average
Govt Tax Take							
Rental Property	\$0.12b	\$0.41b	\$0.78b	\$1.16b	\$1.56b	\$4.03b	\$0.81b
Rural Property	\$0.08b	\$0.10b	\$0.15b	\$0.23b	\$0.30b	\$0.86b	\$0.17b
Listed Shares	\$0.16b	\$0.43b	\$0.64b	\$0.80b	\$0.92b	\$2.95b	\$0.59b
Savings	\$0.09b	\$0.09b	\$0.09b	\$0.10b	\$0.10b	\$0.47b	\$0.09b
CGT revenue	\$0.45b	\$1.03b	\$1.66b	\$2.29b	\$2.88b	\$8.31b	\$1.66b
Indicative Admin Costs	(\$0.01b)	(\$0.03b)	(\$0.04b)	(\$0.06b)	(\$0.07b)	(\$0.21b)	(\$0.04b)
Low	(\$0.01b)	(\$0.02b)	(\$0.02b)	(\$0.03b)	(\$0.04b)	(\$0.12b)	(\$0.02b)
High	(\$0.02b)	(\$0.04b)	(\$0.07b)	(\$0.09b)	(\$0.12b)	(\$0.33b)	(\$0.07b)
Net Tax Take for Govt	\$0.44b	\$1.00b	\$1.62b	\$2.23b	\$2.81b	\$8.10b	\$1.62b
Cost to the Economy							
CGT paid	(\$0.45b)	(\$1.03b)	(\$1.66b)	(\$2.29b)	(\$2.88b)	(\$8.31b)	(\$1.66b)
Valuation Day Cost	(\$0.39b)	(\$0.19b)	(\$0.10b)	(\$0.06b)	(\$0.04b)	(\$0.77b)	(\$0.15b)
Low	(\$0.32b)	(\$0.16b)	(\$0.08b)	(\$0.05b)	(\$0.03b)	(\$0.64b)	(\$0.13b)
High	(\$0.50b)	(\$0.25b)	(\$0.12b)	(\$0.07b)	(\$0.05b)	(\$1.00b)	(\$0.20b)
Compliance Cost	(\$0.05b)	(\$0.10b)	(\$0.17b)	(\$0.23b)	(\$0.29b)	(\$0.83b)	(\$0.17b)
Low	(\$0.03b)	(\$0.06b)	(\$0.10b)	(\$0.14b)	(\$0.17b)	(\$0.50b)	(\$0.10b)
High	(\$0.07b)	(\$0.16b)	(\$0.27b)	(\$0.37b)	(\$0.46b)	(\$1.33b)	(\$0.27b)
Total compliance costs	(\$0.43b)	(\$0.30b)	(\$0.26b)	(\$0.29b)	(\$0.33b)	(\$1.60b)	(\$0.32b)
Net Direct Cost	(\$0.88b)	(\$1.33b)	(\$1.92b)	(\$2.58b)	(\$3.21b)	(\$9.91b)	(\$1.98b)
Deadweight Loss	(\$0.09b)	(\$0.21b)	(\$0.33b)	(\$0.46b)	(\$0.58b)	(\$1.66b)	(\$0.33b)
Low	(\$0.08b)	(\$0.19b)	(\$0.30b)	(\$0.41b)	(\$0.52b)	(\$1.50b)	(\$0.30b)
High	(\$0.23b)	(\$0.52b)	(\$0.83b)	(\$1.15b)	(\$1.44b)	(\$4.16b)	(\$0.83b)
Total Cost to Economy	(\$0.97b)	(\$1.53b)	(\$2.25b)	(\$3.03b)	(\$3.78b)	(\$11.58b)	(\$2.32b)
Low	(\$0.88b)	(\$1.44b)	(\$2.14b)	(\$2.89b)	(\$3.60b)	(\$10.94b)	(\$2.19b)
High	(\$1.24b)	(\$1.96b)	(\$2.88b)	(\$3.88b)	(\$4.83b)	(\$14.79b)	(\$2.96b)

NET TAX TAKE FOR GOVERNMENT



CGT COST vs BENEFIT



Notes to the indicative and preliminary estimates

1. We look solely at the gross costs of the gross CGT revenue; we do not consider how the revenue may be recycled and any costs and benefits of that recycling.
2. CGT costs are relative to the \$8.31 billion CGT revenue from the TWG over 5 years, which covers residential property excluding the family home, commercial property and rural property. Full valuation of businesses is not included.
3. Valuation costs are largely an up-front cost; over a longer time period these will become much smaller relative to revenue raised
4. Deadweight loss is notoriously hard to estimate – our central estimate uses 20%
5. A range of assumptions on valuation costs, administration and compliance costs and deadweight losses are possible (see Appendix)

Appendix

A CAPITAL GAINS TAX COMES WITH MATERIAL COSTS

Indicative and Preliminary estimates of Costs of a Capital Gains Tax

Year	2022	2023	2024	2025	2026	Total
1. Deadweight loss						
Low	\$0.08b	\$0.19b	\$0.30b	\$0.41b	\$0.52b	\$1.50b
Mid	\$0.09b	\$0.21b	\$0.33b	\$0.46b	\$0.58b	\$1.66b
High	\$0.23b	\$0.52b	\$0.83b	\$1.15b	\$1.44b	\$4.16b
2. Compliance costs						
Low	\$0.03b	\$0.06b	\$0.10b	\$0.14b	\$0.17b	\$0.50b
Mid	\$0.05b	\$0.10b	\$0.17b	\$0.23b	\$0.29b	\$0.83b
High	\$0.07b	\$0.16b	\$0.27b	\$0.37b	\$0.46b	\$1.33b
3. Administrative costs						
Low	\$0.01b	\$0.02b	\$0.02b	\$0.03b	\$0.04b	\$0.12b
Mid	\$0.01b	\$0.03b	\$0.04b	\$0.06b	\$0.07b	\$0.21b
High	\$0.02b	\$0.04b	\$0.07b	\$0.09b	\$0.12b	\$0.33b
4. Initial valuation costs						
Low	\$0.32b	\$0.16b	\$0.08b	\$0.05b	\$0.03b	\$0.64b
Mid	\$0.39b	\$0.19b	\$0.10b	\$0.06b	\$0.04b	\$0.77b
High	\$0.50b	\$0.25b	\$0.12b	\$0.07b	\$0.05b	\$1.00b
Total costs						
Low	\$0.43b	\$0.42b	\$0.50b	\$0.63b	\$0.77b	\$2.75b
Mid	\$0.53b	\$0.53b	\$0.64b	\$0.80b	\$0.97b	\$3.47b
High	\$0.81b	\$0.97b	\$1.29b	\$1.68b	\$2.07b	\$6.81b

Indicative and Preliminary estimates of Costs of a Capital Gains Tax

- Costs of a CGT include deadweight loss, compliance costs, govt administrative costs and one-off valuation costs
- The tax distorts economic activity – tracked by the overall deadweight loss
- Indicative and preliminary estimates suggest costs of \$3.47 billion over 5 years in our central scenario
- The costs are uncertain with significant variation depending on assumptions used

Notes to the indicative and preliminary estimates

1. We look solely at the gross costs of the gross CGT revenue; we do not consider how the revenue may be recycled and any costs and benefits of that recycling.
2. CGT costs are relative to the \$8.31 billion CGT revenue from the TWG over 5 years, which covers residential property excluding the family home, commercial property and rural property. Full valuation of businesses is not included.
3. Valuation costs are largely an up-front cost; over a longer time period these will become much smaller relative to revenue raised
4. Deadweight loss is notoriously hard to estimate – our central estimate uses 20%
5. A range of assumptions on valuation costs, administration and compliance costs and deadweight losses are possible (see supporting slides)

ASSUMPTIONS ON DEADWEIGHT LOSS & COMPLIANCE AND ADMIN COSTS

- Deadweight loss estimates vary considerably
- Compliance costs range to 16% of revenue (e.g. Professor Evans advice to TWG based on Australian experience in the mid 1990s)
- Compliance costs are typically 2-6 times administrative costs (here we benchmark admin costs as 25% of compliance costs)

1. Deadweight loss							
Low	\$0.08b	\$0.19b	\$0.30b	\$0.41b	\$0.52b	\$1.50b	18%
Mid	\$0.09b	\$0.21b	\$0.33b	\$0.46b	\$0.58b	\$1.66b	20%
High	\$0.23b	\$0.52b	\$0.83b	\$1.15b	\$1.44b	\$4.16b	50%

2. Compliance costs							
Low	\$0.03b	\$0.06b	\$0.10b	\$0.14b	\$0.17b	\$0.50b	6%
Mid	\$0.05b	\$0.10b	\$0.17b	\$0.23b	\$0.29b	\$0.83b	10%
High	\$0.07b	\$0.16b	\$0.27b	\$0.37b	\$0.46b	\$1.33b	16%

3. Administrative costs							
Low	\$0.01b	\$0.02b	\$0.02b	\$0.03b	\$0.04b	\$0.12b	1.50%
Mid	\$0.01b	\$0.03b	\$0.04b	\$0.06b	\$0.07b	\$0.21b	2.50%
High	\$0.02b	\$0.04b	\$0.07b	\$0.09b	\$0.12b	\$0.33b	4.00%

ASSUMPTIONS ON VALUATION COSTS FROM A CGT

- Costs driven by assumptions on price and coverage of CGT on second houses, commercial and rural property (see our assumptions below)
- Assumptions drive cost estimate (see right)

Valuation assumptions				
Cost of one-off valuation				
Houses:	703,114	\$50	\$500	\$800
	Low	90.0%	5.0%	5.0%
	Mid	80.0%	10.0%	10.0%
	High	50.0%	25.0%	25.0%
Commercial:	65,000	\$3,000	\$7,500	\$12,000
	Low	90.0%	5.0%	5.0%
	Mid	75.0%	12.5%	12.5%
	High	60.0%	20.0%	20.0%
Rural:	87,000	\$3,000	\$7,500	\$12,000
	Low	90.0%	5.0%	5.0%
	Mid	85.0%	7.5%	7.5%
	High	80.0%	10.0%	10.0%

4. Indicative and Preliminary Valuation Costs of a Capital Gains Tax						
Year	2022	2023	2024	2025	2026	Total
Residential Property						
Low	\$0.08b	\$0.08b	\$0.08b	\$0.08b	\$0.08b	\$0.39b
Mid	\$0.12b	\$0.12b	\$0.12b	\$0.12b	\$0.12b	\$0.60b
High	\$0.25b	\$0.25b	\$0.25b	\$0.25b	\$0.25b	\$1.23b
Commercial Property						
Low	\$0.24b	\$0.24b	\$0.24b	\$0.24b	\$0.24b	\$1.19b
Mid	\$0.30b	\$0.30b	\$0.30b	\$0.30b	\$0.30b	\$1.52b
High	\$0.37b	\$0.37b	\$0.37b	\$0.37b	\$0.37b	\$1.85b
Rural Property						
Low	\$0.32b	\$0.32b	\$0.32b	\$0.32b	\$0.32b	\$0.32b
Mid	\$0.35b	\$0.35b	\$0.35b	\$0.35b	\$0.35b	\$0.35b
High	\$0.38b	\$0.38b	\$0.38b	\$0.38b	\$0.38b	\$0.38b
Total indicative valuation costs (input to total costs of CGT)						
Low	\$0.32b	\$0.16b	\$0.08b	\$0.05b	\$0.03b	\$0.64b
Mid	\$0.39b	\$0.19b	\$0.10b	\$0.06b	\$0.04b	\$0.77b
High	\$0.50b	\$0.25b	\$0.12b	\$0.07b	\$0.05b	\$1.00b
% valuations	2022	2023	2024	2025	2026	
By year	50.0%	25.0%	12.5%	7.5%	5.0%	

