The Treasury

Budget 2023 Tax Initiatives Information Release

July 2023

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Inland Revenue
Te Tari Taake

POLICY AND STRATEGY

TE TAI ŌHANGA
THE TREASURY

Tax Policy Report: Delivering a net wealth tax for Budget 2023

Date:	17 February 2023	**Report No:**	T2023/217 IR2023/067
		File Number:	SH-13-5-3-7

Action Sought

	Action Sought	Deadline
Minister of Finance (Hon Grant Robertson)	**Agree** to the recommendations in this report	20 February 2023
Minister of Revenue (Hon David Parker)	**Agree** to the recommendations in this report	20 February 2023

Contact for Telephone Discussion (if required)

Name	Position	Telephone		1st Contact
Shane Domican	Senior Analyst, Tax Strategy, The Treasury	[39]	N/A (mob)	✓
Stephen Bond	Manager, Tax Strategy, The Treasury		N/A (mob)	
Phil Whittington	Chief Economist, Inland Revenue	[35]		

Actions for the Minister's Office Staff (if required)

Return the signed report to Treasury.

Note any feedback on the quality of the report	

Enclosure: No

Tax Policy Report: Delivering a net wealth tax for Budget 2023

Purpose of Report

1. In this report we seek your agreement to our proposed approach to design a net wealth tax in time for announcement in Budget 2023.

2. We also outline the key design choices that will require further consideration, as well as those that need to mirror decisions already taken in the context of the minimum tax, to enable a Budget announcement.

Background and Context

3. Yesterday you directed officials to focus on designing a net wealth tax for Budget 2023, instead of a minimum tax. This decision has a number of benefits, and it will simplify the design and implementation process (Table 4 details issues that no longer need to be resolved). However, the proximity to Budget 2023 also means that any substantial changes to policy design introduces delivery risk, particularly with respect to costing the policy.

Costing a net wealth tax in time for Budget

4. Estimating the likely fiscal impacts of a net wealth tax, to a standard that will support robust fiscal forecasts in Budget 2023, remains challenging in the time available. This is because of the incomplete wealth data and modelling assumptions required to estimate the revenue

5. To minimise risks to the Budget, we propose mirroring the design of the minimum tax as far as possible. This would mean applying previous decisions taken on the design of the minimum tax to the net wealth tax (where such decisions are applicable). Those decisions have been included in three recent reports:

   - T2022/2703; IR2022/516. 13 December 2022. Initial advice on a minimum tax
   - T2023/74; IR2023/009. 2 February 2023. Minimum tax – Further design
   - T2023/164; IR2023/030 13 February 2023. Minimum tax – Remaining design decisions

6. This approach will enable officials to utilise the costing models we have built already for the minimum tax, considerably simplifying the design and costing process. In most cases, officials would make the same recommendations on design. However, as discussed below, this will also constrain alternative design choices for a net wealth tax in some ways.

7. Without this approach, robust costings are unlikely to be ready in time for Budget 2023, presenting several risks:

   - In the context of a tax switch, the uncertainty associated with the revenue raising initiative would present a considerable risk to the overall fiscal impacts of any change. For example, a package that was intended to be fiscally neutral may be found to be revenue reducing overall. This would have consequences for both the fiscal forecasts and the fiscal strategy.

- If the net wealth tax meets the criteria for inclusion in the forecasts, the Budget documents would need to make clear that the fiscal forecasts are subject to increased uncertainty due to the limitations to costing the net wealth tax. Moreover, the Treasury's next set of forecasts, which will be PREFU 2023, may be subject to a considerable revision.

- In the event that estimates are particularly uncertain, the fiscal forecasts may exclude the net wealth tax entirely. This was the case for the changes to interest deductibility in BEFU 2021. In that situation, the Budget documents included the changes as risks to the fiscal forecasts. This would have implications for the fiscal forecasts and fiscal strategy, particularly if the net wealth tax is intended to offset personal income tax cuts.

Implications for the design of a net wealth tax

8. As signalled above, basing the net wealth tax on the relevant decisions taken to date on a minimum tax will constrain your design options in the near term.

9. It will still be possible to refine the design for changes that do not structurally alter the nature of the tax (and consequently do not require fundamental changes to the costing). However, a robust costing will not be possible in the event of fundamental changes.

10. In general, officials do not consider this creates significant policy design issues. The decisions taken to date on the minimum tax (and our recommendations where decisions are outstanding) are largely suitable for a net wealth tax, subject to a few minor changes.

11. This constraint will, however, limit our ability to model approaches that differ significantly from the minimum tax. For example, there may be elements of the Norwegian approach that we may not be able to replicate.

12. Design changes to the net wealth tax that can not be accommodated before Budget can of course be made after Budget, either through the Parliamentary process to or through later amendments. In that case, any design changes that have fiscal implications would affect future fiscal forecasts and would need to be funded through future Budgets.

Design features we think require reconsideration

13. Table 2 outlines four issues that may require reconsideration if you switch to a net wealth tax. This is because the rationale for these were linked specifically to the minimum tax. Changing these four parameters will not create significant difficulty for modelling revenue. We propose to report to you further on these on 27 February as outlined in Table 1 below.

Design features we assume will mirror the minimum tax

14. Table 3 outlines the design decisions you have made, or we have reported to you on, that we assume will apply to a net wealth tax. Table 3 is split into design decisions that you had previously agreed to (either in the 13 December report or the 2 February report), or that officials recommended in the 13 February report (and are yet to be agreed, but are still relevant and for which your agreement is still sought).

15. In table 3 we also outline which issues will have a fiscal impact, and where deviating from the minimum tax creates greater risk for our ability to forecast revenue. There is some scope for us to change some issues not marked as high difficulty, however these changes will need to be minimal and we would propose urgently discussing any you wish to reconsider.

Table 1. Proposed decision-making timeframe for a minimum tax

Date	Action
27 February	Officials will report to you seeking decisions on issues outlined in Table 2.
10 March	Officials will report to you with: • Our views on the policy and revenue impacts of a net wealth tax • Any legal risks with a net wealth tax, including potential risks under Te Tiriti o Waitangi
17 March	A draft of the Cabinet Paper and officials Regulatory Impact Assessment
5 April	Cabinet paper lodged
11 April	Cabinet decision

Recommended Action

We recommend that you:

a **agree** to proposed design features for a net wealth tax outlined in Table 3 (that broadly mirror those for minimum tax)

Agree/disagree. *Agree/disagree*

b **note** there are outstanding and relevant design issues outlined in our report on 13 February that still require your decision (T2023/164; IR2023/030)

c **indicate** in Table 3 any areas you require further advice on

d **agree** for officials to advise further on the four issues outlined in Table 2

Agree/disagree *Agree/disagree*

Stephen Bond
Manager, Tax Strategy
The Treasury

Phil Whittington
Chief Economist
Inland Revenue

Hon Grant Robertson
Minister of Finance

_____/_____/_______

Hon David Parker
Minister of Revenue

_____/_____/_______

Table 2. Design issues officials plan to advise further on

Issue	Why we think further reporting required	Fiscal impact of a change	Difficulty of implementing a change into our forecast models	Indicate if want further advice
Exemption for wealth under threshold	Officials had recommended to apply the minimum tax to wealth below the exemption threshold.	High impact: changing to an exemption will reduce revenue.	Low difficulty	
Is tax calculated on family or individual basis	The approach for families in minimum tax was to calculate on a family basis whether wealth is above the threshold, and if family above threshold, then every member of the family calculates the minimum tax on an individual basis. If you decide to exempt wealth under the threshold, the current approach for families versus individuals may need to be modified.	High impact	Low difficulty	
Applying the tax to trusts	We previously reported on a system for applying the thresholds to trusts. We think we can apply the same approach, although some details may change.	Low impact: could raise or reduce revenue depending on suggested changes.	Low difficulty if changes are largely technical	
Timing of when assets are valued, when any tax return is filed, and when tax is paid	As a net wealth tax is separate from income tax, you will need to decide when the tax is calculated, filed, and paid.	High impact: timing decisions will change the forecast growth in revenue and when revenue can be booked.	Low difficulty	

Table 3. Design issues officials recommend mirror the minimum tax

Issue	Previous decision/recommendation	Fiscal impact of a change	Difficulty of implementing a change into our forecast models	Indicate if you require further advice
Decisions made as part of 13 December report and 2 February report				
NZ residents only	The minimum tax only applied to New Zealand tax residents	Unknown: could increase revenue if non-resident land was added to the wealth base.	High difficulty	
Assets and liabilities subject to tax	All assets which are likely to increase in value or earn income **other than**: • Family home (subject to a cap on value) • Consumer durables (e.g. cars, boats), small amounts of cash, and defined benefit funds • Māori interests in communally owned assets managed by Māori entity structures • Personal assets such as art and collectables	Moderate to high impact depending on suggested changes.	Moderate to high difficulty depending on suggested changes.	
Foreign assets	Foreign assets, including shares in a controlled foreign company would be subject to the tax	Unknown impact	High difficulty	
Valuation rules	Open market value used for all assets, with power delegated to Commissioner of Inland Revenue to prescribe valuation methods for specific assets Officials will consult on proposed valuation methods	Impact depends on suggested changes	Difficulty depends on suggested changes. For example using book values for unlisted businesses could be relatively simple to model. Other changes likely harder.	

Asset splitting/gifting	No specific rules be in place to prevent gifting of assets	Medium impact: adding gifting rules could raise revenue	High difficulty	

Officials' recommendations from 13 February report				
Applying the tax to farms	Officials recommended to not have a specific concession for farms	High impact	Medium difficulty	
Broad discretionary powers to vary application of the tax	Officials recommended not including a general discretion to vary the application of the tax	Unknown impact	Cannot be modelled	
No concessions for start-ups	Officials recommended no specific deferral or exemption for start-ups	Unknown impact	Cannot be modelled	
Deferral mechanism	Officials recommended not to proceed with a general deferral mechanism	Unknown impact	Cannot be modelled	
Applying transitional resident exemption	Officials recommended that the transitional resident rule apply to the tax, which would exempt foreign assets held by recent migrants for four years	Unknown impact but expected to be minor	Cannot be modelled	

Table 4 – Design issues for a minimum tax that are no longer relevant for a net wealth tax

Issue	Why issue is no longer relevant
Comparing minimum tax to taxable income or tax paid	Income earned and tax paid by a taxpayer is not relevant to their net wealth tax liability
Whether to include labour income in calculation	Related to determining "ordinary taxable income", which is not relevant to determining net wealth tax liability
How to attribute income from PIEs individual taxpayers	Related to determining "ordinary taxable income", which is not relevant to determining net wealth tax liability
Whether to attribute income from listed companies to taxpayers	Related to determining "ordinary taxable income", which is not relevant to determining net wealth tax liability
How to attribute undistributed income from closely held companies to taxpayers	Whether income of a closely held company is retained in the company or distributed is no longer relevant to determining net wealth tax liability
How to treat income earned by a company that could be attributed to either a return from capital, or labour income	Whether income in a company is capital income or labour income is not relevant to determining new wealth tax liability
What tax rate to apply to deemed income	No longer need to determine two separate tax rates (the rate of deemed income, and the tax rate to apply to that income).
Carry-forward mechanism	Carry-forward was intended to smooth out timing differences, so taxpayers with high taxable income in one year and low taxable income in another were not unduly burdened by the deemed minimum tax