SPEAKMAN LAW

Don’t we already tax Capital Gains?...

If you ask that question of a property developer they will say yes. Gains from development of land are invariably taxed, unless held for investment purposes only, ie developing a commercial building for long term rental. These rules are reinforced by exhaustive associated persons rules that in some cases overreach and tax gains on privately held properties.

Similarly, gains from property dealing are taxed. A common question is how many property trades in a year will cause you to be a dealer and trigger a tax liability. There is no set answer to that but a generally held view is that 3 sales in a year is at the threshold.

The same issue arises for share dealers. Moreover, if it is established that a property or share parcel is purchased with an intention of resale then even a one off trade can be within the tax net. Likewise shares gained as part of your employment are automatically within the tax net.

Further examples of capital gains being inside the tax net are such gains made by companies and certain trusts. Companies are not able to distribute capital gains tax free except on liquidation. These gains are therefore effectively pregnant with a tax liability that can only be avoided by deferring their distribution until liquidation. In the case of non-resident corporate shareholders (holding more than a 20% interest) these gains will attract a tax liability, even on liquidation. Trusts can be problematic here too. If the trust is a "non complying trust" (essentially it has foreign sourced passive income) that is retained at the trust level, distribution of capital gains to beneficiaries attract a colossal 45% tax. In the case of foreign trusts, related party capital gains attract a 33% tax on distribution.

Our financial arrangement rules (which generally apply to all debt instruments) provide another instance of capital gains being within the tax net. Those rules, for the most part, do not distinguish between capital and revenue items.

Mr Cunliffe's concern I expect is the impact of foreign buyers on the New Zealand property market. No tax liability arises for them on buying residential properties (unless a pattern of dealing emerges) or on acquiring and disposing blocks of land in the country (notably Queenstown). If this is indeed the concern, a tax regime could target those areas. A broad CGT regime would on the other hand extend to gains on business sales and may well undermine efforts to stimulate genuine business activity. Is a gain on sale of a business to be taxed where sale proceeds are deferred or are not in cash and instead are received in the form of a share swap? What happens if there is a warranty claim that reduces the sale price? Are existing gains to be excluded? If so, does that mean that all existing businesses will need to be valued? If so, how?

All very complicated. Introduction of a CGT system would by no means be easy.