

# Reconceptualisation of Income Tax Graduation as Public Equity

paper by

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*A portion of the product of a society should be shared by all of those who inhabit that society. To establish such a **patrimony** is equivalent to recognizing shared ownership of a significant fraction of the resources, physical and intellectual, that enable the society to produce what it produces.*

Herbert Simon, 2000.

# Evolution of an Idea – my Journey

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- Rankin, Keith (2016). "Prospects for a Universal Basic Income in New Zealand", *Journal of Sociology & Social Welfare* 43(3): 97-120, September
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# Tax Benefits, and Path-Dependent Accounting

## Path Dependent **Income Tax** concepts

- conceived before System of National Accounts, and informed by Classical Economics
- large exemptions to exclude labour incomes and normal profits
- evolved into systems of exemptions, **graduations** and rebates (aka 'tax benefits')

## **Benefits**

- transfer benefits and credits (taper [abate] upwards)
- tax benefits and credits (taper downwards)
- dividends (universal; no taper)

# Appendix Table: Historical Tax Benefits in NZ in the 1960s

**Exemptions:** In the case of individuals certain statutory deductions are made from the assessable income, and income tax is paid on the balance ... Exemptions in 1966-67 were:

- A personal exemption of \$936.
- An exemption of \$312 in respect of a dependent wife (or husband), diminished by \$1 for every \$1 on the wife's income in excess of \$312.
- An exemption not exceeding \$312 in respect of a housekeeper employed by a widow, widower, or divorced person to have the care and control of any child or children of the taxpayer. This is included with the wife's exemption in the statistics.
- An exemption for contributions not exceeding \$156 towards the support of a relative by blood, marriage, or adoption, who was dependent on the taxpayer. Children of the taxpayer were included in this definition, the exemption normally continuing until the child reaches the age of 18 years.
- Life assurance premiums, National Provident Fund, superannuation, and similar contributions. An exemption up to a maximum of \$500, was allowed for life insurance premiums, National Provident Fund, superannuation and similar contributions, in the case of a contributor to the Government Superannuation Fund or a contributor to a subsidised staff superannuation scheme. In the case of other taxpayers, the maximum exemption allowed was \$650.
- Donations and school fees. Exemptions for donations to charities (maximum \$50), gifts of money and/or school fees to private schools (maximum \$100) were allowed. Where exemptions were available under more than one of these headings the total maximum allowed was \$100.

**Quoted** from New Zealand Official Yearbook, 1971,

[https://www3.stats.govt.nz/New\\_Zealand\\_Official\\_Yearbooks/1971/NZOYB\\_1971.html](https://www3.stats.govt.nz/New_Zealand_Official_Yearbooks/1971/NZOYB_1971.html)

Note that to an individual, the size of a *tax benefit* is the exemption times the marginal tax rate.

# Simplifications and Accounting Reforms

## Taxing Income 'at source'

- labour incomes: PAYE 1958
- capital incomes: Residents Withholding Tax

## Personal Rebate – 1974 to 1978

- replaced personal exemption
- would today be called a Tax Credit

## National Superannuation 1976

- extension of former 'Universal Superannuation'
- has dividend component; age qualification only

## Flattening of Graduations – Fewer Tax Brackets

- 1974 to 1988

# Central Idea: Language and Labels Matter

## Gross Public Revenue:

- GDP × *Anchor Rate of Income Tax* (33% in NZ since 1988)
- plus indirect taxation
- plus government revenue from other sources

## All exemptions, graduations and other discounts, relative to this, become:

- benefits; or subsidies (consider company tax)

## The benefit represented by the graduations:

- I have called it *Public Equity Benefit (PEB)*
- its annual value tapers down from \$9,080 to \$0
- every 'economic citizen' grossing \$70,000+ gets \$9,080

# Table 1: Graduation – Public Equity – Benefits

## Projected New Zealand Income Distribution for Year to March 2018

Annual individual taxable income (\$)	Number of people (000)	%	Bracket Midpoint \$	individual PEB \$	aggregate PEB \$m
Zero	319	9	0	0	0
1-10,000	359	10	5,000	1,125	404
10,001-20,000	628	17	15,000	3,305	2,076
20,001-30,000	491	13	25,000	4,855	2,384
30,001-40,000	353	10	35,000	6,405	2,261
40,001-50,000	328	9	45,000	7,955	2,609
50,001-60,000	288	8	55,000	8,630	2,485
60,001-70,000	217	6	65,000	8,930	1,938
70,001-80,000	169	5	75,000	9,080	1,535
80,001-90,000	108	3	85,000	9,080	981
90,001-100,000	87	2	95,000	9,080	790
100,001-125,000	128	4	112,500	9,080	1,162
125,001-150,000	59	2	137,500	9,080	536
150,001+	108	3	200,000	9,080	981
<b>All</b>	<b>3644</b>	<b>100</b>			<b>20,140</b>

<https://2017.budget.govt.nz/budget/2017/economic-fiscal-outlook/facts-taxpayers.htm>

# Table 2: a much larger nominal revenue base

## Projected Central Government Revenue to March 2018

	Path Dependent Method	Public Equity Method
	\$m	\$m
Total Income Tax	50,171	95,040 *
individuals	34,897	55,037 §
companies	13,070	15,400 #
other	2,204	24,603
Indirect Taxes	27,366	27,366
GST	20,580	20,580
other	6,786	6,786
Other Government Revenue	6,263	6,263
Core Crown Revenue	83,800	128,669
percent of GDP	29.1%	44.7%
GDP (expenditure, est.)	288,000	288,000

\* 33 percent of GDP

§ adding in estimate of \$20,140 million for total Public Equity Benefits

# grossing up company tax paid from 28% to 33%

<https://2017.budget.govt.nz/budget/2017/economic-fiscal-outlook/what-we-earn.htm>

# Table 3: Equity Benefits and Implicit Subsidies

## Projected Central Government Expenses to March 2018

	Path Dependent Method	Public Equity Method
	\$m	\$m
Benefits	26,247	71,116
NZ Superannuation	13,671	13,671
transfer benefits	12,576	12,576
equity benefits (PEB)	0	20,140 *
implicit subsidies	0	24,729 §
Core Services	4,843	4,843
Health	17,096	17,096
Education	13,985	13,985
Other Spending	18,329	18,329
Core Crown Expenses	80,500	125,369
percent of GDP	28.0%	43.5%
Balance	3,300	3,300
GDP (expenditure, est.)	288,000	288,000

\* estimated from 2017/18 income distribution table (Budget 2017)

§ accommodaing item

<https://2017.budget.govt.nz/budget/2017/economic-fiscal-outlook/what-we-spend.htm>

# Aside: Budget 2017

Budget 24 May 2017 increased the *maximum* PEB from \$9,080 to \$10,140

– adjusting bracket income thresholds increased the tax-benefits associated with graduation

- increase of \$20pw from \$175 to \$195

– subsequently reversed in November 2017 Mini-Budget

The following set of graduations can raise the average PEB without changing the maximum

income brackets (\$)	tax rate
0 - 9,370	0.0%
9,371 - 48,000	17.5%
48,001 +	33.0%

potentially a good political fit for the present government

# Stage 2 Reform: Public Equity Dividends

- a person grossing \$70,000 (or more) market income per year without any transfer benefits, would be re-accounted as paying 33% income tax and receiving an annual PED of \$9,080
- a person grossing \$48,000 ... would be re-accounted as paying 33% income tax and receiving an annual PED of \$9,080 and paying an annual *surcharge tax* of \$660
- a person grossing \$48,000 market income per year plus total annual *transfers* of \$1,000, would be re-accounted as paying 33% income tax and receiving an annual PED of \$9,080 and receiving an annual *transfer benefit* of \$340
- a person with neither market income nor *transfers*, would be re-accounted as receiving an annual PED of \$9,080 and paying an annual *surcharge tax* of \$9,080

# Table 5: Stage 2 Reform

## Projected Central Government Expenses to March 2018

	Path Dependent Method	Public Equity Method
	\$m	\$m
Benefits	26,247	71,116
public equity dividends (PED)	0	31,780 *
universal superannuation	13,671	1,960 #
transfer benefits (net of surcharge taxes)	12,576	12,647 §
implicit subsidies	0	24,729
Core Services	4,843	4,843
Health	17,096	17,096
Education	13,985	13,985
Other Spending	18,329	18,329
Core Crown Expenses	80,500	125,369
percent of GDP	28.0%	43.5%
Balance	3,300	3,300
GDP (expenditure, est.)	288,000	288,000

\* based on 3.5 million economic citizens

# estimate based on \$2,800 in addition to PED for 0.7m economic citizens

§ accommodaing item

# Stage 3 Reform: Public Equity Royalties

Tax all income at source, at *Anchor Rate* (eg 33%)

- Gross Personal Income becomes a redundant concept

Income Tax is in fact a 'Production Tax'

- we may call it a *royalty*

All incomes would be cited 'after tax'

- persons grossing \$100,000 would in fact earn \$67,000

Marginal Tax Rates become redundant

Effective Marginal Tax Rates not redundant

- need a new name for EMTR:

eg Marginal Taper Rate (MTR)

- MTR cited with respect to 'after tax' personal income

# Table 6: Stage 3 Reform

## Projected Central Government Revenue to March 2018

	Path Dependent Method	Public Equity Method
	\$m	\$m
Public Equity Royalty	50,171	95,040 *
Taxes	27,366	27,366
GST	20,580	20,580
other	6,786	6,786
Other Government Revenue	6,263	6,263
Core Crown Revenue	83,800	128,669
percent of GDP	29.1%	44.7%
GDP (expenditure, est.)	288,000	288,000

\* 33 percent of GDP

<https://2017.budget.govt.nz/budget/2017/economic-fiscal-outlook/what-we-earn.htm>

Public Equity Royalty is the sum of all income taxes as shown in Stage 1 Reform (otherwise as Table 2).

# *economic citizen with small transfer and a pay increase*

**Table 7: Stages of Reform, re an adult economic citizen grossing \$48,000 with a \$2,000 transfer tapering at 20 cents in the dollar.**

## Public Equity Reform, in relation to an example economic citizen

		Path Dependent	Reform Stage 1	Reform Stage 2	Reform Stage 3
		\$	\$	\$	\$
Before change	Gross market	48,000	48,000	48,000	32,160
	Net market	40,580	32,160	32,160	32,160
	Equity benefit	0	8,420	9,080	9,080
	Transfer benefit (net)	2,000	2,000	1,340	1,340
	Net income	<b>42,580</b>	<b>42,580</b>	<b>42,580</b>	<b>42,580</b>
After change	Gross market	50,000	50,000	50,000	33,500
	Net market	41,980	33,500	33,500	33,500
	Equity benefit	0	8,480	9,080	9,080
	Transfer benefit (net)	1,600	1,600	1,000	1,000
	Net income	<b>43,580</b>	<b>43,580</b>	<b>43,580</b>	<b>43,580</b>
Marginal tax rate		30.0%	33.0%	33.0%	0.0%
Effective Marginal tax rate		50.0%	50.0%	50.0%	25.4%

# *economic citizen with a pay increase, without a transfer*

**Table 8:**

**Stages of Reform, re an economic citizen grossing \$48,000 without any transfer benefits.**

**Public Equity Reform, in relation to an example economic citizen**

		Path Dependent	Reform Stage 1	Reform Stage 2	Reform Stage 3
		\$	\$	\$	\$
Before change	Gross market	48,000	48,000	48,000	32,160
	Net market	40,580	32,160	32,160	32,160
	Equity benefit	0	8,420	9,080	9,080
	less Surcharge tax	0	0	-660	-660
	<b>Net income</b>	<b>40,580</b>	<b>40,580</b>	<b>40,580</b>	<b>40,580</b>
After change	Gross market	50,000	50,000	50,000	33,500
	Net market	41,980	33,500	33,500	33,500
	Equity benefit	0	8,480	9,080	9,080
	less Surcharge tax	0	0	-600	-600
	<b>Net income</b>	<b>41,980</b>	<b>41,980</b>	<b>41,980</b>	<b>41,980</b>
Marginal tax rate		30.0%	33.0%	33.0%	0.0%
Effective Marginal tax rate		30.0%	30.0%	30.0%	-4.5%

# Some Implications

- Accounting is not an end in itself. Accounting informs actions, in business, and in public policy. The most obvious accounting-informed policymaking would be to resolve anomalous subsidies and surcharge taxes; indeed, the top priority for future 'tax cuts' might become the elimination of surcharge taxes in low incomes.
- Once all surcharge taxes are eliminated, the *public equity dividend* becomes a patrimony, a 'universal basic income' as defined in 1991; a vehicle for equitably sharing productivity – the public fruits of the 'four capitals' – with all economic citizens.
- *Public equity fiscal accounting* concepts can open-up new 'adjacent possible' options in our thinking around income distribution. In turn, more-imaginative thinking can further stimulate the evolutionary development of the policy contribution of public accounting to addressing and resolving the inequality issues that have beset high-productivity economies.