

1 March 2019

**INEQUALITY OF NET INCOME**  
**INEQUALITY OF NET ASSETS**  
**TWENTY THOUGHTS**

We are all going to read about this many, many times over the next few years - what is it? It is the perception that many people around the world have got left behind in financial terms - this, to some degree, has sparked Brexit, Trump, and more recently, the ongoing riots in Paris.

A few thoughts and comments:

1. Our NZ government has a phrase they like to use called "wellbeing" - a part of the background for the Capital Gains Tax Group is about wellbeing.
2. There are 33,000 empty houses in Auckland at the present time - some are apartments, but if you apply, say, a conservative potential rental for those houses of, say, \$600 per week each, you end up with an annual potential rental income of \$1,029,600,000 - yes, \$1.029 billion. If you apply an average Auckland house value (after allowing for quite a number of apartments) of, say, \$750,000, you end up with the current market value of these houses of some \$2,475,000,000 - \$24.75 billion.
3. The NZ 'powers that be' do not seem to comprehend that while helping people own their own houses is certainly a good thing to do, and is very much to be encouraged, that there will always be around a 33% NZ group who will be long term house tenants most, if not all, of their life - we need to plan for this group and encourage long-term house rental arrangements, security of tenure etc. Around 50% of the people of Germany (the richest country in Europe) are long-term dwelling renters.
4. The whole NZ home ownership issue needs more Plan B thinking - maybe climate control costs as well - until politicians work out who is going to pay for climate control, then any Plan B will be elusive. The French President tried very hard to build up financial reserves, in the main to deal with fuel emissions, but the public rioted about the costs and are still rioting at the time of writing - mainly they are rioting about inequality issues for the lower income group.
5. The American Democrats are warming up for the next USA election and their media is full of inequality issues regarding income and wealth and how it must be dealt with at their next election - this issue is running neck and neck with climate control. In the main, they are focusing on taxing the rich much harder and somehow or other giving this tax money to the less well-off group - there are many more inequality issues in the USA than NZ or Australia, but it is here and it is called 'wellbeing' by our government.
6. The latest NZ treasury model of who pays how much Income Tax for the year to end 31 March 2019 is an interesting read:
  - There are 3,773,000 NZ people above 16 years of age who are expected to file a Tax Return.
  - There are 367,000 people who have no taxable income.
  - There are 718,000 people who earn more than \$70,000 per year.
  - The 718,000 (19.03% of the total taxpayers) will pay \$22 billion of Income Tax, which is 63.56% of the total Income Tax receipt of \$34.31 billion.
  - This data does not include GST income or corporate income.

7. The median net wealth of NZ households at 30 June 2018 was \$340,000 - up from \$289,000 three years ago. If you take the view that the average NZ couple have, say, two children, then the average NZ inheritance will be of the order of \$170,000 plus per child - but it won't be received until these children are probably in their 60s or 70s.
8. The number of NZ millionaires at the present time is of the order of 270,000, with this figure being in \$US terms. Our NZ/USA exchange rate presently is around \$1.45 (that is, one USA dollar would purchase \$1.45 of NZ dollars) and includes the net equity in any house owned.
9. A worldwide concern is the low wealth of young people around the world - student debt, less access to pensions, and lower income mobility are all playing a role here.
10. Another approach for dealing with inequality of income is the proposition of a country paying out a "universal basic income" to all of its citizens over, say, 18 years of age every year. Finland and Switzerland have had a good look at this concept and there are several major trials under way in Sweden, but as yet nothing has come out of this one way or the other - the idea being that one payment like this would substitute for a number of social welfare-type allowances. The cost, for example, in NZ might be something along the following lines:

|                                                                                                                                                |                                  |
|------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------|
| Say, 3,500,000 NZ people above 18 years of age at an annual payout rate of, say, \$1,000 per month - that is, \$12,000 per year (\$42 billion) | \$42,000,000,000                 |
| Less, the effect of reducing, say, 75% of the present NZ social welfare annual budget of \$25 billion, say                                     | \$18,750,000,000                 |
| <i>Leaving a net cost of \$23.25 billion</i>                                                                                                   | <u>\$23,250,000,000</u><br>===== |

There would need to be some adjustment to the National Superannuation existing payouts for those over 65 years, but the very broad figure of \$23.25 billion would be an enormous cost and would turn the present NZ Income Tax system probably upside down.

11. India is presently having a good look at this "universal basic income" concept - India has one big advantage here in at least mathematical terms - India has a present population of 1.34 billion, but to double the average annual Indian household income would cost only around \$150 per year (\$NZ) per household (Wall Street Journal). The birth fertility rate in India is 2.33 per woman, which would suggest about 310 million households which at \$150/household which would mean the Indian government would have to find around \$46.5 billion (\$NZ) - just how much of the Indian present social welfare budget would be able to be offset with this payment is anybody's guess - the real point is that relative to the number of its adult population (some 620 million), the cost of a universal basic income for India is a quite different financial exercise.
12. The NZ Prime Minister currently earns \$470,000 per year, approximately eight times the NZ median salary/wage of around \$59,000. The average NZ household had, in the 2018 year, an income (before tax) of \$105,719 - in 2007 this figure was around \$75,000 - an increase of 41% over the last 11 years.
13. It would not take much push back from someone in the present government coalition and the CGT report may only come to, perhaps, a Capital Gains Tax on rental houses/apartments - even now, though there is a five year "bright line" test that already applies in these situations. A CGT on share market profits (and losses?) and on the sale of business profits (and losses?) looks very messy - a valuation day with valuation established by independent valuers looks quite impractical - it would have to be automated in some way with a benchmark against something, but what?
14. The NZ treasury has estimated that the government would raise, perhaps, \$8.3 billion over five years from their suggested CGT report - treasury is also saying that there are 3,055,000 NZ people who earn less than \$70,000 per year. The government is keen to get most of that \$8.3 billion to this group below \$70,000 - this would mean that, potentially, this group of 3,055,000 could perhaps expect to receive \$2,717 each (\$8.3 billion divided by 3,055,000) but spread over five years this would represent an average of \$543 each per year - allowing for the administration costs and set up costs, this five year average would quickly drop below \$543. Hard to see how this exercise is worthwhile.

15. The writer has been dealing in financial terms now, with NZ people, for some 50 years - I have found that 25% of NZ people have poor money management and that this invariably leads into poor business management and poor household financial management - the children of this group learn little across the family kitchen table, which should be the cornerstone of their education. Don't pitch too much of the country's financial planning, brainpower and opportunity at this group - yes, they need it; yes, it is how democracy works; yes, all children are worth it; yes, the better off will help without being forced into it, but the future of any country is dependent upon people taking business risks, employing people, taking bold steps, paying taxes, encouraging people, encouraging education, coping with change, accepting innovation, helping their neighbours, and bouncing back from losses or mistakes. This latter group also deserves considerable focus and listening too.
16. Tackling inequality of income issues is going to be very hard to get even close to fixing, if only because a large group of people want to work, they want to save, they want to invest, they want to get job satisfaction, they want to grow their business, their thinking and their ability, and become good with money. Even if you somehow got this group more even for a period with everybody else, within 12 months the gap would again start to widen - fighting inequality of income is like stopping the tide: you are fighting human nature and you will lose.

If you gave 1,000 people \$100,000 each and then drilled down to see what happened after, say, three years, various financial surveys would suggest you would find something like as follows:

|                                                                        |                                                                       |
|------------------------------------------------------------------------|-----------------------------------------------------------------------|
| 20% would not only have nothing left but would have a debt of \$25,000 | } The last two surveys I read suggest this would only take two years. |
| 20% would only have \$25,000 left                                      |                                                                       |
| 20% would still have \$75,000 left                                     |                                                                       |
| 20% would have increased it to \$125,000                               |                                                                       |
| 20% would have increased it to \$150,000                               |                                                                       |

This is how human nature works and has worked all my life – human nature, like the tide, always prevails.

17. Inequality of income will be very hard to deal with as regards to putting something in place that is sustainable long-term, but dealing with inequality of assets/wealth will be much more difficult again to deal with.
18. Whatever the government does, they need to build it around, not through, our present NZ taxation system - they must keep it simple. Something that would have a long term beneficial effect would be to simply alter the present Income Tax rates, taxing the higher group more and the lower group less. Treasury would need to work through the numbers and brackets, but having no Income Tax on, say, the first \$7,500 of taxable income would be a good start. Don't forget that at present a couple with a combined taxable income of around \$52,000 and with two children under 18 years of age would pay no tax in that situation because the Family Tax Credits claimable would completely offset the Income Taxes due. 19.03% of NZ taxpayers are already paying 63.56% of the Income Tax that our government hopes to collect – why do we, it seems, always have to keep hammering this group.
19. The world media seems to overlook the point that there are thousands and thousands of people out in the marketplace (the writer is one of these) whose job is to try and ensure that their business clients are doing better than average - that is, trying to make sure their clients have higher than average income and higher than average wealth. There is a major industry (the whole financial industry) around the world working very hard to widen this inequality gap, not narrow it.
20. The problem with inequality of income and inequality of assets is that if it continues to get worse rather than better around the world, then it will lead to civil unrest and this has already happened with the Paris riots. The whole issue here is a little like climate control in that Plan A is struggling and Plan B has not arrived - when you take a helicopter view here you do wonder just who is going to pay for the enormous capital costs here - the default option seems to always be: load it up on the people paying most of all government taxes already.



Pita Alexander is an accountancy and agribusiness director at Alexanders.

PS: Any proposed Capital Gains Tax is really a punishment for planning, thinking, saving, investing and distributing to those who don't.