

Reconceptualisation of Income Tax Graduation as Public Equity

paper by

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Abstract

A 'Universal Basic Income' in 2016 became a genuine policy option for a major political party (Labour) in New Zealand. It is thus a concept – like negative income tax – that requires more public understanding. In particular, something close to a Universal Basic Income can be created, in New Zealand, as a pure accounting exercise.

The argument here is that the Universal Basic Income – described in 1991 as a "universal tax credit" coupled with a "moderately high flat tax" – need not be the radical change to the fiscal state that it is frequently painted as, by both proponents and opponents. The approach adopted has been called 'Basic Income Flat Tax', as distinct from the prevailing 'Conditional Income Graduated Tax' conceptualisation of the tax-transfer interface.

The suggested reconceptualisation of income tax considers an additional share of GDP to be included as public revenue, by regarding existing income-tax graduations as 'public equity benefits'. This exercise in fiscal arithmetic shows that – by grouping Public Equity Benefits, Work and Income Benefits, Family Tax Credits and Student Allowances all as alternative forms of publicly-sourced private income – New Zealand and other similar countries already have something close to universal personal tax credits.

A reformulation of the May 2017 and 2018 Budget aggregates contrasts alternative approaches to determining gross public revenue. 'Public equity benefits' may be seen as a conceptual precursor to 'public equity dividends', which represent an affordable Universal Basic Income with constructive labour market incentives.¹

Introduction

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.

The way we think about taxation in general – and income tax in particular – is historically path dependent. In particular, tax policies informed by classical macroeconomics saw taxes on both labour and capital as costs that would undermine the drivers of growth. The resulting view was that taxation was a necessary evil that should be minimised, and that certain classes of people – especially labourers – should be exempt from taxes on their incomes.

Income tax was so born as a graduated tax, with a zero percent bottom rate. In 1891 – when income tax was first introduced in New Zealand – there were two non-zero marginal rates, thereby creating a three-rate scale (Goldsmith 2008, Vosslander 2009). Subsequent developments in the history of income tax have been largely extensions, complications and simplifications of this multistep scale. In New Zealand's 1973 Budget, the bottom (zero percent) rate (exemption) was removed; replaced

¹ This paper has been written to give critical attention to the essential accounting aspects discussed in my 2018 report 'Public Equity and Tax-Benefit Reform' (Rankin 2017, published by the AUT Policy Observatory), in a number of foreign publications (Rankin 2012, Rankin 2016a, Rankin 2016b), and in earlier New Zealand publications (Rankin 1997, Rankin 1998, Rankin 2011a, Rankin 2011c). The paper includes a glossary (as per Rankin 2017), with glossaried items presented throughout this text in *italics*.

by a non-refundable (non-indexed) tax credit which itself was removed in 1978 (Rankin 2006).

These initial (and substantial) exemptions helped to create an artificial split, in perception, between taxable and non-taxable income; a split that encouraged people to think of exemptions as something distinct from a zero-percent bottom rate.² This division also enabled a form of social-policy – a policy of variable tax exemptions (called 'allowances') and rebates – that would run for many years in parallel (as *tax benefits*) with a social security apparatus that began (in New Zealand) in 1898 with the old-age pension. For NZ examples from the 1960s, see Appendix Table 2 (NZOYB 1971).

Public Equity: Language and Definitions Matter

Applying new language and a new accounting apparatus to the income tax component of a country's Budget can mean much more than a new government's marketing makeover.³

Among the most slippery metrics in our language of public finance are those of *gross public revenue* – the total size of the public component of gross domestic product (GDP) – and gross public disbursements (general government outlays including benefits, government consumption, and government capital spending).⁴ Benefits such as New Zealand Superannuation can be accounted gross or net of income tax. And "putting more cash in workers' pockets" is accounted for very differently if done so via the raising of income tax thresholds, compared to raising a *transfer* such as the Supported Living Payment, formerly known as Domestic Purposes Benefit.

My focus here is on *gross public revenue*, with the proposal to define it as the sum of:

- x percent of GDP, where 'x' can be called the *actual rate of income tax*
- all indirect tax revenue
- all other (non-taxation) government revenue

The important component is the first. The size of 'x' can be derived from what elsewhere (Rankin 2017) I have called the *anchor rate of income tax*, and which in New Zealand (since 1988) has been 33 percent (33 cents in the dollar).⁵

² Because many jurisdictions regard some market income as non-taxable, in this paper I refer to gross market income in preference to gross taxable income. In a New Zealand context, the two concepts can be regarded as equivalent.

³ An example of language change that came about in New Zealand as a marketing device was the general replacement of the word 'pension' by the word 'benefit', in the 1938 Social Security legislation. (McClure 1998 p.83)

⁴ As macroeconomic concepts, these relate to 'general government'. The analysis here, however, is confined to central government.

⁵ In a contemporary developed economy, the anchor rate of income tax can usually be identified from both of the following criteria:

1. the prevailing marginal tax rate experienced by most senior professional workers (such as managers, academics and public servants).
2. between 30 and 45 percent.

In Australia in 2018, the anchor rate of tax would be 37 percent (www.exfin.com/australian-tax-rates).

There are three main implications of this:

- For individual tax residents (or *economic citizens*), the difference between their income tax liability calculated entirely at the *anchor rate* and their income tax liability as calculated using prevailing graduated statutory tax rates⁶, is in fact a benefit. This benefit deserves a name. I have used the name *public equity benefit*, on the basis that gross public revenue reflects the total collective equity of the New Zealand public in the New Zealand economy, and because all public benefits are funded from *gross public revenue*. (From here on, the *anchor rate of income tax* will be referred to as the *actual rate* – or simply 'the rate' – of income tax.)
- For businesses, whenever the company tax rate is less than the *actual rate* of income tax, then, properly accounted, businesses are receiving a subsidy – a benefit – equal to profits times the difference between the *actual rate of income tax* and the company rate.⁷ A new accounting approach says nothing about whether such subsidies are good or bad; it simply acknowledges that a discounted rate of company tax is equivalent to a benefit.
- For the macroeconomy, the size of the government share – the public share – is greater than we traditionally regard it as being. It is appropriate to talk of the public 'half' of the economy, using the word 'half' to mean one part out of a whole made up of two large parts.⁸ Tables shown below suggest that this 'half' in New Zealand in 2018 is around 45 percent of GDP. (We are more accustomed to thinking of the public share as being about one-third of GDP.)

Tax Benefits

Tax Benefits here are all those benefits which are paid as income tax concessions, exemptions, rebates or allowances. (See Appendix Table A for a list of historical tax benefits; benefits that largely ceased to exist in New Zealand from the 1980s.) The best known current example of this type of tax benefit is the \$521 per year KiwiSaver credit; a benefit which is less for people on lower incomes. I largely exclude those explicit benefits which today are called 'tax credits', but which actually work very much like social security benefits, despite being administered by the

⁶ At present, since 2011: 10.5%, 17.5%, 30% and 33%.

⁷ An additional example of such implicit subsidies relates to the non-taxation of imputed rental income on owner-occupied dwellings. Also, 'tax avoidance' would be accounted for as subsidisation; taxation policy informed by the public equity principles proposed here should, through simplification, make tax avoidance more difficult.

⁸ While this conceptual division can be applied to 'general government', not just to central government, the focus here is on central government.

taxation authority.

In most cases *tax benefit* payments are implicit, meaning that presently – that is, path dependently – they are accounted for as reductions in liable tax, and not as explicit payments. The particular form of tax benefit addressed here, I have called *public equity benefit*; a *graduation benefit* that arises from the very process of *graduated income taxation*.

Tax benefits generally *taper* downwards, unlike social security transfers which generally taper upwards.⁹ The most important of these tax benefits is the previously noted *public equity benefit* (PEB), which in New Zealand (and based on an *actual tax rate* of 33 percent) is \$9,080 per year for all economic citizens grossing \$70,000 or more of market income, and a lesser (tapering) amount for those earning less, tapering to zero for a person with zero gross income.¹⁰ Table 1 below shows individual and aggregate PEBs for bracket-midpoint incomes.

Table 1

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
All	3644	100			20,140

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

The *public equity benefit* in New Zealand has been set (implicitly) at a maximum of \$9,080 (per year) since the last round of income tax changes in 2010. The 2017 Budget raised it to \$10,140 (\$195 per week), through what was usually described as a tax reduction of \$1,000 per year (or

⁹ In New Zealand we tend to use the word 'abate' rather than 'taper'. Tapering downwards means that people on lower incomes receive lower benefits. Tapering upwards means that people on higher incomes receive lower benefits.

¹⁰ Each income-bracket on the tax scale represents a component of the \$9,080 annual benefit. The 10.5% bracket confers a benefit of upto \$3,150. The 17.5% bracket confers a benefit of upto \$5,270. The 30% bracket confers a benefit of upto \$660.

\$20 per week) to all middle- and high-income earners (and a lesser amount to others). The incoming government's late 2017 'mini-Budget' reversed this PEB increase before it was due to take effect in April 2018.

The PEB has all the usual properties of historical *tax benefits*. It is unconditional. It is administered by the country's tax authority, calculated in accordance with the economic citizen's income and declared tax code.¹¹ And it tapers downwards.

Fiscal Accounting Example: 'Year to March 2018 forecasts' from Budget 2017

Table 2 below shows projected central government revenue for the year to March 2018, taken from Budget 2017. It shows that, under the prevailing *path dependent fiscal accounting* method, 'Core Crown Revenue' is \$83.8 billion (29 percent of GDP). By contrast, in the *public equity fiscal accounting* approach, gross central government revenue is \$128.7 billion (nearly 45 percent of GDP). The difference is that total accountable income tax, set at 33 percent of GDP, covers all implicit benefits and subsidies.

Table 2

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		

In Table 2, individual income tax is boosted by an estimate of total PEBs (*public equity benefits*) from Table 1. Paid company taxes are grossed up to 33 percent (from 28 percent). The 'other' income tax is an accounting residual. In practice, the very large boost to this item will

¹¹ Re the 'declared tax code', persons eligible for the Independent Earner Tax Credit receive a higher public equity benefit than those with the same market income who are not eligible. (<http://www.ird.govt.nz/income-tax-individual/tax-credits/ietc/independent-earner-tax-credit.html>)

have arisen from a mix of explicit tax exemptions (such as those on the imputed rental income on owner-occupied housing) and (legal, though sometimes questionable) tax avoidance practices.¹² This 'other' entry will include (undoubtedly) some outright tax evasion.

Table 3 shows government disbursements, on the basis of both *path dependent fiscal accounting*, and the public equity approach. The difference is in the addition of *public equity benefits*, and implicit subsidies. Here the PEB represents the implicit benefit arising from the graduation of personal income tax marginal rates. And the 'implicit subsidies' represents – among other things, as the balancing item – company tax subsidies, owner-occupier subsidies, tax avoidance benefits and tax evasion benefits.

Table 3

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>

All economic citizens of New Zealand grossing over \$70,000 of annual market income presently receive an unconditional annual PEB of \$9,080 when considered to be paying all their tax at an actual rate of 33 cents in the dollar. Likewise, all economic citizens of New Zealand grossing from \$1 to \$69,999 of annual market income receive an unconditional annual PEB of less than \$9,080 when accounted to be incurring all their tax at 33 cents in the dollar.

All *economic citizens* with any market income – and most with no market income – presently receive some mix of benefit payments. Most – including many economic citizens grossing less

¹² The matter of tax avoidance by trans-national companies through transfer pricing will not be reflected here, because transfer pricing diminishes the measured GDP of victim countries, while inflating the GDP in beneficiary jurisdictions.

than \$70,000 per year – receive *total benefits* of at least \$9,080 per year. The concept of *total benefit* is an important one. It represents the share of a person's monetary income that should be accounted as deriving from the public 'half' of the private-public GDP split.

Table 4: Using Budget 2017 Income Tax Thresholds announced for 2018/19

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	3,865	2,427
20,001-30,000	491	13	25,000	5,415	2,659
30,001-40,000	353	10	35,000	6,965	2,459
40,001-50,000	328	9	45,000	8,515	2,793
50,001-60,000	288	8	55,000	9,690	2,791
60,001-70,000	217	6	65,000	9,990	2,168
70,001-80,000	169	5	75,000	10,140	1,714
80,001-90,000	108	3	85,000	10,140	1,095
90,001-100,000	87	2	95,000	10,140	882
100,001-125,000	128	4	112,500	10,140	1,298
125,001-150,000	59	2	137,500	10,140	598
150,001+	108	3	200,000	10,140	1,095
All	3644	100			22,382

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

Projected Central Government Expenses to March 2018		
	Path Dependent Method	Public Equity Method
	\$m	\$m
Benefits	26,247	73,358
NZ Superannuation	13,671	13,671
transfer benefits	12,576	12,576
equity benefits (PEB)	0	22,382 *
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	127,611
percent of GDP	28.0%	44.3%
Balance	3,300	1,058 §
GDP (expenditure, est.)	288,000	288,000

* estimated from 2017/18 income distribution table (Budget 2017)
§ accommodating item

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

Budget 2017 increased maximum annual *public equity benefits* from \$9,080 to \$10,140 (\$175 to \$195 per week). Table 4 represents a recalculation of Tables 1 and 3, using the revised income tax thresholds announced in May 2017 (though revoked in November 2017). Though intended not to apply until the 2018/19 fiscal year, Table 4 nevertheless reveals a surplus fiscal balance of over one billion dollars.

Reconceptualisation, New Zealand, Stage 2

In this stage, *public equity benefits* are replaced by *public equity dividends*.¹³ A *public equity dividend* is, in essence, the same as a Universal Basic Income (UBI) – as defined in 1991 (Rankin 1991) and noted in 2017 (Standing 2017, p.19) – though not as a UBI is commonly understood.¹⁴ It can also be called a 'refundable tax credit' (Atkinson 1995), or the 'basic income' component of the 'Basic Income Flat Tax' (Atkinson 1995, Rankin 2011a) approach to benefits and income taxes.

Each *economic citizen* – receiving (from Stage 1) a mix of *total benefits* – now has their total benefit categorised as a *public equity dividend* (PED; \$9,080) plus a *transfer benefit* or minus a *surcharge tax*. Consider the following examples:

- A person grossing \$70,000 (or more) market income per year without any transfer benefits, would be re-accounted as paying 33 percent income tax and receiving an annual PED of \$9,080.
- A person grossing \$48,000 market income per year without any transfer benefits, would be re-accounted as paying 33 percent 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* (after tax) of \$1,000, would be re-accounted as paying 33 percent income tax and receiving an annual PED of \$9,080 and receiving an annual *transfer benefit* of \$340.
- A person grossing \$14,000 market income per year without any transfer benefits, would be re-accounted as paying 33 percent income tax and receiving an annual PED of \$9,080 and paying an annual *surcharge tax* of \$5,930.

¹³ Simon (2000) refers to a "patrimony" as a "portion of the product of a society that should be shared by all of those who inhabit that society". While a *public equity dividend* is set here as an accounting construct (offset by *surcharge taxes*), it is likewise conceived as an equal share from *gross public revenue*. Simon's estimate of the contribution of public domain inputs to productivity is far in excess of the 30 to 45 percent suggested by my *anchor tax rate* criteria. Pragmatism suggests that, subsequent to public equity accounting being adopted, the *actual tax rate* and the *public equity dividend* amount should reflect productivity gains.

¹⁴ The UBI, in common discourse, is no longer linked, by definition, to a single rate of income tax. It is generally understood by advocates on the political left to represent a benefit that on its own represents some 'adequate' level of subsistence. Van Parijs (2000) follows this 'subsistence' approach (Rankin 2018). And a UBI is sometimes represented by those on the political right as a full-replacement benefit; a payment that would enable the abolition of the Social Security infrastructure.

- A person grossing \$14,000 market income per year plus total annual *transfers* (after tax) of \$10,000, would be re-accounted as paying 33 percent income tax and receiving an annual PED of \$9,080 and receiving an annual *transfer benefit* of \$4,070.
- 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.
- A person without market income but with *transfers* (after tax) of \$20,000, would be re-accounted as receiving an annual PED of \$9,080 and receiving an annual *transfer benefit* of \$10,920.

Table 5 shows Table 3 revised for Stage 2 public equity accounting reform.

The points to note are that 3.5 million economic citizens are each accounted to receive an annual *public equity dividend* (PED) of \$9,080. Further,

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		
	§ accommodating item		
	https://2017.budget.govt.nz/budget/2017/economic-fiscal-outlook/what-we-spend.htm		

Economic citizens receiving (from Stage 1) *total benefits* of less than \$9,080, now have a *public equity dividend* (PED) of \$9,080, plus a *surcharge tax*. *Low-income surcharge taxes* are, essentially, regressive. For countries like Australia which have a top marginal income tax of 45 percent on very high-income recipients, such a tax would be called a *high-income surcharge*

tax, which is progressive, raising a person's average income tax with increased market income.¹⁵

This would mean that, in an accounting sense, all economic citizens would receive, universally, an unconditional publicly-sourced income (eg \$9,080 per year; \$175 per week). In addition, some would receive transfer benefits, while others would incur surcharge taxes.

New Zealand presently has a semi-universal (taxable) retirement dividend, called New Zealand Superannuation. Using rates set on 1 April 2017 – for consistency with other metrics presented here – the gross weekly payment (married rate) of \$340.80 translates to an annual universal retirement benefit of \$2,800 with the application of the anchor tax rate of 33 percent. This is incorporated, separately from transfer benefits, into the public equity accounting schema, as an addition to a senior citizen's *public equity dividend*. The variable components of New Zealand Superannuation are treated as *transfer benefits*.

Reconceptualisation, New Zealand, Stage 3

Once the income-tax accounting method recognises income-tax graduation as an underlying benefit, then all income tax can be taxed at source, in both an accounting sense and in the PAYE sense that income taxes are collected from producers rather than from 'taxpayers'.

Table 6: Stage 3 Reform --- compare with Table 2

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		

Just as income and production are congruent – with the same macroeconomic symbol Y – a flat-rate income tax is identical to a flat-rate production tax. Further, by regarding the public domain as a factor of production (eg Simon 2000), then a single-rate income/production tax can be interpreted as a *public equity royalty* charge for the use of public domain resources. If such a charge is fully levied at source, then all other factor payments may be accounted for (and indeed

¹⁵ An obvious policy prescription, informed by public equity accounting, would be to prioritise the elimination of surcharge taxes over other forms of tax reductions.

distributed) as after-tax income. Table 6 shows a version of Table 2, with a revised name – *public equity royalty* – for 'income tax', and without any breakdowns between individuals and companies.

In this context, the concept of gross market income becomes redundant (a convenient fiction that ceases to be convenient when graduated tax rates disappear); all personal incomes are cited free of income tax (though not of surcharge taxes). This also makes the concept of *marginal tax rates* redundant, though not the concept of *effective marginal tax rates*.

Table 7: Stages of Reform, re an 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	42,580	42,580	42,580	42,580
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	43,580	43,580	43,580	43,580
Marginal tax rate		30.0%	33.0%	33.0%	0.0%
Effective Marginal tax rate		50.0%	50.0%	50.0%	25.4%

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
	Net income	40,580	40,580	40,580	40,580
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
	Net income	41,980	41,980	41,980	41,980
Marginal tax rate		30.0%	33.0%	33.0%	0.0%
Effective Marginal tax rate		30.0%	30.0%	30.0%	-4.5%

It means that persons who today would say they have annual market earnings of \$100,000 would come to say that they earn \$67,000. And persons who today would say they earn \$30,000 would come to say that they earn \$20,100 from the market. In addition, both would say that they receive *public equity dividends* of \$9,080. Further, depending on their individual circumstances, either may be receiving a *transfer benefit* or paying a *surcharge tax*. In an accounting sense, a *surcharge tax* is a negative *transfer benefit*.

As an example, Table 7 considers persons today grossing \$48,000 and each receiving transfer benefits of \$2,000 that abate at 20 cents in the gross dollar. If their gross incomes increase to \$50,000, then their transfer benefits would decrease by \$400 to \$1,600. And Table 8 considers persons today grossing \$48,000 and but receiving no transfer benefits.

Implications

All changes suggested here have been purely accounting changes; changes to the language of fiscal accounting. Most importantly, benefits disguised as tax exemptions and discounts are revealed as benefits that taper off as recipients' incomes decrease. By way of contrast, social security transfer benefits taper off when recipients' incomes increase. Accounting changes can expose this contradictory tapering. Accounting-informed policy changes can resolve this contradictory tapering.

Because the reforms suggested are all accounting reforms, there are no question marks over the affordability of the reforms, or of the possibility of unwanted labour supply effects. The reforms are no more than an application of common equity principles to fiscal accounting, thereby addressing the path-dependent – and only semi-coherent – procedures of the twentieth century.

Accounting is not an end in itself, however. 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 and some of the revealed subsidies.

Once 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 gains with economic citizens. Productivity gains imply capital-labour substitution, with a substantial and increasing proportion of societies' tangible and intangible capital belonging in the public domain. *Public equity dividends* and *royalties* could increase to reflect productivity gains,¹⁶ conservation priorities, and current account surpluses. Dividends could be held at lower levels in countries with poor (or crumbling) infrastructure, and countries with current account deficits.

Public equity fiscal accounting concepts can open-up new 'adjacent possible' (Johnson 2011)

¹⁶ However, the global 'race to the bottom' – rivalrous exporting, mercantilism in action (Rankin 2011b) – may be a major sticking point, impeding the growth of public equity royalties and dividends. This is arguably the real reason for the twenty-first century practice of discounting – subsidising – company taxation.

options in our thinking around income distribution. In turn, more imaginative thinking can further stimulate the evolutionary development of the policy contribution of public finance to addressing and resolving the inequality issues that have beset high productivity economies.

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Glossary

- Anchor rate of income tax:** the marginal rate of income tax that, under *path dependent fiscal accounting*, more than any other defines a country's income tax scale. In New Zealand this rate has been 33 percent since 1988. In developed market economies, this rate will normally be between 30 and 45 percent, and will be the marginal tax rate of most senior professionals such as managers, academics, and public servants.
- Actual rate of income tax:** the single or flat rate of income tax, as used in *public equity fiscal accounting*. It is derived from the *anchor rate of income tax*.
- Economic citizen;** for present accounting purposes, an economic citizen is a 'tax resident'.
- Graduated income taxation:** a set of stepwise marginal income tax rates, with lower marginal tax rates applied to lower earnings. It represents a form of *progressive taxation*.
- Graduation benefit:** the specific *tax benefit* that arises from some or all of one's income tax being levied at a rate lower than the *anchor rate*; the *public equity benefit*.
- Gross public revenue:** the sum of government revenue. In the public equity approach, the income tax component of public revenue is defined as the *actual rate of income tax* times gross domestic product (GDP).
- Progressive taxation:** Forms of taxation for which average tax incurred is proportionately higher for higher income earners.
- Path dependent fiscal accounting:** the traditional form of accounting for income tax using *graduated income taxation*.
- Public equity benefit:** a presently implicit benefit that arises from the graduation of income tax rates.
- Public equity dividend:** an equal entitlement, from public funds, to all *economic citizens*
- Public equity royalty:** an alternative name for income tax, when income tax is fully deducted at source, and accounted for as deducted prior to (or as a part of) the distribution of market incomes
- Public equity fiscal accounting:** the alternative (to *path dependent fiscal accounting*) form of fiscal accounting whereby an identified *anchor rate of income tax* becomes the *actual rate of income tax*.
- Social security benefits:** monetary transfers paid by a government agency other than the taxation authority.
- Surcharge tax** (public equity accounting Stage 2): a negative *transfer benefit*.
- Tax benefits:** benefits paid – often implicitly – as tax exemptions, allowances or graduations.
- Total benefits:** the sum of *transfer benefits* and *tax benefits*; in public equity accounting Stage 2, *tax benefits* are superseded by *public equity dividends*.

Transfer benefits (path dependent accounting):

money benefits paid as Social Security benefits, New Zealand Superannuation, Family Tax Credits, Accommodation Supplements, Student Allowances etc.

Transfer benefits (public equity accounting Stage 1):

money benefits to individuals that are not *tax benefits*.

Transfer benefits (public equity accounting Stage 2):

money benefits in excess of *public equity dividends* (net of *surcharge taxes*).

Universal superannuation (public equity accounting Stage 2):

the difference between the present universal component of New Zealand Superannuation (and reflecting its indexation) and the *public equity dividend*.

Appendix

Table A: Historical *Tax Benefits* in New Zealand 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

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