

The Introduction of Income Tax in New Zealand

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I INTRODUCTION

This article aims to explain the introduction of income tax in New Zealand. It examines the key people and relevant legislation at the time income tax was introduced, with a view to assessing the political and economic climate that caused this shift in taxation policy.

In the general elections before the introduction of New Zealand's first income tax in 1891, a plural voting system was employed in New Zealand, allowing men who owned or leased property in several different electorates to enrol and vote in each of them. The general taxation policy in New Zealand at the time protected the conservative interests of landowners. In 1891 this system was replaced by the principle of 'one man, one vote', which brought about a new liberal Premier¹, John Ballance, who addressed the House of Representatives in 1891 with a radical new idea for tax reform – a land and income tax.

Prior to the introduction of income tax, New Zealand had been in recession for over a decade, which had had a negative effect on land values. The fall in land values, in turn, had a detrimental effect on government revenue which had been heavily reliant on land tax and proceeds from the sale of public land. An alternative source of government revenue was needed, so a new tax was imposed on company, business and employment income.

An ordinary flat tax was placed on land. Based on the difficulties expressed in defining farming income, it appears that the flat land tax was used as a surrogate for the imposition of an income tax on farmers. A progressive tax was also imposed on land, which was intended to have the effect of breaking up large estates into smaller, more efficient units in order to realize the full benefit of refrigeration technology. Refrigeration meant that small farmers could raise sheep for meat and wool, paving the way for tax reform to allow settlement of people onto small farms. The Land and Income Assessment Act was passed in 1891.

II NEW ZEALAND POLITICAL AND LEGISLATIVE BACKGROUND

Political Background

Until the late nineteenth century, political parties did not exist in New Zealand. In the general election of 1890, "[t]he Premier, Harry Atkinson, and his rival, John

* BCom/LLB (Hons). Thank you Michael Littlewood for the many hours that you have invested into this paper, and for giving me the inspiration to write it. Thank you Autumn Grogan for proof reading this paper and for putting up with me during many a late night in front of nineteenth century Hansard.

¹ In colonial New Zealand, the terms Premier and Prime Minister were both used, but Premier was the more common and official title of the Head of Government.

Ballance,² led loosely organised teams, not parties, to the polls”.³ Rather than formally belonging to a political party, candidates pledged their support for the ministry or for the opposition. Because of these less formal ties, the concerns of the constituents in a candidate’s region would usually trump the general policies of the ministry or opposition.⁴

The ideology gap between the Government and the Opposition was slight. Both advanced economy, protection for colonial industries, and land settlement. They differed principally over the question of taxation.

During the second half of the nineteenth century, colonial New Zealand was largely funded by loans from England. These loans, primarily sourced to build infrastructure and fight against the Maori,⁵ were putting significant pressure on the government to table an income tax bill in order to stabilize public debt.

The New Zealand government toyed with the idea of an income tax for some time. In 1864 the Premier, Edward Stafford,⁶ moved to impose an income and property tax to meet the growing expenses of the “Native Rebellion”.⁷ He cited the £3 million loan from the United Kingdom taken to finance the rising costs of the Maori “rebellion” as just cause for an income and property tax. The magnitude of this growing debt was so extensive that “[b]y the mid-1870s New Zealand had borrowed heavily from London to pay for public infrastructure, per-capita more than any of the Australian Colonies. Direct taxation was inevitable”.⁸

Land Tax Act 1878

In 1878 the Grey Government acted on this pressure to meet growing debt, passing the Land Tax Act 1878. Although the Act did not incorporate an income tax, it did provide a surrogate at the time, as the economy was principally reliant on agriculture.

1 Why should New Zealand Introduce a Tax on Land?

Under the direction of Premier George Grey,⁹ Colonial Treasurer John Ballance

² John Ballance (1839-1893) was born in Ireland. He immigrated to New Zealand in 1866, and established the *Evening Herald*. In 1875 he entered parliament, winning the Rangitikei seat. He joined George Grey's Ministry in 1878 and later became Colonial Treasurer. He introduced the Land Tax Act 1878, and after forming New Zealand's first liberal government in 1891, he introduced the Land and Income Assessment Act 1891, which forms the basis of this paper. (McIvor, “Ballance, John 1839 – 1893” *Dictionary of New Zealand Biography*, <<http://www.dnzb.govt.nz/dnzb/>> (at 27 August 2006)).

³ Richardson *The Oxford History of New Zealand: Parties and Political Change* (2 ed, 1992) 202.

⁴ *Ibid.*

⁵ Driven by the confiscation of Maori land by the Crown.

⁶ Edward Stafford (1819-1901) was born in Edinburgh, Scotland, moving to New Zealand in 1843. At the 1855 election he became a member of the House of Representatives for Nelson. He was Premier on three different occasions from 1856 to 1872 and remained an MP until 1878. (Bohan, “Stafford, Edward William 1819 – 1901” *Dictionary of New Zealand Biography*, <<http://www.dnzb.govt.nz/dnzb/>> (at 27 August 2006)).

⁷ (13 December 1864) 1864-1866 NZPD 182-183 (Edward W Stafford).

⁸ Harris, *Metamorphosis of the Australasian Income Tax 1866 to 1922* (2002) ch 3, 46.

⁹ Grey (1812-1898) was born in Lisbon Portugal and was Governor of South Australia in 1841. He arrived in New Zealand in 1845, assuming office as Governor and was knighted shortly after. In 1877 he became Premier. (“Sinclair, “Grey, George 1812 – 1898” *Dictionary of New Zealand Biography*, <<http://www.dnzb.govt.nz/dnzb/>> (at 27 August 2006)).

delivered an address to the House of Representatives, calling for the introduction of direct taxation for the following reasons:¹⁰

- a. to meet the growing burden of interest due on foreign loans (well in excess of £UK1 million per year);
- b. it was fitting that landowners, who derived a permanent benefit from the new railways and roads (causing an increase in the value of land), should be directly contributing to the colony's revenue; and
- c. with a liberal immigration policy in place, the population of the colony was growing rapidly,¹¹ contributing to the rising value of land. This general policy was likely to continue, thus landowners, who gained a significant benefit from immigration policy, should contribute to the revenue of the colony.

With the introduction of direct taxation, Ballance proposed "to extend the taxable basis, with the double object of establishing more firmly the finance and credit of the colony, and of fairly adjusting the fiscal burdens according to the capacity of the different classes to bear them."¹²

2 *Land Minus Improvements*

An important aspect of Ballance's proposal was that tax was to be imposed on land *minus* improvements. This qualification served two primary purposes. First, it did not penalize industry and entrepreneurial behaviour by taxing capital investment in land. Capital investment was vital to the new and developing New Zealand colony. Secondly, Ballance sought to discourage speculation. When neighbouring land was developed by the government¹³ or through the efforts of neighbouring farmers, the value of speculators' land would increase through these efforts: "By exempting improvements we award a premium to industry, and discourage a system of speculation which thrives only upon the labour of others."¹⁴

3 *Introducing the Land Tax*

The Grey Government opted for the tax to be calculated by reference to triennial valuations. In the Government's view, the primary benefit of this method was that any increase in land value, often a result of expenditure on infrastructure, would see a corresponding increase in tax revenue. This would also ensure that those who were receiving the greatest benefit from the colony's infrastructural developments would incur a corresponding increase in their liability for tax.

Looking to England for guidance, the Government elected to exempt land below a certain value. This was initially set at £500, so that "the settler commencing

¹⁰ (6 August 1878) 28 NZPD 90 (John Ballance).

¹¹ In the seven years from 1874 to 1881 the population of the New Zealand colony grew from 344,984 to 534,030 (55% increase). (*General Info Working Class* (2003) The People's Embassy <<http://www.embassy.org.nz/encycl/nz.htm>> (at 28 November 2004)).

¹² *Supra* note 10.

¹³ For example road, rail, amenities and lines of communication.

¹⁴ *Supra* note 10.

with small means is left unburdened until, in making a start in life, he rises above his difficulties...”¹⁵

Income Tax Bill 1879

In the year following the Land Tax Act 1878 there was a significant drop in the amount of Crown land sold. One reason was that large portions of land located near planned railroads were set aside from sale.¹⁶ The new government policy was to wait until after construction before selling land, in order to attain the greatest financial benefit from the increased value of land near a railway line. Secondly, the Governor¹⁷ at the time, George Augustus Constantine, identified the drop in Crown land sales as being a result of a worldwide commercial depression.¹⁸

In his Governor’s Speech on 16 July 1879, Constantine said that this depression was set to continue, rendering it necessary to look to other sources of tax revenue to ensure stability of the colony’s revenue. He discussed the proposal to introduce an income tax to sit alongside the existing regime. In addition to stabilizing the government’s finances, an income tax would help equalize the incidence of taxation by removing the primary burden of taxation from landowners.

The Bill did not get any further than the first reading in the House of Representatives. *The New Zealand Herald* was scathing of the proposals, pointing to the administrative difficulties of collecting an income tax across a country with so sparse a population. The *Herald* preferred the adoption of a broad-based property tax, which would be, it said, easier to collect and assess, based on information obtained from municipal councils. A vote of no confidence was passed shortly after the Bill received its first reading,¹⁹ and the Governor was forced to dissolve Parliament and order a re-election.²⁰

Property Assessment Act 1879 (The 1879 NZ Act)

The re-election brought about a change of government and a renewed interest in tax reform. Harry Atkinson²¹ was the new Colonial Treasurer and he delivered his first Financial Statement to the House on 17 November 1879. Atkinson dismissed the idea of an income tax as inquisitory and inequitable.²² Furthermore, the administrative realities of managing an income tax were seen as elaborate and expensive. He moved that a broad-based property tax be introduced into the House. This proposal took the form of two Acts that would sit alongside one another. The Property Assessment Act

¹⁵ Ibid 91.

¹⁶ (15 July 1879) 31 NZPD 6 (Governor George Augustus Constantine)

¹⁷ This title was upgraded to Governor-General in 1917, although by the 1860s the Governor had largely become a symbolic figurehead. (“Governor and Governor-General” (2004) NZHistory.net.nz <<http://www.nzhistory.net.nz/Gallery/parlt-hist/parlt-govt.html>> (at November 2004)).

¹⁸ Supra note 16.

¹⁹ (29 July 1879) 31 NZPD 304.

²⁰ (29 July 1879) 31 NZPD 304 (Governor George Augustus Constantine) in Harris, supra note 8, 51.

²¹ Harry Albert Atkinson (1831 - 1892) was born in England, immigrating to New Zealand in 1853. Atkinson was elected a member of the House of Representatives in 1861. In 1864 he became Minister for Colonial Defence. Atkinson was Colonial Treasurer for 10 years between 1875 and 1891, through most of the worst years of the depression. He was Premier twice during the 1880’s, eventually being defeated by the liberal John Ballance. (Bassett, “Atkinson, Harry Albert 1831 – 1892” *Dictionary of New Zealand Biography*, <<http://www.dnzb.govt.nz/dnzb/>> (at 27 August 2006)).

²² (17 November 1879) 33 NZPD 298 (Harry Atkinson).

1879 was to contain the machinery and it would be accompanied by an annual rates Act. This would allow rates of tax to be set by reference to the government's requirements at the time.

Atkinson said there was no reason why hardworking settlers involved in agriculture should bear a burden any greater than those holding wealth in the form of mortgages, bank shares and other forms of property. The proposal before the House took the form of a broad-based property tax, where no distinction was drawn between land and other forms of property. All realized forms of wealth were regarded as suitable measures with which to evaluate a taxpayer's ability to contribute to the colony's revenue. Atkinson then addressed the major reasons why the Grey Government had passed the Land Tax Act 1878 and why he believed these reasons were unsatisfactory.

First, the land tax was introduced to raise revenue. In response to this, he explained how this tax policy contradicted pro-settlement ideologies. The government had 26 million acres of land for sale in order to promote settlement in the colony but as the Land Tax Act imposed special burdens on those with land, it effectively defeated this object of promoting settlement.

Secondly, the land tax sought to encourage large landowners to break up their land, penalizing those who held their land for speculative purposes. Atkinson queried why the government would tax a special class of people, whose hard work was necessary for the development of the colony, in order to prevent abuse by a few. Here, Atkinson's reasoning is not especially convincing, and he failed to accurately consider earlier analysis in the House. For example, Ballance sought to discourage speculation because speculators were benefiting from the hard work of others.²³

Atkinson then explained his preference for the New York property tax model.²⁴ This involved taxing residents of the colony on all property, real or personal, subject to certain deductions. Using this model, Atkinson discussed the Government's proposal, choosing to adopt the American model, but exempting the first £300 pounds of property owned. By the time the Bill was passed into law, the exemption was raised to the first £500 of one's property. Although highly unpopular,²⁵ broad-based property taxes remained as the New Zealand government's primary source of income for the following decade.

III LAND AND INCOME ASSESMENT ACT 1891 – THE DEBATE

Introduction

On 24 January 1891, John Ballance was appointed Premier and Colonial Treasurer, leading a period of liberal reform that continued until 1912, well after he left office.²⁶ During this time in office, the organized liberal "team" came to form New Zealand's first official political party – the Liberal Party.

After Ballance was called on to form a Ministry, Atkinson resigned from the House, opting to finish his political career on the Legislative Council. At the same

²³ See text at note 14 *supra*.

²⁴ *Supra* note 22, 299.

²⁵ *Supra* note 8, 108.

²⁶ John Ballance remained as Premier for over two years until, on 27 April 1893, he died in office. (McIvor, *supra* note 2).

general election, the long-time political figure John Bryce²⁷ was favoured by conservatives as a suitable replacement for Harry Atkinson. As leader of the Opposition, Bryce was vocal in his discontent with the Liberal-driven Land and Income Assessment Bill.²⁸

The Financial Statement: June 16 1891

In his role as Colonial Treasurer, Ballance addressed the House of Representatives on 16 June 1891. During this address, he proposed to overhaul the broad-based property tax system, and introduce a land and income tax instead. This proposal eventually led to the first income tax in New Zealand, which survives as the primary form of taxation in force today. The Bill was primarily devoted to procedure and the method of imposing tax, and was to be followed by a supplementary Bill detailing the rates of tax.

1 The Case to Reintroduce Land Tax

In his opening address on the incidence of taxation, Ballance defined the scope of the land tax as tax on the value of land, less improvements,²⁹ explaining that taxation on improvements penalized industry and entrepreneurial behaviour. This was reminiscent of Ballance's 1878 proposals under the Grey Government, to introduce a tax on land minus improvements.³⁰

Despite these strong words, Ballance asserted that taxation of improvements was required by the government's finances. He indicated a preference to tax improvements to meet finances, rather than increasing the rates of tax through customs, which would be borne by those purchasing the necessities of life. These words were spoken amid tight financial times, with the previous Atkinson Government seeing out the worst years of the depression. It was probably this that led Ballance to exercise caution, and not rule out taxation on improvements altogether, despite his opposition in principle to this form of taxation. Ballance then announced his initial proposal:³¹

We propose to introduce a Bill to abolish the property-tax, and to provide for a land- and income-tax, and in respect of the land-tax to grant an exemption on improvements up to the value of £3,000 for each owner, and also to impose a graduated tax upon all persons and companies the value of whose land, less £3,000 for improvements, shall amount to £5,000...[i]n addition to the deduction for improvements there will be the exemption of £500 from an owner's land...[and] in the assessment of the tax an owner will be allowed to deduct from his land the amount of any mortgages.

²⁷ John Bryce (1833 – 1913) was born in Scotland, immigrating to Wellington, New Zealand in 1840. Bryce entered local politics in 1859 and was elected to the Wellington Provincial Council in 1862. He was Minister for Native Affairs. In 1890, he took the Waikato seat, and was briefly leader of the Opposition representing conservative rural interests. Amid great controversy he resigned his seat when he refused to withdraw words critical of Ballance. (Riseborough, "Bryce, John 1833 – 1913" *Dictionary of New Zealand Biography*, <<http://www.dnzb.govt.nz/dnzb/>> (at 27 August 2003)).

²⁸ *Ibid.*

²⁹ (16 June 1891) 71 NZPD 65 (Premier John Ballance).

³⁰ See text at notes 13 and 14, *supra*.

³¹ *Supra* note 29.

Below is a formula, constructed to illustrate how Ballance anticipated the *ordinary* tax would work:

$$\text{Taxable Land Value} = \text{Capital Land Value} - \text{Improvements (up to } \pounds 3000) - \text{Mortgage}$$

Using this formula, an owner would pay 1d in the pound sterling³² in land tax (0.42%) on the capital value of the land, subject to an exemption for the first £500 pounds

The formula and table below illustrate how the *graduated* tax was to apply to holders of more valuable estates, payable on the capital value of the land. Under the graduated tax regime, a landowner was not entitled to deduct the value of any mortgage.

$$\text{Taxable Land Value} = \text{Capital Land Value} - \text{Improvements (up to } \pounds 3000)$$

Total taxable land value		Graduated Tax	Graduated Tax Rate
£5,000 -	£10,000	$\frac{1}{8}$ d	0.05%
£10,000 -	£20,000	$\frac{2}{8}$ d	0.10%
£20,000 -	£50,000	$\frac{3}{8}$ d	0.15%
£50,000 -	£100,000	$\frac{4}{8}$ d	0.21%
£100,000	+	$\frac{5}{8}$ d	0.26%

The following three examples illustrate how Ballance intended this tax to work.

1. A farmer owns land valued at £800, including improvements valued at £300. His taxable land value using the formula above would be:

$$\text{Taxable Land Value} = \pounds 800 - (\pounds 300 \text{ (up to a maximum of } \pounds 3,000))$$

$$\text{Taxable Land Value} = \pounds 500$$

After the allowable exemption of up to £500 is taken from this taxable land value, this taxpayer would have no liability to pay land tax on this property.

2. A farmer owns land valued at £1,200, including improvements worth £400. His taxable land value would be:

$$\text{Taxable Land Value} = \pounds 1,200 - (\pounds 400 - (\text{up to a maximum of } \pounds 3,000))$$

$$\text{Taxable Land Value} = \pounds 800$$

Using the table above, this taxpayer would pay the ordinary land tax at 1d in the pound (0.42%) and only on the £300 of his taxable land value which is above the £500 exemption (i.e. no graduated tax).

3. A farmer owns land valued at £22,000, including improvements worth £8,000. His taxable land value for the ordinary land tax would be:

$$\text{Taxable land value} = \pounds 22,000 - (\text{up to } \pounds 3,000)$$

$$\text{Taxable land value} = \pounds 19,000 \text{ (liable at 0.42\% above the } \pounds 500 \text{ exemption (i.e. } \pounds 18,500 \times 0.42\%))$$

His taxable land value for the graduated tax would be:

$$\text{Taxable land value} = \pounds 22,000 - (\text{up to } \pounds 3,000)$$

$$\text{Taxable land value} = \pounds 19,000$$

Using the table above, the farmer's marginal rate of graduated tax is 0.1%.

Ballance estimated these taxes would raise £266,847 per annum.³³

³² British Sterling was used until 1933 when New Zealand adopted its own currency.

³³ (16 June 1891) Vol 71 NZPD 67 (Premier John Ballance).

2 The Case to Introduce an Income Tax

In 1879, Atkinson had said that income taxes were unavoidably open to great inequalities. He claimed that this formed part of his decision to opt instead for a broad-based property tax.³⁴ In his Financial Address in 1891 Ballance used these same grounds to strike down the Property Tax Act 1879, calling it “grossly unjust in its operation, imposing without discrimination burdens on capital whether productive or unproductive, and discouraging industry”.³⁵

The income tax proposal tabled by John Ballance dealt separately with: (a) corporate profits; (b) profits of unincorporated firms; and (c) income from professions and employment.

First, an income tax was to be imposed on the profits and debentures of companies, omitting profits from land and mortgages over land. Ballance did not propose to allow companies an exemption for the first portion of income earned. The proposed tax rate was to be a low one at five percent,³⁶ not penalizing developing corporations, while ensuring that more profitable companies contributed a proportionately greater share of the tax burden. In delivering his initial proposal to the House, Ballance estimated that the company tax would raise £47,300.

Secondly, Ballance proposed to impose a tax on income derived from trade and commerce. The effect of this would be to extend the tax to cover merchants, recognising that agriculture was no longer the only major source of revenue in New Zealand. Ballance proposed that individual profits obtained via trade and commerce be afforded an exemption of up to £150. The proposed rate of income tax on trade and commerce was one shilling in every pound sterling, or five percent. Ballance estimated that this would raise approximately £40,000.

Finally, Ballance proposed to tax income derived from a profession or from a salary. Exemptions were more generous for professional and salary income-earners, exempting from tax those who earned professional or salary income below £300. Ballance proposed a progressive tax rate, which had the following effect:

Income		Marginal tax rate
£0 -	£300	Exempt
£300 -	£500	3 d per pound (1.25%)
£500	+	6 d per pound (2.5%)

The income tax on professional income and salaries was projected to raise £15,000.

The House of Representatives

1 The Origins of the Bill

The Bill had its origin in two pieces of legislation. First, in the income tax legislation in South Australia, which was used as a guide in developing appropriate income tax

³⁴ Supra note 22.

³⁵ Supra note 29, 66.

³⁶ One shilling in the pound.

legislation in New Zealand; and secondly, in New Zealand's Property Assessment Act, which prevailed at the time.³⁷

Ballance also copied provisions from the English income tax acts compelling secrecy in matters relating to the assessments of income. He stressed, however, that these provisions would only apply to income tax assessment. Although assessments in relation to land were not to be publicly disclosed, no secrecy requirement was imposed on the government in relation to land assessments.³⁸

2 John Ballance Moves for a Second Reading: The Land Tax

In the initial drafting of the Bill, Ballance proposed to use triennial assessments of the value of a taxpayer's land.³⁹ The South Australian approach did not use periodical land assessments, rather land value was regularly adjusted and an inspector was appointed for this purpose. While this was much cheaper than carrying out periodic valuations, the accuracy of this method had been questioned. Unless the concerns regarding accuracy could be corrected, Ballance preferred to adopt an approach that utilized periodic assessments, until the government became more experienced in this matter.

These triennial assessments would be overseen by the Board of Review, which was created under the Property-Assessment Act 1879. In previous debate, objections had been raised as to the detachment of this Board. The men who sat on the Board came from a class of people who had large land holdings, and who had a personal interest in low valuations of large estates, as this would produce a lower liability for tax.⁴⁰ Ballance tabled a suggestion to ensure the government maintained the integrity of the tax base. Where owners of land refused to accept the value placed on their land for the purposes of taxation, the government would have the power to purchase their land at that valuation plus ten percent. This way, landowners would be hesitant to debate their respective valuations unless their land actually was significantly overvalued.⁴¹

Ballance then identified that under the Property-Assessment Act, many deserving and hardworking people were burdened with an unfair proportion of tax liability. Ballance's solution to this problem was to give the Commissioner an unusually wide discretion. Where age or ill-health affected a landholder's or mortgage-holder's ability to earn an income above £120, the Commissioner was given discretion to increase the taxpayer's exemption to tax from £500 up to £2,000, if the Commissioner was satisfied that the payment of tax in full would entail hardship on such owner.⁴²

In response to suggestions made by members of the House, it was proposed that the graduated tax not be imposed on improvements, rather that it be imposed only on the unimproved value of the land. This would lower the effective rate of taxation on those settlers who had improved their land and increase the proportionate burden on speculators who had not done so:⁴³

³⁷ (4 August 1891) 73 NZPD 96 (Premier John Ballance).

³⁸ *Ibid.*

³⁹ *Ibid.* 97.

⁴⁰ *Ibid.*

⁴¹ *Ibid.*

⁴² *Ibid.* 98.

⁴³ *Ibid.* 99.

[A]s between the man who is a great improver and the man with a large estate who does not improve his land, or does not improve it to any great extent, the tax is perfectly just; and it has a tendency, and must have a tendency, to cause the holders of large quantities of land which are held for purposes of speculation – it must have a tendency to force these men to cut up their estates.

Ballance thus had an ulterior motive. In addition to securing the colony's finances, he wanted to see the end of speculation and force speculators to "assist the Government in the great work of colonisation"⁴⁴ to renew prosperity in New Zealand.

All the regional Chambers of Commerce situated throughout the country opposed Ballance's proposal, in particular, the Auckland Chamber of Commerce, who voiced their opinions regarding the Bill directly to John Ballance in a telegram. In the telegram the Chamber expressed its disquiet with the graduated taxation, and the £500 exemption offered.⁴⁵ The conservative motives of the Auckland Chamber of Commerce were clear, with the graduated tax and £500 exemption moving the burden of taxation from the poorer landowners to those with large estates.

3 John Ballance Moves for a Second Reading: The Income Tax

Ballance commenced his discussion of the proposed income tax by briefly dealing with taxation of the income of banks and other corporations. The existing legislation⁴⁶ did not specifically provide for the taxation of banks. Peculiarly, the banks paid taxation based on a gentlemen's agreement with the Colonial Treasurer. The banks approximated what they believed to be fair and paid tax on this basis. Ballance proposed to charge tax on the banks' annual incomes. Building companies and investment societies were to be treated in a like manner.

Under the Property-Assessment Act 1885, all companies, irrespective of size, were liable to pay tax on all of their capital. Ballance emotively labelled this an act of confiscation. Under the Land and Income Assessment Bill, a new company would no longer have to struggle to meet burdensome tax bills while not making a profit: "We do not ask them to pay a single penny until they have begun to earn money, and then we only ask them to pay income-tax upon their profits at the end of the year."⁴⁷

Ballance noted the distinction between (a) trade and commerce, and (b) professional incomes, proposing differing tax treatment with respect to each. The distinction he drew was that trade and commerce did not rely on the continuing health of one individual. If the head of a firm were to pass away, in most cases the firm would continue to run and make an income.⁴⁸ By contrast, if a professional's health deteriorated (or he or she passed away), his or her professional income would be affected accordingly. It was for this reason that Ballance maintained that each form of income should have separate tax treatment.⁴⁹

Ballance invited response from the floor as he closed his speech and moved the second reading of the Land and Income Assessment Bill. John Bryce was prompt to voice his disapproval of the Bill.

⁴⁴ Ibid 99.

⁴⁵ Ibid 101.

⁴⁶ Property Assessment Act 1885.

⁴⁷ Supra note 37, 100.

⁴⁸ He explained that this was primarily with reference to larger firms in which money was invested, however, this reasoning does not necessarily apply to sole traders who earn income through trade and commerce.

⁴⁹ Supra note 37, 100-101.

4 John Bryce Voices Concern

(a) Bryce on the Land Tax

Influenced by conservative rural interests, Bryce spoke out against the anti-avoidance provision that allowed the government to purchase people's land at its respective valuation plus ten percent. There were various ways in which the Commissioner could enforce this clause. As the potential injury to property owners was significant, Bryce indicated that the provision needed to be strict, given that it relied on the will of the Commissioner. If the Commissioner were to exercise his⁵⁰ power in such a manner as to make the Act "irksome and obnoxious...he may bring the Act into disrepute".⁵¹

Bryce then made reference to the proviso contained in the first schedule of the Act, which provided that the draining and clearing of land and laying of grass were only to receive status as an improvement for a ten year period. He said that it was unjust to presume that at the end of ten years the principal cost of these activities would be recovered, preferring to adopt a time period of thirty-three years that approximated the length of a generation.⁵²

Bryce went on to criticize the tax exemption for improvements. He spoke of an injustice where a hypothetical "good colonising settler"⁵³ who had spent £30,000 on improvements, would be taxed for doing his duty over and above a fellow settler who had spent no money on improvements.⁵⁴ Ballance and Bryce agreed in principle on this point, but Ballance felt that the need to secure government revenue was of greater concern. Bryce believed that in addition to penalizing "good colonising settlers" for making improvements, this form of taxation would prevent further improvements being made.⁵⁵

Bryce then condemned the graduated land tax's aim of breaking up large estates. He considered that this purpose unjustly inflicted punishment on large land holders.⁵⁶ Some years earlier landowners had purchased blocks of land from the Crown. Bryce questioned the justice of the state inferring that such purchasers have "committed a crime because [they] hold land that we sold to [them]".⁵⁷ Here, Bryce was visibly advocating the conservative interests of the Opposition.

(b) Bryce on the Income Tax

Having dealt with a number of his concerns with the land tax, Bryce then turned to the income tax. His primary concern was the "vice that it infuses into the community".⁵⁸ He made reference to the magnitude of false declarations in England. Not only did this include dishonest members of society, who had deliberately withheld details of

⁵⁰ The use of the word 'his' or any derivative of it is not intended as sexist language. It would be misleading to use an alternative as the Commissioner and almost all landowners in 1891 were male.

⁵¹ *Supra* note 37, 102 (John Bryce).

⁵² *Ibid* 103 (John Bryce).

⁵³ This term was used by members of the House to describe settlers who went about improving their land.

⁵⁴ *Ibid* 105 (John Bryce).

⁵⁵ *Ibid*.

⁵⁶ *Ibid* 106 (John Bryce).

⁵⁷ *Ibid*.

⁵⁸ *Ibid* 104 (John Bryce).

their income, but also many honest citizens had also found it difficult to ascertain exactly what their income was.⁵⁹

According to Bryce, a man with every honest intention may try to state his income, but he would find great difficulty in saying what that income actually was. With over a century of experience, the government still struggles to define income, providing no definition in the Income Tax Act 2004. It is, therefore, of no surprise that the leader of the Opposition during New Zealand's first attempt at income tax also had difficulty with this concept.⁶⁰

If, then, a man who honestly tries to make a true return of his income finds such a difficulty in doing so, what opportunities must be given to those who are not honestly inclined, and who desire to evade tax?

Ballance had looked to follow the English Income-tax Acts in compelling secrecy in respect of the assessment of incomes.⁶¹ Bryce accepted Ballance's observations on the English system, but noted the alternative approach taken in the United States. Rather than compelling secrecy, the Americans required public disclosure of tax matters, so as to cure corruption by effectively making one's neighbour a detective. Bryce advocated that much was to be said for this approach given the "beneficial result of securing the law in question from being viciously abused".⁶² Despite this, the idea of making tax matters public in England was deemed repugnant to the feelings of the people of England, and therefore the Ballance Ministry chose to take the same approach to secrecy in New Zealand.

Bryce also expressed concern with the amount of discretion that the Land and Income Assessment Bill 1891 afforded the Commissioner to alter a taxpayer's liability to tax in certain circumstances in order to prevent injustices. Bryce maintained that the level of suspicion to which the Commissioner would subsequently be subject would interfere with his functions.⁶³

IV LAND AND INCOME ASSESSMENT ACT – THE ACT

Introduction

The Land and Income Assessment Act 1891 is a 23 page Act consisting of 48 sections and six schedules. Ballance explained the basic structure of the Act as based on New Zealand's Property Assessment Act 1885⁶⁴ and the South Australian Taxation Act 1884.⁶⁵

[T]he body of the Bill, as far as possible, consists of machinery which we consider applicable, and which we have derived to some extent from the legislation upon the subject of the income-tax in South Australia, where the tax has been in operation for some time, and has worked very satisfactorily, and to some extent from the Property-assessment Act prevailing in this colony.

⁵⁹ Ibid 106 (John Bryce).

⁶⁰ Ibid 104 (John Bryce).

⁶¹ Ibid 96 (Premier John Ballance). See text at note 38 supra.

⁶² Ibid 101 (John Bryce).

⁶³ Ibid 102 (John Bryce).

⁶⁴ 1879 and later consolidated as the Property Assessment Act 1885.

⁶⁵ Supra note 37, 96 (Premier John Ballance).

The Act was divided into five parts, each briefly discussed below. Part II (in conjunction with the schedules to the Act), which contained the charging provision and general exemptions from tax, is examined in greater detail, because it determined what was taxable and at what rate.

Although the Act was passed in 1891, no tax was collected in that year. The Act was instead used to make assessments so that tax could be levied in 1892. On 8 October 1892 the Land-tax and Income-tax Act was passed.

Part I: Administration of the Act.

A Commissioner of Taxes and his Deputy were appointed⁶⁶ to carry out general official duties under the Act.⁶⁷ The appointment of other assessors, clerks and receivers to assist in the administration of the Act was also provided for.⁶⁸ Those appointed under the Act were required to take an oath of fidelity and secrecy.⁶⁹ The Governor in Council was permitted to make regulations consistent with the Act which would have the force of law.⁷⁰ Companies were required to appoint a representative to be their “public officer,” who would be answerable to the Commissioner of Taxes for matters in relation to his company’s respective obligations under the Act.⁷¹ Finally, agents and trustees of taxpayers who were permanently or temporarily absent from New Zealand were answerable to the Commissioner of Taxes for matters relating to the assessment of land, mortgages or income which the agent or trustee represented.⁷²

Part II and the Schedules: Nature of the taxation

Section 15 was the charging section, and in conjunction with schedules A through F determined what was taxable and by how much. The ordinary tax on land was provided for by Schedule A and the graduated tax by Schedule B. Schedules C, D, and E dealt with income from companies, businesses and employment respectively. Finally, Schedule F contained some miscellaneous rules regarding the assessment of income.

1 The Land Tax

Schedule A was divided into two parts. The first contained provisions relating to the ordinary tax on land, and the second related to the tax on mortgages.

(a) Schedule A: The Ordinary Tax on Land

The first part of Schedule A imposed a tax on every person and company that was an owner of land.⁷³ The amount of tax was set at one penny in the pound under the

⁶⁶ Land and Income Assessment Act 1891, s 4.

⁶⁷ *Ibid* ss 5 and 6.

⁶⁸ *Ibid* s 7.

⁶⁹ *Ibid* ss 8 and 9.

⁷⁰ *Ibid* ss 10 and 11.

⁷¹ *Ibid* s 13.

⁷² *Ibid* s 14.

⁷³ *Ibid* sch A, art 1, r 1.

Land-tax and Income-tax Act 1892⁷⁴ (0.42%). This tax was to be levied upon the capital value of the land for which the fee simple of land with all improvements could be purchased for cash,⁷⁵ but for a deduction of up to £3000 for any improvements. If a landowner had more than one holding of land, he would only be able to receive a maximum combined exemption of £3000. Furthermore, landowners could make a deduction for any mortgages they had on the land. Despite Parliamentary debate on this matter, this provision had substantially the same effect as the ordinary tax on land proposed by Ballance in his Financial Statement on 16 June 1891.

One notable change since Ballance's Financial Statement on 16 June 1891, was the effect of the £500 exemption from taxation. Under Ballance's original proposal, a single £500 exemption was to be granted for each landowner for all the land that he owned. Under Schedule A, however, the effect of this exemption was somewhat limited. Rule 2 provided that once a landowner had been assessed for tax based on all of his land holdings (less allowable exemptions for improvements and mortgages), he would only be entitled to an additional exemption of £500 if the assessed amount of the property did not exceed £1,500. The amount of this £500 exemption diminished by £1 for every £2 that the assessed value of the property increased so as to leave no exemption on assessed values of more than £2,500.⁷⁶ The following example illustrates the effect of the exemption under Schedule A:

John has two properties. Together they are valued at £4,500 (including £1,000 of improvements). There is a £1,500 mortgage over one of the properties. The assessed value of John's property for the purposes of tax would be:

	£4,500 (total value of the properties)
(less)	£1,000 (deduction for improvements allowed up to a maximum of £3000)
(less)	£1,500 (deduction for the value of mortgage still owing on the land)
	<u>£2,000</u> (assessed value of John's land subject to allowable deduction under rule 2)

Under rule 2 a £500 exemption would be allowed if the assessed value of John's land was £1,500 or less. However, the amount of this exemption diminished by £1 for every £2 that the assessed value of the property was above £1,500. In John's case the assessed value is £500 above £1,500, therefore the allowable exemption is reduced by £250. Taking this additional £250 exemption into account, John would be assessed to tax based on £1,750.

Rule 2 contained a proviso, affording to the Commissioner of Taxes a discretion to increase a taxpayer's exemption from £500 up to a maximum of £2,000 where age or ill-health affected a land or mortgage holder's ability to earn an annual income above £120⁷⁷ if the Commissioner was satisfied that the payment of tax in full would entail hardship on the owner. Despite strong argument by John Bryce that such a provision would foster a climate of suspicion and thus interfere with the

⁷⁴ Land-tax and Income-tax Act 1892, s 2(1). The section imposed land tax "[f]or every pound sterling of the actual value of land and mortgages on land of which any person or company is the owner or the mortgagee and chargeable under schedule A of the 'Land and Income Assessment Act, 1891' a duty, by way of land tax of one penny."

⁷⁵ Supra note 66, sch A, art 1, r 1.

⁷⁶ Ibid r 2.

⁷⁷ Increased to £200 under the Land and Income Assessment Act Amendment 1892.

Commissioner's functions,⁷⁸ the provision remained unchanged from its introduction into the House by Ballance.⁷⁹

Rule 4 briefly dealt with how leasehold land was to be taxed. The leasehold was to be assessed to tax based upon the value of the leaseholder's interest in such land. Deductions of £3000 for improvements were to be apportioned between the leaseholder and owner in fee in relation to their respective interests in those improvements. The mechanics of this were to be provided by regulations.

Finally, rule 6 provided that occupiers of land for mining purposes were exempt from tax on this land, as they were liable for business income tax.

(b) Schedule A: The Tax on Mortgages

The second part of Schedule A provided for the effect that the ordinary land tax had on mortgages. Mortgagees were liable for taxation with respect to the mortgages they held, in the same way that landowners were assessed.⁸⁰ There was a notable proviso applying to mortgages held by companies registered in New Zealand whose sole or principle business was a loan, building, or investment company, and whose head office and management were situated and conducted in New Zealand.⁸¹ Companies fitting this description were effectively exempt from the land tax as they were liable to pay tax on their income under Schedule C. The purpose of this provision was to avoid double taxation, by preventing companies in the business of lending from being liable both for land tax on their mortgage interests and income tax on the profit from these interests.

(c) Schedule B: The Graduated Tax on Land

The graduated tax was introduced to encourage holders of large estates, in particular those holding land for speculative purposes, to break up their land. This was the first example of progressive taxation in Australasia.⁸² The scope of the graduated tax was different from the scope of the ordinary tax on land in Schedule A.

The graduated tax was assessed and levied on the amount of the assessed value of the land less all improvements, in accordance with Ballance's preference not to punish settlers who went about improving their land. As opposed to the ordinary tax on land, the graduated tax did not allow for any deduction in respect of any mortgage over land. Mortgagees who were liable to pay the ordinary land tax on their mortgage interests were relieved from liability to pay the graduated tax on those interests.⁸³ Given that a principal purpose of the graduated tax was to encourage taxpayers to break up their land, there would have been little point in subjecting mortgagees to the same onerous graduated tax.

⁷⁸ *Supra* note 37, 102 (John Bryce).

⁷⁹ *Ibid* 98 (Premier John Ballance).

⁸⁰ *Supra* note 66, sch A, art 2, r 1.

⁸¹ *Ibid*.

⁸² *Supra* note 8, 111.

⁸³ *Supra* note 66, sch A, art 2, r 3.

In addition to the ordinary tax on land detailed in Schedule A, the Act imposed the following *further* graduated annual taxes on land:

Total taxable land value		Graduated Tax	Graduated Tax Rate	Rate for Absentees
£5,000 -	£10,000	$\frac{1}{8}$ d	0.05%	0.06%
£10,000 -	£20,000	$\frac{2}{8}$ d	0.10%	0.12%
£20,000 -	£30,000	$\frac{3}{8}$ d	0.15%	0.19%
£30,000 -	£40,000	$\frac{4}{8}$ d	0.21%	0.25%
£40,000 -	£50,000	$\frac{5}{8}$ d	0.26%	0.31%
£50,000 -	£70,000	$\frac{6}{8}$ d	0.31%	0.37%
£70,000 -	£90,000	$\frac{7}{8}$ d	0.36%	0.44%
£90,000 -	£110,000	1 d	0.42%	0.50%
£110,000 -	£130,000	$1\frac{1}{8}$ d	0.47%	0.56%
£130,000 -	£150,000	$1\frac{2}{8}$ d	0.52%	0.62%
£150,000 -	£170,000	$1\frac{3}{8}$ d	0.57%	0.68%
£170,000 -	£190,000	$1\frac{4}{8}$ d	0.62%	0.75%
£190,000 -	£210,000	$1\frac{5}{8}$ d	0.68%	0.81%
£210,000 +		$1\frac{6}{8}$ d	0.73%	0.87%

Finally, in order to hinder foreign attempts to hold large blocks of land for speculative purposes, the graduated tax was even more severe for those who had been absent from, or resident out, of the colony for a period of three years or more. In such cases, the scale of graduated taxes set forth (above) was increased by twenty percent.

2 The Income Tax

The income tax was schedular in nature, requiring taxpayers to calculate the respective profit or gain they obtained from each financial activity in isolation from other activities. This approach to taxation, however, can leave unintended gaps in coverage. For example, under the analysis of the tax on the income of companies to follow, the Act makes no direct reference to whether or not royalties are subject to the income tax. Thus, the failure to tax royalties appears to leave a gap in the coverage of this income tax. Interest also seems to fall into this category. None of the schedules that detail the scope of the income tax⁸⁴ make reference to the taxability of interest as income, so it would appear that interest was simply not taxed.

The relationship between the land tax and the income tax exposes a further gap in this schedular system. For example, if an individual held a piece of land valued at £2,000 (including £1,500 of improvements) and also gained £300 in

⁸⁴ Supra note 66, schs C, D and E.

business or professional income, he would not be liable for any tax. This was because both his land holding and income would come under the respective exemptions to tax under the Act.⁸⁵ If the Act did not treat land and income in this completely separate manner, then landowners who also acquired business or professional income would not be entitled to two exemptions.

(a) Schedule C: Income from Companies

Schedule C of the Land and Income Assessment Act 1891 introduced the first form of company tax in New Zealand, taxing the gains and profits of companies. The Land-tax and Income-tax Act 1892 set the rate of tax at a flat one shilling in the pound sterling, or five percent. No exemption was afforded to companies with low profitability, with tax payable from the first dollar of income earned.⁸⁶ Losses and outgoings incurred by a company in deriving gross income were deductible under rule 1 of Schedule F which contained miscellaneous rules as to the assessment of income.

The Land and Income Assessment Act defined the income of companies as including all dividends earned by the company (before dividends are paid to shareholders), sums carried to reserve funds (retention of profits inside the company) and any other profits made or income derived not divided among shareholders. Furthermore, in the case of banking companies, the income derived or received from mortgages was included in the definition of income. This provision counterbalanced an earlier provision exempting banking companies from the land tax over the mortgages they held. Dividends were simply exempt from tax, based on the premise that the company had already paid tax on that income.

Rule 2 prevented companies from using debentures to avoid tax. Where a company had borrowed money on debentures, the company was deemed an agent of the debenture holder and was required to pay tax on the debenture-holder's behalf. The company was then required to deduct this tax paid each year from any instalment of interest due under the debenture to the debenture holder.

The assessment of income for life insurance companies was exclusive of gains made on investments in land or upon mortgages of land, as these investments would be taxed under the land tax.⁸⁷

A closer look at farmers

Under section 16(2)(e), income derived by an owner or occupier of land from the use or produce of his land was exempt from the income tax.⁸⁸ Thus, income from farming appears to have been exempt from the income tax. The reason for this was that it was covered by the land tax.

It appears that the Ballance Ministry may have intended that the ordinary tax on land would mirror the estimated level of income tax that farmers would have paid were they to be taxed as incorporated companies. Perhaps they realized the great difficulty in working out what a farmer's income actually was, preferring to use land tax as a surrogate to income tax on farming. The following six examples illustrate

⁸⁵ See discussion of schs D and E, *infra*.

⁸⁶ *Supra* note 66, sch C, r 1.

⁸⁷ *Supra* note 66, sch C, r 4.

⁸⁸ See text at note 119 *infra*.

how the ordinary land tax was similar to the income tax on companies, presuming an annual return of five percent on the value of the land.⁸⁹

Example number:	1	2	3	4	5	6
Value of land only:	2000	3000	4000	4000	5000	5000
Value of improvements:	1000	1000	2000	3000	2000	3500
Total value of the land:	3000	4000	6000	7000	7000	8500
Income from the land (5%):	150	200	300	350	350	425
Ordinary tax on land:	7.35⁹⁰	12.6	16.8	16.8	21	21
Income tax (5%):	7.5	10	15	17.5	17.5	21.25

Each of the six examples above only concerns the ordinary tax on land. The graduated tax would not have been intended to mirror income tax on companies in this way, as it was intended to encourage holders of large estates to break up their land.⁹¹ The examples do illustrate, however, that in so far as the ordinary tax on land was concerned, there was a very close relationship between the amount of land tax payable, and the amount of income tax that would have been payable if the land produced an annual return of 5%. Perhaps it was the great difficulty in determining farming income, or the ease of evasion,⁹² that prompted the Ballance Ministry to construct the tax system in this way and use land tax as a surrogate for income tax on farming and agriculture.

(b) Schedule D: Income from Business

Schedule D imposed a tax on incomes derived from trade and commerce by natural persons, thus the tax base was extended to cover merchants for the first time. Every person was liable to pay tax in respect of income derived from business on the full amount of the balance of the profits or gains of such business. The definition “income derived from business” reveals a lot about the scope of this taxation on the income from business. Rule 1 of Schedule D provided that: “Income derived from business’ means the gains or profits derived or received in New Zealand from any trade, manufacture, adventure, or concern in the nature of trade...”⁹³

This definition was copied from the prevailing 1842 UK Act.⁹⁴ Thus, New Zealand presumably adopted all of the associated United Kingdom case law. Furthermore, the use of the word “means” rather than “includes” in the definition above suggests that the scope of the New Zealand income tax on business was no wider than the scope of the analogous part of the 1842 UK Act, and, therefore, there would appear to have been no room for an increased scope in New Zealand.

⁸⁹ An estimated return of five percent on the total value of the land was used for illustrative purposes in the House by Mackay John Scobie MacKenzie without objection. ((3 August 1891) 73 NZPD 110 (Mackay MacKenzie)). While many factors will affect the annual return derived from land, five percent is used as a reasonable estimate.

⁹⁰ A farmer under this example would be entitled to a £250 exemption as his land is valued at only £2000.

⁹¹ See text above at note 43.

⁹² For example, by taking cash receipts, inflating deductions and claiming personal deductions.

⁹³ Supra note 66, sch D, r 1.

⁹⁴ Supra note 8, 111.

The definition of “income derived from business” is not clear as to the treatment of profits obtained by those who carried on the business of speculating in land. Given that New Zealand appears to have taken wholesale the English case law in this area, this definition is likely to have covered profits from speculation in land as it covered an “adventure...in the nature of trade”. English case law has long held that the singular nature of “adventure” allowed a single land transaction to constitute income derived from business.⁹⁵

All doubt over this matter was removed in the following year, when the definition of “income derived from business” was amended⁹⁶ to include gains or profits derived or received “from the purchase, sale, or other disposition of real or personal property, or of any rights, estate, or interest therein”.⁹⁷ This amendment confirmed that the profits of those who carried on a business of speculating in land were deemed to be “income derived from business”, and thus liable to income tax under schedule D.

The Land-tax and Income-tax Act of 1892⁹⁸ set two rates of tax. Furthermore, rule 2 of Schedule D afforded a £300 exemption to those earning business income, twice the £150 exemption under Ballance’s original proposal. The combined effect was thus:

		Marginal Tax Rate	
£0 -	£300	0	0%
£300 -	£1000	One Sixpence per Pound Sterling	2.5%
£1000	+	One Shilling per Pound Sterling	5%

All losses and outgoings incurred by the business in deriving gross income were deductible from that gross income.⁹⁹ In addition to this, individuals were permitted a single annual deduction of up to £50 for life insurance taken for their own benefit or for the benefit of immediate family members.¹⁰⁰

(c) Schedule E: Income from Employment or Emolument

Schedule E provided for the taxation of professional and salary income. Rule 1 stated that every person was liable in respect of income derived from employment or emolument that was not derived from business under Schedule D. The tax was progressive, with two rates above a £300 exemption. If a single taxpayer derived both (a) income from business, and (b) income from employment, he was not entitled to more than one £300 exemption.

⁹⁵ It is, however, not within the scope of this paper to trace the precise point in time that this principle was established by the Courts of England. Hence, my treatment of profits obtained by those carrying on the business of speculating in land as business income under the original drafting of the Act is not definitive.

⁹⁶ Land and Income Assessment Amendment Act, 1892.

⁹⁷ *Ibid* s 17 (4).

⁹⁸ This is the annual rates Act that sets the level of tax.

⁹⁹ *Supra* note 66, sch F, r 1.

¹⁰⁰ *Ibid* sch F, r 7.

		Marginal Tax Rate	
£0 -	£300	0	
£300 -	£1000	One Sixpence per Pound Sterling	2.5%
£1000	+	One Shilling per Pound Sterling	5%

“Income”, for the purposes of this schedule, encompassed gains or profits derived or received in New Zealand from the exercise of any profession, employment, or vocation not otherwise liable to taxation under the Act, or from any salary, wage, allowance, pension, stipend, charge or annuity not charged on land. Individuals deriving income from employment or emolument were also entitled to deduct losses and outgoings incurred in the production of their income.¹⁰¹ As with taxation on business income, taxpayers were permitted a further annual deduction from their employment income of up to £50 for life insurance taken for their own benefit or for the benefit of immediate family members.¹⁰²

Rule 4 in Schedule F compelled companies, local authorities and every person carrying on a business to provide the Commissioner of Taxes with a list of all the people employed by them and the salary, wage, stipend or other allowances or emolument paid or allowed to such people. This ensured that taxpayers gave an accurate statement of their total income.

In an early attempt to limit fringe benefits, the Act deemed that certain allowances were to be taken into account as income:¹⁰³

Allowances made to any person by way of house-rent, and all amounts received or receivable by way of extra salary, bonus, allowance, or emolument, shall be taken into account as part of the annual income liable to taxation.

This provision prevented employers and employees from, for example, colluding and arranging for the employee to be remunerated in part by house-rents which would otherwise be exempt from tax.

(d) Other Special General Rules for Deductions

The entitlement of companies and individuals to deduct all losses and outgoings incurred in the production of gross income¹⁰⁴ was subject to a number of provisos. These provisos applied in relation to individual income derived from business or employment. Interestingly, no deduction was allowed for:

- i. expenditure on repairs to premises occupied for the purposes of the business;¹⁰⁵
- ii. losses not connected to the business or employment or capital expenditure¹⁰⁶ or interest that would have been made but for the capital expenditure;¹⁰⁷
- iii. bad debts,¹⁰⁸

¹⁰¹ Ibid sch F, r 1.

¹⁰² Ibid sch F, r 7.

¹⁰³ Ibid sch F, r 5.

¹⁰⁴ Ibid sch F, r 1.

¹⁰⁵ Ibid sch F, r 2 (a).

¹⁰⁶ Ibid sch F, r 2 (b).

¹⁰⁷ Ibid sch F, r 2 (c).

¹⁰⁸ Ibid sch F, r 2 (d).

- iv. any expenditure not wholly and exclusively expended for the purposes of the business;¹⁰⁹
- v. any personal expenditure or expenditure on one's family or domestic establishment, including rent to the extent that the property was not used for the purposes of business.¹¹⁰

Part II: General Exemptions from Tax

There were a number of exemptions to the land tax, principally granted on the basis that the land was being used for a charitable purpose or was of a general good to the community. Exemptions included places of worship; public schools (up to 15 acres); universities; public libraries; museums; cemeteries; meeting places for agricultural societies, friendly societies or building societies; public charitable institutions; public gardens; public domains; public roads; public railways; and land owned and occupied by Maori.¹¹¹ Except where a tenant was liable to pay land tax, land vested in the Crown, including land vested in local government, was also not subject to the land tax.

There was also a small number of exemptions to the income tax.¹¹² These included the general revenues of the Crown;¹¹³ the employment income received by the Governor for Office as Governor;¹¹⁴ revenues in relation to local government, community boards and public educational institutions;¹¹⁵ friendly societies;¹¹⁶ and income derived by the owner or occupier of land or from the use or produce of land, or mortgages¹¹⁷ (exempt as this is liable for land tax), except where specifically provided.¹¹⁸

Part III: Assessment of Land and Income

The taxes established by the Land and Income Assessment Act 1891 were reliant on the assessment of taxpayers' land or income. Part III of the Act detailed how the government was to achieve this.

The assessment of land and mortgages was carried out every three years for individuals and annually for companies.¹¹⁹ All forms of income were assessed on an annual basis.¹²⁰ These assessments were entered onto rolls and registers for the purposes of taxation.¹²¹ Agents and trustees were assessed separately for the land and income they respectively held or received on behalf of those absent from New Zealand.¹²²

¹⁰⁹ *Ibid* sch F, r 2 (f).

¹¹⁰ *Ibid* sch F, r 2 (g), (h) & (i).

¹¹¹ *Ibid* ss 16 (1) (a) – (j).

¹¹² *Ibid* s 16 (2).

¹¹³ *Ibid* s 16 (2) (a).

¹¹⁴ *Ibid* s 16 (2) (b).

¹¹⁵ *Ibid* s 16 (2) (c).

¹¹⁶ *Ibid* s 16 (2) (d).

¹¹⁷ *Ibid* s 16 (2) (e).

¹¹⁸ For example, income earned from mortgages by banking companies was taxable under Schedule C.

¹¹⁹ *Supra* note 66, s 17 (1) (a).

¹²⁰ *Ibid* s 17 (1) (b).

¹²¹ *Ibid* s 17 (2).

¹²² *Ibid* s 17 (3).

In order to prevent New Zealand residents obtaining mortgages from non-resident mortgagees to avoid tax (as the non-resident mortgagee could not be compelled to pay New Zealand land tax), the mortgagors were liable to pay tax if the non-resident mortgagee could not be located.¹²³ This was an early example of the government compelling New Zealand residents to bear the tax liability of non-residents.

Once an individual or company assessment had been carried out, the taxpayer would receive notice in writing of his assessment on the assessment-roll¹²⁴ and be given an opportunity to dispute this.¹²⁵ Where no objection was made or sustained, this assessment remained on the assessment-roll in respect of the applicable land, mortgage, or income. A Board of Review of Assessments was appointed by the Governor¹²⁶ and had the power to make final and conclusive decisions relating to assessments.¹²⁷

Part IV: Procedure to Enforce Taxation

Part IV broadly covered procedure. The Commissioner was required to give taxpayers at least fourteen days notice in respect of tax payable.¹²⁸ Section 25 specified the court procedure where a taxpayer failed to pay a tax bill.

Section 26 provided for the remedies available to the Commissioner where a taxpayer died with outstanding tax liability.¹²⁹ For example, where tax had not been paid on income earned, the Commissioner was entitled to remedies against the executor or administrator of the taxpayer's estate.¹³⁰ In each case where a taxpayer had paid too little or too much tax this was to be corrected forthwith by the taxpayer or Commissioner paying the difference to the other party.¹³¹ The Act expressly confirmed that no statute of limitations would bar an action or remedy for the recovery of tax under the Act.¹³²

Section 30 gave the government considerable power to compel taxpayers to accept the land assessment as accurate. The government was entitled at any time to buy a taxpayer's land at the sum at which the land was valued plus ten percent. The only ways in which a taxpayer could prevent the government from doing this were either to accept an assessment at a value which the Commissioner deemed to be the fair actual value or to successfully lodge an appeal the Board of Review to determine such fair actual value.

Section 31 counterbalanced the considerable power that section 30 afforded the government. Where taxpayers were aggrieved with the amount at which their land was assessed, they were entitled to require the Commissioner to purchase their land at the value of the assessment, or to reduce the value of the assessment.

¹²³ *Ibid* s 17 (4).

¹²⁴ *Ibid* s 19 (1).

¹²⁵ *Ibid* s 19 (3).

¹²⁶ *Ibid* s 20.

¹²⁷ *Ibid* s 21 (3).

¹²⁸ *Ibid* s 24.

¹²⁹ *Ibid* s 26.

¹³⁰ *Ibid* s 26 (2).

¹³¹ *Ibid* ss 27 & 28.

¹³² *Ibid* s 29.

Part V: General Provisions

The final part of the Act contained some general provisions relating to the tax. These provisions were for the most part concerned with tax avoidance and tax evasion. Any agreement made between two parties attempting to alter the nature of an interest in land or mortgage for the purpose of evading the payment of tax was deemed void.¹³³ This is the first example of a general anti-avoidance rule in New Zealand.

Where taxpayers made false returns in respect of tax owing, they were subject to a fine of between £5 and £50.¹³⁴ In addition to this, in cases of tax evasion, offending parties were liable for three times the amount of tax which they sought to evade as a penalty.¹³⁵

Any tax outstanding on a given piece of land was given absolute priority over any other interest, change or encumbrance over that piece of land.¹³⁶

V THE CONTEXT AND ANALYSIS

Having examined the effect of the Land and Income Assessment Act in detail, it is now appropriate to put this legislation into a historical context. This section seeks to determine what prompted the New Zealand government to make such sweeping reform of the tax system.

The End of the Plural Voting System

The Constitution Act 1854 (UK) provided that all males aged over 21 who owned or leased land were entitled to vote for the House of Representatives.¹³⁷ The Qualifications of Electors Act 1879 drastically modified the right to vote. With the passing of this Act, the entitlement to vote was extended to all British men over the age of 21, provided that they either owned land, or had been living in New Zealand for twelve months or more and in an electorate for at least six months.¹³⁸ This was known as universal male suffrage, allowing all European¹³⁹ men to vote regardless of whether or not they owned or rented land.

Despite this radical change to the voting system, New Zealand was yet to reach a stage of “one man, one vote”, as the plural voting system remained. Plural voting allowed men who owned or leased property in multiple electorates to vote in each of those electorates.¹⁴⁰ Those constituents with land holdings across more than one electorate would have naturally been inclined to vote for a candidate who

¹³³ *Ibid* s 40.

¹³⁴ *Ibid* s 43.

¹³⁵ *Ibid* s44 (1).

¹³⁶ *Ibid* s 41.

¹³⁷ Although a small number of Maori men voted (as they owned or leased land), most were effectively excluded because they owned land under communal title. (“Key Dates in New Zealand Electoral Reform” (2006) Elections New Zealand

<http://www.elections.org.nz/administration/key_dates_electoral_reform.html> (at 27 August 2006).

¹³⁸ “Voting Rights” (2004) Auckland City Libraries

<<http://www.aucklandcitylibraries.com/general.aspx?ct=900&id=3017>> (at 28 November 2004).

¹³⁹ This increase in the size of the franchise did not include Maori men, who were still required to own or lease land in order to vote.

¹⁴⁰ *Supra* note 138.

represented their conservative interests. However those without multi-electorate land holdings condemned this system as undemocratic.

This system affected tax policy. Prior to the 1890 election, Atkinson was Premier and, with his Ministry, he broadly represented rural conservative interests. The Property Assessment Act that had been operating for the preceding decade went some way toward protecting the interests of large landowners. When Atkinson introduced the Property Assessment Act he said there was no reason why hardworking settlers involved in agriculture should bear a burden any greater than those holding wealth in the form of improvements, mortgages, bank shares and other forms of property.¹⁴¹ The taxation of improvements was particularly onerous on small and middling farmers.¹⁴²

It was not until 1889 that plural voting was finally abolished, confirming the principle of 'one man, one vote'. Premier George Grey had contributed to the introduction of universal male suffrage in 1879. Ten years later, while sitting in opposition, Grey moved an amendment to the Qualifications of Electors Act 1879 that saw the end of the plural voting system.¹⁴³

The abolition of the plural voting system would have brought renewed hope to liberal-minded constituents and politicians in the 1890 election. In that general election, the conservative Atkinson was defeated by the liberal John Ballance. After forming a Ministry, one of Ballance's top priorities was tax reform in line with more liberal ideologies. According to historian David Hamer,¹⁴⁴ most liberals "simply wanted the benefits of private ownership of property spread more widely".¹⁴⁵ Hamer, noted, furthermore, that Ballance and his followers "wanted the [social] hierarchy to be open to the reception of the 'hard-working and morally worthy...The Liberals' policies aimed at removing barriers to social mobility."¹⁴⁶

By ousting the undemocratic plural voting system, and finally giving every man an equal vote, the path was set for the sweeping tax reform that we have seen above in the Land and Income Assessment Act.

Refrigeration

The discussion in Hansard above,¹⁴⁷ illustrates an ulterior motive behind the graduated land tax, in that it was designed to encourage holders of large estates to break up their land.¹⁴⁸ The viability of this policy decision lay in a key technological advancement at the time: the advent of refrigeration.

On 11 February 1882, the *Dunedin* set sail from Port Chalmers destined for the United Kingdom, carrying nearly 5,000 carcasses of frozen pork, mutton and lamb. A little over three months later, on 24 May 1882, the carcasses were sold at prices nearly twice the market prices in New Zealand.¹⁴⁹

¹⁴¹ Supra note 22.

¹⁴² Richardson, supra note 3.

¹⁴³ Sinclair, supra note 9.

¹⁴⁴ David Hamer was the major historian of the liberal party.

¹⁴⁵ King, *The Penguin History of New Zealand* (2003) 259.

¹⁴⁶ Ibid.

¹⁴⁷ Supra note 37, 99 (Premier John Ballance).

¹⁴⁸ Ibid.

¹⁴⁹ Elliot, "The nineteenth century heritage: refrigeration and the meat industry" (2004) Tech History <<http://www.techhistory.co.nz/19thcentury/Meat.htm>> (at 29 August 2006).

The inception of a refrigerated meat trade coincided with agitation for the introduction of a direct steamship service and, after a few sailing ships had been fitted out for the trade, the Shaw Savill and Albion Company and the New Zealand Shipping Company both introduced monthly services with specially designed steamships.

Technological changes can affect the structure and functioning of the economy and society. The Ministry of Economic Development noted, however, that refrigeration itself was not enough for New Zealand to acquire an economic benefit. It was not until larger land holdings were separated into smaller efficient units, that the full benefit of refrigeration technology could be realized.¹⁵⁰ In 1890, less than one per cent of all people in the colony owned 64 per cent of all freehold land. With the new refrigeration technology, meat and dairy farming became not only viable, but also profitable,¹⁵¹ paving the way for substantive reform to allow settlement by smaller landholders.

With these new export commodities, in meat and dairy, the nature of farming in New Zealand was changed forever. Michael King identified that:¹⁵²

Previously sheep farmers had been forced to slaughter animals – sometimes by simply driving them over cliffs. Now they could raise sheep for meat and wool, which made smaller farms considerably more viable than they had been.

The Land and Income Assessment Act 1891 was to be the vehicle by which Ballance sought to go about breaking up larger estates. As has been seen, he achieved this by placing a graduated tax on land and even steeper rates on landowners residing out of New Zealand, as these landowners were not contributing to the development of the colony.

Anecdotal evidence indicated this policy was a success. Graham Miller¹⁵³ talks of one failed attempt by the trustees of a large North Canterbury estate who appealed against the trusts tax rate. The trustees were subsequently forced to subdivide and sell their land in small holdings, increasing the population on the land from 83 to 650 in 1891.¹⁵⁴

Depression

From around 1876, New Zealand entered a long depression. A reduction in wool prices worldwide in 1877 triggered the depression, and the New Zealand economy did not grow for another 16 years.¹⁵⁵ The depression had an immediate effect on government finances, due to a system heavily reliant on revenue sourced from taxation on land, customs duties and the sale of public land.

The depression caused a drop in consumption, which reduced the yield collected from indirect taxation, most notably customs and excise duties. Furthermore, this decline in consumption had a profound flow-on effect, reducing the value of land. With lower land values, the government yield from the Property Tax

¹⁵⁰ Ministry of Economic Development *Digital Strategy: A Draft New Zealand Digital Strategy for Consultation* (2004) ch 1.2.

¹⁵¹ Supra note 145, 261.

¹⁵² Ibid 237.

¹⁵³ Graham Miller is a New Zealand historian primarily interested in land.

¹⁵⁴ "Farming in New Zealand – The ups and downs in profitability since the 1860s" (2004) NZine <<http://www.nzine.co.nz/features/farming1.html>> (at 29 August 2006).

¹⁵⁵ Supra note 145, 235.

began to decline. The recession also reduced the value of public land suitable for sale, which, in turn, further reduced government revenue.¹⁵⁶

The development of the colony did not come without significant cost. Government revenue was on the decline and the government was still required to service large loans from England that were necessary for the construction of public infrastructure and to fund the war against the “Native Rebellion”.¹⁵⁷ Although the years preceding the Ballance Ministry had seen significant public sector retrenchments to reduce expenditure, these were not enough.¹⁵⁸ The government was forced to look elsewhere to stabilize its finances.

When Ballance introduced the Land Tax Act 1878 he highlighted good reasons to single out landowners and embrace direct taxation on land. He identified that landowners obtained the greatest permanent benefit from government expenditure on road and rail, as this caused land values to increase. Furthermore, landowners benefited from the government’s liberal immigration policy, which contributed to higher land values.¹⁵⁹

By the time Ballance became Premier in 1891, during a worldwide depression, these arguments to single out landowners were less convincing. While land tax remained an important source of revenue, “the reduction in value of land removed the speculation opportunities particularly along the railway and road lines and, therefore, largely removed any justification for singling out land as a special subject of taxation.”¹⁶⁰ The Ballance Ministry began to look elsewhere to secure revenue for the colony. With this came the birth of income tax in New Zealand.

VI CONCLUSION

This article has examined the political and legislative framework that existed in the years leading up to the introduction of the Land and Income Assessment Act 1891. Initially, the House of Representatives was uneasy at the prospect of an income tax, opting instead to tax landowners. Landowners were viewed as receiving the greatest benefit from government spending on public infrastructure and its liberal immigration policies, as these variables were causing land values to steadily increase.

In the following year the Property Assessment Act 1879 was passed, which treated all forms of property in the same manner for the purposes of taxation. This approach to taxation favoured by conservatives survived for over a decade, until the more liberal John Ballance Ministry came to power in 1891.

In spite of the inequalities created by the Property Tax Act, the reason for its longevity is clear. In the general elections of 1881, 1884 and 1887 while the Property Tax Act was in force, a plural voting system existed in New Zealand. This allowed men who owned or leased property in several different electorates to enrol and vote in each of them. It was therefore of no surprise, that the general taxation policy in New Zealand at the time protected the conservative interests of landowners. It is also of no surprise, that when this plural voting system was ousted, significant reform followed including the birth of income tax in New Zealand.

¹⁵⁶ *Supra* note 8, 94.

¹⁵⁷ *Ibid* 94.

¹⁵⁸ *Ibid*.

¹⁵⁹ *Supra* note 10, 80-93.

¹⁶⁰ *Supra* note 8, 94.

Prior to the introduction of income tax, New Zealand had been in recession for well over a decade, which had had a negative effect on land values. The fall in land values had a detrimental effect on government revenue which had been heavily reliant on land tax and the proceeds from sales of public land. As the government was still required to service large loans from England, an alternative source of revenue was needed.

After entering office as Premier, John Ballance introduced income tax in New Zealand. Today, income tax remains as a fundamental part of New Zealand's tax base, albeit in a much more complicated form.

A land tax was implemented to sit alongside the income tax, consisting of an ordinary and a graduated tax on land. Based on the difficulties expressed in defining farming income, it appears that a land tax was used as a surrogate for the imposition of an income tax on farmers. The graduated tax, meanwhile, was intended to break up large estates of land. It took advantage of new refrigeration technology, which meant that small farmers could raise sheep for meat and wool, paving the way for tax reform to allow settlement of people onto small farms.

The Land and Income Assessment Act was passed in 1891. New Zealanders are indebted to John Ballance for his work in introducing income tax into this country as a fairer, more equitable approach to taxation policy. John Ballance is the father of income tax in New Zealand and his model formed the foundation of the system of income tax that survives today. To this day, exports reliant on refrigeration technology remain a crucial export commodity in this country and by using tax policy to break up large estates, Ballance facilitated the realisation of the full benefit that refrigeration technology had to offer. Although Ballance died in office less than two years after introducing the Act, the impact of his work remains today.