

Hon Stuart Nash, Minister of Revenue

Information Release

Taxation (Use of Money Interest Rates) Amendment Regulations 2019

Tax policy report, Cabinet paper, and minute

July 2019

Availability

This information release is available on Inland Revenue's Tax Policy website at <http://taxpolicy.ird.govt.nz/publications/2019-ir-cab-leg-19-sub-0096/overview>.

Documents in this information release

1. IR2019/280 – Tax policy report: Use of money interest rates review (6 June 2019)
2. LEG-19-SUB-0096 – Cabinet paper: Taxation (Use of Money Interest Rates) Amendment Regulations 2019 (25 June 2019)
3. LEG-19-MIN-0096 – Minute: Taxation (Use of Money Interest Rates) Amendment Regulations 2019 (25 June 2019)

Additional information

The Cabinet paper was considered by the Cabinet Legislation Committee on 25 June 2019 and confirmed by Cabinet on 1 July 2019.

One attachment to the Cabinet paper is not included in this information release as it is publicly available:

- Taxation (Use of Money Interest Rates) Amendment Regulations 2019.

Information withheld

Some parts of this information release would not be appropriate to release and, if requested, would be withheld under the Official Information Act 1982 (the Act). Where this is the case, the relevant sections of the Act that would apply are identified. Where information is withheld, no public interest was identified that would outweigh the reasons for withholding it.

Sections of the Act under which information was withheld:

- 9(2)(a) to protect the privacy of natural persons, including deceased people

Copyright and licensing

Cabinet material and advice to Ministers from the Inland Revenue Department and other agencies are © Crown copyright but are licensed for re-use under the Creative Commons Attribution 4.0 International (CC BY 4.0) licence (<https://creativecommons.org/licenses/by/4.0/>).





POLICY AND STRATEGY

Tax policy report: Use of money interest rates review

Date:	6 June 2019	Priority:	High
Security level:	In Confidence	Report number:	IR2019/280

Action sought

	Action sought	Deadline
Minister of Revenue	<p>Agree to the recommendations.</p> <p>Sign and refer attached paper to Cabinet Office for consideration at LEG meeting on 25 June 2019.</p> <p>Refer a copy of this report to the Minister of Finance.</p>	10am, Thursday 20 June 2019.

Contact for telephone discussion (if required)

Name	Position	Telephone
Jess Rowe	Team Lead	s 9(2)(a)
s 9(2)(a)	Policy Analyst	

6 June 2019

Minister of Revenue

Use of money interest rates review

Executive summary

1. This report seeks your agreement to adjust the use of money interest rates (UOMI) as part of the regular review of the UOMI rates.
2. The UOMI rates are reviewed regularly to ensure that they align with market interest rates. The UOMI rates are calculated using formulae based on the results of the Reserve Bank (RBNZ) survey of interest rates. These formulae are set down in regulations.
3. The current underpayment UOMI rate is 8.22% and the overpayment UOMI rate is 1.02%. We recommend that the underpayment rate be increased to 8.35%, and that the overpayment rate be reduced to 0.81%, in line with movements in market rates. Your approval is sought to make these rate changes, and for the Parliamentary Counsel Office to draft an Order in Council to set the new rates.
4. If you agree, the new rates will come into force on 29 August 2019, the day after the due date for the first standard instalment of provisional tax. We confirm that this complies with the 28-day rule.
5. In anticipation of your approval, officials have advised the Parliamentary Counsel Office that a draft Order in Council changing the rates will need to be prepared.
6. Attached is a paper to the Cabinet Legislation Committee recommending that it approve the Order in Council and authorise its submission to Cabinet and the Executive Council. For the paper to be considered by the Cabinet Legislation Committee at its meeting on 25 June 2019, it should be referred to Cabinet Office by 10am, Thursday 20 June 2019.
7. A draft press statement will be forwarded for your consideration once the Order in Council has been made.
8. The Treasury has been consulted and agrees with the recommendations in this report. A copy should be referred to the Minister of Finance for his information.

Recommended action

We recommend that you:

- (a) **Agree** that the UOMI underpayment and overpayment interest rates be changed to 8.35% (from 8.22%) and 0.81% (from 1.02%) respectively.

Agreed/Not agreed

- (b) **Agree** that the new UOMI rates come into force on 29 August 2019.

Agreed/Not agreed

- (c) **Note** that agreeing to recommendations (a) and (b) is expected to have the following impact on tax revenue and impairment expenditure with an overall net increase in the operating balance of around \$6 million in the 2019/20 fiscal year with the effective date of 29 August 2019, and an operating balance increase of \$7 million for 2020/21 and later years:

		\$ millions increase / (decrease)			
Vote Revenue Minister of Revenue	2018/19	2019/20	2020/21	2021/22	2022/23 & Outyears
Crown Revenue and Receipts: Tax Revenue	-	9.000	10.000	10.000	10.000
Total Operating	-	9.000	10.000	10.000	10.000

		\$ millions increase / (decrease)			
Vote Revenue Minister of Revenue	2018/19	2019/20	2020/21	2021/22	2022/23 & Outyears
Non-Departmental Other Expense: Impairment of debt and debt write-offs (funded by Revenue Crown)	-	3.000	3.000	3.000	3.000
Total Operating	-	3.000	3.000	3.000	3.000

Noted

- (d) **Agree** that the Parliamentary Counsel Office draft an Order in Council to adjust the UOMI rates.

Agreed/Not agreed

- (e) **Sign** and **refer** the attached paper to the Cabinet Office by 10am Thursday 20 June 2019 for consideration by Cabinet Legislation Committee at its meeting on 25 June 2019.

Signed and referred

- (f) **Refer** a copy of this report to the Minister of Finance.

Referred

Jess Rowe
Team Lead
Policy and Strategy

Hon Stuart Nash
Minister of Revenue
/ /2019

Background

9. The UOMI rates are an important component of the tax compliance rules. By changing in line with underlying market rates, the UOMI rates provide taxpayers with the incentive to pay the right amount of tax at the right time. They apply to all revenue and duties.
10. The UOMI rates are set according to the Taxation (Use of Money Interest Rates Setting Process) Regulations 1997. The Regulations provide that the methodology for setting the interest rate for underpaid tax is the latest Reserve Bank New Zealand (RBNZ) floating first mortgage new customer housing rate plus 250 basis points. The floating first mortgage new customer housing rate reflects the variable interest rate offered by surveyed institutions to new borrowers for residential property, weighted by each surveyed institution's total lending outstanding for housing purposes.
11. The floating first mortgage new customer housing rate is a proxy for a debt that a taxpayer might prioritise over their tax obligations. In the absence of a UOMI charge, a taxpayer wanting to borrow money could simply underpay their tax and use Inland Revenue as a bank rather than borrow from a bank at a commercial interest rate. A conservative margin of 250 basis points is added to the mortgage rate in calculating the underpayment UOMI rate because the Commissioner does not have information about the likelihood of any individual taxpayer paying the UOMI charged to them (i.e. the taxpayer's credit-worthiness).
12. The Regulations provide that the methodology for setting the interest rate for overpaid tax is the latest RBNZ 90-day bank bill rate less 100 basis points. The RBNZ 90-day bank bill rate is the monthly average of the daily standard rates, and approximates the return a taxpayer might expect on a low-risk investment in the New Zealand Government. Ensuring that the Commissioner pays less interest to the taxpayer on overpaid tax than the taxpayer would receive as a return from a low-risk bond aims to prevent Inland Revenue being used as an investment.
13. Because the two UOMI rates are based on two different Reserve Bank interest rate measures that can move independently of each other, the underpayment rate can increase while the overpayment rate decreases, as is the case in this rates review.
14. The current underpayment rate is 8.22% and the current overpayment rate is 1.02%.

Principles to be applied in resetting UOMI rates

15. In 2010 the Minister of Revenue agreed that the following principles be applied in setting new UOMI rates (PAD 2010/287 refers):
 - adjust both UOMI rates where there has been a 1% increase or 1% decrease (since the time the rates were last set) in the RBNZ 90-day bank bill rate or the floating first mortgage new customer housing rate;
 - adjust both UOMI rates every 12 months where there has been an increase or decrease in the Reserve Bank 90-day bank bill rate or the floating first mortgage new customer housing rate of 20 basis points or more (since the time the rates were last set), if the previous 12-month movement has not been sufficient to trigger a change, in order to avoid long-term misalignment of the rates; and
 - apply the adjustment from the next standard provisional tax payment date.

16. Inland Revenue officials are responsible for monitoring the RBNZ 90-day bank bill rate and the floating first mortgage new customer housing rate throughout the year.
17. The UOMI rates were last changed by Order in Council with effect from 8 May 2017 and were based on the interest rates for February 2017.

Annual review of UOMI rates

18. The Reserve Bank's survey results for the relevant market interest rates in February 2017 and April 2019 are below:

Month ended	Floating first mortgage new customer housing rate (%)	90-day bank bill rate (%)
February 2017	5.72	2.02
April 2019	5.85	1.81

Note: add 250 basis points to the floating first mortgage new customer housing rate to get the UOMI under-payment interest rate and subtract 100 basis points from the 90-day bank bill rate to get the UOMI overpayment rate.

19. The results for April 2019 indicate that, since the rates were last set, the floating mortgage new customer housing rate has increased by 13 basis points, and the 90-day bank bill rate has decreased by 21 basis points. To avoid a long-term misalignment, officials consider an adjustment to the UOMI rates is necessary.
20. Officials recommend that the underpayment and overpayment rates be changed to 8.35% and 0.81% respectively.

Approval for drafting

21. The UOMI rates are set at regular intervals by Order in Council and it has become a routine matter to amend them. Paragraph 7.91(d) of the Cabinet Office Manual provides that where the making of an Order in Council will not involve any further policy considerations, the Minister may authorise drafting without reference to Cabinet.
22. Your approval is sufficient for the Parliamentary Counsel Office to draft the Order in Council.

Financial implications

23. UOMI applies to both overpayments and underpayments of tax. Although more is charged by the Commissioner on underpayments than is paid to the taxpayer on overpayments, the charges to underpayments are impaired by 80% in the Crown accounts to reflect that most UOMI charged is never paid, and therefore must be written-off. This means that an increase in the underpayment rate also produces an increase in impairment expenditure.

24. The full year net saving for the 2019/20 fiscal year is estimated to be \$6 million, and \$7 million per annum for 2020/21 and later years. These savings comprise a revenue increase of \$9 million in 2019/20 and \$10 million per annum for 2020/21 and later years, and an increase in impairment expenditure of \$3 million per annum. This is shown in the following tables:

		\$ millions increase / (decrease)			
Vote Revenue Minister of Revenue	2018/19	2019/20	2020/21	2021/22	2022/23 & Outyears
Crown Revenue and Receipts: Tax Revenue	-	9.000	10.000	10.000	10.000
Total Operating	-	9.000	10.000	10.000	10.000

		\$ millions increase / (decrease)			
Vote Revenue Minister of Revenue	2018/19	2019/20	2020/21	2021/22	2022/23 & Outyears
Non-Departmental Other Expense: Impairment of debt and debt write-offs (funded by Revenue Crown)	-	3.000	3.000	3.000	3.000
Total Operating	-	3.000	3.000	3.000	3.000

25. We note that these revenue implications are a forecasting change only as they result from an existing policy; therefore there is no impact on the scorecard from the proposed adjustment to the UOMI rates.

Consultation

26. The Treasury has been consulted in the preparation of this report and agrees with its contents.

Next steps

27. To enable the UOMI rates to come into force on 29 August 2019 it is proposed that the Order in Council be submitted to Cabinet Office by 10am, Thursday 20 June 2019 for the Cabinet Legislation Committee meeting on Tuesday 25 June 2019 and to Cabinet and the Executive Council for approval on Monday 1 July 2019.

In Confidence

Office of the Minister of Revenue

Chair, Cabinet Legislation Committee

TAXATION (USE OF MONEY INTEREST RATES) AMENDMENT REGULATIONS 2019

Proposal

1. This paper seeks the Cabinet Legislation Committee's agreement to submit an Order in Council amending the Taxation (Use of Money Interest Rates) Regulations 1998 to the Executive Council.
2. It is proposed to amend the regulation so the underpayment use-of-money (UOMI) interest rate is set at 8.35% and the overpayment UOMI rate is set at 0.81%.

Policy

3. The UOMI rates play an important role in the tax compliance rules. By moving in line with underlying market rates, the UOMI rates provide taxpayers with the incentive to pay the right amount of tax at the right time. The rates apply to all revenue and duties.
4. The Tax Administration Act 1994 provides for the UOMI underpayment and overpayment interest rates to be set by Order in Council. Once the rates are set, they remain the prescribed UOMI rates unless subsequently changed by Order in Council.
5. The methodology for calculating the rates is set out in the Taxation (Use of Money Interest Rates Setting Process) Regulations 1997 (the Regulations). The Regulations provide that the interest rate for underpaid tax should be set at the Reserve Bank of New Zealand (RBNZ) floating first mortgage new customer housing rate plus 250 basis points. The floating first mortgage new customer housing rate reflects the variable interest rate offered by surveyed institutions to new borrowers for residential property, weighted by each surveyed institution's total lending outstanding for housing purposes.
6. The Regulations provide that the interest rate for overpaid tax is set at the latest RBNZ 90-day bank bill rate less 100 basis points. The RBNZ 90-day bank bill rate is the monthly average of the daily standard rates.
7. The current underpayment and overpayment rates are 8.22% and 1.02% respectively. The UOMI rates were last changed by Order in Council with effect from 8 May 2017 and were based on the interest rates for February 2017.
8. The RBNZ interest rates for April 2019 indicate that the floating first mortgage new customer housing rate and the 90-day bank bill rate have changed by 13 and 21 basis points respectively since the rates were last adjusted. I consider that an adjustment of the UOMI rates is necessary to avoid a long-term misalignment.

9. Therefore, I recommend that the underpayment rate be changed to 8.35% and the overpayment rate be changed to 0.81%.

Timing and 28-day rule

10. I propose to submit the Order in Council giving effect to the changes in UOMI rates to Cabinet for approval and submission to the Executive Council at its meeting on 1 July 2019. In order to minimise compliance costs it is proposed that the new UOMI rates come into force on 29 August 2019, the day after the due date for the first standard instalment of provisional tax. This also complies with the 28-day rule.

Compliance

11. The regulations comply with the principles, Acts, guidelines, and requirements set out below as follows:
- | | | |
|------|---|----------------|
| 11.1 | the principles of the Treaty of Waitangi | Not applicable |
| 11.2 | the New Zealand Bill of Rights Act 1990 | Not applicable |
| 11.3 | the Human Rights Act 1993 | Not applicable |
| 11.4 | the principles and guidelines set out in the Privacy Act 1993 | Not applicable |
| 11.5 | relevant international standards and obligations | Not applicable |
| 11.6 | the <i>Legislation Guidelines</i> (2018 edition), which are maintained by the Legislation Design and Advisory Committee | Complies |

Regulations Review Committee

12. There are no anticipated grounds for the Regulations Review Committee to draw the Order in Council to the attention of the House.

Certification by Parliamentary Counsel

13. The Parliamentary Counsel Office has certified that the attached Order in Council is in order for submission to Cabinet.

Impact Analysis

14. A regulatory impact assessment is not required as the proposal is of a minor and routine nature and does not substantially alter existing arrangements.

Financial Implications

15. The proposal is estimated to result in net positive revenue of \$27 million over the forecast period, with the effective date of 29 August 2019. The increase in tax revenue arises due to both a decrease in the Commissioner's paying rate and an increase in the underpayment rate for taxpayers. The tax revenue implications are shown below:

Vote Revenue Minister of Revenue	\$ millions increase / (decrease)				2022/23 & Outyears
	2018/19	2019/20	2020/21	2021/22	
Crown Revenue and Receipts: Tax Revenue	-	9.000	10.000	10.000	10.000
Total Operating	-	9.000	10.000	10.000	10.000

16. The tax revenue increase is offset by an increase in expenditure for impairment of debt and debt write-off costs, arising from an increase in the underpayment rate. Revenue from the underpayment rate is impaired by 80% in the Crown accounts to reflect that most UOMI charged is never paid. This impact on appropriations is shown in the table below:

Vote Revenue Minister of Revenue	\$ millions increase / (decrease)				2022/23 & Outyears
	2018/19	2019/20	2020/21	2021/22	
Non-Departmental Other Expense: Impairment of debt and debt write-offs (funded by Revenue Crown)	-	3.000	3.000	3.000	3.000
Total Operating	-	3.000	3.000	3.000	3.000

Publicity

17. I will issue a media statement once the Order in Council is made by the Executive Council.
18. Inland Revenue will publish an item about these changes in its *Tax Information Bulletin*.

Proactive Release

19. I propose to proactively release this Cabinet paper, associated minutes, and key advice papers in whole within 30 working days of Cabinet making final decisions.

Consultation

20. Inland Revenue and the Treasury have been consulted in the preparation of this paper and agree with its recommendations.

Recommendations

The Minister of Revenue recommends that the Cabinet Legislation Committee:

1. **agree** that the use-of-money interest underpayment rate be changed to 8.35% from 8.22%;
2. **agree** that the use-of-money interest overpayment rate be changed to 0.81% from 1.02%;
3. **agree** that the Taxation (Use of Money Interest Rates) Amendment Regulations 2019 give effect to the new rates referred to in paragraphs 1 and 2 above;
4. **agree** that the Taxation (Use of Money Interest Rates) Amendment Regulations 2019 come into force on 29 August 2019.
5. **note** the following changes as a result of the decision in recommendations 1 and 2 above, with a corresponding impact on the operating balance:

	\$ millions increase / (decrease)				
Vote Revenue Minister of Revenue	2018/19	2019/20	2020/21	2021/22	2022/23 & Outyears
Crown Revenue and Receipts: Tax Revenue	-	9.000	10.000	10.000	10.000
Total Operating	-	9.000	10.000	10.000	10.000

6. **approve** the following forecast change in appropriations for Non-Departmental Other Expenses, as a result of the decision in recommendations 1 and 2, with a corresponding impact on the operating balance:

	\$ millions increase / (decrease)				
Vote Revenue Minister of Revenue	2018/19	2019/20	2020/21	2021/22	2022/23 & Outyears
Non-Departmental Other Expense: Impairment of debt and debt write-offs (funded by Revenue Crown)	-	3.000	3.000	3.000	3.000
Total Operating	-	3.000	3.000	3.000	3.000

7. **authorise** the submission to the Executive Council of the Taxation (Use of Money Interest Rates) Amendment Regulations 2019.

Authorised for lodgement

Hon Stuart Nash
Minister of Revenue



Cabinet Legislation Committee

Minute of Decision

This document contains information for the New Zealand Cabinet. It must be treated in confidence and handled in accordance with any security classification, or other endorsement. The information can only be released, including under the Official Information Act 1982, by persons with the appropriate authority.

Taxation (Use of Money Interest Rates) Amendment Regulations 2019

Portfolio Revenue

On 25 June 2019, the Cabinet Legislation Committee:

- 1 **agreed** that the use-of-money interest underpayment rate be changed to 8.35 percent from 8.22 percent;
- 2 **agreed** that the use-of-money interest overpayment rate be changed to 0.81 percent from 1.02 percent;
- 3 **agreed** that the Taxation (Use of Money Interest Rates) Amendment Regulations 2019 give effect to the new rates referred to in paragraphs 1 and 2 above;
- 4 **agreed** that the Taxation (Use of Money Interest Rates) Amendment Regulations 2019 come into force on 29 August 2019.
- 5 **noted** the following changes as a result of the decision in paragraphs 1 and 2 above, with a corresponding impact on the operating balance:

Vote Revenue Minister of Revenue	\$ millions increase / (decrease)				
	2018/19	2019/20	2020/21	2021/22	2022/23 & Outyears
Crown Revenue and Receipts: Tax Revenue	-	9.000	10.000	10.000	10.000
Total Operating	-	9.000	10.000	10.000	10.000

- 6 **approved** the following forecast change in appropriations for Non-Departmental Other Expenses, as a result of the decision in paragraphs 1 and 2, with a corresponding impact on the operating balance:

Vote Revenue Minister of Revenue	\$ millions increase / (decrease)				
	2018/19	2019/20	2020/21	2021/22	2022/23 & Outyears
Non-Departmental Other Expense: Impairment of debt and debt write-offs (funded by Revenue Crown)	-	3.000	3.000	3.000	3.000
Total Operating	-	3.000	3.000	3.000	3.000

- 7 **authorised** the submission to the Executive Council of the Taxation (Use of Money Interest Rates) Amendment Regulations 2019 [PCO 22181/2.0].

Vivien Meek
Committee Secretary

Present:

Rt Hon Winston Peters
Hon Andrew Little
Hon Stuart Nash
Hon Iain Lees-Galloway (Chair)
Hon Tracey Martin
Hon Eugenie Sage
Hon Ruth Dyson (Senior Government Whip)

Officials present from:

Office of the Prime Minister
Officials Committee for LEG

Hard-copy distribution:

Minister of Revenue