Hon Stuart Nash, Minister of Revenue

Information Release

Business Transformation: KiwiSaver policy changes for inclusion in the next omnibus taxation bill

Cabinet paper, regulatory impact assessment, 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-dev-19-sub-0038/overview.

Documents in this information release

1. DEV-19-SUB-0038 – Cabinet paper: Business Transformation: KiwiSaver changes for inclusion in the next omnibus taxation bill (20 March 2019)
2. DEV-19-SUB-0038 – Regulatory impact assessment: Business Transformation related KiwiSaver refinements (1 March 2019)
3. DEV-19-MIN-0038.01 – Minute: Business Transformation: KiwiSaver changes for inclusion in the next omnibus taxation bill (20 March 2019)

Additional information

The Cabinet paper was considered by the Cabinet Economic Development Committee on 20 March 2019 and confirmed by Cabinet on 25 March 2019.

Information withheld

No information was withheld for this information release.

Copyright and licensing

In Confidence

Office of the Minister of Revenue

Chair, Cabinet Economic Development Committee

BUSINESS TRANSFORMATION RELATED KIWISAVER POLICY CHANGES FOR INCLUSION IN THE NEXT OMNIBUS TAXATION BILL

Proposal

1. This paper seeks the Cabinet Economic Development Committee's agreement to the Crown funding the payment of employer contribution amounts passed to KiwiSaver scheme providers until these amounts are received from the employer, as well as a number of other measures which would increase the administrative efficiency of KiwiSaver and enhance members' experience with the scheme.

Executive Summary

2. As part of Inland Revenue's Business Transformation programme, the administration of KiwiSaver is scheduled to be transferred into a new administrative system on 1 April 2020. Business Transformation provides the opportunity to enhance the administration of KiwiSaver and improve the KiwiSaver member experience. Ensuring that members receive the correct contribution amounts and facilitating the faster transfer of contributions would assist in achieving these outcomes.

3. The main change this paper recommends is to allow Inland Revenue to pass employer contribution amounts to KiwiSaver scheme providers, before the contribution amount has been received by Inland Revenue (essentially acting as a Government guarantee of these contributions). This would improve the administrative efficiency of KiwiSaver, as it would facilitate earlier transfers of contributions to KiwiSaver scheme providers; meaning members would receive the benefit of their contributions being invested with scheme providers sooner. It would also be consistent with the existing treatment of employee contributions and other PAYE deductions, such as those made for student loans and child support.

4. This paper also proposes the following technical policy changes to KiwiSaver settings:

    4.1 change the date the calculation of interest on employer and employee contributions commences, to align with the pay date a member's employer has reported;

    4.2 reduce the KiwiSaver provisional period (during which individuals who are automatically enrolled in KiwiSaver are provisionally allocated to a default KiwiSaver scheme) from 3-months to 2-months;

    4.3 reduce the maximum period an old scheme provider has to share information and transfer funds to a new provider when a member transfers schemes, from 35-days to 10-days;

4.4 allow members to change contribution rates through their scheme provider or Inland Revenue, rather than only through their employer;

4.5 remove the 3-month grace period for members who have been incorrectly automatically enrolled in KiwiSaver, to gain New Zealand residence; and

4.6 require employers to provide Inland Revenue with KiwiSaver information about a member's employer superannuation contribution tax rate and the income their contributions are calculated from.

5. All the changes proposed would be phased in so that system changes are aligned with Inland Revenue's Business Transformation timelines. This would mean the proposals would apply from 1 April 2020.

6. If Cabinet agrees, necessary legislative amendments to give effect to the changes would be included in the next omnibus taxation Bill, which is scheduled for introduction in mid-2019.

Guarantee of employer contributions

7. Under current KiwiSaver settings, where an employee contribution has been deducted from a member's salary or wages but has not been paid, the amount is treated as having been received by Inland Revenue and is passed to the member's KiwiSaver scheme provider. The effect of this is the Crown funds the payment of the employee contribution until the amount is received from the employer, it also means in situations where the amount is never received by the employer these Crown funds are not recovered (effectively creating a Government guarantee of employee contributions and for simplicity will be referred to as such throughout the rest of the paper). This approach was adopted as it aligns with the treatment of other PAYE deductions, including for child support and student loans.

8. There is currently no comparable arrangement with employer contributions. This means that where an employer fails to pay an employer contribution amount, no contribution is paid to the member's KiwiSaver account and the member's savings would be adversely impacted as a result of their employer's late payment or non-payment.

9. The decision not to guarantee employer contributions when KiwiSaver was first introduced, is attributable to the fact they were considered an additional benefit "on-top" of a member's salary and wages. However, as the KiwiSaver regime has become more established, there has been a decline in any conceptual distinction between employer and employee contributions. The KiwiSaver Act 2006 now explicitly allows for employer contributions to form part of a total remuneration package (so long as the employee is receiving at least the minimum wage excluding the employer contribution in the total remuneration package). Employer contributions are also now generally understood by employees to be their money, similar to the way employee contributions deducted from salary or wages are.

10. The current state (with no guarantee of employer contributions) results in employer contribution taking on average 5-days longer to be transferred to scheme providers than employee contributions. This gap would increase once payday filing reforms, requiring employers to file employment income information with Inland Revenue

within 2 days of a payday (or within 10 days for employers with annual PAYE deductions of less than $50,000), become compulsory from 1 April this year. As Inland Revenue would have KiwiSaver contribution information sooner, these reforms would allow employee contributions to be passed to scheme providers sooner after a member's payday. However, as the date that actual payments must be made to Inland Revenue is not changing, if a guarantee was not introduced, employer contributions would still be unable to be passed until the contribution amount was received.

11. Inland Revenue is also required to allocate resources to time consuming administrative reconciliation processes as a result of employer contributions not being guaranteed. These include allocation of part payments of employer contributions to employees' KiwiSaver accounts and employer contribution refund requests to KiwiSaver scheme providers (where an amount was incorrectly identified as an employer contribution and must be returned to Inland Revenue from the provider). These complex transfer processes also make it difficult for members to reconcile the amounts in their KiwiSaver account with the contribution amounts listed on their payslips.

12. I propose that the existing approach for employee contributions be extended to employer contributions – that is employer contributions would be guaranteed. This would mean these contributions would be able to be passed to scheme providers as soon as information from an employer had been filed with Inland Revenue, rather than having to wait until the contribution amount had been paid. This would facilitate the faster transfer of employer contributions to scheme providers, which would have flow on benefits for members, as contributions would be subject to market investment returns sooner. As contributions could be passed to scheme providers in full, it would also reduce confusion caused by complex reconciliation processes.

13. The guarantee would need to apply to both compulsory and voluntary employer contributions. A guarantee that only covered compulsory employer contributions would not recognise that voluntary employer contributions are generally understood by members as forming part of their remuneration, nor would it create the same administrative efficiencies (as it would require Inland Revenue to still hold some contributions until the contribution amounts were received). Given the number of employers making voluntary employer contributions is small, with voluntary employer contributions estimated to make-up only approximately 2% of all employer contribution in the year ending 30 June 2018, this would not have a significant impact on the proposed change.

14. Total levels of employer and employee contribution debt are comparable (as at 30 June 2018, $18 million in employer contribution debt and $24 million in employee contribution debt, since the commencement of KiwiSaver in 2007). This suggests that the existing guarantee of employee contributions has had limited behavioural impact on employers. Based on this precedent, as employer contributions are generally treated as forming part of an employee's remuneration, it would be expected that guaranteeing employer contributions would have a similar minimal behavioural impact on employers. That is, employers would not be less likely to pay these amounts. Inland Revenue monitors levels of unpaid employee and employer contributions and has existing recovery mechanisms and penalties that can be applied in relation to these debts. These would remain in place if a guarantee of

employer contributions was agreed to and could be used to maintain employer compliance levels.

Date calculation of interest payments commences

15. Once Inland Revenue has received notification that an employer has deducted KiwiSaver employee contributions or paid employer contributions, these contributions are held in Inland Revenue's KiwiSaver holding account. Inland Revenue pays interest on contributions that are held in this account, until they are forwarded to the member's KiwiSaver scheme.

16. When KiwiSaver was introduced it would not have been possible for Inland Revenue to collect the information necessary to calculate interest from the date of the payday deductions were made or employer contributions paid, without imposing significant compliance costs on employers. As a result, for the purposes of calculating the interest due, employee contributions are treated as received into Inland Revenue's holding account on the 15th day of the month in which the deduction is made by the employer. Employer contributions are treated as received on the first day of the month in which the money is actually received by Inland Revenue. These approaches result in the under and over payment of interest on employee contributions and the underpayment of interest on employer contributions.

17. As part of the payday filing reforms, outlined above in paragraph 10, Inland Revenue will receive employment income sooner after an employee's payday (this information would include KiwiSaver employee and employer contribution information). Based on the improved information available with payday filing, I propose that interest calculations on KiwiSaver employee contributions held by Inland Revenue should now be calculated from the pay date the employer has reported. If the proposal to guarantee employer contributions is agreed to, it is also proposed that interest on employer contributions is calculated from the member's payday. If a guarantee of employer contributions was not introduced, it would not be appropriate to commence interest calculations on these amounts from the member's payday. Under current settings, as employer contributions can only be passed to scheme providers when the amount has been received, if interest was calculated from a member's payday and there was delay in the contribution amount being received by Inland Revenue, this would create a risk that Inland Revenue would be required to pay interest on contributions for significant periods of time.

Reducing the KiwiSaver provisional period

18. When automatically enrolled in KiwiSaver, members are provisionally allocated to a default KiwiSaver scheme provider. If the member does not make an active choice to join a different KiwiSaver scheme within their first 3-months of membership, they will be treated as having offered to become a member of the default scheme to which they were provisionally allocated. This 3-month period is referred to as the provisional period and is distinct from the KiwiSaver opt-out period (which is between weeks 2-8 after a person is automatically enrolled in KiwiSaver).

19. Inland Revenue does not transfer the member's contributions to scheme providers until the end of the 3-month provisional period, meaning providers are unaware they have been allocated the member during this period. A consequence of this is providers are unable to contact these members until 3-months after they are enrolled

in KiwiSaver. Feedback from KiwiSaver scheme providers indicates by this time these members (who will be default allocated to a conservative fund type) have often become disengaged about decisions relating to KiwiSaver investment options.

20. I recommend the provisional period be reduced from 3-months to 2-months. This would allow KiwiSaver scheme providers to engage with members about investment options earlier, while retaining a 2-month provisional period would ensure that members wanting to actively choose a scheme still had the option to do so.

21. Reducing the provisional period from 3-months to 2-months, would mean that the period Inland Revenue would be required to hold members' initial KiwiSaver contributions could also be reduced from 3-months to 2-months. As a result, member's contributions would be invested with scheme providers sooner and the amount of interest on initial contributions paid by Inland Revenue would also reduce. Members would still have the opportunity to transfer between schemes after the provisional period ended.

Timeframe for transfer of member's information and funds to new scheme provider

22. When a KiwiSaver member decides to transfer schemes, the new scheme is required to notify the member's old scheme about the transfer. Arrangements with default KiwiSaver scheme providers require them to transfer information they hold on the member and the member's funds to the new scheme within 10-days. However, for non-default schemes the KiwiSaver Act 2006 provides that they have 35-days to fulfil this transfer process. I propose that this transfer period should be reduced to 10-days for all KiwiSaver schemes. Reducing the legislatively mandated period to 10-days would align timeframes for the transfer of information across all KiwiSaver scheme providers.

Changing employee contribution rates

23. Currently, members can only change their employee contribution rate by giving notice to their employer. However, employers may not be members' first point of contact on matters relating to their KiwiSaver account – this will often be their KiwiSaver scheme provider or Inland Revenue. This includes when members are considering what rate they should be contributing at to achieve their preferred retirement savings outcomes.

24. As contribution rate change applications cannot be made through a scheme provider or Inland Revenue this imposes unnecessary compliance costs on members (following a discussion with their scheme provider or Inland Revenue members would then have to contact their employer to change rates). These compliance costs may mean members will not follow through on contribution rate changes, that would have been in their financial interests.

25. I recommend, that in addition to existing processes, members should be able to change their contribution rate through their KiwiSaver scheme provider or Inland Revenue.

KiwiSaver invalid enrolments – residence grace period

26. Where a person who does not meet all the KiwiSaver enrolment criteria has been incorrectly enrolled, generally the KiwiSaver invalid enrolment rules apply and the person's membership will be terminated. However, there are some limited exceptions to the invalid enrolment rules. This includes situations where a person does not meet the criteria of being a New Zealand resident when enrolled in KiwiSaver, but gains New Zealand residence in the 3-month period subsequent to their enrolment.

27. This 3-month grace period was intended to reduce compliance costs for members and administrative costs for Inland Revenue, as individuals who became a New Zealand resident during the 3-month period would not have their account closed and then have to re-enrol again soon after (when they did meet the membership criteria).

28. However, in practice members who are invalidly enrolled on the basis of the residence ground, will not become a New Zealand resident within the requisite 3-month grace period. For example, non-residents enrolled in KiwiSaver are often individuals with temporary work visas, who have no intention of becoming New Zealand residents in the short-term. Being required to keep these accounts active during the 3-month grace period imposes an additional administrative burden on Inland Revenue and there is no benefit to the member (as their account will be closed at the end of the 3-month period).

29. As it has not operated as intended, I recommend the 3-month grace period for an individual to gain New Zealand resident status after being invalidly enrolled in KiwiSaver be removed. When a person does not meet the New Zealand resident requirement their account would immediately be closed, and they would have the opportunity to open a new account on gaining New Zealand residence. This would help ensure a consistent approach was adopted for people who were incorrectly enrolled in KiwiSaver.

KiwiSaver income and ESCT rate information

30. As part of the KiwiSaver on-boarding process, employers are required to provide Inland Revenue with information about new employees who have been automatically enrolled in KiwiSaver or existing employees opting-in to the scheme (this includes their personal information and IRD number).

31. To improve Inland Revenue's ability to ensure that KiwiSaver members are receiving the correct KiwiSaver contribution amounts and that these amounts are being taxed at the correct rate, I propose that employers should also provide the following information to Inland Revenue about new employees or existing employees where this information has changed:

    31.1 any difference between an employee's income for PAYE purposes and their income for the purpose of calculating KiwiSaver contributions (some amounts that are treated as income for PAYE are exempt from the definition of KiwiSaver salary and wages); and

    31.2 the employee's employer superannuation contribution tax (ESCT) rate.

32. Under current settings (where Inland Revenue is not provided with this information), if it appears amounts received from an employer may be incorrect, Inland Revenue will contact the employer to obtain this information. This imposes compliance costs on Inland Revenue and the employer. As it can take up to six weeks for contact to be made, where the employer has undercalculated the amount, this can also mean the employer will be subject to penalties. If this information was already provided by the employer, the number of contacts would decrease. Inland Revenue would also be able to be more accurate and efficient in detecting potential miscalculation of contributions and ESCT amounts. This would help ensure that member's savings were not impacted due to miscalculations and employers would be less likely to be subject to penalties.

33. To accurately calculate a member's contributions and deduct the correct amount of tax from employer contributions, employers already need to hold information on an employee's ESCT rate and their KiwiSaver salary and wage income. Therefore, the only change would be that employers would now be required to communicate this information to Inland Revenue. It is expected that any compliance costs associated with doing so would be minimal.

34. For new employees this information would be provided as part of the existing KiwiSaver new employee process. It is expected that updates to this information for existing employees would be infrequent (and would be provided using the same form as is used for new employees). Consistent with PAYE tax, members are subject to the same ESCT rate for the full income tax year, so this information would be provided once a year (or less frequently if the employee stayed on the same rate). And any differences between income for PAYE purposes and for KiwiSaver purposes, generally do not change during the course of an employment relationship (some examples of amounts not treated as income for KiwiSaver purposes include the value of accommodation, a benefit from an employer share scheme or a redundancy payment).

Consultation

35. The Treasury and the Ministry of Business, Innovation and Employment have been consulted on this paper. The Financial Markets Authority and KiwiSaver scheme providers have also been consulted on the proposals and support them.

Financial Implications

Guarantee of employer contributions

36. Introducing the guarantee is not expected to have an additional impact on the operating balance. Inland Revenue already recognise an expense for any write-offs and impairment in relation to KiwiSaver employer contributions - for the fiscal year ending 30 June 2018 the write-off was $2.6 million (including interest and penalties). This is because the KiwiSaver employer contributions are currently treated as a receivable asset until paid, which is the same treatment as all other taxes and payments collected by Inland Revenue. The only change is that there may be a cash impact to the Crown if the receivable is uncollected, which would impact on net core Crown debt.

37. Employer contributions would be treated as public money for the purposes of the Public Finance Act 1989, to enable the transfer of employer contributions to scheme

providers prior to Inland Revenue receiving the contributions. Public money requires a permanent legislative authority, which is currently provided for in the KiwiSaver Act 2006 in respect of employee contributions only. If a guarantee of employer contributions is agreed to, this would need to be extended to employer contributions.

38. A single appropriation would be established for both employer and employee contributions to report public money spending. The Public Finance Act 1989 requires a permanent legislative authority to be managed and accounted for in the same way as an annual appropriation. Currently, there is no appropriation covering amounts of employee contributions paid out of public money. This new appropriation will be reported on in the 2019/20 Supplementary Estimates.

39. The KiwiSaver Act 2006 will also be amended so that the permanent legislative authority only applies to KiwiSaver contributions passed by Inland Revenue to KiwiSaver scheme providers from public money, not to the total amount of employee and employer contributions Inland Revenue passes to KiwiSaver scheme providers.

Other proposals

40. Financial implications related to aligning the calculation of interest on employee contributions with a member's payday would be expected to be negligible, as current over and under payments of interest should broadly offset. Calculating interest on employer contributions from a member's payday would increase interest payable. However, this would be more than offset by the faster transfer of employer contributions to scheme providers, resulting in an overall reduction in KiwiSaver interest payable of under $400,000 per year.

41. As the proposal to reduce the provisional period from 3-months to 2-months would allow Inland Revenue to pass initial employee and employer contributions to scheme providers a month earlier, this would reduce the amount of KiwiSaver interest payable by Inland Revenue by under $100,000 per year.

42. No other proposals in this paper are expected to have financial implications.

Compliance and Administrative implications

43. Although the proposals would improve the efficiency of Inland Revenue's administration of KiwiSaver and reduce compliance costs for KiwiSaver members, the changes would require communication to employers, KiwiSaver scheme providers, and some staff training. There would also need to be updates to public communications material.

44. The proposals would be phased in so that system changes are aligned with Inland Revenue's Business Transformation timelines which would improve efficiency. This would mean the proposals would apply from 1 April 2020, to align with the transfer of KiwiSaver into its new administrative system (START).

Legislative Implications

45. Implementing these proposals would require changes to the KiwiSaver Act 2006.

46. If approved, I propose including the legislative changes resulting from these recommendations in the next omnibus taxation Bill scheduled for introduction in mid-2019.

Impact Analysis

47. The Quality Assurance reviewer at Inland Revenue has reviewed the *Business Transformation related KiwiSaver refinements* RIA prepared by Inland Revenue, and considers that the information and analysis summarised in the RIA meets the quality assurance criteria.

Human Rights

48. The changes I am recommending in this paper are not inconsistent with the New Zealand Bill of Rights Act 1990 or the Human Rights Act 1993.

Gender Implications

49. There are no gender implications arising from the proposals in this paper.

Disability Perspective

50. The proposals do not affect people with disabilities any differently.

Publicity

51. I will make an announcement on the contents of the proposed omnibus taxation Bill, including these proposals, when the Bill is introduced in mid-2019. A commentary on the Bill will also be released at this time. Inland Revenue will include details of the new legislation in a *Tax Information Bulletin* after the Bill is enacted.

Proactive Release

52. I propose to delay the proactive release of this Cabinet paper in full and associated minutes until the introduction of the proposed omnibus taxation Bill, which necessary legislative changes to give effect to these changes will be included in. The expected introduction date for this Bill is mid-2019.

Recommendations

The Minister of Revenue recommends that the Cabinet Economic Development Committee:

Guarantee of employer contributions

1. **agree** to Inland Revenue paying an amount of employer contribution out of public money to a KiwiSaver scheme provider in advance of the contribution amount being received, but where an employer has filed information with Inland Revenue that an employer contribution has been made.

2. **note** that an appropriation is required to make such payments out of public money.

3. **agree** to establish a permanent legislative authority enabling Inland Revenue to transfer employer contribution amounts to KiwiSaver scheme providers before the contribution amount has been received.

4. **agree**, that if you agree to recommendation 3, to combine the permanent legislative authority established under that recommendation with the existing permanent legislative authority in section 73(3) of the KiwiSaver Act 2006 (which applies to the

transfer of employee contributions to KiwiSaver scheme providers) into a single permanent legislative authority.

5. **agree** to provide in the KiwiSaver Act 2006 that the reporting required under section 11(2) of the Public Finance Act 1989 in respect of the permanent legislative authority in recommendation 4 be limited to the amount of KiwiSaver contributions paid by Inland Revenue to KiwiSaver scheme providers in advance of contribution amounts being received from employers (not the total amount of employee and employer contributions Inland Revenue pays to KiwiSaver scheme providers).

6. **agree** that the legislative implications of the proposed change in recommendations 1-5 be included in amendments to the KiwiSaver Act 2006**.**

7. **agree** that**,** provided the necessary legislative amendments have been passed and come into force, the financial implications associated with the proposed change in recommendations 1-5 be included in the 2019/20 Supplementary Estimates.

Other changes

8. **agree**, that if you agree to recommendation 1, to interest calculations on employer contributions held by Inland Revenue commencing from the pay date a member's employer has reported.

9. **agree** to interest calculations on employee contributions held by Inland Revenue, commencing from the pay date a member's employer has reported.

10. **agree** to reduce the provisional period (that applies to members who are automatically enrolled in KiwiSaver) from 3-months to 2-months.

11. **agree**, that if you agree to recommendation 10, to the period that Inland Revenue must hold initial KiwiSaver employee and employer contributions being reduced from 3-months to 2-months.

12. **agree** to the period a scheme provider has to share member information and transfer funds to a new provider when a member transfers schemes being reduced from 35-days to 10-days.

13. **agree** to KiwiSaver members being able to change contribution rates through their scheme provider or Inland Revenue (in addition to their employer).

14. **agree** to the removal of the 3-month grace period, for people who were incorrectly enrolled in KiwiSaver, to gain New Zealand residence.

15. **agree** to employers providing the following information to Inland Revenue about new employees and existing employees where this information has changed:

    15.1 the income amount members' contributions are calculated from; and

    15.2 an employee's employer superannuation contribution tax (ESCT) rate.

Legislative vehicle

16. **agree** that legislation to give effect to the changes recommended in this paper be included in the next taxation omnibus Bill for 2019.

17. **invite** the Minister of Revenue to instruct Inland Revenue to draft the necessary amendments to give effect to the changes recommended in this paper.

Authorised for lodgement

Hon Stuart Nash
Minister of Revenue

Impact Summary: Business Transformation related KiwiSaver refinements

Section 1: General information

Purpose
Inland Revenue is solely responsible for the analysis and advice set out in this Regulatory Impact Statement, except as otherwise explicitly indicated. This analysis and advice has been produced for the purpose of informing final decisions to proceed with policy changes to be taken by or on behalf of Cabinet.

Key Limitations or Constraints on Analysis

Timing

To maximise the administrative efficiencies of the proposals, changes need to align with Inland Revenue's Business Transformation timelines for transferring KiwiSaver into its new administrative system. KiwiSaver is scheduled to be transferred into START on 1 April 2020.

To ensure that policy decisions are taken, and legislation passed in this timeframe, this has created a constraint on the time available to analyse options. Despite this, officials are confident that the proposed approach would be the most effective option to address the problem definition.

Consultation and testing

Inland Revenue has undertaken targeted consultation with KiwiSaver scheme providers. However, as a result of time constraints, wider public consultation has not been carried out. Due to the largely technical administrative nature of the changes proposed, they are unlikely to have generated public interest. Moreover, taken as a whole, the package of options proposed would be beneficial to KiwiSaver members.

There would be some compliance costs for employers, although these are expected to be small (they would be required to communicate information that they already hold to Inland Revenue, on a one-off or infrequent basis). While not consulted on directly, the RIA has been informed by employer feedback generated as part of public consultation undertaken on similar requirements that were introduced as part of the wider Business Transformation work programme.

Assumptions underpinning impact analysis

In relation the proposal to guarantee employer contributions, additional funding is not expected to be required. The primary caveat to this is that it assumes static behaviour. If the introduction of the proposal created a behavioural change amongst employers (that is it results in more unpaid employer contributions), this would increase the fiscal cost of the proposed approach. However, given that levels of employer contribution debt are currently comparable to levels of employee contribution debt (which are already guaranteed), this suggests that the proposal should not have a significant impact on employer's behaviour.

Responsible Manager (signature and date):
Chris Gillion Policy Manager Policy and Strategy Inland Revenue 1 March 2019

Section 2: Problem definition and objectives

2.1 What is the policy problem or opportunity?
As part of Inland Revenue's Business Transformation programme, the administration of KiwiSaver is scheduled to be transferred from its current system to its new administration system on 1 April 2020. This provides an opportunity to make refinements to KiwiSaver settings to improve administrative efficiency and enhance members' experience with the scheme. The following are areas that would assist in achieving these outcomes: • facilitating the faster transfer of contributions from Inland Revenue to KiwiSaver scheme providers (and between scheme providers); and • improving information flows between members, employers, scheme providers and Inland Revenue. **Transfer of contributions** Part of Inland Revenue's role as the central administrator for KiwiSaver, involves receiving KiwiSaver employer and employee contributions from employers and then forwarding these contributions on to KiwiSaver scheme providers. A reduction in the time taken to transfer contributions would improve the efficiency of the central administration of KiwiSaver. Payday filing reforms, which become compulsory from 1 April 2019, will result in Inland Revenue having employer information sooner after a payday (within 2 days of a payday for large employers and with 10 days for smaller employers). This will include information about KiwiSaver employee and employer contributions. The reforms will allow KiwiSaver employee contributions to be passed to scheme providers sooner after a member's payday. This is because current KiwiSaver settings permit the use of Crown funds to pay employee contributions to scheme providers before contribution amounts have been paid to Inland Revenue by employers (effectively creating a Government guarantee of employee contributions). This Government guarantee does not currently extend to employer contributions. To ensure that the benefits of Inland Revenue being in receipt of earlier payday information are fully realised in relation to KiwiSaver, this RIA considers how to enable Inland Revenue to forward employer contribution amounts to scheme providers as soon as payday reporting information from employers has been received, rather than having to wait until the employer has actually paid the amount of the contribution to Inland Revenue (the current state). This RIA also considers other refinements that would facilitate the faster transfer of contributions. **Improving information flows** Inland Revenue is in the unique position of having on-going contact with KiwiSaver scheme providers and employers. This means Inland Revenue is able to facilitate the flow of information between relevant KiwiSaver parties (employers, providers and members) and also should have access to information to ensure that members are receiving the correct KiwiSaver contribution entitlements.

Currently, in some instances, Inland Revenue does not have access to sufficient information to effectively police the accuracy of contribution amounts received from employers. For example, Inland Revenue does not receive information from employers about the employer superannuation contribution (ESCT) rates they are taxing employees at (ESCT is the tax payable on employer contribution amounts). However, based on ESCT amounts paid to Inland Revenue, potentially up to 63% of employers could be incorrectly calculating their employees' ESCT rate.[1]

This RIA considers refinements that could be made to improve existing KiwiSaver information flows, to help ensure that KiwiSaver members are receiving their correct contribution entitlements. Consideration is also given to how information flows could be utilised to give members increased flexibility (for example whether the application process for changing an employee contribution rate could be simplified for members).

2.2 Who is affected and how?

KiwiSaver members

Taken as a whole, KiwiSaver members would benefit from the package of proposals – the changes would result in them earning market investment returns on contributions sooner, help ensure they are receiving the correct contribution amounts and give them additional flexibility in respect of how they can change their contribution rate.

KiwiSaver scheme providers

KiwiSaver scheme providers would benefit from the faster transfer of contributions, as it would result in them having more funds under management. Schemes have also indicated enabling KiwiSaver contribution rates to be changed through providers, would enhance member-provider relationships.

Employers

Helping to ensure members are receiving correct contribution amounts, would result in employers being required to communicate some additional information they should already hold to Inland Revenue. Employers would not be directly affected by any other proposals.

Inland Revenue

The proposals would enhance Inland Revenue's central administration of KiwiSaver and create administrative savings. As implementation of the proposals would be aligned with Business Transformation, there would be no additional implementation costs.

[1] Figure based on analysis of early adopters of payday filing reforms for the month of June 2018.

2.3 Are there any constraints on the scope for decision making?
There are no constraints on the scope for decision making.

Section 3: Options identification

3.1 What options have been considered?

The following criteria were used to assess the options considered:

- *Compliance*: compliance costs should be minimised as far as possible.
- *Administration*: administrative costs should be minimised as far as possible.
- *Equity*: the option should ensure that KiwiSaver members are receiving the correct contribution amounts.
- *Sustainability*: the option should be consistent with wider KiwiSaver settings.

Option One: Status quo

Administration: The status quo would not reduce administrative costs.

Compliance: The status quo would not reduce compliance costs.

Equity: The status quo results in some KiwiSaver members not receiving employer contributions that other members are receiving (as a result of employers not paying the correct contribution amounts or not paying employer contribution amounts at all).

Sustainability: As far as practical, the KiwiSaver regime settings are intended to facilitate administrative efficiency. The problem definition identifies that there are some aspects of the regime that would be more efficient if subject to further refinements.

Option Two: build on payday filing reforms

This option would build on the improved information available through payday filing reforms to facilitate the faster transfer of employer contributions to scheme providers and to improve the accuracy of contribution entitlements passed to scheme providers. Specifically, it would involve passing employer contribution amounts to scheme providers based on payday information received by employers, before Inland Revenue had received the contribution amount (essentially a Government guarantee, that would align with the existing treatment of employee contributions). Based on the improved information received through payday filing, this option would also align the commencement of interest paid while contributions are held by Inland Revenue with a member's payday.[2]

Administration: This option would increase administrative efficiency, as employer contributions could be passed to scheme providers sooners. However, as it does not include other administrative enhancements to KiwiSaver, savings may not be maximised.

Compliance: This option should make it easier for members to reconcile the amounts in their KiwiSaver accounts with the KiwiSaver contributions recorded on their payslips (as employer contributions would be passed in full to KiwiSaver providers sooner after the member payday). Consequently, this should also reduce the level of contacts from members to scheme providers.

Equity: This option would ensure that all KiwiSaver members receive the employer

[2] Currently, interest on employee contributions commences on the 15th of the month the amount was deducted from the member's salary or wages and interest on employer contributions commences on the 1st of the month the contribution amount was paid to Inland Revenue.

contributions amounts they are entitled to. It would also improve the accuracy of interest paid on contributions by Inland Revenue (the current rules result in under and over payment of interest on employee contributions and under payment of interest on employer contributions). However, this option would not address situations where a member's employer is incorrectly calculating contributions amounts.

Sustainability: This option would ensure that the benefit of information obtained via payday filing reforms were fully utilised in the KiwiSaver context. It would also align the treatment of employer contributions with employee contributions and other PAYE deductions (which are guaranteed).

Option Three: Additional transfer, information and administrative refinements

In addition to the changes proposed under option 2, this option would use the opportunity created by Business Transformation, to make further refinements to KiwiSaver settings.

Refinements aimed at facilitating faster transfers would be to reduce the initial KiwiSaver provisional period from 3-months to 2-months (this would mean initial contributions could be transferred to providers a month earlier) and to reduce the period schemes have to send funds and member information, when a member decides to transfer to a new scheme from 35 to 10 days. The later change would only impact non-default providers, as arrangements with default providers already require them to complete transfers in 10-days.

Information flows would be utilised to ensure members were receiving their correct contribution amounts, by requiring employers to provide information to Inland Revenue about the income KiwiSaver contributions have been calculated from[3] and the ESCT rate used. This information would be provided in respect of new employees and existing employees where the information had changed. To recognise that members will have different first points of contact for information on their KiwiSaver account, this option also proposes that members should be able to apply to change their contribution rate through their scheme provider or Inland Revenue (in addition to their employer).

As a further administrative refinement, is also proposed that the 3-month grace period – that a person who has been incorrectly enrolled in KiwiSaver has to gain New Zealand residence before their account is shut – be removed. This period has not operated as intended and is not utilised by members.

The below analysis of this option against the assessment criteria, identifies impacts that are additional to those set out in the analysis of option 2 above.

Administration: Reducing the provisional period and the removing the 3-month grace period would increase administrative efficiency.

Compliance: The option would reduce compliance costs for members looking to change contribution rates. There would be some additional compliance costs for scheme providers and employers (relating to the proposals to reduce the period schemes have to send funds and information to a new provider when a member transfers schemes and the additional employer information requirements, respectively). These compliance costs are expected to

[3] Some amounts that are treated as income for PAYE are exempt for the purposes of calculating KiwiSaver contribution amounts. Examples includes the value of accommodation and a benefit from an employer share scheme.

be small.

Equity: The additional employer information should make it easier for Inland Revenue to identify situations where contribution amounts have been calculated or taxed incorrectly. Based on this information it would be possible to follow-up with employers, so these issues could be resolved sooner and would not arise again.

Sustainability: This option identifies enhancements to KiwiSaver administrative settings in addition to the changes proposed in option 2 – to maximise improvements to KiwiSaver it would be logical to implement all changes. Implementing a package of changes is also more sustainable in terms of the legislation (as opposed to making singular refinements to KiwiSaver legislative settings on an on-going basis).

Other options not considered

Aligning payment of KiwiSaver contributions with an employee's payday

As part of the work on the payday filing reforms, consideration was given to the option of employers being required to pay PAYE and other deductions from salary or wages (including KiwiSaver employee and employer contributions) to Inland Revenue to align with an employee's payday. If employers were required to pay KiwiSaver contribution amounts to Inland Revenue sooner after their employees' payday, this would facilitate the faster transfer of these contributions to scheme providers.

However, the decision was made only to require employers to file information sooner after a member's payday, as feedback from employers was that requiring them to pay the actual monetary amounts of deductions (including KiwiSaver contributions) in a shorter timeframe would be too onerous comply with.

3.2 Which of these options is the proposed approach?
The proposed approach is option 3. This package of refinements is comprised of the following proposals: • the Crown funding the payment of employer contribution amounts passed to KiwiSaver scheme providers until these amounts are received from the employer (essentially a Government guarantee of employer contributions); • changing the date the calculation of interest on employer and employee contributions commences, to align with the pay date a member's employer has reported; • reducing the KiwiSaver provisional period from 3-months to 2-months; • reducing the maximum period an old scheme provider has to share information and transfer funds to a new provider when a member transfers schemes, from 35-days to 10-days; • allowing members to change contribution rates through their scheme provider or Inland Revenue, rather than only through their employer; • removing the 3-month grace period for members who have been incorrectly automatically enrolled in KiwiSaver, to gain New Zealand residence; and • requiring employers to provide Inland Revenue with KiwiSaver information about a member's employer superannuation contribution tax rate and the income their contributions are calculated from. Of the options considered this package would be most effective in facilitating the faster transfer of contributions to (and between) KiwiSaver scheme providers, and reducing on-going administrative costs for Inland Revenue. It is also the most coherent and equitable option for KiwiSaver members as it will help ensure members are receiving the correct contribution amounts and these contribution entitlements are being passed to scheme providers. The proposed approach is not incompatible with the Government's '*Expectations for the design of regulatory systems*'.

Section 4: Impact Analysis (Proposed approach)

4.1 Summary table of costs and benefits

Affected parties	Comment	Impact
Additional costs of proposed approach, compared to taking no action		
Regulated parties (*KiwiSaver members, scheme providers and employers*)	*KiwiSaver members* Aligning KiwiSaver interest payments to a member's payday would result in a reduction in interest paid on employee contributions for some members with paydays after the 15th of the month. The impact of this would be small given interest is paid at a rate of 0.91% per annum and would be offset by their contributions earning market investment returns sooner and an increase in interest on employer contributions in many cases.[4]	Low.
	Scheme providers Reducing the time scheme providers have to send members' information and funds to a new provider in scheme transfer situations from 35-days to 10-days would have compliance costs for non-default providers, who are not already required to comply with the 10-day transfer time. Feedback from providers indicates this would be manageable and would align with industry best practice.	Low.
	Employers Employers would need to provide information on KiwiSaver income and employee's ESCT rates to Inland Revenue. Compliance costs should be small, as employers would already need to hold this information to accurately calculate contribution amounts and the information would only need to be provided about new employees or existing employees where the	Low.

[4] A decrease in interest payable on employee contributions would be expected to be offset by an increase in interest on employer contributions for employees with a payday between the 15th and 23rd of the month.

	information has changed. For new employees the information would be provided as part of employee on-boarding processes and it is expected that updates to this information for existing employees would be infrequent.[5]	
Regulators (*Inland Revenue*)	The proposals do not require additional funding. Inland Revenue already writes-off amounts of unpaid employer contributions. For the financial year ending 30 June 2018 the write-off of employer contributions was $2.6 million. The only change would be Inland Revenue would pass on contribution amounts to scheme providers, in addition to writing them off. System changes to implement the proposals would be absorbed as part of Business Transformation baselines.	Nil.
Wider government	None identified.	Nil.
Other parties	None identified.	Nil.
Total Monetised Cost		Nil.
Non-monetised costs		*Low.*

Expected benefits of proposed approach, compared to taking no action		
Regulated parties (*KiwiSaver members, scheme providers and employers*)	*KiwiSaver members* The package of proposals would have a number of benefits for members. It would result in members earning market investment returns sooner, mean their savings are with their scheme of choice sooner in transfer situations, help ensure they are receiving the correct contribution entitlements (including addressing current interest underpayment issues) and give them additional flexibility in respect of how a contribution rate change can be made. *Scheme providers* The proposals would result in	Medium. Medium.

[5] Differences between amounts treated as income for PAYE purposes and amounts treated as income for KiwiSaver purposes generally do not change over the course of an employment relationship and ESCT rates apply for the full income tax year (and employees' rates will not change each year).

	contributions being transferred to scheme providers sooner (from Inland Revenue and potentially from other schemes not currently subject to the 10-day transfer rule), which would increase the funds under their management and fees chargeable. *Employers* Most of the changes would not directly impact employers. The additional employer information requirements may reduce employer contact time with Inland Revenue. (Currently, where it appears employers may have calculated contributions incorrectly, Inland Revenue will contact the employer to obtain the relevant information).	Low.
Regulators (*Inland Revenue*)	The package of proposals would increase the efficiency of Inland Revenue's administration of KiwiSaver and create on-going administrative savings. The faster transfer of employer contributions to KiwiSaver providers and reduction of the holding period for initial contributions would decrease KiwiSaver interest payable by Inland Revenue.	Medium (the proposal to guarantee employer contributions would result in an estimated $260,000 in savings per annum). Under $500,000 per annum.[6]
Wider government	None identified.	Nil.
Other parties	None identified.	Nil.
Total Monetised Benefit		$760,000.
Non-monetised benefits		*Medium.*

[6] This savings is after the reduction in interest payable due to faster transfer of employer contributions to scheme providers has been offset by the increase in interest payable on employer contributions with interest calculations commencing from a member's payday. Costs associated with calculating employee contributions from a payday would be negligible (as current under and over payments would broadly offset).

4.2 What other impacts is this approach likely to have?
There is the potential that the proposal to guarantee employer contributions could have a behavioural impact on employers - that is employer's may be less likely to pay employer contributions. (While only $2.6 million in employer contribution debt was written-off for the financial year ending 30 June 2018, approximately $2 billion in employer contributions were passed to KiwiSaver scheme providers during this same year). Current levels of employer and employee contribution debt are broadly comparable (as at 30 June 2018, employer contribution debt since the commencement of KiwiSaver was $18 million, while employee contribution debt was $24 million). This suggests that the existing guarantee of employee contributions has had limited behavioural impact on employers and that introducing a guarantee of employer contributions would also have a minimal behavioural impact. Moreover, Inland Revenue has processes to monitor and recover unpaid amounts of employer contributions from employers, which would remain in place after the introduction of this proposal. These include interest and penalties available under the Tax Administration Act 1994.

Section 5: Stakeholder views

5.1 What do stakeholders think about the problem and the proposed solution?
The Ministry of Business Innovation and Employment and the Treasury have been consulted on the proposals and support them. The proposals also reflect feedback on the operation of the KiwiSaver regime from the Financial Markets Authority. Inland Revenue has undertaken targeted consultation with KiwiSaver scheme providers (in the form of Business Transformation focused co-design workshops). Providers are supportive of the proposals. General consultation with KiwiSaver members has not been undertaken. On a whole, the package of changes should be beneficial for KiwiSaver members and given the technical nature of the proposed changes, they are unlikely to have generated public interest. The only proposal to directly impact employers would be for them to communicate to Inland Revenue the income amounts a member's KiwiSaver contributions are calculated from and the member's ESCT rate. This is information the employer already needs to hold, and they would only be required to provide it to Inland Revenue in relation to new employees or existing employees where the information has changed. While consultation with employers has not been carried out on these specific requirements, the proposal has been informed by the extensive public consultation that has been undertaken as part of the wider Business Transformation programme. In particular, feedback on the discussion document *Making Tax Simpler – Better administration of PAYE and GST: a Government discussion document* which was released in November 2015 and sought feedback on the payday filing reforms. This included, proposals aimed at refining the new employee on-boarding process, by merging PAYE and KiwiSaver reporting requirements and requiring employers to provide Inland Revenue with additional information about new employees – such as date of birth and other employee details. Although not universally supported, in consultation these new information requirements received majority support from employers. The additional

information requirements proposed in this RIA, would support the shifts in employee on-boarding processes.

Before the proposals are implemented there will be the opportunity for public consultation, as employers and KiwiSaver members would be able to make submissions on the omnibus taxation Bill the legislative changes are included in.

Section 6: Implementation and operation

6.1 How will the new arrangements be given effect?
The proposals would require amendment to the KiwiSaver Act 2006. Amendments would be included in the next available omnibus taxation Bill. To align with the transfer of the administration of KiwiSaver from its current operating system into its new operating system, the changes would come into effect from 1 April 2020. The Minister of Revenue would make an announcement, on the contents of the proposed omnibus taxation Bill (including these proposals) when it is introduced in the House. Inland Revenue would be responsible for the on-going administration of the new arrangements. Aligning implementation of the proposals with Inland Revenue's Business Transformation programme, would mean the cost of system changes would be absorbed into Business Transformation.

Section 7: Monitoring, evaluation and review

7.1 How will the impact of the new arrangements be monitored?
Inland Revenue would monitor the outcomes of the proposals pursuant to the Generic Tax Policy Process (GTTP) to confirm that they match the policy objectives. Inland Revenue collects KiwiSaver data which could be used to assess the effectiveness of the changes in facilitating the faster transfer of employer contributions and enhancing information flows.

7.2 When and how will the new arrangements be reviewed?
No formal review is planned. However, the final step in the GTTP is the implementation and review stage, which involves post-implementation review of legislation, and the identification of remedial issues. Post-implementation review is expected to occur around 12 months after implementation. All KiwiSaver scheme providers have an on-going relationship with Inland Revenue, which includes an annual meeting to discuss policy and operational issues that have arisen over the past year. This would provide an opportunity for scheme providers to give feedback about the effectiveness of the proposed approach.

DEV-19-MIN-0038.01

Cabinet Economic Development Committee

Minute of Decision

Business Transformation: KiwiSaver Changes for Inclusion in the Next Omnibus Taxation Bill

Portfolio **Revenue**

On 20 March 2019, the Cabinet Economic Development Committee:

Payment of employer contributions

1 **agreed** that Inland Revenue pay an amount of employer contribution out of public money to a KiwiSaver scheme provider in advance of the contribution amount being received, but where an employer has filed information with Inland Revenue that an employer contribution has been made;

2 **noted** that an appropriation is required to make such payments out of public money;

3 **agreed** to establish a permanent legislative authority enabling Inland Revenue to transfer employer contribution amounts to KiwiSaver scheme providers before the contribution amount has been received;

4 **agreed** to combine the permanent legislative authority with the existing permanent legislative authority in section 73(3) of the KiwiSaver Act 2006 (which applies to the transfer of employee contributions to KiwiSaver scheme providers) into a single permanent legislative authority;

5 **agreed** that the reporting required under section 11(2) of the Public Finance Act 1989 in respect of the permanent legislative authority be limited to the amount of KiwiSaver contributions paid by Inland Revenue to KiwiSaver scheme providers in advance of contribution amounts being received from employers (not the total amount of employee and employer contributions Inland Revenue pays to KiwiSaver scheme providers);

6 **agreed** that the legislative implications of the proposals in paragraphs 1-5 above be included in amendments to the KiwiSaver Act 2006;

7 **agreed** that, provided the necessary legislative amendments have been passed and come into force, the financial implications associated with the above proposals be included in the 2019/20 Supplementary Estimates;

Other changes

8 **agreed** that interest calculations on employer contributions held by Inland Revenue commence from the pay date a member’s employer has reported;

9 **agreed** that interest calculations on employee contributions held by Inland Revenue commence from the pay date a member's employer has reported;

10 **agree**d that the provisional period (that applies to members who are automatically enrolled in KiwiSaver) be reduced from three months to two months;

11 **agreed** that the period that Inland Revenue must hold initial KiwiSaver employee and employer contributions be reduced from three months to two months;

12 **agreed** that the period a scheme provider has to share member information and transfer funds to a new provider when a member transfers schemes be reduced from 35 days to 10 days;

13 **agreed** that KiwiSaver members be able to change contribution rates through their scheme provider or Inland Revenue (in addition to their employer);

14 **agreed** to the removal of the three-month grace period, for people who were incorrectly enrolled in KiwiSaver, to gain New Zealand residence;

15 **agreed** that employers be required to provide the following information to Inland Revenue about new employees and existing employees where this information has changed:

15.1 the income amount members' contributions are calculated from; and

15.2 an employee's employer superannuation contribution tax (ESCT) rate;

Legislative implications

16 **agreed** that the above proposals be included in the next omnibus taxation bill, which is scheduled for introduction in mid-2019;

17 **invited** the Minister of Revenue to issue drafting instructions to Inland Revenue to give effect to the above proposals.

Janine Harvey
Committee Secretary

Present:
Hon Kelvin Davis
Hon Phil Twyford
Hon Chris Hipkins
Hon David Parker (Chair)
Hon Nanaia Mahuta
Hon Stuart Nash
Hon Damien O'Connor
Hon Tracey Martin
Hon Willie Jackson
Hon James Shaw
Hon Eugenie Sage

Officials present from:
Office of the Prime Minister
Officials Committee for DEV

Hard-copy distribution:
Minister of Revenue