# Hon Stuart Nash, Minister of Revenue

## Information Release

## PIE, KiwiSaver, and student loan changes made to the Taxation (KiwiSaver, Student Loans, and Remedial Matters) Bill

## January 2020

### Availability

This information release is available on Inland Revenue's Tax Policy website at http://taxpolicy.ird.govt.nz/publications/2020-ir-cab-dev-19-sub-0258/overview.

### Documents in this information release

1. IR2019/366 – Tax policy report: Taxation of PIE income: items for inclusion in current tax bill (22 August 2019)
2. IR2019/463 – Tax policy report: Cabinet paper – Changes to the PIE regime, student loan scheme and KiwiSaver for inclusion in current Bill (6 September 2019)
3. DEV-19-SUB-0258 – Cabinet paper: Items for inclusion in the Taxation (KiwiSaver, Student Loans, and Remedial Matters) Bill (25 September 2019), includes three regulatory impact assessments:
   - Changes to the PIE regime (18 September 2019)
   - Business Transformation related KiwiSaver refinements (revised proposal) (12 September 2019)
   - Lowering the student loan repayment threshold for non-salary and wage income and repealing withholding changes for student loan income (18 September 2019)
4. CAB-19-MIN-0500.01 – Minute: Items for inclusion in the Taxation (KiwiSaver, Student Loans, and Remedial Matters) Bill (30 September 2019)

### Additional information

The Cabinet paper was considered by the Cabinet Economic Development Committee on 25 September 2019 and confirmed by Cabinet on 30 September 2019.

Three regulatory impact assessments attached to the Cabinet paper are included in this information release, and are also available separately:

- Changes to the PIE regime (18 September 2019)
- Business Transformation related KiwiSaver refinements (revised proposal) (12 September 2019)
- Lowering the student loan repayment threshold for non-salary and wage income and repealing withholding changes for student loan income (18 September 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

not in scope

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## POLICY AND STRATEGY

**Tax policy report:** **Taxation of PIE income: items for inclusion in current tax bill**

| **Date:** | 22 August 2019 | **Priority:** | High |
|---|---|---|---|
| **Security level:** | In Confidence | **Report number:** | IR2019/366 |

### Action sought

| | **Action sought** | **Deadline** |
|---|---|---|
| Minister of Revenue | **Agree** to recommendations<br>**Refer** a copy of this report to your colleague the Minister of Finance | 3 September 2019 |

### Contact for telephone discussion (if required)

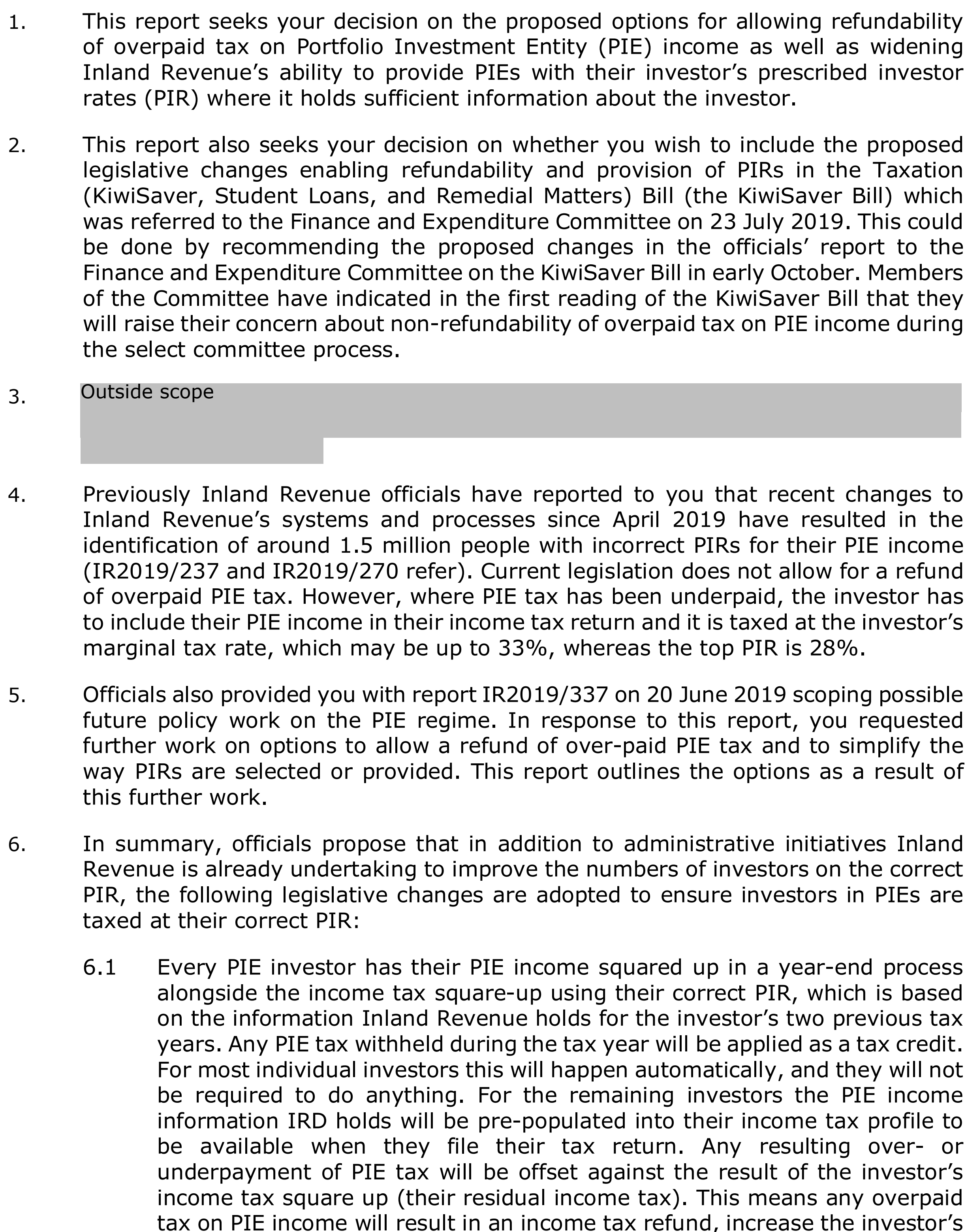
| **Name** | **Position** | **Telephone** |
|---|---|---|
| Paul Young | Policy Team Leader | s 9(2)(a) |
| s 9(2)(a) | Policy Analyst | |

22 August 2019

Minister of Revenue

## Taxation of PIE income: items for inclusion in current tax bill

### Executive summary



1. This report seeks your decision on the proposed options for allowing refundability of overpaid tax on Portfolio Investment Entity (PIE) income as well as widening Inland Revenue's ability to provide PIEs with their investor's prescribed investor rates (PIR) where it holds sufficient information about the investor.

2. This report also seeks your decision on whether you wish to include the proposed legislative changes enabling refundability and provision of PIRs in the Taxation (KiwiSaver, Student Loans, and Remedial Matters) Bill (the KiwiSaver Bill) which was referred to the Finance and Expenditure Committee on 23 July 2019. This could be done by recommending the proposed changes in the officials' report to the Finance and Expenditure Committee on the KiwiSaver Bill in early October. Members of the Committee have indicated in the first reading of the KiwiSaver Bill that they will raise their concern about non-refundability of overpaid tax on PIE income during the select committee process.

3. Outside scope

4. Previously Inland Revenue officials have reported to you that recent changes to Inland Revenue's systems and processes since April 2019 have resulted in the identification of around 1.5 million people with incorrect PIRs for their PIE income (IR2019/237 and IR2019/270 refer). Current legislation does not allow for a refund of overpaid PIE tax. However, where PIE tax has been underpaid, the investor has to include their PIE income in their income tax return and it is taxed at the investor's marginal tax rate, which may be up to 33%, whereas the top PIR is 28%.

5. Officials also provided you with report IR2019/337 on 20 June 2019 scoping possible future policy work on the PIE regime. In response to this report, you requested further work on options to allow a refund of over-paid PIE tax and to simplify the way PIRs are selected or provided. This report outlines the options as a result of this further work.

6. In summary, officials propose that in addition to administrative initiatives Inland Revenue is already undertaking to improve the numbers of investors on the correct PIR, the following legislative changes are adopted to ensure investors in PIEs are taxed at their correct PIR:

   6.1 Every PIE investor has their PIE income squared up in a year-end process alongside the income tax square-up using their correct PIR, which is based on the information Inland Revenue holds for the investor's two previous tax years. Any PIE tax withheld during the tax year will be applied as a tax credit. For most individual investors this will happen automatically, and they will not be required to do anything. For the remaining investors the PIE income information IRD holds will be pre-populated into their income tax profile to be available when they file their tax return. Any resulting over- or underpayment of PIE tax will be offset against the result of the investor's income tax square up (their residual income tax). This means any overpaid tax on PIE income will result in an income tax refund, increase the investor's

income tax refund or reduce the investor's income tax bill. Any underpayment of PIE tax will result in an income tax bill, increase the investor's income tax bill or reduce the investor's income tax refund. If the correct PIR was used to withhold tax on the investor's PIE income, the income tax result of the investor will remain unchanged. Officials recommend that this change apply from the current (2019-20) tax year to enable refundability for the people on lower incomes that should be on a lower PIR if fiscal circumstances permit. Otherwise this change could apply prospectively from 1 April 2020 to the 2020-21 tax year. Officials recommend that this change be included in the KiwiSaver Bill as part of the select committee process.

6.2 The changes allowing for refundability of overpaid PIE tax could apply from the 2019-20 tax year going forward allowing for refundability of PIE tax for the current tax year with an estimated fiscal cost of -$23.2 million. Alternatively, refundability could apply for the following 2020-21 tax year with an immaterial fiscal cost.

6.3 Inland Revenue will provide PIE entities with the correct PIRs for their investors during the tax year for existing PIE investments, and for new PIE investments if sufficient information is available to Inland Revenue. This would significantly reduce the number of investors with a credit or debit outcome of their PIE income square-up at the end of the tax year. Officials recommend that this change apply from 1 April 2020 and be included in the KiwiSaver Bill as part of the select committee process.

7. Outside scope

**Next steps**

8. If you agree to the recommendations in this report, officials will draft a Cabinet paper for your consideration and referral to the Cabinet Office seeking a decision according to your directions. A draft Cabinet paper could be provided by 6 September 2019 and be referred to Cabinet Office on 19 September 2019 for consideration at the Cabinet meeting of 30 September 2019.

9. Subject to your and Cabinet's decision, the proposed changes will be included in the officials' report to the Finance and Expenditure Committee on the Taxation (KiwiSaver, Student Loans, and Remedial Matters) Bill. Officials are due to report to the Committee on this Bill in early October.

**Recommended action**

10. We recommend that you:

a) **agree** that all PIE investors should have their PIE income squared up at the end of the tax year using their correct PIR, which is based on the information Inland Revenue holds for the investor's two previous tax years, with the result forming part of their income tax outcome for that year.

Agreed/Not agreed

b) **note** that recommendation a) could apply from the current 2019-20 tax year with an estimated fiscal cost of -$23.2 million or prospectively from the 2020-21 tax year with an immaterial fiscal cost.

Noted

c) **indicate** whether you wish for recommendation a) to apply

i. from the current 2019-20 tax year

Yes/No

OR

ii. prospectively from the 2020-21 tax year

Yes/No

d) **agree** that Inland Revenue should provide PIE entities with the correct PIR for their investors during the income year for existing PIE investors and for new investors in PIEs if sufficient information is available to Inland Revenue with application from 1 April 2020**.**

Agreed/Not agreed

e) **agree** that the amendments in a), c) and d) be included in the officials' report to the Finance and Expenditure Committee on the Taxation (KiwiSaver, Student Loans, and Remedial Matters) Bill.

Agreed/Not agreed

f) **direct** officials to draft a Cabinet paper reflecting your decisions for consideration at the Cabinet meeting of 30 September 2019.

Directed

g) **note** that if agreeing to recommendation c) i. the Cabinet paper will seek funding for the fiscal costs to be charged as a pre-commitment against the 2020 Budget's operating allowance or funded through the between-Budget Contingency set up at Budget 2019.

Noted

h) Outside scope

Noted

i) **agree** that officials start limited consultation with PIE entities on recommendation d) to allow enough time for them to adjust their systems.

Agreed/Not agreed

j) **refer** a copy of this report to the Minister of Finance for their information.

Referred/Not referred

**Paul Young**
Policy Team Leader
Policy and Strategy

**Hon Stuart Nash**
Minister of Revenue
/ /2019

## Background

11. Previously Inland Revenue officials have reported to you that recent changes to Inland Revenue's systems and processes since April 2019 have resulted in the identification of around 1.5 million customers with incorrect prescribed investor rates (PIRs) for their PIE income (IR2019/237 and IR2019/270 refer).

12. For the year ended 31 March 2019, it is estimated that approximately:

    12.1 550,000 people are on a PIR that is too low and as a result, have underpaid their PIE tax by $42.4 million and therefore have additional income tax to pay at their marginal tax rates of between $45 million to $50 million. The average amount owing is between $82 to $91.

    12.2 950,000 people are on a PIR that is too high and have overpaid tax by approximately $42.6 million, the average amount of overpaid tax is $44. These people will have had taxable income of less than $48,000 in at least one of the two previous income years.

13. Where tax on PIE income was underpaid, the PIE income is included in the investor's personal income tax return and is taxed at the investor's marginal tax rate with a tax credit for the PIE tax that has already been paid. Overpaid tax on PIE income is full and final and current legislation does not allow for a refund.

14. Fairness concerns have been raised in the media and at the Estimates hearing for Vote Revenue before the Finance and Expenditure Committee in June 2019, in particular in relation to the non-refundability of overpaid tax on PIE income.

15. Officials provided you with report IR2019/337 on 20 June 2019 scoping possible future policy work on the PIE regime. In response to this report, you requested further work on options to allow a refund of over-paid PIE tax and on ways to simplify how PIRs are selected or provided.

16. The KiwiSaver Bill contains a proposed amendment to widen an existing ability to enable Inland Revenue to notify a PIE where it is using an incorrect PIR for an investor and provide an alternative rate that the PIE must then use. More recently fairness concerns around PIE tax non-refundability were also raised at the first reading of the KiwiSaver Bill on 23 July 2019 where members of the Finance and Expenditure Committee have indicated that they intend to raise this matter during the select committee process.

## Current law

17. Under current legislation a person investing in a multi-rate PIE (most PIEs are multi-rate PIEs) elects a tax rate, referred to as their PIR, which approximates their marginal tax rate based on (the lower of) one of the previous two tax years. However, as opposed to marginal income tax rates which can be up to 33%, PIE rates are capped at 28%. The investor notifies their elected PIR to their PIE providers. The PIE provider pays tax on the investment income based on the PIR the individual has notified. If an investor does not provide their PIE provider with their elected PIR, they default to the highest PIR of 28%.

18. Generally, the tax paid by a PIE based on investors' PIRs is a final tax for the individual investor, which means the investor does not have to include the PIE income in their tax return. However, where an investor elects a rate that is too low, any PIE tax deducted from PIE income is no longer a full and final tax. In this case the investor has to include the amount of PIE income in their personal income tax return and is taxed on their PIE income at their marginal tax rate of up to 33%, whereas the top PIR is 28%. The investor receives a tax credit for the PIE tax already paid.

19. Where an investor has elected a rate that is too high, or they have defaulted to the highest PIR but could have elected a lower PIR, the tax paid remains full and final and the legislation does not allow for a refund of the overpaid amount of PIE tax.

20. Where the Commissioner considers the PIR notified by the investor to be incorrect, the Commissioner currently has the ability to direct a PIE to use a PIR she considers appropriate rather than the rate the investor notified. A proposed legislative change contained in the KiwiSaver Bill widens this ability so that the Commissioner can also provide the appropriate PIR where an investor defaulted onto the 28% PIR rather than notified the incorrect rate. This is proposed to apply from the 1 April 2020.

## Problem definition

21. As outlined above, there are two main areas of concern:

    21.1 a large number of people are on a wrong PIR; and

    21.2 currently legislative provisions do not allow for overpaid tax on PIE income to be refunded.

22. As outlined in earlier reports mentioned above, Inland Revenue is working on a range of initiatives to help ensure people are on the correct PIRs for the future. This involves proactively contacting customers who are on an incorrect rate and suggesting they contact their PIE provider to change their rate. Inland Revenue has commenced these initiatives.

23. To further address the above concerns officials have been asked to consider policy options for:

    23.1 legislative changes allowing refunds of overpaid PIE tax; and

    23.2 legislative changes simplifying the way a PIR is selected or provided.

## Allowing for refunds of overpaid PIE tax

24. You have asked officials to consider and potentially further develop a legislative change allowing refunds of overpaid PIE tax.

25. Current legislation provides that PIE income is excluded income of the investor. This means it is not included in the investor's assessable income which is subject to income tax at the investor's marginal income tax rate (between 10.5% and 33% depending on the investor's taxable income for the tax year).

26. Instead tax on PIE income is withheld by the PIE provider using the individual PIR their investor has notified. The PIR approximates the investor's marginal tax rate based on one of the previous two tax years. There are three PIRs: 10.5%, 17.5% and 28%. In some cases, the PIR is concessionary compared with marginal income tax rates. Where the investor has not notified a rate, the default rate of 28% applies. If the investor has notified their PIE provider with the correct PIR or with a rate that is too high, the tax withheld on the PIE income, whether correct or overpaid, is a full and final tax. This means in the current PIE rules there is no legislative ability and mechanism to refund any tax overpaid on PIE income. The people affected by the non-refundability are people with lower income and will have had taxable income of less than $48,000 in at least one of the two previous income years. These people would have been entitled to a lower PIR but cannot receive a refund of overpaid tax on their PIE income.

27. If the investor has notified their PIE provider of a rate that is too low, the investor's PIE income ceases to be excluded income. This means the PIE income is subject to income tax at the investor's marginal income tax rate which could be up to 33%,

whereas the top PIR is 28%. The investor gets a tax credit for the PIE tax that has already been paid in respect of the income. This policy was designed as an incentive for investors to notify the correct PIR. Investors who have notified a rate that is too low have to include their PIE income in their tax return. For individual investors who have notified a rate that is too low and who have their income tax automatically squared up at the end of the tax year, their PIE income is automatically included in their income tax assessment.

28. Officials' preferred option to achieve refundability of over-withheld PIE income is that all PIE income would be squared up at the end of the tax year using the PIE investor's correct PIR based on one of the previous two income years. This means that PIE tax would no longer be a full and final tax, but every PIE investor would have their PIE income squared up in a year-end process alongside the income tax square-up using their correct PIR. Any PIE tax withheld during the tax year would be applied as a tax credit.

29. The outcome of the PIE tax square-up would be offset against the person's income tax outcome (their residual income tax). Any resulting over- or underpayment of PIE tax will be offset against the result of the investor's income tax square up (their residual income tax). This means any overpaid tax on PIE income will result in an income tax refund, increase the investor's income tax refund or reduce their tax bill. Any underpayment of PIE tax will result in an income tax bill, increase the investor's income tax bill or reduce their tax refund. If the correct PIR was used to withhold tax on the investor's PIE income, the income tax result of the investor will remain unchanged. Officials recommend that this change apply from the current tax year.

30. For most individual investors this square up would happen automatically and they would not be required to do anything. It would be an automated process similar to and alongside the year end auto-calculation process for income tax. The result would be an overall tax bill or refund. For the remaining investors the PIE income information Inland Revenue holds would be pre-populated into their income tax profile to be available when they file their income tax return. For them the PIE income calculation would happen alongside the income tax assessment once they have filed their tax return for the year.

31. The outlined proposal would preserve the current PIR rates based on one of the previous two tax years, including the maximum tax rate for PIEs (including KiwiSaver PIEs) being 28% and the current thresholds for investors in these PIEs.

32. The proposal would mean a change compared to the current treatment for investors who have notified a PIR that is too low, under the current rules they have their marginal tax rates (up to 33%) applied to their PIE income as an incentive to notify the correct PIR. In future it would not be relevant whether a too low or too high PIR has been notified and who has notified the PIR (the investor or Inland Revenue). All PIE income would have the correct PIR applied to it in the year-end square up, regardless of whether it has been correctly, over- or under-withheld during the tax year. Officials consider that the current incentive for an investor to notify the correct PIR may be less relevant in future as Inland Revenue would from 1 April 2020 in most cases provide the PIR to the PIE provider or correct the PIR where it considers it to be incorrect.

33. We indicated in our scoping report dated 21 June 2019 (IR2019/337 refers) that depending on the design of any proposed legislative change, refundability could be complicated to implement. The preferred option outlined above could be implemented from 1 April 2020, applying either from that date going forward or for the current (2019-20) tax year.

34. Other options for achieving refundability were considered but disregarded as being too complex giving some unreasonable outcomes or having wide reaching effects

on Inland Revenue's technology platform START, including the system design of the income tax auto-calculation for individuals.

## Simplifying the way a PIR is selected or provided

35. Inland Revenue can provide the PIR it considers appropriate for an investor directly to a PIE if Inland Revenue thinks the PIR the investor has notified is incorrect. As outlined earlier, the KiwiSaver Bill proposes a legislative change to also allow Inland Revenue to provide the PIE with the investor's correct PIR where they have not notified a PIR and defaulted onto the 28% rate.

36. To simplify the way PIRs are determined for an investor, officials propose to go a step further and provide Inland Revenue with the ability to proactively provide the PIE with their investors' PIRs during the tax year for existing investors and for new investors if Inland Revenue holds sufficient information to determine the PIR applicable for the tax year.

37. This would result in most people being on the correct PIR and having correct PIE tax withheld from their PIE income. For example, when a new employee is auto-enrolled in KiwiSaver, Inland Revenue would, upon being notified of the enrolment by the employer, calculate the new employee's PIR. This would be based on the employee's previous two years' income information that Inland Revenue holds and the PIR would be provided to the relevant PIE. Inland Revenue would inform the investor of their calculated PIR and the fact that Inland Revenue has provided it to their PIE provider.

38. There would be some limited circumstances where Inland Revenue is unable to provide a PIR:

    38.1 Where Inland Revenue does not hold sufficient information to calculate an individual's PIR for the tax year. For example, a person required to file a tax return has not filed their return for one of the previous two tax years;

    38.2 Inland Revenue would not be aware of a new investor starting to invest in a non-KiwiSaver PIE until tax on the PIE income has been withheld and therefore could not proactively advise the PIR. However, investors in such PIEs are more likely to have a higher income and more likely to be on a 28% PIR, therefore over-taxation is less likely (although still possible).

Outside scope

Outside scope

## Financial implications

45. We estimate that the fiscal impact of squaring up PIE income for all PIE investors (and not just those who are under-taxed) is a revenue loss of approximately -$23.2 million for the 2019-20 tax year, and an immaterial loss in the following years. Timing and accrual accounting might cause the initial amount to be spread over two fiscal years and work is being done to estimate the extent to which the cost will spill over into the second fiscal year.

46. The estimated cost of refunding overpaid PIE tax is based on the overpayment data for the tax year ended 31 March 2019, which is approximately $42.6 million of overpaid tax on PIE income. Subsequent actions were also incorporated. These include Inland Revenue's initiatives to get more people on the correct rate through information supplied to investors, and media attention. Both of these will have resulted in a large number of investors contacting their PIE providers to change their PIR, particularly investors who have received a tax bill for the 2018-19 tax year. To capture these impacts, we assumed that $20 million of the $42.6 million will be corrected through non-square-up means in the current tax year. This leaves a residual of $22.6 million of overpaid PIE tax, contributing a fiscal cost of -$22.6 million if corrected by way of a square up mechanism at year end.

47. In addition, the proposal is to square up the PIE income of those who *underpay* PIE tax to their correct PIR, and not to their marginal tax rate as is currently the case. We estimate that this change would cost an additional -$0.6 million as PIR rates are capped at 28%.

48. For the years following the current income years, Inland Revenue would provide PIEs with the correct PIRs for most of their investors. The fiscal cost directly attributable to additional square up activity would therefore be immaterial.

49. For the years following the current income years, Inland Revenue would provide PIEs with the correct PIRs for most of their investors. This would mean that almost all investors would be on the correct PIR and the fiscal cost would therefore be immaterial.

50. This fiscal cost would need to be charged as a pre-commitment against the 2020 Budget's operating allowance or funded through the between-Budget Contingency set up at Budget 2019.

**Administrative implications**

51. Implementation and on-going administration costs, estimated at $1.5 million, will be met through baseline funding.

## Consultation

52. The Treasury has been consulted and agree with the content of this report.

## Next steps

53. If you consider that the recommended changes should be made, officials will draft a Cabinet paper for your consideration and referral to the Cabinet Office.

54. We suggest the following timeline:

| Action | Date |
|---|---|
| Draft Cabinet paper provided to Minister's Office | 6 September 2019 |
| Referral to Cabinet Office | 19 September 2019 |
| DEV meeting | 26 September 2019 |
| Cabinet consideration | 30 September 2019 |

55. Officials will include Cabinet's decision in the officials' report to the Finance and Expenditure Committee on the KiwiSaver Bill.

56. We recommend that a copy of this report is referred to your colleague the Minister of Finance.

## POLICY AND STRATEGY

**Tax policy report:** **Cabinet paper – Changes to the PIE regime, student loan scheme and KiwiSaver for inclusion in current Bill**

| **Date:** | 06 September 2019 | **Priority:** | Medium |
|---|---|---|---|
| **Security level:** | In Confidence | **Report number:** | IR2019/463 |

### Action sought

| | Action sought | Deadline |
|---|---|---|
| Minister of Revenue | **Agree** to the recommendations<br>**Authorise** the attached Cabinet paper for lodging with the Cabinet Office | 10am on Thursday, 19 September 2019 |

### Contact for telephone discussion (if required)

| Name | Position | Telephone |
|---|---|---|
| Martin Neylan | Principal Policy Advisor | s 9(2)(a) |
| s 9(2)(a) | Policy Advisor | |

06 September 2019

Minister of Revenue

## Cabinet paper - Changes to the PIE regime, student loan scheme and KiwiSaver for inclusion in current Bill

### Executive summary

1. Attached to this report is a Cabinet paper for your consideration and authorisation. The paper seeks Cabinet's approval for a number of policy changes for inclusion in the Taxation (KiwiSaver, Student Loans, and Remedial Matters) Bill (the KiwiSaver Bill) which is currently before the Finance and Expenditure Committee. Submissions to the Committee on the KiwiSaver Bill closed on 4 September 2019.

2. The draft Cabinet paper proposes two changes to the PIE regime which you have previously approved for inclusion in the Cabinet paper (IR2019/366 refers). These proposals are:

   2.1 to allow for refundability of overpaid PIE tax from the 2020-21 tax year all PIE investors have their PIE income squared up at the end of the tax year. This is done by using their correct prescribed investor rate (PIR), which is based on the information Inland Revenue holds for the investor's two previous tax years;

   2.2 that Inland Revenue provide PIE entities with the correct PIR for their investors during the income year for existing PIE investors and for new investors in PIEs if sufficient information is available to Inland Revenue with application from 1 April 2020;

3. This report also seeks your approval to the following amendments:

   3.1 repeal the provisions requiring the withholding of student loan repayments to be deducted from schedular, election day and casual agricultural income with effect from 1 April 2020. This change is as a result of consultation with employers who advise that significant compliance costs would be incurred in implementing this change;

   3.2 lowering the $1500 student loan scheme exemption for non-salary and wage income (including schedular, casual agricultural, and election day income) to $500;

   3.3 deferring KiwiSaver members being able to change their employee contributions rates through their KiwiSaver scheme provider and Inland Revenue; and

   3.4 removing a proposal from the KiwiSaver Bill that would require employers to provide employer superannuation contribution tax (ESCT) rate information to Inland Revenue and modifying a proposal relating to the provision of KiwiSaver income information to Inland Revenue, so employers would only be required to provide this information for new employees. These changes were previously agreed to by Cabinet.

## Next steps

4. If you agree to the proposals and the attached draft, we propose that this Cabinet paper be referred to Cabinet Office on 19 September 2019 for the Cabinet Economic Development Committee (DEV) meeting on 26 September 2019 and Cabinet consideration on 30 September 2019.

5. Subject to your approval of the student loans and KiwiSaver changes and Cabinet's decision the proposals will be included in the officials' report to the Finance and Expenditure Committee on the Taxation (KiwiSaver, Student Loans, and Remedial Matters) Bill for the Committee's consideration. Officials are due to report to the Committee on 11 October 2019.

## Recommended action

We recommend that you:

1. **note** the contents of this report and the attached Cabinet paper;

   Noted

2. **agree** to repeal changes requiring student loan repayments to be deducted from schedular, election-day, and casual agricultural income with effect from 1 April 2020;

   Agreed/Not agreed

3. **agree** that the $1500 student loans scheme exemption for non-salary and wage income for New Zealand-based borrowers, above the annual repayment threshold, be lowered to $500;

   Agreed/Not agreed

4. **agree** that the application date of the change to allow KiwiSaver members to change their employee contribution rate through their KiwiSaver scheme provider and Inland Revenue be deferred until 1 April 2022 or an earlier date to be set by Order in Council;

   Agreed/Not agreed

5. **agree** to rescind your earlier decision to require employers to provide employer superannuation contribution tax (ESCT) rate information to Inland Revenue;

6. Agreed/Not agreed

7. **agree** to employers only being required to provide information to Inland Revenue about the income members' KiwiSaver contributions are calculated from for new employees (not for existing employees where this information has changed);

   Agreed/Not agreed

8. **authorise** the lodging of the attached Cabinet paper with the Cabinet Office by 10am on Thursday, 19 September 2019.

   Authorised

**Martin Neylan**
Principal Policy Advisor
Policy and Strategy

**Hon Stuart Nash**
Minister of Revenue
/ /2019

## PIE regime items approved for inclusion in the Cabinet paper

9. You have previously agreed to two changes to the PIE regime (IR2019/366 refers) that would allow for refundability of overpaid PIE tax an simplify the way a PIR is selected or provided. These changes are that:

   9.1 from the 2020-21 tax year all PIE investors should have their PIE income squared up at the end of the tax year using their correct prescribed investor rate (PIR), which is based on the information Inland Revenue holds for the investor's two previous tax years; and

   9.2 Inland Revenue provides PIE entities with the correct PIR for their investors during the income year for existing PIE investors and for new investors in PIEs if sufficient information is available to Inland Revenue with application from 1 April 2020.

10. The attached draft Cabinet paper seeks Cabinet's approval to include these changes in the KiwiSaver Bill to be considered by the Finance and Expenditure Committee.

11. One of the submissions the Finance and Expenditure Committee has received on the KiwiSaver Bill suggests that a mechanism should be introduced to provide a form of refund for an over-taxed investor.

12. While none of the other submissions received to date raise the point of PIE tax non-refundability, we note that the Committee has indicated that it will accept some late submissions. Any late relevant submission received will not have been considered in the drafting of the attached Cabinet paper.

13. Officials are currently working with the Quality Assurance reviewer at Inland Revenue to finalise and review the required regulatory impact assessment which will be provided to your Office at a later point in time.

## Items for approval in this report

14. Ministerial approval is sought from you on the inclusion of the following changes to policy items in the KiwiSaver Bill.

### Changes to Student Loan Scheme

*Repeal requirement to deduct student loan repayments from certain income*

15. Recently enacted provisions require student loan repayments to be deducted from schedular, election-day, and casual agricultural income each payday from 1 April 2020. Submissions on the policy proposals to Inland Revenue focussed on the merits of the policy intent, rather than the compliance costs for employers. Also, there were no submissions received on this proposal during the Select Committee process.

16. In preparing for implementing these changes, Inland Revenue has undertaken targeted consultation on the detailed design questions with employers who have advised that significant compliance costs would be incurred in implementing these changes. This cost would be imposed at a time when employers are already facing a large number of changes as a result of earlier Business Transformation releases. Inland Revenue is now reconsidering whether withholding is the right approach for these sources of income or if there are other policy options that could address

compliance issues for this group. As a result, officials recommend repealing this change with effect from 1 April 2020.

*Reducing the exemption limit for non-salary and wage income*

17. The student loan scheme currently has a $1500 exemption for non-salary and wage income (including schedular, casual agricultural and election day income) for New Zealand-based borrowers, above the annual repayment threshold. Recent changes to the administration of individuals' income tax mean that now all taxpayers either file a return or have their income tax return automatically generated. As a result, there is no longer a significant compliance cost for borrowers associated with advising Inland Revenue of their non-salary and wage income. Therefore, officials recommend reducing the exemption limit from $1500 to $500. This would mean that a larger number of borrowers would be required to make repayments and if payments are made, these would reduce the term of the loan. However, if borrowers do not make payments, provisions in the Student Loan Scheme Act 2011 currently allow unpaid amounts of less than $334 to be capitalised back onto the loan balance, so no borrowers whose total non-salary and wage income is between $500 and $1,500 will be subject to penalties if they do not make repayments.

18. Inland Revenue officials are in discussions with the Treasury Regulatory Impact Analysis team, regarding meeting regulatory impact analysis requirements. Initial advice is that an exemption applies to repealing the requirement to withhold student loan repayments from schedular, casual agricultural, and election day payments.

19. However, the change to lower the $1,500 exemption for non-salary and wage income to $500 may require a short regulatory impact analysis. Should the requirement for a regulatory impact analysis be confirmed, we will provide the analysis at a later time.

## KiwiSaver changes

20. You previously agreed to the following changes to the KiwiSaver scheme, that were subsequently agreed to by Cabinet and included in the KiwiSaver Bill:

- allowing KiwiSaver members to change their employee contribution rate through their KiwiSaver scheme provider or Inland Revenue (in addition to through their employer, which is the current process);
- requiring employers to report employer superannuation contribution tax (ESCT) rates to Inland Revenue for new employees and where this information has changed; and
- requiring employers to report information about the income members KiwiSaver contributions are calculated from[1] for new employees and where this information has changed (IR2019/023, DEV-19-MIN-0038.1 and CAB-19-MIN-0109 refer).

21. Your approval is now sought to the following modification to these previously agreed to changes:

- deferring the change to allow KiwiSaver members to change their employee contribution rate through their KiwiSaver provider and Inland Revenue, until 1 April 2022 or and earlier date to be set by Order in Council; and
- rescinding your earlier decision to require employers to provide ESCT rate information to Inland Revenue and modifying the decision relating to the provision of KiwiSaver income information to Inland Revenue, so employers

[1] Some amounts that are included as income when calculating PAYE deductions are not treated as income for the purposes of calculating KiwiSaver contributions.

would only be required to provide this information to Inland Revenue for new employees.

22. These proposed modifications would respond to concerns about employer compliance costs, that were raised during targeted consultation with stakeholders, as well as submissions to the Finance and Expenditure Committee has received on the KiwiSaver Bill.

23. Three submissions on the KiwiSaver Bill so far raised concerns about the additional employer reporting requirements. In particular, that the compliance costs of requiring employers to report ESCT rates, is likely to outweigh the benefit to Inland Revenue of receiving this information.

24. Seven of the submissions received on the KiwiSaver Bill touch on the proposal to allow employees to change their contribution rate through their KiwiSaver scheme provider or Inland Revenue. Submitters views are mixed, with some noting the change would introduce additional compliance costs for employers, while other submitters support the proposal on the basis it would improve the KiwiSaver member experience. Deferring the application date for this change would allow officials to undertake additional consultation with stakeholders and consider ways to make this change easier for employers to implement.

25. A regulatory impact analysis, entitled *Business Transformation related KiwiSaver refinements*, was prepared when original Cabinet decisions were made. A modified version of this regulator impact analysis, reflecting the changes recommended in this report, will be provided at a later time.

## Consultation

26. The Treasury has been consulted and agree with the content of the draft Cabinet paper.

## Next steps

27. We have drafted the attached Cabinet paper on the basis that you agree to the recommendations in this report. Please advise if there are any changes to the Cabinet paper you wish to make.

28. We suggest the following timeline:

| Action | Date |
|---|---|
| Referral to Cabinet Office | 19 September 2019 |
| Cabinet Economic Development Committee meeting | 26 September 2019 |
| Cabinet consideration | 30 September 2019 |

29. Officials will include Cabinet's decision in the officials' report to the Finance and Expenditure Committee on the Taxation (KiwiSaver, Student Loans, and Remedial Matters) Bill for the Committee's consideration. Officials are due to report to the Committee on 11 October 2019.

In Confidence

Office of the Minister of Revenue

Chair, Cabinet Economic Development Committee

**ITEMS FOR INCLUSION IN THE TAXATION (KIWISAVER, STUDENT LOANS, AND REMEDIAL MATTERS) BILL**

**Proposal**

1. This paper seeks the Cabinet Economic Development Committee's agreement to amendments to the Portfolio Investment Entity (PIE) regime, student loan scheme and to KiwiSaver settings. This paper proposes that the Committee:

   1.1 amend the PIE regime to allow for refundability of overpaid tax on PIE income and to simplify the way prescribed investor rates (PIRs) are selected or provided;

   1.2 repeal the student loan scheme provisions requiring the withholding of student loan repayments from schedular, election day and casual income and to lower the $1500 exemption threshold for non-salary and wage income to $500;

   1.3 defer KiwiSaver members being able to change employee contribution rates through their KiwiSaver scheme provider or Inland Revenue; and

   1.4 remove the provision in the Taxation (KiwiSaver, Student Loans, and Remedial Matters) Bill requiring employers to provider employer superannuation contribution tax (ESCT) rate information to Inland Revenue, and only requiring employers to provide information about income KiwiSaver contributions are calculated from to Inland Revenue for new employees.

2. I propose that these changes be included in the officials' report to the Finance and Expenditure Committee on the Taxation (KiwiSaver, Student Loans, and Remedial Matters) Bill for the Committee's consideration. Officials are due to report to the Committee on this Bill in mid-October.

**Executive Summary**

*Changes to PIE regime*

3. Recent changes to Inland Revenue's systems and processes since April 2019 have identified around 1.5 million people with incorrect PIRs for their PIE income.

4. Where PIE tax has been underpaid, the investor must include their PIE income in their income tax return and it is taxed at the investor's marginal tax rate, which may be up to 33%, whereas the top PIR is 28%. However, legislation does not allow for a refund of overpaid PIE tax.



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5. To allow overpaid PIE tax to be refunded, I propose that every PIE investor has their PIE income squared up in a year-end process alongside their income tax square-up. Inland Revenue will use investors' correct PIR, which is based on the information Inland Revenue holds for the investor's two previous tax years. Any PIE tax withheld during the tax year will be applied as a tax credit. Any resulting over- or underpayment of PIE tax will be offset against the result of the investor's income tax square up (their residual income tax). I propose that this change apply from the 2020-21 tax year.

6. In addition, I propose to widen Inland Revenue's ability to provide PIE entities with their investor's PIRs where it holds sufficient information. Inland Revenue will provide PIE entities with the correct PIRs for their investors during the tax year for existing PIE investments, and for new PIE investments if sufficient information is available to Inland Revenue. This would significantly improve the accuracy of PIE tax paid through the year and reduce the number of investors with a credit or debit outcome of their PIE income square-up at the end of the tax year. I propose that this change apply from 1 April 2020.

*Student loan scheme changes*

7. Recently enacted legislation requires student loan repayments to be deducted from schedular, election-day, and casual agricultural income each payday from 1 April 2020. Submissions on the policy proposal in the discussion document entitled *Making Tax Simpler – Better administration of social policy* focussed on the merits of the policy design, rather than the compliance costs for employers. Also, there were no submissions received on this proposal during the Select Committee process.

8. In preparing for implementing these changes, Inland Revenue has undertaken targeted consultation with employers who have advised that significant compliance costs would be incurred in implementing these changes. Inland Revenue is now reconsidering whether withholding is the right approach to make it easier for recipients of these sources of income to comply with their obligations. As a result, I recommend repealing this change with effect from 1 April 2020.

9. The student loan scheme currently has a $1500 exemption for non-salary and wage income (including schedular, casual agricultural and election day income) for New Zealand-based borrowers, above the annual repayment threshold. Recent changes to the administration of individuals' income tax mean that now all taxpayers either file a return or have their income tax return automatically generated. As a result, there is no longer a significant compliance cost for borrowers associated with advising Inland Revenue of their non-salary and wage income. I therefore propose reducing the exemption limit from $1500 to $500 with effect from 1 April 2020. This would mean that a larger number of borrowers would be required to make repayments and if payments are made, these would reduce the term of the loan.

*Changes to KiwiSaver*

10. Cabinet previously agreed to a number of changes to enhance the administration of KiwiSaver as part of Business Transformation Release 4 which have been included in the Taxation (KiwiSaver, Student Loans and Remedial Matters) Bill. To ensure

compliance costs to employers are minimised, I propose the following modifications to these changes:

10.1 deferring the application date of a change requiring employers to start deducting KiwiSaver contributions from employee's salary or wages based on contribution rate changes advised by Inland Revenue until 1 April 2022 or an earlier date to be set by Order in Council.

10.2 rescinding an earlier Cabinet decision that would require employers to provide ESCT information to Inland Revenue and modify a decision relating to the provision of KiwiSaver income information to Inland Revenue, so employers would only be required to provide this information for new employees.

*Legislative implications*

11. I propose that these changes be included in the officials' report to the Finance and Expenditure Committee on the Taxation (KiwiSaver, Student Loans, and Remedial Matters) Bill for the Committee's consideration.

**Changes to the PIE regime**

*Background*

12. Recent changes to Inland Revenue's systems and processes since April 2019 have resulted in the identification of around 1.5 million people with incorrect PIRs for their PIE income. For the year ended 31 March 2019, it is estimated that approximately:

12.1 550,000 people are on a PIR that is too low and as a result, have underpaid their PIE tax by $42.4 million. These people have additional income tax to pay at their marginal tax rates of between $45 million to $50 million. The average amount owing is between $82 to $91.

12.2 950,000 people are on a PIR that is too high and have overpaid tax by approximately $42.6 million. The average amount of overpaid tax is $44. These people will have had taxable income of less than $48,000 in at least one of the two previous income years.

13. A person investing in a multi-rate PIE (most PIEs are multi-rate PIEs) elects a tax rate, referred to as their PIR, which approximates their marginal tax rate based on (the lower of) one of the previous two tax years. However, as opposed to marginal income tax rates which can be up to 33%, PIE rates are capped at 28%. The investor notifies their elected PIR to their PIE providers. The PIE provider pays tax on the investment income based on the PIR their investor has notified. If an investor does not provide their PIE with their elected PIR, they default to the highest PIR of 28%.

14. Where tax on PIE income was underpaid because the investor has notified a rate that is too low, the PIE income is included in the investor's personal income tax return and is taxed at the investor's marginal tax rate. A tax credit is given for the PIE tax that has already been paid.

15. Where an investor has elected a rate that is too high, or they have defaulted to the highest PIR but could have elected a lower PIR, the overpaid tax on their PIE income is currently full and final. Current legislation does not allow for a refund. The people



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affected by the non-refundability are people with lower income and will have had taxable income of less than $48,000 in at least one of the two previous income years. These people would have been entitled to a lower PIR but cannot receive a refund of overpaid tax on their PIE income.

16. One submission the Finance and Expenditure Committee received on the Taxation (KiwiSaver, Student Loans, and Remedial Matters) Bill raises concerns that the Bill as introduced does not contain a proposal that will enable a refund for people who have overpaid PIE tax. It was submitted that a mechanism should be introduced to provide a form of refund for an over-taxed investor.

*Allowing for refunds of overpaid PIE tax*

17. To achieve refundability of over-withheld PIE tax, I propose that all PIE income is squared up at the end of the tax year using the PIE investor's correct PIR based on the information Inland Revenue holds about the previous two income years. This preserves the current PIR rates based on one of the previous two tax years, including the maximum tax rate for PIEs (including KiwiSaver PIEs) being 28% and the current thresholds for investors in these PIEs.

18. This means that PIE investors would have their PIE income squared up in a year-end process alongside their income tax square-up. Any PIE tax withheld during the tax year would be applied as a tax credit.

19. The outcome of the PIE tax square-up is offset against the result of the investor's income tax square up (their residual income tax). This means any overpaid tax on PIE income will result in an income tax refund, increase the investor's income tax refund or reduce their tax bill. Any underpayment of PIE tax will result in an income tax bill, increase the investor's income tax bill or reduce their tax refund. If the correct PIR was used to withhold tax on the investor's PIE income, the income tax result of the investor will remain unchanged.

20. For most individual investors this square up would happen automatically and they would not be required to do anything. It would be an automated process similar to and alongside the year-end auto-calculation process for income tax. The result would be an overall tax bill or refund. For the remaining investors the PIE income information Inland Revenue holds would be pre-populated into their income tax profile to be available when they file their income tax return. For them the PIE income calculation would happen alongside the income tax assessment once they have filed their tax return for the year.

21. I propose that this change will apply from the 2020-21 tax year.

*Simplifying the way a PIR is determined*

22. Inland Revenue can already provide the PIR it considers appropriate for an investor directly to a PIE if Inland Revenue thinks the PIR the investor has notified is incorrect.

23. To simplify the way PIRs are determined for an investor in a PIE, I propose to provide Inland Revenue with the ability to proactively provide PIEs with their



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investors' PIRs during the tax year for existing investors and for new investors if Inland Revenue holds sufficient information to determine the PIR applicable for the tax year. This would result in most people being on the correct PIR and having correct PIE tax withheld from their PIE income.

24. For example, when a new employee is auto-enrolled in KiwiSaver, Inland Revenue would, upon being notified of the enrolment by the employer, calculate the new employee's PIR. This would be based on the employee's previous two years' income information that Inland Revenue holds and the PIR would be provided to the relevant PIE. Inland Revenue would inform the investor of their calculated PIR and the fact that Inland Revenue has provided it to their PIE provider.

25. There are some limited circumstances where Inland Revenue is unable to provide a PIR:

    25.1 Where Inland Revenue does not hold sufficient information to calculate an individual's PIR for the tax year. For example, a person required to file a tax return has not filed their return for one of the previous two tax years;

    25.2 Inland Revenue would not be aware of a new investor starting to invest in a non-KiwiSaver PIE until tax on the PIE income has been withheld and therefore could not proactively advise the PIR. However, investors in such PIEs are more likely to have a higher income and more likely to be on a 28% PIR, therefore over-taxation is less likely (although still possible).

26. I propose that this change will apply from 1 April 2020.

27. I have asked officials to start limited consultation with PIE entities on this proposal to allow enough time for them to adjust their systems.

**Student loan scheme changes**

*Deferring withholding student loan repayments on certain payments*

28. Changes to the student loan scheme planned as part of Release 4 of Inland Revenue's Business Transformation programme in April 2020 would require student loan repayments to be deducted from schedular, election-day, and casual agricultural income each payday. These changes were previously agreed by Cabinet [SWC-18-MIN-0093 and CAB-18-MIN-0382 refer]. They were included in the Taxation (Annual Rates for 2019-20, GST Offshore Supplier Registration and Remedial Matters) Act 2019 which was enacted on 26 June 2019.

29. Submissions on the policy proposals in the *Making tax simpler – Better administration of social policy* discussion document focussed mainly on the merits of the policy rather than compliance costs. Also, no submissions were received on the proposal as part of the Select Committee process.

30. In preparation for implementing these changes as part of Inland Revenue Business Transformation process, targeted consultation on the detailed design has been undertaken with employers who have advised that significant compliance costs would be incurred in implementing this change. This cost would be imposed at a time when employers are already facing a large number of changes as a result of earlier



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Business Transformation releases. Inland Revenue is now reconsidering whether withholding of student loan repayments is the right approach for these sources of income or if there are other policy options that could minimise compliance issues for this group of borrowers. As a result, I recommend repealing the requirement for employers to deduct student loan repayments from schedular, election-day, and casual agricultural income each payday and instead rely on student loan repayments on these forms of income continuing to be made through the student loan interim payments mechanism (similar to provisional tax payments) during the year.

*Lowering the $1500 exemption for non-salary and wage income to $500*

31. The student loan scheme currently has a $1500 exemption for non-salary and wage income for New Zealand-based borrowers, above the annual repayment threshold. Borrowers who earn less than $1500 of non-salary and wage income (including schedular, casual agricultural, and election day income) in a year are not required to notify Inland Revenue of this income for student loan purposes and do not have to make student loan repayments on it. If a borrower earns more than $1500 of non-salary and wage income, they are required to make repayments on the full amount.

32. This threshold was introduced when most salary and wage earners were not required to file a tax return and recognised the compliance costs associated with borrowers advising Inland Revenue of their income. Following changes to the administration of individual's income tax, all taxpayers now either file a return or have their income tax automatically squared up at the end of the tax year. As a result, there is no longer a significant compliance cost for borrowers in advising Inland Revenue of their non-salary and wage income. I therefore recommend reducing the exemption limit from $1500 to $500. This would mean that a larger number of borrowers would be required to make repayments and if payments are made, these would reduce the term of the loan. However, if borrowers do not make payments, provisions in the Student Loan Scheme Act 2011 allow unpaid amounts of less than $334 to be capitalised back onto the loan balance, so no borrowers whose total non-salary and wage income is between $500 and $1,500 will be subject to penalties if they do not make repayments.

***KiwiSaver changes***

33. Cabinet previously agreed to a number of changes to enhance the administration of KiwiSaver as part of Business Transformation Release 4 [DEV-19-MIN-0038.1 and CAB-19-MIN-0109 refer], which have been included in the Taxation (KiwiSaver, Student Loans and Remedial Matters) Bill. I propose modifications to two of these changes, to ensure compliance costs to employers are minimised, at a time when they are already facing a number of changes as a result of earlier Business Transformation releases.

*Changing employee contribution rates*

34. Cabinet agreed to allow KiwiSaver members to change their employee contribution rate through their KiwiSaver scheme provider or Inland Revenue (in addition to through their employer, which is the current process), from April 2020. This change would require employers to start deducting KiwiSaver contributions from employee's salary or wages based on contribution rate changes advised by Inland Revenue.



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35. Targeted consultation in the lead up to Release 4 has indicated this would create additional compliance cost for employers. Submissions on the proposal to the Finance and Expenditure Committee considering the Taxation (KiwiSaver, Student Loans, and Remedial Matters) Bill have been mixed – with some submitters noting the change would have compliance costs for employers, while others support the change on the basis it would improve the KiwiSaver member experience. Therefore, I propose deferring the application date of this change to 1 April 2022 or an earlier date to be set by Order in Council. This would enable officials to undertake further consultation with stakeholders and investigate approaches to minimise the compliance cost of this change on employers.

*Changes to KiwiSaver income and ESCT rate information required*

36. Cabinet agreed to employers being required to provide the following information to Inland Revenue about new employees or existing employees where the information had changed since the employer last provided it:

    36.1 the income amount members' KiwiSaver contributions are calculated from;[1] and

    36.2 an employee's ESCT rate.

37. Further analysis of incorrect ESCT payments by employers indicates the problem may arise as a result of an employer not determining the correct ESCT rate in the first place rather than calculating the ESCT deduction incorrectly. Therefore, while collection of ESCT rates would make it easier for Inland Revenue to detect potential miscalculations of ESCT deductions, the compliance costs on employers outweigh these benefits. This view is consistent with concerns raised in three submissions to the Finance and Expenditure Commission on the Taxation (KiwiSaver, Student Loans, and Remedial Matters) Bill, that did not support employers being required to report ESCT rates to Inland Revenue. Therefore, I propose that the requirement for employers to report ESCT rates to Inland Revenue should be removed from the bill and not enacted.

38. It is still proposed that employers provide Inland Revenue with information about the income amount members' KiwiSaver contributions are calculated from for new employees. However, I propose employers should not be required to provide this information to Inland Revenue about existing employee's where the information has changed since it was last reported. It would be more difficult for employers to provide information to Inland Revenue in this situation, as it could not be incorporated into new employee on-boarding processes. Moreover, as any differences between income for PAYE purposes and for KiwiSaver purposes generally does not change during the course of an employment relationship, collecting this information in relation to new employees only is likely to be sufficient for Inland Revenue to more effectively detect miscalculations of KiwiSaver contributions.

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1 Some amounts that are included as income when calculating PAYE deductions are not treated as income for the purposes of calculating KiwiSaver contributions (such amounts include the value of accommodation, a benefit from an employer share scheme or a redundancy payment).



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## Consultation

39. The Treasury has been consulted on this paper.

40. The Ministry of Education has been consulted on the proposals relating to the student loan scheme changes and have no concerns regarding the proposals.

## Financial Implications

*PIE regime changes*

41. The proposals relating to the PIE regime will have no fiscal cost if applied from 1 April 2020 and from the 2020-21 tax year. Enabling Inland Revenue to notify PIE providers of their investors' PIRs is expected to result in PIE providers using the correct PIR for almost all their investors when withholding tax on their PIE income. The remaining fiscal cost would be immaterial.

42. Implementation and on-going administration costs, estimated at $1.5 million, will be met through baseline funding.

*Student Loans*

43. The first change, to repeal withholding requirements, will not change a borrower's student loan repayments as it maintains the status quo. The second change, to lower the $1,500 exemption threshold to $500 will have fairly minor positive impacts as repayments amounts are small and no penalties will be imposed on borrows for non-payment.

## Legislative Implications

44. Implementing these proposals requires changes to the Income Tax Act 2007, the Tax Administration Act 1994, the Student Loan Scheme Act 2011 and the KiwiSaver Act 2006.

45. If approved, I propose including the legislative changes resulting from these recommendations in the Taxation (KiwiSaver, Student Loans, and Remedial Matters) Bill which was introduced on 27 June 2019 and referred to the Finance and Expenditure Committee on 23 July 2019. The proposed amendments to give effect to the recommendations would be included in the report back version of the Bill.

## Impact Analysis

*Changes to PIE regime*

46. The Quality Assurance reviewer at Inland Revenue has reviewed the *Changes to the PIE regime* RIA prepared by Inland Revenue, and considers that the information and analysis summarised in the RIA partially meets the quality assurance criteria.

47. In light of the time constraints on the policy development process that are identified in the Key Limitations or Constraints on Analysis section, the reviewer considers that the information in the RIA is as complete as could be expected. However, the time constraint has limited the consultation to KiwiSaver PIEs. Wider public consultation including with other affected PIEs or PIE investors has not been carried out. Consequently, the reviewer cannot be sure that the full range of impacts have been identified or that the proposed option is the best option to address the problem and achieve the desired objectives.

*Student loans*

48. The Quality Assurance reviewer at Inland Revenue has reviewed the *Lowering the student loan repayment threshold for non-salary and wage income and repealing withholding changes for student loan income* RIA prepared by Inland Revenue, and considers that the information and analysis summarised in the RIA partially meets the quality assurance criteria.

49. In light of the time constraints on the policy development process that are identified in the Key Limitations or Constraints on Analysis section, the reviewer considers that the information in the RIA is as complete as could be expected. However, the time constraint has meant that public consultation particularly with affected parties has not been carried out. Consequently, the reviewer cannot be sure that the full range of impacts have been identified or that the preferred option is the best option to address the problem and achieve the desired objectives.

*KiwiSaver*

50. A RIA was prepared to inform the Cabinet decisions made on 21 March 2019. I am now recommending that Cabinet make some changes to the proposal to address feedback that was subsequently received through targeted consultation (focus groups including KiwiSaver employers) and public submissions. Accordingly, the RIA has also been updated to reflect the revised proposal. The revised RIA is attached and the coversheet to this RIA analyses the recommended changes to the original proposal.

51. The Quality Assurance reviewer at Inland Revenue has reviewed the attached 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**

52. There are no human rights implications as a result of the proposals in this paper.

**Gender Implications**

53. The proposals in this paper are gender neutral.

**Disability Perspective**

54. There are no specific disability implications as a result of the proposals in this paper.

**Publicity**

55. I propose to announce the changes contained in this cabinet paper once the Finance and Expenditure Committee has reported back the Taxation (KiwiSaver, Student Loans, and Remedial Matters) Bill. Inland Revenue will include details of the new legislation in a *Tax Information Bulletin* after the Bill is enacted.

**Proactive Release**

56. I propose to delay the proactive release of this Cabinet paper, associated minutes, and key advice papers until the Finance and Expenditure Committee has reported back the Taxation (KiwiSaver, Student Loans, and Remedial Matters) Bill which is due 24 January 2020.



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**Recommendations**

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

1. **agree** that all PIE investors should have their PIE income squared up at the end of the tax year using their correct PIR, which is based on the information Inland Revenue holds for the investor's two previous tax years, with the result forming part of their income tax outcome for that year

2. **agree** that the amendments recommended in 1 apply from the 2020-21 tax year

3. **agree** that Inland Revenue should provide PIE entities with the correct PIR for their investors during the income year for existing PIE investors and for new investors in PIEs if sufficient information is available to Inland Revenue with application from 1 April 2020

4. **note** that on 8 August 2018, the Cabinet Social Wellbeing Committee (SWC)

    agreed to amendments to require student loan deductions from withholding income

    [SWC-18-MIN-0093, paragraph 4]

5. **agree** to recommend that Cabinet rescind the decision referred to in recommendation 4; and instead

6. **agree** to repeal the changes requiring student loan repayments to be deducted from schedular, election-day, and casual agricultural income with effect from 1 April 2020

7. **agree** that the $1500 student loans scheme exemption for non-salary and wage income for New Zealand-based borrowers, above the annual repayment threshold, be lowered to $500

8. **agree** that the application date of the change to allow KiwiSaver members to change their employee contributions rate through their KiwiSaver scheme provider or Inland Revenue be deferred until 1 April 2022 or an earlier date to be set by Order in Council.

9. **note** that on 21 March 2019, the Cabinet Economic Development Committee (DEV)

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

    the income amount members' contributions are calculated from; and

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

    [DEV-19-MIN-0038.1 and CAB-19-MIN-0109]

10. **agree** to recommend that Cabinet rescind the decision referred to in recommendation 9; and instead

11. **agree** that employers be required to report information to Inland Revenue about the income KiwiSaver members' contributions are calculated from for new employees

12. **agree** that the proposed amendments be included in the Taxation (KiwiSaver, Student Loans, and Remedial Matters) Bill for the Finance and Expenditure Committee's consideration

13. **invite** the Minister of Revenue to instruct Inland Revenue and Parliamentary Counsel Office to draft legislation to give effect to the policy proposals and their intent contained in this paper

14. **note** that this Cabinet paper, the associated Cabinet minute, and key advice papers will be proactively released on Inland Revenue's website once the Finance and Expenditure Committee has reported back the Taxation (KiwiSaver, Student Loans, and Remedial Matters) Bill to Parliament.

Authorised for lodgement

Hon Stuart Nash
Minister of Revenue



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# Impact Summary: Changes to the PIE regime

## 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 a policy change to be taken by or on behalf of Cabinet. |

**Key Limitations or Constraints on Analysis**

**Timing**

The system development and testing required to make changes to the Inland Revenue tax administration system START mean that decisions need to be made in advance of the time these changes take effect from. In order for the proposed changes to be able to take effect for the 2019-20 tax year, it is necessary to include any changes in a tax bill at the earliest opportunity.

The Taxation (KiwiSaver, Student Loans, and Remedial Matters) Bill (the KiwiSaver Bill) is currently before the Finance and Expenditure Committee (FEC) and submitters have raised the issue of non-refundability of overpaid PIE tax under the current rules.

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 PIEs (mainly KiwiSaver scheme providers) in relation to a related proposal already in the KiwiSaver Bill. However, as a result of time constraints, wider public consultation has not been carried out.

**Assumptions underpinning impact analysis**

Assumptions have been made in estimating the number of people who are likely to change their prescribed investor rates (PIRs) as a result of Inland Revenue's administrative actions. These assumptions have been based on the amount of PIE tax an investor has over- or underpaid and general behavioural assumptions.


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| Responsible Manager (signature and date): |
| --- |
| **Mike Nutsford**<br><br>Policy Lead<br>Policy and Strategy<br>Inland Revenue<br><br>18 September 2019 |



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## Section 2: Problem definition and objectives

### 2.1 What is the policy problem or opportunity?

The PIE tax rules apply to collective investment vehicles where investors combine resources to make different types of passive investments, for example a managed fund. There are several types of PIEs, each with different tax requirements. In practice most PIEs are multi-rate PIEs. A multi-rate PIE attributes income, losses and tax credits to investors. The tax rate applied to these types of PIEs varies from investor to investor. There are locked-in PIEs where the funds are locked into the scheme (for example all KiwiSaver PIEs and some other locked-in retirement schemes and superannuation funds) and other PIEs that are not locked in.

Under current law, a person investing in a multi-rate PIE elects a tax rate, referred to as their PIR, which approximates their marginal tax rate based on (the lower of) one of the previous two tax years. A person's marginal tax rate is the tax rate that applies to the last dollar they earn. If a person earns more than $70,000 their marginal tax rate would be 33%. However, while marginal income tax rates can be up to 33%, PIE rates are capped at 28%. The investor notifies their elected PIR to their PIE providers. The PIE provider pays tax on the investment income of each investor based on the PIR the investor has notified. If an investor does not provide their PIE with their elected PIR, they default to the highest PIR of 28%.

There are three PIRs: 10.5%, 17.5% and 28%. To determine the correct PIR, an investor in a PIE needs to look at what their taxable income and their PIE income were for the last two income years before the tax year in which the PIR is to be applied. If they have considered the two previous income years and would qualify for two different rates, the PIR is the lower rate. The following table outlines how to work out the PIR to be applied to PIE income:

| **Taxable income** (in either of the last two income years) was… | **and the total income** Taxable income plus PIE income (in either of the last two income years) was… | before the relevant tax year for … | the **PIR** is … |
|---|---|---|---|
| $0 – $14,000 | $0 - $14,000 | Either year | 10.5% |
| $0 – $14,000 | $14,001 - $48,000 | Either year | 10.5% |
| | $48,001 - $70,000 | Either year | 17.5% |
| $14,001 – $48,000 | Up to $48,000 | Either year | 17.5% |
| $48,001 or more | Over $48,000, but under $70,000 | Both years | 28% |
| Any amount | $70,001 or more | Both years | 28% |

When the correct PIR has been used or where a too high rate has been used, the income from PIE investment is excluded income[1], which means it is a final tax and the PIE income does not flow through to the investors' individual income tax return and assessment.

[1] Certain types of income are expressly treated as "excluded income" by specific provisions of the Income Tax Act 2007. Excluded income is omitted from a person's calculation of income tax for an income year.

Therefore, where an investor has elected a rate that is too high, or they have defaulted to the highest PIR but could have elected a lower PIR, the overpaid tax on their PIE income can't be refunded. To use a PIR below 28% and therefore potentially be affected by the non-refundability, people must have had taxable income of less than $48,000 in at least one of the two previous income years.

However, where tax on PIE income has been underpaid because the investor has notified a rate that is too low, the PIE income ceases to be excluded income and is required to be included in the investor's income. It is taxed at the investor's marginal tax rate. A tax credit is given for the PIE tax that has already been paid. This is intended to incentivise the investor to notify the correct PIR as they can be subject to a marginal tax rate of up to 33%, while the top PIR is capped at 28%.

The difference between the treatment of over- and underpaid PIE tax raises equity concerns, in particular in relation to the non-refundability of overpaid tax on PIE income.

Data analysis enabled by Inland Revenue's new technology platform START estimates that approximately 1.5 million people have used incorrect PIRs for the year ended 31 March 2019. Inland Revenue is working on a range of administrative initiatives to help ensure people are on the correct PIRs. This involves proactively contacting investors who are on an incorrect rate and suggesting they contact their PIE provider to change their rate.

Under current legislation Inland Revenue has the power to notify a PIE provider of the PIR that should be used where someone has notified the wrong rate. However, because of the way the legislation is worded, this is limited to people who have notified their PIE provider of their rate as opposed to people who have not provided a rate and therefore have defaulted to a 28% rate. Inland Revenue is unable to determine from the information held in its systems, whether a person on a 28% rate has notified that rate or defaulted to it and therefore cannot notify PIE providers of the PIR for anyone on the 28% rate.

*Change currently proposed in the KiwiSaver Bill*

A legislative change proposed in the KiwiSaver Bill, which is currently being considered by the Finance and Expenditure Committee, would allow Inland Revenue, when it holds sufficient information about an investor's income for the previous two income years, to directly notify the PIE provider of the PIR that should be used in all cases where an incorrect PIR is being used. This proposed change would apply from 1 April 2020.
This change will not remove the issue that overpaid PIE tax is not refundable. Inland Revenue advising the PIE provider directly to change to a correct rate where Inland Revenue systems identify that an incorrect PIR is used is expected to significantly reduce the numbers of people on a wrong rate (too high or too low). However, there will still be some situations where an incorrect PIR is used resulting in over- or underpayment of tax.

For example, where people who have to provide income information to Inland Revenue have an extension of time to provide that information, they may not be required to provide that additional information until 31 March of the following year. This information could be received too late to allow Inland Revenue to take it into account when providing PIRs to PIE providers. This could mean that their PIR was only based on the earlier of the two relevant previous. If they earned less income in the more recent year, they might be entitled to use a lower PIR



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than the one Inland Revenue might be able to provide. Without legislative change Inland Revenue would not be able to provide a refund in those cases.

Also, for new members of PIEs , there would have to be one incidence of using a wrong PIR for the new investor, before Inland Revenue could determine that the rate used is incorrect and can notify the PIE of the correct PIR.

When an investor exits a PIE, this triggers a calculation and payment of their PIE tax at that time. There is a risk that some investors could exit from their PIE investment before the correct rate had been able to be provided by Inland Revenue and could over- or underpay PIE tax.

There is also a small risk that Inland Revenue could provide an incorrect PIR if it held incorrect information. This should only happen when a person has not provided required information.

## 2.2 Who is affected and how?

*Inland Revenue*
Inland Revenue cannot currently refund overpaid PIE tax and has limited ability to provide correct PIRs to PIE providers.

*PIEs*
PIEs are not currently provided with correct PIRs by Inland Revenue. They are often not notified of their investors' PIRs and therefore have to use the 28% default rate.

*PIE investors*
PIE investors are currently required to notify their PIE provider of their correct PIR. This requirement is not effective for a large number of PIE investors. Rather than changing PIE investor behaviour, it is more effective to widen Inland Revenue's ability to directly provide PIRS to PIE providers and for PIE providers to use the provided rate.

## 2.3 Are there any constraints on the scope for decision making?

No constraints were identified.

# Section 3: Options identification

## 3.1 What options have been considered?

The following criteria were used to assess the options considered:

- *Equity*: the option should ensure that all PIE investors pay the correct amount of tax on their PIE income.
- *Sustainability*: the option should ensure that the PIE regime is certain and predictable for both PIE providers and investors. The PIE regime should be seen as being fair for investors.
- *Compliance*: compliance cost should be minimised for investors and PIE providers as far as possible.
- *Administration*: implementation and administration costs for Government departments should be minimised as far as possible.

**Option 1: Status quo**

Should the proposed legislative change already in the KiwiSaver Bill be enacted, this would enable Inland Revenue to advise PIE providers directly to change to a correct rate where Inland Revenue systems identify that an incorrect PIR is used. This is expected to significantly reduce the number of people on a wrong rate (too high or too low).

Some PIE investors would still have incorrect PIE tax deducted before Inland Revenue could determine the PIR used is incorrect and advise the PIE provider of the correct PIR to be used for their investors.

The status quo would not remove the issue that some PIE investors would have been on the wrong PIR and may have overpaid PIE tax. Any amount of overpaid PIE tax would continue to not be refundable.

The inconsistent treatment of under- and overpaid PIE tax under the current law is not equitable and the difference potentially threatens the sustainability of the PIE tax regime can be thought of as being unfair.

The status quo does involve some increase in compliance and administrative costs compared to previous years due to Inland Revenue providing PIRs directly to PIE providers where people are on incorrect PIRs (and notifying people that their PIR has been changed) and the need for PIE providers to process increased numbers of PIR change requests.

**Option 2: Mirror the existing treatment of underpayment of PIE tax for overpaid PIE tax**

This option would mirror the existing legislative rules for PIE investors who have notified their PIE provider with a rate for their PIE income which is lower than their correct PIR. This would mean that if an incorrect rate had been used, either lower or higher, the PIE income would cease to be excluded income. The income would then be required to be included in the individual investors' income tax return. It would be taxed at the investor's marginal tax rate for the tax year. A tax credit would be given for the PIE tax that has already been paid.

This option would in some cases result in an inequitable outcome. This is because while the PIR approximates the investor's marginal tax rate, it is based on (the lower of) one of the



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previous two tax years. In some cases an investor who has their PIE income taxed at their current year's marginal tax rate because they have overpaid the tax on their PIE income using a too high PIR, may still have a tax bill when their marginal tax rate is higher than both their correct PIR and the rate used.

As well as being inequitable, the cases where a person would have to pay more tax at their marginal tax rate when they had been on too high a PIR could also reduce the sustainability of the PIE regime. Potential media coverage of such situations could reduce public and political trust in the PIE regime.

This option would be more complex to implement in Inland Revenue's systems than option 3 due to the need to identify where a person has been on an incorrect rate before making the adjustment to their taxable income. It would therefore have a level of additional administrative cost (this cost hasn't been estimated).

As with all options, there would also be some increase in compliance and administrative costs compared to previous years. This is due to Inland Revenue providing PIRs directly to PIE providers where people are on incorrect PIRs (and notifying people that their PIR has been changed) and the need for PIE providers to process increased numbers of PIR change requests.

**Option 3: Ability to proactively provide PIRs to PIES effective from 1 April 2020 and a year-end square-up**

**a. with application of the year-end square-up from the 2019-20 tax year**

**b. with application of the year-end square-up from the 2020-21 tax year**

This option would enable Inland Revenue to pro-actively provide PIRs for all investors to the PIE providers where Inland Revenue holds sufficient information to determine the PIR applicable for the tax year. Inland Revenue would also advise the investors that their PIR had been changed. This would mean that investors would largely be placed on the correct PIR which PIE providers would use to calculate tax during the tax year.

There would still be a risk that some investors could exit from their PIE investment before the correct rate had been able to be provided. These investors could under- or overpay PIE tax. There is also a risk that Inland Revenue could possibly provide an incorrect PIR if it held incorrect information.

An additional year-end square-up applying the correct PIRs would address any over- or underpayment of PIE tax during the tax year.

All PIE income would have the correct PIR applied to it in the year-end square-up, regardless of whether it has been correctly, over- or under-withheld during the tax year. It would not be relevant whether a correct, too low or too high PIR has been notified. This would be a change compared to the current treatment for investors who have notified a PIR that is too low, as their PIE income would no longer be subject to their marginal tax rates, but to their correct PIR.

The year-end square-up would involve Inland Revenue taking a person's PIE income and applying their correct PIR to it to determine the PIE tax payable. The PIE tax that had been deducted would be a tax credit against the PIE tax payable. Any refund due or tax payable would be added to the person's end of year tax position and would either be refunded,



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payable or reduce the person's tax payable.

For most individual investors the square-up would happen automatically and they would not be required to do anything. It would be an automated process similar to and alongside the year end auto-calculation process for income tax. Investors would have additional PIE information added to their income profile information.

For investors who are required to file an income tax return, the PIE income information Inland Revenue holds would be pre-populated into their income tax profile to be available when they file their income tax return. For them the PIE income calculation would happen alongside the income tax process once they have filed their tax return for the tax year.

While the timing of the PIE square-up would be aligned with that of the general income tax year-end process for each individual, the PIE square-up would be a separate process, using current PIRs and thresholds. That is, a PIE square-up would be undertaken and the difference, if any, would be included in the income tax year-end process. The difference would either increase a person's refund, reduce tax payable, reduce the refund or increase the amount payable. Refunds would be made directly to the individual investors and not to the PIEs. Similarly, PIE tax payable would be paid by the investor and not out of their PIE funds.

The PIE square-up would not affect a person's provisional tax liability. This is because any PIE tax payable or refundable would be added after the calculation of the person's residual income tax (which is the basis for a person's provisional tax liability).

The first measure would get most people onto the correct PIR before any PIE tax is deducted during the tax year. In situations where this did not occur the second measure, the year-end square-up, would ensure that the person still only paid the correct amount of PIE tax. The combination of the two measures, therefore, gives the most equitable outcome.

This option would preserve the current PIRs based on one of the previous two tax years, including the maximum tax rate for PIEs being 28% and the current thresholds for investors in these PIEs. It would also ensure that all people are taxed at their correct PIR so would give consistent and understandable outcomes. These factors support the sustainability of the PIE regime.

This option would involve some initial compliance costs as the PIE providers would have to adjust their systems to be able to receive and apply PIRs from Inland Revenue in more situations than just for corrected PIRs where the rate the investor had notified is incorrect. This is not expected to be materially greater than the additional compliance costs that would be caused under the status quo and option 2 by Inland Revenue providing PIRs directly to PIE providers where people are on incorrect PIRs and notifying people that their PIR has been changed and the need for PIE providers to process increased numbers of PIR change requests.

There would be some one-off administrative costs in developing the year end square-up which Inland Revenue will absorb within existing Business Transformation baselines.

***Option 3 a***

This sub-option would ensure that these benefits would apply to the current tax year (2019-20). Inland Revenue's current efforts to notify people that they are on incorrect PIRs would reduce the number of PIE investors on an incorrect PIR but would still leave a large number



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of people on incorrect rates during the 2019-20 tax year. Officials have estimated that approximately 830,000 people would still be on a rate that is too high.

The proposed year-end square-up would have a one-off fiscal cost if applied from the 2019-20 tax year. This is because it would correct the PIE tax position for the 830,000 people estimated to be on a rate that is too high. This sub-option would have immaterial fiscal costs for the following years as the changes already in the KiwiSaver Bill that would allow Inland Revenue to inform PIE providers of the correct PIRs for their investors would mean that almost all PIE investors will be on the correct PIR in the 2020-21 tax year.

***Option 3 b***

This sub-option would mean that approximately 830,000 people (who have earnt less than $48,000 of taxable income in one of the two previous income years) would pay too much PIE tax in the 2019-20 tax year without the ability to get the overpaid tax refunded. As such it is less equitable than sub-option 3 a.

If the PIR changes are enacted with application from 1 April 2020, Inland Revenue would be able to significantly reduce the number of PIE investors on an incorrect rate for their PIE income during the 2020-21 tax year. This would mean that the application of the year-end square-up to that tax year would not have an effect on many people and therefore would have immaterial fiscal costs.

## 3.2 Which of these options is the proposed approach?

The preferred approach is option 3 a which:

- Provides Inland Revenue with the ability to proactively provide PIEs with their investor's PIRs during the tax year where Inland Revenue holds sufficient information to determine the PIR applicable for the tax year.
- Square up all PIE income at the end of the tax year using the PIE investors' correct PIR based on the information Inland Revenue holds about the previous two income years with application from the 2019-20 tax year.

Of the considered options, option 3 a would be most effective in assuring that people are on the correct PIR and refunds of overpaid PIE tax for people on PIRs that were too high are allowed.

It is also the most coherent and equitable option as it will ensure that most investors have the correct amount of tax deducted from their PIE income from the start. All investors will pay the correct amount of tax on their PIE income through a year-end square-up process, including those who have over- or under-paid tax during the year.

Option 3 b would mean that approximately 830,000 people (who have earnt less than $48,000 of taxable income in one of the two previous income years) would pay too much PIE tax in the 2019-20 tax year without the ability to get the overpaid tax refunded.



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Option 3 a would address unfairness concerns for the current tax year, however it does have a one-off fiscal cost.

It is the option that is the least complex and is therefore easiest to understand for investors, as all PIE income, whether correctly, over-, or undertaxed, has the same year-end process.

It is the option that is easiest to implement in Inland Revenue systems.

Officials recommend option 3 a as it gives an equitable outcome for PIE investors and has manageable compliance and administrative costs given the benefits being delivered.



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## Section 4: Impact Analysis (Proposed approach)

### 4.1 Summary table of costs and benefits

| **Affected parties** *(identify)* | **Comment**: nature of cost or benefit (eg ongoing, one-off), evidence and assumption (eg compliance rates), risks | **Impact** *$m present value, for monetised impacts; high, medium or low for non-monetised impacts* |
|---|---|---|
| Additional costs of proposed approach, compared to taking no action | | |
| Regulated parties (*PIE providers, PIE investors* ) | *PIE providers*<br>PIE providers may have to adjust their systems to be able to receive and apply their investors' PIRs provided by Inland Revenue as opposed to current law where they would only be required to receive PIRs from Inland Revenue for those investors that have notified them with an incorrect rate or have defaulted onto the default PIR and could have elect a lower rate.<br><br>*PIE investors*<br>PIE investors will see some additional information regarding their PIE income and tax in their end of year tax calculation. This will be prepopulated by Inland Revenue so will not require PIE investors to provide additional information. | Low (one-off and ongoing)<br><br>Low |
| Regulators (*Inland Revenue*) | This proposal does not require additional funding in relation to administrative costs. System changes to implement the proposals would be absorbed as part of Business Transformation baselines.<br><br>Fiscal cost of amount of overpaid PIE tax that would be refunded in the 2019-20 tax year. | Administrative costs estimated at $1.5 million<br><br>Approximately $23.2 million (one-off in relation to the 2019-20 tax year, immaterial fiscal ongoing cost from the following year going forward)<br>This cost contains of<br>• $22.6 million of overpaid PIE tax corrected by way of the square-up mechanism; and |



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| | | • $0.6 million of underpaid PIE tax corrected by way of the square-up mechanism using their correct PIR and not to their marginal tax rate as is currently the case.<br>(option 3b - if the year-end square-up applied from the 2020-21 tax year there would be no material fiscal cost as PIE investors would, if the law change in the KiwiSaver Bill is enacted, largely be on the correct PIR during the tax year from 1 April 2020.) |
|---|---|---|
| Wider government | None identified. | Nil |
| Other parties | None identified. | Nil |
| **Total Monetised Cost** | | Administrative costs estimated at $1.5 million<br>Fiscal cost approximately $23.2 million (one-off, immaterial fiscal ongoing cost) |
| **Non-monetised costs** | Compliance costs on PIE providers | Low |

| Expected benefits of proposed approach, compared to taking no action | | |
|---|---|---|
| Regulated parties<br>(*PIE investors*) | *PIE investors*<br>PIE income for most investors will be deducted during the tax year using the correct PIR and will no-longer be subject to over-taxation without refundability.<br>PIE investors who are choosing a too low rate will only be moved up to their correct PIR (instead of marginal tax rate) | Approximately $23.2 million (one-off in relation to the 2019-20 tax year, immaterial fiscal ongoing cost from the following year going forward)<br>This cost contains of<br>• $22.6 million of overpaid PIE tax corrected by way of the square-up mechanism; and<br>• $0.6 million of underpaid PIE tax corrected by way of the square-up mechanism using their correct PIR and not to their marginal tax rate |



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| | | as is currently the case. (option 3b - if the year-end square-up applied from the 2020-21 tax year there would be no material fiscal cost as PIE investors would, if the law change in the KiwiSaver Bill is enacted, largely be on the correct PIR during the tax year from 1 April 2020.) |
|---|---|---|
| Regulators (Inland Revenue) | None identified. | Nil |
| Wider government | None identified. | Nil |
| Other parties | None identified. | Nil |
| **Total Monetised Benefit** | | Approximately $23.2 million (made up of amounts that will be refunded in relation to the 2019-20 tax year and amounts that will not be charged at higher marginal tax rates). |
| **Non-monetised benefits** | Increase in those PIE investors' retirement savings who will be put on a correct PIR and will no longer have overpaid their PIE tax. | Low |

### 4.2 What other impacts is this approach likely to have?

Where an investor in a locked in PIE such as KiwiSaver went back to their PIE provider and asked to be put back on a PIR that was too high, the year-end square up would enable them to get a refund of money that should have remained in their locked-in PIE investment. While this is a cash in hand benefit for the investor it is also a future disadvantage for them as it will reduce their retirement savings and it undermines the reason for their PIE fund being locked-in.

Investors may go back and may notify a lower rate than their correct PIR to their PIE provider to receive a time value of money advantage during the year until the end-of-year square-up. Previously investors were incentivised not to notify a rate that is too low, as in those cases the PIE income becomes part of the investor's income tax assessment and is then taxed at the investor's marginal tax rate. A person's marginal tax rate is the tax rate that applies to the last dollar they earn. If a person earns more than $70,000 their marginal tax rate would be 33% (whereas the top PIR is 28%).

Notifying a lower PIR than the correct PIR would mean that more money would be paid into the person's PIE investment but also that they would subsequently have to pay more tax at the end of the year. If the PIE was a locked in PIE, such as KiwiSaver, they would effectively be making a further contribution to their retirement savings as they would have to fund the PIE tax that they would have to pay at the end of the year from their other income.

Officials propose to monitor whether people are manipulating the rules to their advantage to determine whether any specific action is required to prevent this.

## Section 5: Stakeholder views

### 5.1 What do stakeholders think about the problem and the proposed solution?

Inland Revenue has undertaken targeted consultation with KiwiSaver PIE providers around the initial proposal to widen the ability to provide PIRs for all PIE investors where Inland Revenue holds sufficient information.

PIE providers are generally supportive of the proposal to enable Inland Revenue to provide PIEs with their investor's correct PIR. As previously stated, this is widening the Commissioner's existing ability to provide the PIE with their investor's correct PIR where the investor has notified the PIE with an incorrect rate.

However, submissions by PIE providers and their representatives to the Finance and Expenditure Committee in response to the proposal on correcting PIRs already contained in the Taxation (KiwiSaver, Student Loans, and Remedial Matters) Bill highlight the need for sufficient lead in time to allow PIEs to change their systems to incorporate rate changes notified by Inland Revenue.

General consultation with PIE investors has not been undertaken. However, the proposals are beneficial to PIE investors as most investors will have tax on their PIE income deducted

using their correct PIR and all investors will have their PIE tax squared for a tax year using their PIR.

Media attention in mid-2019 and a Parliamentary petition also raised fairness concerns around the non-refundability of overpaid tax on PIE income. The Parliamentary petition also requests, amongst other points, to place an annual obligation on Inland Revenue to notify all KiwiSaver PIE providers what their members' PIRs should be. The main concern the petition is trying to address is that many New Zealanders (particularly those auto-enrolled into KiwiSaver) are over-taxed and unaware. At the time this Regulatory Impact Assessment was written, the petition was still open for signatures and had 348 signatures.

One submission to the Finance and Expenditure Committee on the Taxation (KiwiSaver, Student Loans, and Remedial Matters) Bill suggests that a mechanism should be introduced to provide a form of refund for an over-taxed PIE investor.

The Treasury have been consulted on the proposals and support them.

# Section 6: Implementation and operation

## 6.1 How will the new arrangements be given effect?

The proposals would require amendments to the Income Tax Act 2007 and the Tax Administration Act 1994. One submission the Finance and Expenditure Committee received on the KiwiSaver Bill raises concerns that as introduced it does not contain a proposal that will enable a refund for people who have overpaid PIE tax. It was submitted that a mechanism should be introduced to provide a form of refund for an over-taxed investor. Amendments to the KiwiSaver Bill would be proposed in the officials' report to the Finance and Expenditure Committee for the Committee's consideration. However, this will not allow for public opportunity to comment.

The changes would come into effect from 1 April 2020. This would align with the date the proposal on allowing the Commissioner to correct all PIRs contained in the KiwiSaver Bill as introduced which was timed to align with the transfer of the administration of KiwiSaver from Inland Revenue's FIRST operating system into its new START operating system.

Inland Revenue would proactively advise PIE providers of the correct PIRs for their customers on incorrect PIRs. The PIE providers would need to be able to receive and apply the PIRs and this is likely to mean that PIE providers will need to make systems changes. Inland Revenue has begun discussions with PIE providers about how the correct PIR information could be provided and will work with PIE providers to ensure that the information is passed in a way that can be used by them.

The square-up of PIE tax would apply from the 2019-20 tax year and would happen for the first time around June 2020 for individuals who do not have to file a tax return. For all others the PIE tax square-up will happen when they file a tax return and their income tax assessment is completed. The square-up would not require any change to the information that is currently being provided by PIE providers.

The Minister of Revenue would make an announcement, on the proposal when the Finance and Expenditure Committee has reported back the KiwiSaver Bill.

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 and annual income tax refresh, would mean the cost of system changes would be absorbed into existing Business Transformation baselines.



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## 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 already collects data on PIE income and tax paid on that income. This data would be used to assess the effectiveness of the changes. The number of year-end square-ups that gave rise to an amount of PIE tax payable or refundable would show the effectiveness of the proposed changes to get PIE investors on the correct PIRs.

### 7.2 When and how will the new arrangements be reviewed?

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.

In relation to KiwiSaver PIEs, 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 to providing them with their investor's PIR.

# Cover page: revised proposal

**Summary of revised proposal**

The original version of the attached impact summary entitled, *Business Transformation related KiwiSaver refinements*, was prepared to inform Cabinet decisions made on 21 March 2019. The RIA proposed a number of KiwiSaver administrative refinements to form part of Release 4 of Inland Revenue's Business Transformation programme. Subsequent concerns raised by stakeholders about the employer compliance costs of certain proposals, have resulted in officials revising the impact of these proposals and recommending the following changes:

- deferring KiwiSaver members being able to change their contribution rate through their scheme provider or Inland Revenue to 1 April 2022 or an earlier date set by Order in Council;
- removing the change requiring employers to report an employee's employer superannuation contribution tax (ESCT) rate to Inland Revenue; and
- only requiring employers to report to Inland Revenue the income KiwiSaver contributions are calculated from for new employees (the attached regulatory analysis proposed this information be reported for existing employees where it had changed since it was reported, in addition to new employees).

All other aspects of the proposed approach remain unchanged, and the re-assessment below relates only to the proposals that officials are recommending changes to. The attached RIA has also been updated to reflect the revised recommendations.

**Problem definition**

Stakeholders have raised concerns about employer compliances costs in relation to the proposals to allow KiwiSaver members to change their contribution rate through their scheme provider or Inland Revenue (as this would require employers to apply contribution rates advised by Inland Revenue) and the proposals to require employers to report ESCT rates and KiwiSaver income information to Inland Revenue, for new employees and existing employees where this information has changed. Concerns raised about additional compliance costs on employers hold particular weight at this time, given the number of earlier Business Transformation changes that are currently bedding in with employers (for example payday filing, which became compulsory for employers to comply with from 1 April 2019).

Officials have also undertaken further analysis of the issue of incorrect ESCT payments by employers, which has indicated the problem may often arise as a result of an employer not determining the correct ESCT rate in the first place, rather than calculating the ESCT deduction incorrectly. As a result, the benefit of collecting ESCT rate information may not be as significant as officials originally considered it to be.

**Options considered**

*Option A: proceed with all proposals agreed to by Cabinet on 21 March 2019*

Under this option no changes would be made to the proposals previously agreed to by Cabinet. This would be undesirable as it would result in concerns about employer compliance costs not being addressed.



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*Option B: do not proceed with proposals*

Under this option both the contribution rate change and employer reporting requirement proposals would not be proceeded with. This outcome would be undesirable as it would not address the issues raised in the problem definition in the attached RIA about improving existing information flows to help ensure KiwiSaver members are receiving their correct contribution entitlements and giving members more flexibility about how they change their contribution rate.

Removing the proposal to allow members to change their contribution rates through a scheme provider or Inland Revenue, would also not recognise this change has received positive feedback from the KiwiSaver industry and KiwiSaver members.

*Option C: modify proposals to minimise compliance costs and allow for further stakeholder engagement*

The application date of the proposal to allowing members to change their contribution rate through their scheme provider or Inland Revenue would be deferred until 1 April 2022 (or an earlier date set by Order in Council). Deferring the application date would enable officials to undertake further consultation with stakeholders to explore concerns raised in more detail and to investigate operational processes that would minimise the compliance cost of this change on employers.

The proposal to require employers to report employees' ESCT rates to Inland Revenue would be removed from the Bill. Based on feedback received about the compliance cost of this change for employers, in addition to the fact further analysis has indicated the root of the problem may not be employers miscalculating ESCT deductions, officials now consider the costs of this change to employers is likely outweigh the benefits to Inland Revenue.

Under this option employers would also only be required to report to Inland Revenue the income KiwiSaver contributions are calculated from for new employees (not for existing employee's where this information has changed since last reported, as was previously proposed). Employer compliance costs would be minimised, as this information would be provided on a "one-off" basis, as part of existing new employee on-boarding processes. While it would still ensure Inland Revenue received the benefit of KiwiSaver income information, which could be used to identify miscalculation of contributions.

**Proposed approach**

For the reasons outlined above, the proposed approach is Option C.

**Stakeholder views**

The original RIA noted that limited consultation had been a constraint on decision making. The proposal has been revised to incorporate feedback that was subsequently received through targeted consultation (focus groups including employers) and public submissions received by Select Committee. These changes are described in option C above and are expected to reduce compliance costs compared to the original proposal.



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# 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 was not carried out prior to original Cabinet decisions being made in March 2019. 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 (they would be required to communicate information they already hold to Inland Revenue, on a one-off basis and apply KiwiSaver employee contribution rates advised by Inland Revenue). Targeted consultation with employers was undertaken subsequent to March 2019 Cabinet decisions being made. Feedback from this consultation has informed officials revising the assessment of certain proposals.

**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.


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| Responsible Manager (signature and date): |
| --- |
| Chris Gillion<br>Policy Lead<br>Policy and Strategy<br>Inland Revenue<br>12 September 2019 |


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## 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. However, in some instances, Inland Revenue does not have access to sufficient information to effectively police the accuracy of contribution

amounts received from employers.

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. While the proposal enabling KiwiSaver members to change their contribution rate through their scheme provider or Inland Revenue, would require employers to deduct employee contributions from salary and wages at rates advised by Inland Revenue. These changes would create additional compliance costs for employers.

**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.



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



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# 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.[1]

*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

[1] 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.



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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,[2] in respect of new employees. 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). Employers would be advised of the employee's contribution rate change request by Inland Revenue.

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 removing the 3-month grace period would increase administrative efficiency.

*Compliance:* The option would reduce compliance costs for members looking to change contribution rates. However, this would increase compliance costs for employers, as they would be required to apply contribution rates advised by Inland Revenue. There would also 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

[2] 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.

provider when a member transfers schemes and the additional employer information requirements, respectively.

*Equity:* The additional employer information should make it easier for Inland Revenue to identify situations where contribution amounts have been calculated 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.


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| 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:<br><br>• 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);<br>• 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;<br>• reducing the KiwiSaver provisional period from 3-months to 2-months;<br>• 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;<br>• allowing members to change contribution rates through their scheme provider or Inland Revenue, rather than only through their employer;<br>• removing the 3-month grace period for members who have been incorrectly automatically enrolled in KiwiSaver, to gain New Zealand residence; and<br>• requiring employers to provide Inland Revenue with information about the income KiwiSaver contributions are calculated from for new employees.<br><br>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.<br><br>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.<br><br>The proposed approach is not incompatible with the Government's '*Expectations for the design of regulatory systems*'. |


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## 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*<br>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 0.72% 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.[3] | Low. |
| | *Scheme providers*<br>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*<br>Employers would need to provide Inland Revenue with information about the income KiwiSaver contributions are calculated from. 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 as part of employee on-boarding processes.<br><br>Employers would also need to start applying contribution rate changes | Low. |

[3] 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.



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| | | |
|---|---|---|
| | advised by Inland Revenue. This would create a more complex system of record keeping and communication for employers. | |
| Regulators (*Inland Revenue*) | The proposals do not require additional funding.<br><br>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.<br><br>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*<br>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.<br><br>*Scheme providers*<br>The proposals would result in 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. | Medium.<br><br><br><br><br><br><br><br><br><br><br>Medium. |



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| | | |
|---|---|---|
| | *Employers*<br>Most of the changes would not directly impact employers. The additional employer information requirement 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.<br><br>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).<br><br>Under $500,000 per annum.[4] |
| Wider government | None identified. | Nil. |
| Other parties | None identified. | Nil. |
| **Total Monetised Benefit** | | $760,000. |
| **Non-monetised benefits** | | *Medium.* |

[4] 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).


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### 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 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.

Consultation with KiwiSaver members was not undertaken prior to original Cabinet decisions in March 2019. 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. Some subsequent consultation has been undertaken with KiwiSaver members, in the form of focus groups. Participants were supportive of the proposals.

The original proposed approach included employers being required to provide Inland Revenue with KiwiSaver income information and ESCT rates for new employees and existing employees where this information had changed since it was last provided. It also included KiwiSaver members being able to change their contribution rate through Inland Revenue or their KiwiSaver scheme provider from 1 April 2020. The impacts of the proposals were not tested with employers prior to original Cabinet decisions in March 2019. However, subsequently targeted consultation has been undertaken with employers and payroll providers (in the form of focus groups). Public submissions have also been received through the Select Committee process.

Feedback on the above proposals was that the compliance costs on employers were likely to outweigh the benefit to KiwiSaver members and Inland Revenue. Officials have taken this feedback into account by modifying the additional employer information requirements, so that

under the revised approach employers would only be required to provide information about income KiwiSaver contributions are calculated from for new employees (not every time this information changed) and would not be required to report ESCT rates. As a result, the modified reporting requirements could be incorporated into the employee onboarding process, therefore, reducing employer compliance costs. Moreover, the application date for the contribution rate change proposal has been deferred (this change would now apply from 1 April 2022 or an earlier date set by Order in Council). The later application date would enable further consultation with employers and allow time to devise an operational approach that would minimise employer compliance costs.



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# 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.<br><br>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 only exception to this would be the proposal to allow members to change their contribution rate through their KiwiSaver scheme provider or Inland Revenue which would apply from 1 April 2022, or an earlier date set by Order in Council.<br><br>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. |



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## 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.<br><br>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.<br><br>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. |


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# Impact Summary: Lowering the student loan repayment threshold for non-salary and wage income and repealing withholding changes for student loan income

## Section 1: General information

| Purpose |
|---|
| Inland Revenue is responsible for the analysis and advice set out in this Regulatory Impact Statement, except as otherwise explicitly indicated. This analysis and advice have been produced for the purpose of informing key (or in-principle) policy decisions to be taken by Cabinet. |

**Key Limitations or Constraints on Analysis**

The key limitations on the analysis are as follows.

### Threshold changes

In preparation for the transition of Student Loans repayments to IRD's new systems and process, an issue has been discovered. If not addressed, the issue would affect the integrity of the system and introduce inequity. The administration of Student Loans is due to go live as of April 2020, so it is necessary to address this issue immediately. This urgency has imposed a limitation on analysis.

**No consultation with external stakeholders**
The timing around the identification of this issue has meant that no consultation has occurred with borrowers or representative groups. However, only approximately 25 borrowers per year are expected to be affected.

**Scale of the problem and impact on borrowers**
The scale of the problem is low. The proposal is limited to borrowers whose total income is above the $19,760 repayment threshold and who have between $500 and $1500 of non-salary and wage income. From information Inland Revenue holds, the total number of borrowers who earned over the loan repayment threshold and had non-salary and wage income between $500 and $1500 was 25 borrowers for the 2018 income year.

In terms of the impact on borrowers, the maximum increase in repayment obligations will be $179 per annum. If borrowers pay this amount, then the time it will take them to repay their loan will be reduced slightly. If borrowers do not pay, then the amount will be capitalised back onto their loan and the loan balance and term of the loan will remain the same. No penalties will be imposed for non-payment.

**Impact of proposals on the student loan valuation**
The benefits from the proposal will not have a material impact on the student loan valuation

None of the limitations materially affect the analysis.



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### Withholding changes

In the process of consultation on the implementation of changes previously passed into law, officials have been made aware that the change to require student loan repayments to be withheld from schedular, casual agricultural, and election day income earned by borrowers would impose significant compliance costs on employers. These issues were not raised previously in public consultations on the policy proposals or in submissions to select committee.

This urgency does not materially affect the analysis.

| **Responsible Manager (signature and date):** |
| --- |
| Martin Neylan<br>Principal Policy Advisor<br>Policy and Strategy<br>Inland Revenue<br><br>18 September 2019 |



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# Section 2: Problem definition and objectives

## 2.1 What is the policy problem or opportunity?

### Threshold changes

The student loan scheme currently has a $1500 threshold for non-salary and wage income for New Zealand-based borrowers, above the annual repayment threshold. Borrowers who earn $1500 or less of non-salary and wage income (including schedular, casual agricultural, and election day income) in a year are not required to notify Inland Revenue of this income for student loan purposes and do not have to make student loan repayments on it. If a borrower earns more than $1500 of non-salary and wage income, they are required to make repayments on the full amount.

This threshold was introduced when most salary and wage earners were not required to file a tax return and recognised the additional compliance costs associated with borrowers advising Inland Revenue of their income for student loan purposes only.

However, from 1 April 2019, legislative changes were made to the administration of individual's income tax. Now all taxpayers either file a return or have their income tax automatically squared up at the end of the tax year based on information from third parties reported during the year or information provided for tax purposes at the end of the year. As a result, there is no longer a significant compliance cost for borrowers in advising Inland Revenue of their non-salary and wage income. Therefore, the current threshold is set at a level that is higher than the compliance costs involved in providing this information to Inland Revenue.

Inland Revenue's Business Transformation programme is now moving the repayment of student loans into the new computer systems and processes. This process has highlighted the issue of the $1500 threshold being set at a level that does not reflect the compliance costs involved in providing information to Inland Revenue. It is also an opportune time to reduce the threshold and any changes to the threshold would be included in this transformation process.

### Withholding changes

Legislation currently enacted and due to take effect from 1 April 2020 would require Student loan deductions to be made from schedular, casual agricultural, and election day income each pay day. This change would affect approximately 33,000 borrowers and approximately 11,000 employers.

These changes were intended to address non-compliance by some borrowers earning this income. They would impose compliance costs on employers and potentially reduce compliance costs on borrowers. The changes do not affect the borrower's overall student loan repayment obligations but would have changed the way that these are met. Rather than make two interim payments and have an end-of-year square-up, borrowers would instead have deductions made from their income with an end-of-year square-up.

Consultation as part of Inland Revenue's business transformation programme has indicated that this change would impose significant, unforeseen, compliance costs on employers. These costs vary depending on the size of the employer and the complexity of their systems, but consultation has indicated that these costs are typically relatively large, both initially and on an ongoing basis.



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## 2.2 Who is affected and how?

### Threshold changes

The proposal is to reduce the threshold would affect borrowers with non-salary and wage income of between $500 and $1500 above the $19,760 repayment threshold. The number of borrowers likely to be affected is 25 borrowers per year.

The maximum additional repayment amount resulting from lowering the threshold would be $179 per annum per borrower payable with their end of year tax return. Those borrowers with non-salary and wage income either above $1500 or below $500 would not experience a change in their current treatment.

Retaining the current threshold level increases inequity between borrowers with salary and wage income (who make repayments on all income above the repayment threshold) and those with non-salary and wage income (who have an additional $1500 above the $19,760 repayment threshold before repayments apply).

This change would mean that approximately 25 affected borrowers each year would be required to make repayments and if payments are made, these would reduce the term of their loans. If the affected borrowers do not make payments, provisions in the Student Loan Scheme Act 2011 allow unpaid amounts of less than $334 to be capitalised back onto the loan balance, so no borrowers whose total non-salary and wage income is between $500 and $1,500 will be subject to penalties if they do not make repayments and the debt to the Government will not increase.

### Withholding changes

The change to student loan deductions on schedular, casual agricultural, and election day income would impose compliance costs on employers and seeks to reduce non-compliance by recipients of these payments. Repealing these provisions would avoid these compliance costs being imposed.

## 2.3 Are there any constraints on the scope for decision making?

The need for a quick response to this issue and the integrity issues mean that only three options are available for consideration – retaining the current $1500 threshold (the status quo), lowering the threshold to zero, or lowering the threshold to $500 (which is the option preferred by officials).

# Section 3: Options identification

## 3.1 What options have been considered?



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## Threshold changes

There were three options considered, namely: to retain the current threshold; to reduce the threshold to zero; or to reduce the threshold to a lower amount of $500.

The following criteria have been used to assess the options:

- Efficiency
- Equity between borrowers
- Compliance costs
- Economic (maintaining the value of the loan asset)

**Retaining the existing threshold**

This option would:
Pros

- Not result in any change for borrowers or Inland Revenue or require any legislative change

Cons

- gives an unintended financial benefit to borrowers with non-salary and wage income under the $1500 threshold as they are not required to make loan repayments on this income
- treat borrowers under the $1500 threshold differently to other borrowers
- the student loan scheme becomes inconsistent with how other taxes are administered
- the term of borrowers' loans would be longer than necessary
- the government would carry this student loan debt for longer.

**Reducing the threshold to zero.**
These borrowers would pay the increased obligation as part of their end-of-year assessment process. This option would:

Pros

- remove the financial benefit to borrowers with non-salary and wage income compared to other borrowers
- improves loan repayments/reduces the term of the loan
- reduces the period the government carries the debt

Cons

- this option would introduce another inequity as the threshold would be set at a level that is lower than similar compliance cost reduction thresholds used for the administration of income tax (where outstanding amounts of less than $50 are not pursued).
- Compliance costs would be incurred by affected borrowers in understanding the changes and making repayments, but these would be similar to the costs incurred by other borrowers with repayment obligations.
- Consultation has not occurred with affected borrowers.
- Legislative changes are required to give effect to this proposal

**Reducing the threshold from $1500 to $500 (The preferred option)**
Reducing the threshold to $500 would equate to $60 of loan repayments. This is very close to the $50 threshold for income tax owed from an automated assessment, where amounts less than $50 owed are written off.

These borrowers would pay the increased obligation as part of their end of year assessment process. This option would:

Pros

- Set the threshold at a level that is similar to other thresholds used to administer income tax (where outstanding amounts are not pursued).
- remove the financial benefit to borrowers under the threshold compared to other borrowers
- improve equity among borrowers (between those with non-salary and wage income of $1500 or less and other borrowers)
- increased equity increases the integrity of the loan scheme.
- improve loan repayments/reduce the term of the loan
- reduce the period the government carries the debt

Cons

- Compliance costs would be incurred by affected borrowers in understanding the changes and making repayments, but these would not be material as they would be incurred in complying with their income tax obligations.
- Consultation has not occurred with affected borrowers.
- Legislative change is required

### Withholding changes

For the changes to the student loan withholding requirements, the option that has been considered is to repeal the provisions, so that these changes do not come into force and that the current arrangements continue.

Options briefly considered and rejected were to defer the application date or to make the changes optional for employers. Making the changes optional would create greater complexity and uncertainty for borrowers, employers and Inland Revenue. Deferring the application date would give employers more time to implement the changes but is unlikely to reduce the compliance costs.

## 3.2 Which of these options is the proposed approach?

### Threshold changes

The preferred option is to reduce the threshold level to $500. This would increase equity among borrowers and reflect the original intent that borrowers who are not subject to high compliance costs should make loan repayments.

### Withholding changes

For the changes to the student loan withholding requirements, the preferred option is to repeal the provisions as this minimises compliance costs.



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## Section 4: Impact Analysis (Proposed approach)

| 4.1 Summary table of costs and benefits |
|---|

| **Affected parties** *(identify)* | **Comment**: nature of cost or benefit (eg ongoing, one-off), evidence and assumption (eg compliance rates), risks | **Impact** *$m present value, for monetised impacts; high, medium or low for non-monetised impacts* |
|---|---|---|

### Threshold changes

| Additional costs of proposed approach, compared to taking no action | | |
|---|---|---|
| Regulated parties (borrowers with non-salary and wage income between $500 and $1500) | **Compliance costs**:<br>The ongoing compliance costs are not expected to be material as they would be incurred in complying with income tax obligations.<br><br>One-off cost may be incurred in understanding the changes. These would be short lived.<br><br>**Financial Impact:**<br>The maximum financial impact on the affected borrowers (approximately 25 borrowers per year) is increased repayments of $179 per annum for borrowers who are over the $19,760 repayment threshold. If a borrower is under the repayment threshold, they would not have to make any repayments.<br><br>As the repayment obligation is based on the borrower's income, we expect that most would be able to make the additional repayment.<br><br>If borrowers are unable to make the additional repayments, they would not be subject to any penalties and so would not be made worse off. | Nil<br><br>Low<br><br>Low |
| Regulators (Inland Revenue) | The costs of implementing this change will form part of Inland Revenue's Business Transformation programme and additional costs (above those already funded by Business Transformation) will not be incurred. | Nil |
| Wider government | N/A | Nil |
| Other parties (Student Unions and other representative bodies) | One-off cost. There will be costs for representative bodies in updating informational material on this change for students. However, this change would be included with other student loan | Low |



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| | changes that will be occurring from 1 April 2020. | |
|---|---|---|
| **Total Monetised Cost** | | Low |
| **Non-monetised costs** | | Low |

| Expected benefits of proposed approach, compared to taking no action | | |
|---|---|---|
| Regulated parties (borrowers with non-salary and wage income between $500 and $1500) | Borrowers who pay the increased repayment will slightly reduce the term of the loan.<br><br>Borrowers who do not pay will have the amount added back to their loan. They will not incur any penalties for non-payment and the term of their loan will remain same.<br><br>Increased equity between borrowers with non-salary and wage income and other borrowers which increases the integrity of the loan scheme. | Low |
| Regulators (Inland Revenue) | Consistency of loan scheme with way income tax is administered. | Low |
| Wider government | N/A | N/A |
| Other parties | N/A | N/A |
| **Total Monetised Benefit** | | |
| **Non-monetised benefits** | | Low |

## Withholding changes

| Additional costs of proposed approach, compared to taking no action | | |
|---|---|---|
| Regulated parties (borrowers earning these types of income and their employers) | **Compliance costs**:<br>The changes proposed to be repealed would have imposed compliance costs on employers and potentially reduced compliance costs for borrowers. Repealing these changes would lower compliance costs overall.<br><br>**Financial Impact:**<br>As the change preserves current arrangements, there is not expected to be any financial impact | Low<br><br><br><br><br><br><br><br>Nil |
| Regulators (Inland Revenue) | As the change preserves current arrangements there should not be significant additional costs to repealing the change. | Low |
| Wider government | N/A | Nil |
| Other parties | N/A | Nil |
| **Total Monetised Cost** | | Low |

| **Non-monetised costs** | | Low |
|---|---|---|

| Expected benefits of proposed approach, compared to taking no action | | |
|---|---|---|
| Regulated parties (borrowers earning these types of income and their employers) | Employers have indicated that there are significant compliance costs to implement the changes, so repealing these changes will mean that they do not face these costs. | Medium |
| Regulators (Inland Revenue) | N/A | N/A |
| Wider government | N/A | N/A |
| Other parties | N/A | N/A |
| **Total Monetised Benefit** | | Low |
| **Non-monetised benefits** | | Medium |

### 4.2 What other impacts is this approach likely to have?

#### Threshold changes

Officials have not identified other impacts as a result of the proposal.

There is uncertainty around borrower behaviour towards these loan repayments and the extent to which these amounts will be repaid. Some borrowers will pay, some will have their loan repayments amalgamated with other tax obligations, and others will not pay.

#### Withholding changes

Removing the withholding requirements is likely to mean that compliance rate for the borrowers effected may remain lower than the wider population of student loan borrowers. Inland Revenue are considering ways that this can be addressed operationally.



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## Section 5: Stakeholder views

| 5.1 What do stakeholders think about the problem and the proposed solution? |
|---|

### Threshold changes

Consultation with representative groups has not occurred to date. Consultation will occur with representative groups as part of Business Transformation stakeholder engagement activities in implementing the changes.

### Withholding changes

The proposal to repeal the earlier withholding changes is a direct response to concerns raised by employers during recent consultation that they would face significant and unforeseen compliance costs unless the previous law changes were repealed before the take effect on 1 April 2020.

These issues were not previously identified in earlier public consultation on the policy proposals or in submissions to select committee.

## Section 6: Implementation and operation

| 6.1 How will the new arrangements be given effect? |
|---|

### Threshold changes

Lowering the threshold requires a legislative change to the Student Loan Scheme Act 2011. It is intended that this change be included at the Select Committee stage of the Taxation (KiwiSaver, Student Loans, and Remedial Matters) Bill. The change will apply from 1 April 2020, which is the same date that other student loan changes apply from.

Inland Revenue will be responsible for the ongoing operation of this threshold. The change will be implemented as part of Inland Revenue's Business Transformation Release 4 changes which incorporate the repayment of Student Loans into the new systems and processes. The risks associated with this proposal are being managed as part of the wider risks to do with the Transformation programme.

Information on the change will be incorporated with other communications to affected borrowers once the legislation is enacted.

### Withholding changes

Repealing the withholding changes will not require any implementation as this maintains current arrangements. As part of educating employers before release 4, Inland Revenue would ensure that it is clear that these provisions are intended to be repealed so that no employers make changes to their systems to comply with the repealed provisions.



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## Section 7: Monitoring, evaluation and review

| 7.1 How will the impact of the new arrangements be monitored? |
| --- |
| Inland Revenue will monitor whether there are any issues arising with the enacted legislation. If officials identify anything that suggests the legislation is not operating as intended, then we will undertake a review and report to Ministers on legislative changes to address the issues. |

| 7.2 When and how will the new arrangements be reviewed? |
| --- |
| As described above in 7.1 above |

# Cabinet

# 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.*

## Items for Inclusion in the Taxation (KiwiSaver, Student Loans, and Remedial Matters) Bill

**Portfolio** **Revenue**

On 30 September 2019, following reference from the Cabinet Economic Development Committee (DEV), Cabinet:

### Portfolio Investment Entity regime

1 **agreed** that all Portfolio Investment Entity (PIE) investors should have their PIE income squared up at the end of the tax year using their correct prescribed investor rates (PIR), which is based on the information Inland Revenue holds for the investor's two previous tax years, with the result forming part of their income tax outcome for that year;

2 **agreed** that the above proposal apply from the 2020-21 tax year;

3 **agreed** that Inland Revenue should provide PIE entities with the correct PIR for their investors during the income year for existing PIE investors and for new investors in PIEs if sufficient information is available to Inland Revenue, with application from 1 April 2020;

### Student loan scheme

4 **noted** that on 8 August 2018, the Cabinet Social Wellbeing Committee agreed to amendments to require student loan deductions from withholding income [SWC-18-MIN-0093, paragraph 4];

5 **rescinded** the decision referred to in paragraph 4 above; and instead

6 **agreed** to repeal the changes requiring student loan repayments to be deducted from schedular, election-day, and casual agricultural income with effect from 1 April 2020;

7 **agreed** that the $1,500 student loans scheme exemption for non-salary and wage income for New Zealand-based borrowers, above the annual repayment threshold, be lowered to $500;

### KiwiSaver

8 **agreed** that the application date of the change to allow KiwiSaver members to change their employee contributions rate through their KiwiSaver scheme provider or Inland Revenue [DEV-19-MIN-0038.01] be deferred until 1 April 2022, or an earlier date to be set by Order in Council;

9 **noted** that on 20 March 2019, DEV agreed that employers be required to provide the following information to Inland Revenue about new employees and existing employees where this information has changed:

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

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

[DEV-19-MIN-0038.01, paragraph 15]

10 **rescinded** the decision referred to in paragraph 9 above; and instead

11 **agreed** that employers be required to report information to Inland Revenue about the income KiwiSaver members' contributions are calculated from for new employees;

## Legislative implications

12 **agreed** that the above proposals be included in the Taxation (KiwiSaver, Student Loans, and Remedial Matters) Bill for consideration by the Finance and Expenditure Committee;

13 **invited** the Minister of Revenue to issue drafting instructions to Inland Revenue and Parliamentary Counsel Office to draft legislation to give effect to the above paragraphs.

Michael Webster
Secretary of the Cabinet

***Secretary's Note:*** *This minute replaces DEV-19-MIN-0258. Cabinet agreed to DEV's recommendations to rescind two earlier decisions (paragraphs 5 and 10).*

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**Hard-copy distribution:**
Prime Minister
Deputy Prime Minister
Minister of Revenue