Hon David Parker, Minister of Revenue

Information Release

Tax policy reports related to the New Zealand Income Insurance Scheme

May 2023

Availability

This information release is available on Inland Revenue's tax policy website at https://taxpolicy.ird.govt.nz/publications/2023/2023-ir-nz-income-insurance

Documents in this information release

#	Reference	Type	Title	Date
1	IR2022/225	Report	Tax treatment of income insurance levies and payments	27 May 2022
2	IR2023/007	Report	New Zealand Income Insurance – Consequential amendments to the Income Tax Act 2007	12 January 2023

Information withheld

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Inland Revenue
Te Tari Taake

POLICY AND REGULATORY STEWARDSHIP

Tax policy report: **Tax treatment of income insurance levies and payments**

Date:	27 May 2022	**Priority:**	High
Security level:	In Confidence	**Report number:**	IR2022/225

Action sought

	Action sought	Deadline
Minister of Finance	**Agree** to recommendations **Note** the contents of this report	3 June 2022
Minister of Revenue	**Agree** to recommendations **Note** the contents of this report	3 June 2022

Contact for telephone discussion (if required)

Name	Position	Telephone
Bary Hollow	Principal Policy Advisor	s 9(2)(a)
Hannah Fogarty	Policy Advisor	

27 May 2022

Minister of Finance
Minister of Revenue

Tax treatment of income insurance levies and payments

Executive Summary

Purpose

1. This report seeks joint Ministers' agreement to the proposed tax treatment of the New Zealand Income Insurance Scheme (NZIIS).

Context and background

2. In April 2022, public consultation[1] closed on the income insurance scheme developed by a Tripartite Working Group (NZ Government, Council of Trade Unions and Business NZ), and led by the Ministry of Business, Innovation and Employment (MBIE). Paid for by levies, the scheme proposes to cover no fault job loss resulting from economic displacement and health conditions/disabilities. It would be administered by the Accident Compensation Corporation (ACC) and modelled after the current accident compensation (AC) scheme.

3. In early July, Cabinet will decide whether to proceed with the NZIIS, as well as agree to the final policy design of the scheme if the decision is made to proceed. The tax treatment of the scheme is an outstanding policy issue, and it is important that Ministers agree to a recommended approach before the Cabinet decisions must be made.

Problem definition

4. Income insurance levies and payments will be subject to New Zealand's existing tax framework set out in the Income Tax Act 2007 (ITA). A key factor when considering a preferred tax treatment is maintaining consistency with the treatment of the analogous AC scheme and the overall framework of the tax system.

Tax implications for which no change is recommended

5. Under current law, the employer and employee levies would be subject to goods and services tax (GST). This is consistent with employer and employee ACC levies. Employers who are registered for GST will be able to claim a GST deduction for the GST component of the employer levy. Employees will not be able to claim a GST deduction for the GST component of the employee levy.

6. Both NZIIS entitlements paid by ACC and bridging payments, which are proposed to be paid by employers, will be subject to income tax in the hands of the recipient.

[1] Discussion document: A New Zealand Income Insurance Scheme (published 2 February 2022)

7. Employers will be allowed a deduction for the cost of the employer levy and the bridging payment when calculating their taxable income.

Tax implications for which legislative change is recommended

8. Earnings-related ACC payments are defined as salary and wages under the ITA. As NZIIS payments will be similar in nature, we recommend that these payments are also defined as such. This will make NZIIS payments subject to PAYE and will not leave the recipient with a large tax bill to pay at the end of the year of receipt.

9. An interpretation of current law suggests that employees may be allowed a deduction for the employee levies deducted from their income. From a policy perspective, however, we recommend that employees are not permitted this deduction. Not permitting a deduction would be consistent with both the tax treatment of the ACC Earners' levy and the framework for the taxation of individuals in general, under which employees are not permitted deductions for expenses incurred in producing their employment income.

10. The extent to which self-employed workers are included in the scheme is yet to be determined. If they are included, it would be preferable that self-employed NZIIS levies and entitlements are treated the same way they are under ACC. Some minor legislative change may be required to achieve this.

11. In terms of other deductions that may apply to NZIIS payments under the PAYE schedule:

    a. *NZIIS levies* –it would not be appropriate to apply these levies to NZIIS payments, as these payments are not forms of income insured by the scheme.

    b. *ACC levies* – these levies apply to all PAYE income payments, and this should include NZIIS payments.

    c. *KiwiSaver employee contributions* – should continue to be made. Individuals would continue to have the ability to apply for a KiwiSaver savings suspension while receiving NZIIS payments.

    d. *Student loan repayments* – like ACC and benefit payments, repayments should apply to NZIIS payments above the repayment threshold.

    e. *Child support deductions* – like ACC and benefit payments, child support should be automatically deducted from NZIIS payments.

12. NZIIS levies will also form part of the existing Government guarantee on PAYE payments.

13. Some minor legislative changes may be required to achieve these outcomes.

Fiscal impact

14. There is a fiscal cost of $361 million per year from employers being able to deduct the levy. If self-employed are included, this cost increases to $481.8 million per year. If the decision was taken to allow employees a deduction for the levies they pay, this would further increase the fiscal cost to $934.4 million per year.

15. These impacts count significantly against the previously estimated positive fiscal offsets from the scheme. Advice on the overall fiscal impact of the scheme will be provided as part of advice to Cabinet in early July.

16. There is no direct fiscal impact at this time as all decisions about tax treatment are contingent on the scheme and its final design being agreed to by Cabinet.

Consultation

17. MBIE, ACC, and the Treasury have been consulted on the contents of this report.

Next steps

18. The tax treatment that Ministers agree to will feed into the July Cabinet paper on final NZIIS policy design decisions.

Recommendations

We recommend that you:

a. **agree** that no change is required to the following tax implications of the NZIIS scheme:

   i. All employer and employee levies will be subject to GST.

   ii. Employers who are registered for GST can claim a deduction for the GST component of the levies they pay, and employees cannot.

   iii. NZIIS payments will be subject to income tax.

   iv. Employers will be able to claim a deduction for the cost of employer levies and bridging payments.

   v. If self-employed persons are included in the scheme, they will also be permitted GST and income tax deductions for levies paid.

   vi. ACC levies, KiwiSaver employee contributions, student loan repayments and child support deductions will apply to NZIIS payments.

Agreed/Not agreed Agreed/Not agreed

b. **agree** that NZIIS payments be defined as "salary and wages" under the ITA and therefore subject to PAYE.

Agreed/Not agreed Agreed/Not agreed

c. **agree** that employees cannot claim a tax deduction for the cost of the employee levy.

Agreed/Not agreed Agreed/Not agreed

d. **agree** that NZIIS levies will not apply to NZIIS payments.

Agreed/Not agreed Agreed/Not agreed

e. **agree** that in implementing this scheme, consequential amendments be made to the Revenue Acts to ensure that the scheme is referenced correctly.

Agreed/Not agreed Agreed/Not agreed

f. **refer** a copy of this report to New Zealand Income Insurance Ministers (Social Development and Employment, ACC, and Workplace Relations and Safety) for their information.

Referred/Not referred Referred/Not referred

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[redacted]

Bary Hollow
Principal Policy Advisor
Policy and Regulatory Stewardship

Hon Grant Robertson
Minister of Finance
/ /2022

Hon David Parker
Minister of Revenue
/ /2022

Background

19. In April 2022, public consultation closed on the income insurance scheme developed by a Tripartite Working Group (NZ Government, Council of Trade Unions and Business NZ). The scheme proposes to cover no-fault job loss resulting from economic displacement and health conditions/disabilities. It will be administered by the ACC and modelled after the current AC scheme.

20. Payments would cover 80% of a worker's pre-displacement income, up to a maximum pre-displacement income of $130,911 per annum. In cases of economic displacement, the first four weeks would be paid for by the employer as a bridging payment. After this period, the worker would be eligible to receive NZIIS entitlements for up to six months.

21. It is proposed that the scheme be funded by compulsory levies of 2.78%, which would be split equally between the employee and employer (that is, each would pay 1.39%). These levies would apply to all income insured by the scheme below the $130,911 per annum threshold.

22. In early July, Cabinet will decide whether to proceed with the scheme, as well as agree to the final policy design of the scheme if the decision is made to proceed. The tax treatment of the scheme is an outstanding policy issue, and it is important that Ministers agree to a recommended approach before the Cabinet decisions must be made.

Problem definition

23. Income insurance levies and payments will be subject to New Zealand's existing tax framework set out in the ITA. It is useful to compare the various NZIIS-related transactions with existing transactions as this provides a framework for what the tax treatment will be.

24. A key factor when considering a preferred tax treatment is making sure we are not diverging from general tax principles and frameworks and therefore maintain consistency with the treatment of the analogous AC scheme.

Applying existing tax frameworks

Goods and services tax (GST)

25. To ensure GST remains a simple and efficient tax, it applies equally to most goods and services supplied in New Zealand. This includes insurance cover for loss of earnings, such as ACC and private income protection insurance.

26. Consistent with the GST treatment of insurance schemes, and the existing practice for ACC, levies payable by employers and employees will be subject to GST. This is because they represent consideration for the supply of insurance. The proposed levy rate in the discussion document is already GST inclusive.

27. Employers who are registered for GST will be able to claim a deduction for the GST cost of the employer levy, which is consistent with their ability to claim a deduction for the GST on other business-related expenses. Self-employed workers, if included in the scheme, will also be able to claim a deduction for the GST on the levies that they are

required to pay. Employees will not be able to claim a deduction for the GST cost of the employee levy.

28. The above treatment is preferable from a policy perspective. Not applying GST to the levies would undermine New Zealand's broad-based GST system and could set a precedent for future GST concessions. Also, the ability for GST-registered businesses to claim a deduction for the GST cost of the levy ensures GST remains a cost on the end consumers of the service (the insurance) rather than businesses.

29. NZIIS entitlements and bridging payments will not be subject to GST under current legislation. This is consistent with the GST treatment of regular salary and wages, ACC payments and other income protection insurance payments.

30. The current rules for GST and income protection insurance (such as private income protection insurance and ACC) result in the premiums/levies being taxed (with GST-registered self-employed persons and employers able to recover the GST component of the premiums by claiming a GST deduction) and the compensation payments not being subject to GST on pay out. These rules have been longstanding, and for consistency, we recommend this GST treatment applies to the NZIIS.

Table 1: GST treatment

	NZIIS payment	**Bridging payment**	**Employer levy**	**Employee levy**	**Self-employed levies***
Is it subject to GST?	No	No	Yes	Yes	Yes
Can a GST deduction be claimed?	n/a	n/a	Yes – for GST-registered employers	No	Yes – for GST-registered self-employed persons

**if included in the scheme*

Income tax

31. As NZIIS entitlements and bridging payments fall under the definition of income under ordinary concepts, they will be subject to income tax.

32. Any income earned from part-time work while receiving NZIIS entitlements will have tax withheld at the secondary employment rate.

33. Employers will be able to claim a deduction for the cost of the employer levy and bridging payment in the same manner as any other business expense. This is on the basis that the levies are related to employment of staff and therefore expenditure incurred in carrying on the employer's income-earning activity.

Defining NZIIS payments

34. Under current tax frameworks, NZIIS entitlements paid by ACC would likely be income under ordinary concepts because they would be regular and fund the person's living expenses. They would not fall under the definition of "employment income" as they

would be statute-based, not based on the employment relationship. The payment as a proportion of a worker's pre-displacement income is more a method of calculation than a link to the employer.

35. However, the analogous ACC weekly compensation payments are defined as "employment income" as they fall under the definition of "salary or wages" in the ITA. Furthermore, section 99 of the Accident Compensation Act 2001 treats the first week's payment required to be made by an employer as salary or wages for the purposes of the ITA and Tax Administration Act 1994. This treatment ensures that payments have PAYE deducted at source and are unlikely to leave the recipient with a tax bill in the income year the payment is received.

36. If NZIIS payments are not defined as employment income, there will be no obligation on ACC or the employer to withhold tax. If NZIIS payments are defined as "salary and wages" and are therefore "employment income", PAYE will be deducted at source. This will also mean there is additional consistency with ACC regarding the treatment of employee levies for income tax purposes, as discussed below.

37. Therefore, if there were a policy intention to define NZIIS entitlements and bridging payments as "employment income" for the purposes of the ITA, an amendment could be made to include "a New Zealand Income Insurance earnings-related payment" and "an income insurance employer bridging payment" within the definition of "salary or wages". Officials recommend this treatment.

The deductibility of the employee levy for income tax purposes

38. The employee levy will be deducted from salary and wages as part of the PAYE withheld by employers.

39. Under private income protection insurance schemes, insurance premiums are generally deductible against an employee's taxable income when the insurance receipts are taxable. Generally, insurance payments have been taxable where the payment is based on the insured's pre-displacement income. This might suggest that employees would be able to deduct their employee levies on the basis that the NZIIS payments are both taxable and based on pre-displacement income.

40. However, the NZIIS scheme is modelled after the AC scheme, with both schemes being public goods funded through levies on salaries and wages where claimants receive taxable payments. Under the AC scheme, employees are not able to claim a deduction for the ACC Earners' levy. This is because payments from ACC are included in the definition of "employment income", which means any expenses incurred in deriving this income are denied under the employment limitation in the ITA.

41. The employment limitation exists to simplify employees' interaction with the tax system. PAYE is deducted, and tax returns can be automatically calculated without the need to account for various (and often arbitrary) expenses related to an individual's employment.

42. There is also an equity argument to be made for denying deductions for employee levies. The current proposal is that all employees will be levied at a flat rate. As the personal income tax rate is determined on a progressive schedule, allowing a deduction for NZIIS levies is regressive. This is because those on a higher income, and hence on a higher marginal tax rate, will benefit more if the NZIIS employee levies are tax deductible.

43. To recognise the fact that NZIIS payments function differently from private insurance payouts, and to maintain consistency with the tax treatment of ACC levies, it is officials' view that the employee levy should not be deductible by employees.

44. These issues provide further motivation for an amendment to define NZIIS payments as "salary or wages" under the ITA. By having NZIIS payments (both the bridging payment and the NZIIS entitlement) fall under the umbrella of employment income, the employment limitation will deny employees the ability to claim the cost of the employee levy.

Table 2: Proposed income tax treatment

	NZIIS entitlement	**Bridging payment**	**Employer levy**	**Employee levy**
Is it taxable?	Yes – withheld by ACC	Yes – withheld by the employer	n/a	n/a
Is it deductible?	n/a - ACC is exempt from income tax	Yes – to the employer	Yes	No

Other PAYE deductions

45. In addition to income tax, income earned from employment is also subject to ACC levies, KiwiSaver employee contributions, student loan repayments and child support deductions. Once the scheme is in place, this income will also be subject to NZIIS levies. If income insurance payments are to be defined as employment income, it must be determined whether such payments will be subject to these deductions.

46. If PAYE deductions differ between income while employed and NZIIS payments (NZIIS entitlements and bridging payments), two considerations arise:

    a. This will increase the net replacement rate of the insurance payment. If certain PAYE deductions do not apply to insurance payments, the take-home income received from NZIIS will be greater than 80% of the take-home pay received under employment. The extent to which this will occur will depend on the number and size of deductions that are excluded from these payments.

    b. The employer will be withholding different amounts from the income they pay to their employees compared with the bridging payment they pay to ex-employees. This will impact an individual's end-of-year square up.

47. Given these considerations, the starting point for this analysis is that all PAYE deductions (ACC levies, KiwiSaver employee contributions, student loan repayments, child support deductions and NZIIS levies) will apply to income insurance payments. However, if there is a strong policy rationale to exclude certain deductions, then these options will need to be considered.

NZIIS levies

48. The discussion document stated that NZIIS levies will apply to all income that is insured by the scheme. As claimants will be entitled to 80% of their pre-displacement earnings up to a maximum of 80% of $130,911 per annum, they will be levied at a

flat rate while employed, with maximum leviable income being capped at $130,911 per annum.

49. Arguably, NZIIS entitlements and bridging payments are not income that is being insured by the scheme. This means that these payments should not be subject to NZIIS levies, given that time on NZIIS will not count towards the contribution period for NZIIS eligibility. This will increase the net replacement rate of the payment by the size of the levy (currently estimated to be 1.39% for an employee).

50. The operational implication is that employers will be withholding differently between income while employed and the bridging payment.

ACC levies

51. In the case of ACC, recipients of ACC weekly compensation continue to pay ACC levies on this income. The fact that NZIIS claimants will still be able to receive the benefits of ACC while receiving their income insurance payments suggests that claimants should continue to be liable for ACC levies.

52. Under the current legislation, ACC levies apply to all PAYE income payments, which NZIIS payments will fall within. However, there are some exceptions. For example, main MSD benefit payments are not liable for ACC levies.

KiwiSaver contributions

53. KiwiSaver employee contributions are made at a rate of 3% (the compulsory rate), or 4%, 6%, 8% or 10% (if the employee elects to contribute at a higher rate). KiwiSaver contributions are deducted from ACC payments, but not MSD benefit payments. The reason for not deducting from benefit payments is due to concerns about income adequacy. KiwiSaver contributions are also not deducted from redundancy payments.

54. If KiwiSaver contributions were deducted from NZIIS payments, this might raise concerns about income adequacy of those on the lowest incomes. However, this could be mitigated if they applied for a KiwiSaver savings suspension. This option could be included as part of the NZIIS application process.

55. Consequently, officials consider that deductions for KiwiSaver employee contributions should be made from NZIIS entitlements. It is finely balanced whether bridging payments are more akin to redundancy payments. MBIE are recommending that these payments are not defined as redundancy payments, since they will be paid as regular salary and wages. Therefore, KiwiSaver employee contributions should also apply to bridging payments.

56. Under the KiwiSaver Act 2006, employer contributions are not paid on ACC payments, including the first week compensation paid by the employer. Therefore, NZIIS entitlements and bridging payments would not be subject to KiwiSaver employer contributions consistent with that approach.

Student loan repayments

57. Student loan repayments should be deducted from payments under NZIIS. Student loan repayments become compulsory for earners once their income is above the student loan repayment threshold. Currently, student loan repayments are deducted at a rate of 12% on income above $21,268 per annum for New Zealand-based

borrowers. (This threshold does not apply to income from secondary jobs, meaning that, generally, all income from such jobs is subject to student loan repayments.)

58. The amount an individual needs to repay for student loan purposes depends on salary and wage income plus any adjustable net income. ACC and MSD benefit payments count as income for the purposes of student loan repayments. However, if a person's income is below the threshold, they do not have to make repayments. For NZIIS recipients, current rules would provide a natural buffer for those on low incomes, while still requiring those whose income is above the threshold to make repayments.

59. If NZIIS entitlements did not count as income for student loan repayment purposes, those with incomes well above the threshold would not have to make repayments, which would increase the net replacement rate significantly. This could diminish work incentives, especially in instances where the interaction with the welfare system means net replacement rates approach 100% or higher.

Child support deductions

60. Child support is money paid by parents who do not live with their children or who share care with someone else. Child support is based on both parents' income, and for parents whose income is taxed entirely at source (for example, salary and wage earners), this is their income from the last calendar year (1 January to 31 December). For others, their income from two years ago is used.

61. A liable parent pays their child support by automatic deduction from source deduction payments made by their employer. If a parent experiences a drop in income of at least 15 percent from the income they have been assessed on, they can elect to estimate their income. The ability to estimate would address situations where a person struggles to meet their child support obligation due to the drop in income caused by moving from employment to receiving NZIIS payments.

62. If child support deductions were not made automatically from NZIIS payments, the liable parent would need to pay Inland Revenue independently. This is not consistent with recent policy changes to apply automatic deductions to newly liable parents.

Table 3: Proposed treatment for other PAYE deductions

	Will it be deducted from NZIIS entitlements and bridging payments?
NZIIS levies	No
ACC levies	Yes
KiwiSaver employee contributions	Yes (however employers/ACC will not have to pay KiwiSaver employer contributions)
Student loan repayments	Yes (on income above the repayment threshold)
Child support deductions	Yes

Self-employment

63. The extent to which self-employed workers are included in the scheme is yet to be determined and the conclusions below may have to be given further consideration depending on the final form of their inclusion.

64. We are assuming that, if included, self-employed persons will be liable for both the employer and employee levies, which will be invoiced by ACC. Consistent with current tax legislation, both levies will be costs incurred in carrying on a business activity. This means self-employed workers will be able to deduct these levies when deriving taxable income. They will also be able to claim a deduction for the GST component of these levies if they are registered for GST.

65. As the income generated through self-employment has no nexus to an employment relationship, any NZIIS payments received by a self-employed person would not be employment income. This means self-employed workers will be able to claim the cost of both levies when deriving their taxable income and PAYE will be deducted from any payments made under the NZIIS.

66. Officials recommend that if the self-employed are included in the scheme, any payments made under the scheme should be treated consistently with ACC payments and therefore PAYE should be applied to those payments.

Fiscal impact

67. The negative fiscal impact against the scheme of employers deducting the cost of the employer levy is estimated to be $361 million per year. If self-employed are included in the scheme, this cost increases to $481.8 million per year.

68. If the decision was taken to allow employees a deduction for the levies they pay, this would further increase the fiscal cost against the scheme to $934.4 million per year.

69. These impacts count significantly against estimated fiscal offsets from the scheme (for example, from savings in welfare expenditure and income tax payable on scheme entitlements). Advice on the overall fiscal impact of the scheme will be provided as part of advice to Cabinet in early July.

70. There is no direct fiscal impact at this time as all decisions about tax treatment are contingent on the scheme and its final design being agreed to by Cabinet.

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Inland Revenue
Te Tari Taake

POLICY AND REGULATORY STEWARDSHIP

Tax policy report: **New Zealand Income Insurance – Consequential amendments to the Income Tax Act 2007**

Date:	12 January 2023	**Priority:**	Medium
Security level:	In Confidence	**Report number:**	IR2023/007

Action sought

	Action sought	Deadline
Minister of Finance	**Agree** to recommendations	23 January 2023
Minister for Social Development and Employment Minister for ACC	**Agree** to recommendations	23 January 2023
Minister of Revenue	**Agree** to recommendations	23 January 2023
Minister for Workplace Relations and Safety	**Agree** to recommendations	23 January 2023

Contact for telephone discussion (if required)

Name	Position	Telephone
Bary Hollow	Principal Policy Advisor	s 9(2)(a)
Hannah Fogarty	Policy Advisor	

12 January 2023

Minister of Finance
Minister for Social Development and Employment
Minister for ACC
Minister of Revenue
Minister for Workplace Relations and Safety

New Zealand Income Insurance – Consequential amendments to the Income Tax Act 2007

Summary

Purpose

1. In July 2022, Cabinet delegated authority to the Ministers of Finance, Social Development and Employment, ACC, Revenue, and Workplace Relations and Safety to make additional policy decisions and minor changes in relation to issues that arise in drafting of the New Zealand Income Insurance (NZII) Bill [CAB-22-MIN-0250.02 rec 84].

2. This report seeks agreement from delegated Ministers to further amendments to the Income Tax Act 2007 (ITA) that will be required as part of the NZII bill.

Context and background

3. Instructed by the Ministry of Business, Innovation and Employment (MBIE), the Parliamentary Counsel Office (PCO) is currently drafting legislation which will introduce an income insurance scheme. This legislation is scheduled to be introduced in February 2023 and enacted before the 2023 election.

4. Due to the scheme's interaction with the tax and transfer system, consequential amendments to the ITA and the Tax Administration Act 1994 are required. These are being drafted by Inland Revenue.

5. In this drafting process, we have found two areas which call for further amendments to the ITA. Ministers' agreement is required for these amendments to proceed.

Definition of bridging payments under the ITA

6. In May 2022, we provided advice on the tax treatment of NZII levies and payments [IR2022/225 refers]. We recommended that NZII payments (including the 4-week bridging payment paid by employers) would be defined as "salary and wages" under the ITA. This was to maintain consistency with the treatment of ACC earnings-related payments under the Act.

7. You agreed to this recommendation and the decision was confirmed by Cabinet in July 2022 [CAB-22-MIN-0250.02 rec 21.1].

8. However, recent developments to the bridging payment requirement mean we are inclined to redefine the **bridging payment** as an "extra pay" under the ITA[1]. This

[1] This does not affect the decision to define NZII entitlements paid by ACC as salary and wages.

is consistent with how redundancy and lump sum payments are defined under the ITA.

9. There are two reasons for this change. Firstly, the NZII bill is being drafted in a way which gives employers the option to pay the bridging payment either as a lump sum or as part of the regular salary and wage cycle. If employers choose to pay the bridging payment as a lump sum upon termination of employment, there is a risk that more income tax will be withheld on the payment above what is due on the payment.

10. By defining bridging payments as an extra pay, the risk of over-withholding of tax on lump sum payments is mitigated. However, it maintains the intended tax treatment that the payment is made in connection to employment and subject to income tax.

11. Furthermore, there was a recent in-principal decision to allow employers to satisfy the bridging payment requirement by paying contracted redundancy compensation [CAB-22-MIN-0484 rec 19]. Redundancy payments are defined as "extra pay" under the ITA, so defining bridging payments in the same manner would be consistent.

Implication for KiwiSaver employee contributions

12. We had previously advised that KiwiSaver *employee* contributions should be deducted from bridging payments since they would be paid as regular salary and wages. However, under the KiwiSaver Act 2006, payments that are akin to a redundancy payment do not have employee contributions deducted.

13. The change in the drafting of the NZII Bill making bridging payments more akin to redundancy payments will now result in KiwiSaver *employee* contributions not being deducted from bridging payments. Officials recommend that the tax treatment aligns with this change and treats the bridging payments constantly with redundancy payments with no *employee* contributions being deducted from those amounts.

14. No change is required for KiwiSaver *employer* contributions as these are not payable on these payments consistent with the treatment of ACC payments, including the first week compensation paid by the employer.

Tax credit eligibility for partners of NZII recipients

15. In July 2022, Cabinet decided that NZII recipients would not be eligible for the Minimum Family Tax Credit (MFTC), In-work Tax Credit (IWTC), and Independent Earner Tax Credit (IETC) [CAB-22-MIN-0250.02 rec 20.2]. They would remain eligible for the Family Tax Credit.

16. This decision was made on the basis that it would maintain consistency with the eligibility criteria for those on main benefits.

17. In drafting consequential amendments to the ITA, a question has arisen regarding the eligibility of partners of NZII recipients for the MFTC and IWTC. Under the welfare system, partners of those on main benefits are also not eligible for these tax credits.

18. To extend the intended consistency across main benefits and NZII, we are seeking Ministers' agreement that partners of NZII recipients will also not be eligible for the MFTC and IWTC.

Consultation

19. MBIE, ACC, and MSD and were consulted on the contents of this report. The Treasury were informed of this report.

Fiscal Implications

20. There are no fiscal implications to the proposed changes.

Next steps

21. Ministerial consultation on the NZII bill and associated Cabinet paper is scheduled for 26th January. We therefore require decisions on the recommendations in this report by **23rd January**.

Recommended action

We recommend that you:

Recommendations	Minister of Finance	Minister for Social Development and Employment Minister for ACC	Minister of Revenue	Minister for Workplace Relations and Safety
a. **note** that you have been delegated authority by Cabinet to make additional policy decisions and minor changes in relation to issues that arise in the drafting of the NZII Bill [CAB-22-MIN-0250.02 rec 84]	Noted	Noted	Noted	Noted
b. **agree** to reverse the previous Cabinet decision to define bridging payments as "salary and wages" under the Income Tax Act 2007	Agreed Not agreed	Agreed Not agreed	Agreed Not agreed	Agreed Not agreed
c. **agree** to define bridging payments as an "extra pay" under the Income Tax Act 2007	Agreed Not agreed	Agreed Not agreed	Agreed Not agreed	Agreed Not agreed

d. **agree** that since the bridging payment is now more akin to a redundancy payment, KiwiSaver *employee* contributions will not be deducted from these payments	Agreed Not agreed	Agreed Not agreed	Agreed Not agreed	Agreed Not agreed
e. **agree** that partners of NZII recipients will not be eligible for the Minimum Family Tax Credit and the In-Work Tax Credit (noting this treatment is consistent with that of partners of main benefits recipients)	Agreed Not agreed	Agreed Not agreed	Agreed Not agreed	Agreed Not agreed

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Bary Hollow
Principal Policy Advisor
Policy and Regulatory Stewardship

Hon Grant Robertson
Minister of Finance
/ /2023

Hon Carmel Sepuloni
Minister for Social Development and Employment
Minister for ACC
/ /2023

Hon David Parker
Minister of Revenue
/ /2023

Hon Michael Wood
Minister for Workplace Relations and Safety
/ /2023