

Hon Stuart Nash, Minister of Revenue

Information Release

Income Tax (Fringe Benefit Tax, Interest on Loans) Amendment Regulations 2020

September 2020

Availability

This information release is available on Inland Revenue's Tax Policy website at <https://taxpolicy.ird.govt.nz/publications/2020-ir-cab-leg-20-sub-0072/overview>

Documents in this information release

#	Reference	Type	Title	Date
1	IR2020/225	Tax policy report	Decrease in FBT prescribed rate of interest	7 May 2020
2	LEG-20-SUB-0072	Cabinet paper	Income Tax (Fringe Benefit Tax, Interest on Loans) Amendment Regulations 2020	16 June 2020
3	LEG-20-MIN-0072	Minute	Income Tax (Fringe Benefit Tax, Interest on Loans) Amendment Regulations 2020	16 June 2020

Additional information

The Cabinet paper was considered by the Cabinet Legislation Committee on 16 June 2020 and confirmed by Cabinet on 22 June 2020.

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

- Income Tax (Fringe Benefit Tax, Interest on Loans) Amendment Regulations 2020

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

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POLICY AND STRATEGY

Tax policy report: Decrease in FBT prescribed rate of interest

Date:	7 May 2020	Priority:	Medium
Security level:	In Confidence	Report number:	IR2020/225

Action sought

	Action sought	Deadline
Minister of Revenue	Agree to recommendations	11 June 2020

Contact for telephone discussion (if required)

Name	Position	Telephone
Paul Fulton	Principal Policy Advisor	s 9(2)(a)
s 9(2)(a)	Policy Advisor	

7 May 2020

Minister of Revenue

Decrease in FBT prescribed rate of interest

Purpose

1. This report seeks your agreement to lower the prescribed interest rate used to calculate fringe benefit tax (FBT) on low-interest loans provided by employers to employees from 5.26% to 4.50%. This change is required to align the rate with current market interest rates. The new rate should apply from the beginning of the next quarter – 1 July 2020.
2. An Order in Council is required to make this change. Therefore, this report also seeks your approval for the Parliamentary Counsel Office (PCO) to draft an Order in Council to lower the rate. As changes to the FBT prescribed interest rate have become a routine matter, we consider that your approval is sufficient for PCO to draft the Order. PCO can provide the Order in Council directly to Cabinet Office.

Background

3. The FBT rules tax non-cash benefits provided to employees. Included in the definition of 'fringe benefit' is any employment-related loan on which the employer is charging a rate of interest that is below the market rate. The interest differential is taxable. A prescribed rate set by regulations is used as a proxy for the market rate of interest, to save employers the compliance costs associated with determining the market rate relevant to loans that they have provided to their employees.
4. The Income Tax Act 2007 permits the making of regulations by Order in Council to set a prescribed rate of interest for the purpose of calculating FBT on low-interest loans. Once a rate is set, it remains the prescribed rate until changed by a subsequent Order in Council.
5. The prescribed interest rate was last changed from 5.77% to 5.26%, effective from the quarter beginning 1 October 2019.

Determination of appropriate prescribed rate

6. The Reserve Bank conducts a survey of first mortgage housing interest rates on the last day of each month, producing a 'floating first mortgage new customer housing rate'. The rate is calculated as the weighted average interest rate for the surveyed institutions, the weightings being based on each institution's share of total lending for housing purposes. This Reserve Bank series is a suitable indication of general market interest rates, and is therefore used as the benchmark for setting the FBT prescribed rate.
7. The floating first mortgage new customer housing rate of 4.50% for March 2020 indicates that the current FBT prescribed rate of 5.26% is higher than the prevailing market rate. 4.50% could still be perceived as a high borrowing rate in the context of the current low-interest environment, but this figure is consistent with floating rates offered by major banks.
8. Longstanding administrative policy has been to adjust the FBT prescribed interest rate when there has been a change in the floating first mortgage new customer

housing rate of 20 basis points or more. We recommend that the rate be adjusted to ensure that there is no long-term misalignment.

Process issues

9. When regulations are made declaring the rate of interest applying to employment-related loans, they apply to quarters starting from a date at least 1 month following the date the regulations were made. Regulations that reduce the prescribed rate may apply to a quarter if made at least 1 month before the end of that quarter, however there is not sufficient time for that to be possible for this rate change. Therefore, the reduced rate of 4.50% should apply from the start of the next quarter – 1 July 2020.
10. The Order in Council should be referred to the Cabinet Office by 11 June 2020, so that it can be considered by the Cabinet Legislation Committee on 16 June 2020. PCO has arranged for the Order in Council to be provided directly to the Cabinet Office.
11. A Cabinet paper recommending that Cabinet approve the Order in Council and authorise its submission to the Executive Council is attached. We recommend that you lodge the Cabinet paper with the Cabinet Office by 10am on Thursday 11 June 2020.

Revenue implications

12. Lowering the FBT prescribed interest rate to 4.50% will decrease the amount of FBT that will be collected by approximately \$0.4 million per quarter. This amounts to \$6.4 million over the current forecast period (2020-21 to 2023-24).
13. A forecasting adjustment will be necessary, to account for the decrease in expected FBT revenue. It will not affect the balance of the tax policy work programme scorecard.

Consultation

14. The Treasury has been consulted in the preparation of this report and the attached Cabinet paper.

Recommended action

We recommend that you:

15. **agree** that the FBT prescribed rate of interest for low-interest employment-related loans should be lowered to 4.50%, effective from 1 July 2020.

Agreed/Not agreed

16. **note** that decreasing the prescribed rate to 4.50% will result in a decrease in revenue of approximately \$0.4 million per quarter (\$1.6 million per annum), which amounts to \$6.4 million over the current forecast period (2020-21 to 2023-24).

Noted

17. **agree** that the Parliamentary Counsel Office should be instructed to draft an Order in Council to implement the proposed rate change.

Agreed/Not agreed

Paul Fulton

Principal Policy Advisor
Policy and Strategy

Hon Stuart Nash

Minister of Revenue
/ /2020

In Confidence

Office of the Minister of Revenue

Chair, Cabinet Legislation Committee

INCOME TAX (FRINGE BENEFIT TAX, INTEREST ON LOANS) AMENDMENT REGULATIONS 2020

Proposal

1. This paper seeks the Cabinet Legislation Committee's agreement to submit an Order in Council amending the Income Tax (Fringe Benefit Tax, Interest on Loans) Amendment Regulations 2019 to the Executive Council. The proposal is to lower the FBT prescribed interest rate for low-interest, employment-related loans from 5.26% to 4.50%, in line with a decrease in market interest rates.
2. Changes to the prescribed interest rate are a routine matter and do not involve a change of policy. The methodology used for setting the rate has been applied consistently since the early 1990s.

Policy

3. The fringe benefit tax (FBT) rules tax non-cash benefits provided to employees. Included in the definition of 'fringe benefit' is any employment-related loan on which the employer is charging a rate of interest that is below the market rate. The interest differential is taxable. A prescribed rate set by regulations is used as a proxy for the market rate of interest to save employers the compliance costs associated with determining the market rate relevant to loans that they have provided to their employees.
4. The Income Tax Act 2007 ('the Act') allows regulations to be made to set the prescribed rate. Once a rate is set, it remains the prescribed rate of interest until changed by a subsequent Order in Council. The current FBT prescribed rate, which has applied since 1 October 2019, is 5.26%.
5. The prescribed rate of interest is based on a Reserve Bank survey of first mortgage housing interest rates on the last day of each month ('floating first mortgage new customer housing rate'). This is calculated as the weighted average interest rate for the surveyed institutions, the weightings being based on each institution's share of total lending for housing purposes. This Reserve Bank series is selected as the benchmark for setting the FBT prescribed rate because it is seen as a good indication of market interest rates.
6. The proposed new FBT rate of 4.50%, despite being 76 basis points lower than the current rate, might still be perceived as a high borrowing rate in the current low-interest environment. However, this figure is consistent with floating rates offered by major banks.

Timing

7. The Act provides that when regulations to change the prescribed rate of interest are made, they apply to quarters starting at least one month following the date the regulations were made by the Governor General by Order in Council. Regulations that reduce the rate may apply for the current quarter if made at least one month before the end of the quarter.
8. In accordance with the Act, I recommend that the regulations to lower the rate have effect from 1 July 2020 – the beginning of the next quarter. Because this is a reduction of the rate, the regulations could be made as late as 31 August 2020 and still have effect from 1 July 2020. Therefore, no waiver of the 28-day rule is required.

Compliance

9. The regulations comply with each of the following, where applicable:
 - 9.1 the principles of the Treaty of Waitangi Not applicable
 - 9.2 the New Zealand Bill of Rights Act 1990 Not applicable
 - 9.3 the Human Rights Act 1993 Not applicable
 - 9.4 the principles and guidelines set out in the Privacy Act 1993 Not applicable
 - 9.5 relevant international standards and obligations Not applicable
 - 9.6 the Legislation Guidelines (2018 edition), which are maintained by the Legislation Design and Advisory Committee. Complies

Regulations Review Committee

10. Officials consider that there are no grounds for the Regulations Review Committee to draw the Order in Council to the attention of the House under Standing Order 319.

Certification by Parliamentary Counsel

11. The regulations have been certified by Parliamentary Counsel as being in order for submission to Cabinet.

Impact Analysis

12. The proposal is of a minor and mechanical nature and does not substantially alter existing arrangements. Therefore, a regulatory impact assessment is not required.
13. The proposal will not increase compliance costs as it is simply a change in the prescribed interest rate.

Publicity

14. Inland Revenue will publish an article about these changes in its *Tax Information Bulletin*.

Proactive Release

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

Consultation

16. The Treasury has been consulted in the preparation of this paper.

Revenue implications

17. Lowering the prescribed interest rate to 4.50% will decrease the amount of FBT that will be collected by approximately \$0.4 million per quarter. This amounts to \$6.4 million over the current forecast period (2020/21 to 2023/24).

Recommendations

18. I recommend that the Cabinet Legislation Committee:
- 18.1 **note** that the regulations set the prescribed rate of interest for calculating the taxable benefit of low-interest, employment-related loans;
- 18.2 **agree** that, consistent with the results of the Reserve Bank's survey for March 2020, the FBT prescribed rate of interest should be lowered from 5.26% to 4.50% from the quarter commencing on 1 July 2020;
- 18.3 **note** the following changes as a result of the decision in recommendation 2, with a corresponding impact on the operating balance:

Vote Revenue Minister of Revenue	\$m – increase/(decrease)				
	2019/20	2020/21	2021/22	2022/23	2023/24 & Outyears
Tax Revenue: Fringe Benefit Tax receipts:	0.000	(1.600)	(1.600)	(1.600)	(1.600)
Total Operating	0.000	1.600	1.600	1.600	1.600

- 18.4 **note** that the changes are forecast changes and do not have appropriation implications;
- 18.5 **authorise** the submission to the Executive Council of the Income Tax (Fringe Benefit Tax, Interest on Loans) Amendment Regulations 2020.

Authorised for lodgement

Hon Stuart Nash
Minister of Revenue



Cabinet Legislation Committee

Minute of Decision

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

Income Tax (Fringe Benefit Tax, Interest on Loans) Amendment Regulations 2020

Portfolio **Revenue**

On 16 June 2020, the Cabinet Legislation Committee:

- 1 **noted** that the Income Tax (Fringe Benefit Tax, Interest on Loans) Amendment Regulations 2020 set the prescribed rate of interest for calculating the taxable benefit of low-interest, employment-related loans;
- 2 **noted** that, consistent with the results of the Reserve Bank's survey for March 2020, the Fringe Benefit Tax (FBT) prescribed rate of interest should be lowered from 5.26 per cent to 4.50 per cent from the quarter commencing on 1 July 2020;
- 3 **noted** the following changes as a result of the decision in paragraph 2, with a corresponding impact on the operating balance:

	\$m – increase/(decrease)				
Vote Revenue Minister of Revenue	2019/20	2020/21	2021/22	2022/23	2023/24 & Outyears
Tax Revenue: Fringe Benefit Tax receipts:	0.000	(1.600)	(1.600)	(1.600)	(1.600)
Total Operating	0.000	1.600	1.600	1.600	1.600

- 4 **noted** that the changes are forecast changes and do not have appropriation implications;
- 5 **authorised** the submission to the Executive Council of the Income Tax (Fringe Benefit Tax, Interest on Loans) Amendment Regulations 2020 [PCO 22941/3.0];
- 6 **noted** that the Amendment Regulations come into force on 23 July 2020.

Gerrard Carter
Committee Secretary

Present:

Rt Hon Winston Peters
Hon Chris Hipkins (Chair)
Hon Andrew Little
Hon Nanaia Mahuta
Hon Stuart Nash
Hon Damien O'Connor
Hon Iain Lees-Galloway
Hon Tracey Martin
Hon Aupito William Sio
Hon Eugenie Sage

Officials present from:

Office of the Prime Minister
Officials Committee for LEG