

The Treasury

Budget 2011 Information Release

Release Document

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PAD BN2011/35

Date: 17 March 2011

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To: Minister of Finance
Minister of Revenue

AIDE MEMOIRE: LEGISLATIVE OPTIONS FOR IMPLEMENTING PIE FINANCIAL HUB REFORM

Background

The foreign investment PIE proposals are likely to be agreed by Cabinet on 4 April this year. Under these proposals non-resident investors in PIEs would face a lower level of tax on their PIE investments - including zero percent tax on offshore investment. These proposals are a necessary pre-requisite to the Government's wider financial hub work.

We understand that the Government wants the proposals progressed into legislation as follows:

- Included in a bill in the first half of this year
- Referred to FEC for an abridged select committee process
- Proposals passed before this year's general election.

There are 2 viable options for achieving this. Which one is most appropriate will depend on whether the Government wants the foreign PIE proposals as part of its wider Budget 2011 package.

The 2 viable options are outlined below – including an indicative timetable through to enactment.

In order to decide which option is preferred the main aspects of the overall package for tax and related issues that is planned for Budget 2011 is summarised at the end of this note.

Option 1 – separate Budget day bill

Under this approach the proposals would be introduced in a separate Budget day bill and referred to FEC on Budget day. The timetable would be along the following lines:

- 8 June – FEC resolves to call for submissions (2 week deadline)

- 11 June – FEC advertises for submissions
- 1 July – submissions close
- 6 July – FEC hears submissions
- 13 July – FEC consideration of officials' report
- 3 August – FEC deliberation
- 9 August – Bill referred back to House
- 16 August – 2nd reading
- 18 August – COWH
- By 15 September – Royal assent

Introducing the bill on Budget day would raise the profile of the reform as a major Budget initiative. This could be promoted as a measure to encourage the development of a New Zealand managed funds industry. However, the tax reductions for non-residents could also be contrasted with the reduction of tax incentives for recipients of Working for Families and savers in KiwiSaver. Also, including the measures in the Budget day bill would mean that there would be a separate debate in the House on this issue.

Option 2 – SOP to the November 2010 tax bill

Under this approach the proposals would be included in an SOP. The Minister of Revenue would release the SOP and write to the chair of FEC inviting the Committee to consider the SOP as part of the Taxation (Tax Administration and Remedial Matters) Bill 2010 (the November 2010 bill).

To make this work, the SOP would have to be introduced earlier than Budget day. This is because the November 2010 bill must be reported back to the House by 7 June. Given that FEC is not scheduled to meet in the last 2 weeks of April and between 23 May and 7 June, a timetable along the following lines would be required:

- 4 April – Cabinet approves policy and authorises MOR to release SOP “when settled” without further referral to LEG or Cabinet
- 5-12 April – SOP referred to FEC
- 9 or 16 April – FEC calls for submissions
- 29 April – Submissions close
- 4 May – Briefing to FEC / FEC hears submissions
- 11 May – FEC consideration
- 18 May – FEC deliberation
- 7 June – Report-back to House with November 2010 bill

- Around 12 July – Royal assent

The main advantage of this approach is that it avoids the need for a separate debate on Budget day. It also provides the Government with the flexibility to introduce the measure before the Budget. While announcing the proposal before the Budget would reduce its profile as a Budget initiative, the details of the proposed PIE changes are already widely known due to taxpayer consultation. This means that it would not be a surprise initiative revealed in the Budget anyway.

The main disadvantage of this approach is that it does not provide much time to finalise the details of the SOP.

Fiscal Implications

As we have reported earlier, we estimate the fiscal cost of the PIE reform at about \$10 million per year. In addition, Inland Revenue has indicated that there would be a one-off administrative cost of \$1 million that they would seek funding for.

Overall Budget 2011 package for tax and related issues

The other main proposals to be included in the Budget 2011 package are as follows:

Budget day legislation (through all stages under urgency)

- Changes to KiwiSaver (to be legislated on Budget day) – including:
 - Halving of the member tax credit
 - Removing the ESCT exemption
 - Increasing the default contribution rate from 2%-4%
- Changes to Working for Families (to be legislated on Budget day) – including:
 - Increasing the abatement rate by 1.25 percentage points every indexation round from 1 April 2012 until it reaches 25%
 - Removing the indexation of the Family Tax Credit amounts for children 16 and over

Budget proposals not included in Budget day legislation

- Changes to the student loan scheme (not to be legislated on Budget day) – including:
 - Suspending inflation adjustments for repayment threshold until 2015
 - No access to student loan if borrower in default
- Increasing the minimum equity requirements for foreign-owned banks from 4% to 6%

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