

The Treasury

Budget 2015 Information Release

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Treasury Report: KiwiSaver kick-start removal: forecast savings, implementation and policy issues

Date:	5 March 2015	Report No:	T2015/398
		File Number:	SH-11-4-3-8

Action Sought

	Action Sought	Deadline
Minister of Finance (Hon Bill English)	<p>Direct officials to prepare a draft Cabinet paper proposing that Budget 2015 either:</p> <ul style="list-style-type: none"> i. Remove the kick-start entirely; or ii. Remove the kick-start for 18-65 year olds (but retain it for under-18s). <p>Refer the report to the Associate Ministers of Finance.</p> <p>Refer the report to the Minister of Revenue.</p>	Monday, 9 March 2015 so that officials can prepare a draft Cabinet paper for your review by Monday, 16 March 2015

Contact for Telephone Discussion (if required)

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Actions for the Minister's Office Staff (if required)

Return the signed report to Treasury.

Refer the report to the Associate Ministers of Finance and the Minister of Revenue.

Enclosure: No

Treasury Report: KiwiSaver kick-start removal: forecast savings, implementation and policy issues

Executive Summary

The KiwiSaver kick-start payment of \$1,000 (kick-start) is paid to all new enrollees in KiwiSaver aged under 65 years. Ministers have requested that officials provide advice on the forecast fiscal savings from removing the kick-start altogether. We also understand that Ministers may wish to explore retaining the kick-start for under-18 year olds only, however, a number of policy reasons speak against this. This report sets out the forecast fiscal savings from removing the kick-start under both scenarios on the basis of implementation on Budget day, 21 May 2015.

The KiwiSaver Evaluation will be published on 27 March 2015. It finds that KiwiSaver has provided poor value for money for the Crown due to the high degree of leakage of subsidy payments to individuals outside of the target group of the policy. The Evaluation also finds that the effect on saving has been poor. Removing the kick-start will go some way to reducing the headline cost and will therefore improve value for money (but not target effectiveness).

Recommended Action

We recommend that you:

- a **Direct** officials to prepare a draft Cabinet paper for your consideration proposing either:
 - i. to implement removal of the kick-start for Budget 2015 (*Treasury and Inland Revenue preferred option*)
Agree/disagree.
 - ii. to implement removal of the kick-start for 18-65 year olds (but retaining for under-18s) for Budget 2015
Agree/disagree.
- b **Refer** this report to the Associate Ministers of Finance
Refer/not referred.
- c **Refer** this report to the Minister of Revenue
Refer/not referred.

James Beard
Manager, Financial Markets and International

Hon Bill English
Minister of Finance

Treasury Report: KiwiSaver kick-start removal: forecast savings, implementation and policy issues

Background

1. We have previously reported to you on the KiwiSaver Evaluation and policy options to improve the value for money of the KiwiSaver scheme [T2015/211 refers]. In a meeting with Minister English on 24 February 2015, officials were informed that Budget Ministers wished to explore removing the \$1,000 kick-start payment paid to all new KiwiSaver enrolees (kick-start) and that Ministers were also considering retaining the kick-start for children only.

Purpose of Report

2. The purpose of this report is to seek a decision on what option you wish to take to Cabinet seeking approval for inclusion in Budget 2015. To assist your decision it quantifies the forecast fiscal savings from a removal of the kick-start and outlines the process for implementation and some policy issues you should be aware of.

Fiscal Savings

3. We have forecast the fiscal savings from two options: (1) complete removal of the kick-start and (2) retention of the kick-start for those aged under 18 years only.
4. The forecast fiscal savings are set out in table 1 below. These are based on Inland Revenue preliminary BEFU forecasts of future KiwiSaver membership and enrolment. You should note that there are some limitations with these forecasts and wide confidence intervals around them. Option (1) would deliver \$17 million in savings for 2014/15 (i.e. the remainder of the current fiscal year) and \$175 million in 2015/16. Inland Revenue forecast a decline in new enrolments from 2016/17 onwards. Option (2) would see lower savings of \$148 million in 2015/16 and less in out years.
5. There are significant disparities between the forecast savings based on preliminary BEFU data and the forecast savings based on December 2014 HYEPU data which were contained in our previous report (T2015/211). For example, the 2015/16 estimated saving in Table 1 below is 50% higher than in our previous advice. This is because the preliminary BEFU data has been adjusted for recent increases in KiwiSaver enrolment. Factors affecting this could include a stronger labour market, migration trends and popularity of KiwiSaver.

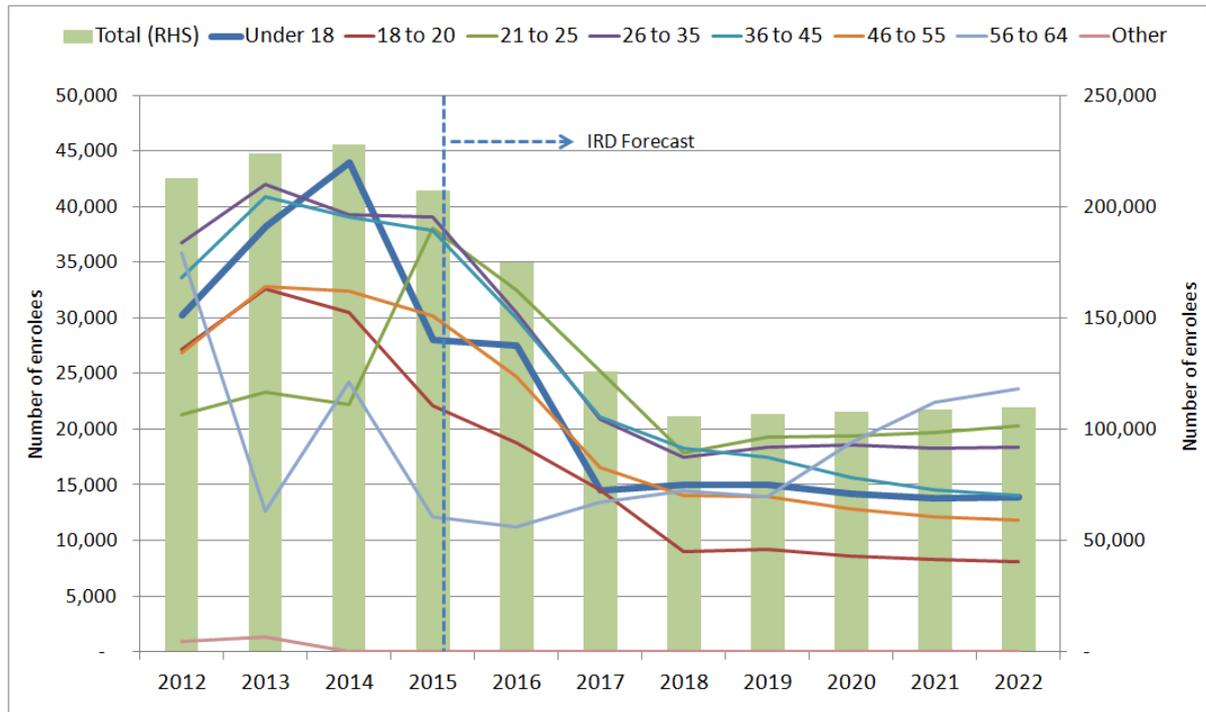
Table 1 – Annual estimated fiscal savings from changes to KiwiSaver kick-start (\$m) – based on preliminary BEFU data

Option	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22
KickStart								
(1) Removed	17 *	175	126	106	107	108	109	110
(2) Retained for under 18's	14 *	148	112	91	92	94	96	97

*Assuming a Budget next-day effective date

6. The historic and forecast total enrolment rate and age distribution for new enrolments in KiwiSaver is set out in figure 1 below. This is based on Inland Revenue historic data and preliminary forecasts provided for BEFU. Inland Revenue note that actual enrolments have consistently exceeded forecasts. If this continues, that would make savings higher than stated. Inland Revenue further note that the balance of risks to these numbers is that under-18s will make up a larger proportion of the new membership than shown in figure 1, and a consequence is that the fiscal savings could also be less than stated.

Figure 1 – Age distribution of KiwiSaver enrolees and total cost forecast



Source: Inland Revenue

Timing and legislative constraints

7. Inland Revenue have provided detailed advice set out in Appendix 1. In summary, Inland Revenue is confident that it can implement a complete removal of the kick-start payment effective from Budget day (and also later dates). No major administrative barriers to implementation have been identified for a complete removal of the kick-start payment. Changes are required in the IRD's SAP system (which sits outside of FIRST) but not to the FIRST system.
8. Inland Revenue would require a minimum of **six weeks** lead time to implement a removal of the kick-start payment. In order for a Budget day effective date to be possible Inland Revenue will need to start development by **9 April 2015 at the latest**. An indication from Ministers to proceed would be required by then.
9. Limiting the kick-start payment to under 18 year olds is more complex to implement. Inland Revenue have low confidence in delivering a robust solution for Budget day or 1 July 2015. A 1 July 2016 implementation date may be possible, but further analysis is required to confirm this.
10. Amendments to the KiwiSaver Act 2006 will be required to give effect to either proposal.

Policy Issues to Consider

Value for money of KiwiSaver

11. Removing the kick-start will have the effect of lowering the headline cost of KiwiSaver and will therefore improve the value for money of the scheme. However, the target effectiveness of the policy will only improve marginally (at best). Removal or reduction by 50% of the annual member tax credit payments as outlined in our report on policy options following the KiwiSaver Evaluation [T2015/211 refers] would have a greater effect on improving value for money but would also not materially change the target effectiveness of KiwiSaver.
12. As outlined in our previous report, it is difficult to better target KiwiSaver subsidies. This is because the purpose of the KiwiSaver Act does not identify a particular group in society that can be targeted with conventional socio-economic metrics or identifiers such as income level. The purpose of the Act refers to boosting savings among “*individuals who are not in a position to enjoy standards of living in retirement similar to those in pre-retirement.*”

Behavioural responses –if policy announced ahead of law change

13. Provided that the kick-start can be removed with immediate effect from the passing of legislation on Budget night, there would be no spike in enrolments to KiwiSaver. However, if the policy change were to be announced in advance of the effective date (say on 1 July 2015), we would expect large numbers of enrolments in that intervening period. This would reduce the fiscal savings.

Retaining kick-start for children not recommended

14. Retaining the kick-start for children only (option (2) above) is not recommended by the Treasury as it would create a strong incentive for the non-target group (children) to join KiwiSaver. KiwiSaver is a work-based retirement savings scheme which locks in contributions until age 65, except in certain circumstances, and is designed to support long-term individual savings. While there is no absolute rule about when to start saving for retirement, it is recognised that for many people, developing an early retirement savings habit and making regular contributions is important for ensuring a pot of funds is built up for retirement. However, at some stages in life, investment in other forms of capital, such as in education to develop future earnings potential, or investment in a business, is more important for longer term wellbeing and comfort. For young people their focus should be on the development of human capital, and saving towards their education and skills development for the labour market. Saving for a first home by young people, even under the new HomeStart policy, would not be affected by removal of the kick-start because the \$1,000 amount is not available for withdrawal under any policy.
15. KiwiSaver members are eligible for the annual member tax credits from age 18. This is consistent with the importance placed by the Government on young people obtaining an education and actively encouraging young people to continue their education by remaining on at secondary school, or joining another educational training facility. Retaining the kick-start for only under-18s would be inconsistent with the remaining KiwiSaver policies and wider Government education and training policy.
16. As noted above under implementation issues, Inland Revenue advise that there is low confidence of successfully implementing a change that retains the kick-start for under-18s only on Budget day or 1 July 2015. Although a 1 July 2016 date may be possible, this can only be confirmed after further analysis by Inland Revenue.

17. Finally, there may be human rights issues under the Bill of Rights Act relating to discrimination based on age. We are consulting with Ministry of Justice in this regard.

Next Steps

18. Officials require a decision by you by Monday, 9 March 2015 so that a draft Cabinet paper can be prepared for your review by Monday, 16 March 2015. Cabinet could then consider that paper at its meeting on Monday, 30 March 2015 to allow a decision by 9 April 2015 (the latest possible date for implementation by Budget 2015).
19. Consideration should be given to the appropriate legislative vehicle. One option is to have a tax omnibus budget bill on the basis that there are at least two tax-related budget issues currently under consideration.
20. Inland Revenue will provide details of the implementation costs after an indication from Ministers to proceed is received. Should there be a cost associated with implementation funding from outside IRD's baselines will need to be sought. This is because Inland Revenue has already made funding commitments from its baselines, such as the tax policy work programme.

Appendix 1 – Inland Revenue Advice

Administrative impacts - KiwiSaver changes

Inland Revenue has been asked to consider implementation timeframes for either:

1. Removing the kick-start payment; or
2. Limiting the kick-start to under 18 years of age.

We have also been asked to indicate:

1. any major barriers to implementation; and
2. whether a Budget day implementation is possible.

The kick-start payment is a tax-free contribution of \$1,000 by the Government to encourage uptake of KiwiSaver. Currently all new KiwiSaver members qualify for the kick-start payment when they first join. The kick-start is paid into the member's scheme provider account about 3 months after Inland Revenue receives either their first contribution, or when notified of the membership by the scheme provider.

Summary

Inland Revenue is confident that it can implement a complete removal of the kick-start payment effective from Budget day (and also later dates).

No major administrative barriers to implementation have been identified for a complete removal of the kick-start payment. Changes are required in the SAP system (which sits outside of FIRST) but not to the FIRST system.

Inland Revenue would require a minimum of six weeks to implement a removal of the kick-start payment. In order for a Budget day effective date to be possible Inland Revenue will need to start development by 9 April at the latest. An indication from Ministers to proceed would be required by then.

Limiting the kick-start payment to under 18 year olds is more complex to implement. We have a low confidence in delivering a robust solution for Budget day or 1 July 2015. A 1 July 2016 implementation date may be possible, but further analysis is required to confirm this.

Officials are undertaking further work to determine timeframes and costs to fully implement the changes.

Consideration of broader budget package

We have assessed the implementation impact of this proposal on Inland Revenue's business. However, Inland Revenue has been asked to provide advice on a number of potential budget proposals. Consideration will need to be given to the overall implementation impact of the broader budget package once final decisions are made. There may need to be some trade-offs made on the various proposals in relation to the implementation impacts of the overall package.

Timetable options and confidence of implementation

	Budget Day	1 July 2015	1 July 2016
Complete removal kick-start payment	High confidence Minimum six weeks lead-in required	High confidence	High confidence
Limit kick-start payment to under 18 years of age	Low confidence	Low confidence	Medium confidence Further analysis is required to ensure a robust solution that can validate age data from providers with age data in IR's core tax system.

As we have had limited time to provide this advice, it is at a high level only at this stage. If Ministers wish to proceed with either of these options, officials will report back on the associated administrative costs, impacts (including IR's transformation programme), timeframes and whether trade-offs in Inland Revenues wider portfolio would be required in order to deliver any agreed changes.

Across the board removal

An across the board change to remove the kick-start payment for all new members is relatively straightforward from an implementation perspective.

Technology

We are confident from a technology perspective that a Budget day implementation can be achieved.

Kick-start payments are managed through our SAP system and would not require any changes to our FIRST system.

Removing the kick-start payment is not anticipated to be complex, based on Inland Revenue experience of other changes made to KiwiSaver. However it will require a minimum lead in time of six weeks for development and testing.

Transitional criteria

Transitional rules will be required to ensure members that have enrolled prior to Budget day and have not yet received their kick-start payment will still receive the payment.

Managing customers

Inland Revenue will only be able to make minimal updates to our website to make customers aware of the changes on Budget day. There would be a period in which existing KiwiSaver collateral will still refer to the kick-start payment and would be issued to customers after the Budget day announcement. Further updating of KiwiSaver collateral will need to be managed after the Budget announcement.

It is expected in the initial period after announcement that there will be increased phone call volumes from customers wanting to know if they will still receive the kick-start payment – particularly those that may have enrolled in the three months prior to Budget day and are still in the provisional/holding period (approx. 40,000 members).

Other issues

Scheme provider investment statements and other collateral will contain information relating to the kick-start payment. Investment statements are issued by both the scheme provider and Inland Revenue (on default providers' behalf). Legislative amendments will likely be necessary to ensure this does not breach securities law until updates can be made.

Later implementation dates

Inland Revenue is also confident that later effective dates of 1 July 2015 or 1 July 2016 are also achievable. A longer lead time allows Inland Revenue to work with key stakeholders (employers, scheme providers, etc) to ensure a smoother implementation approach.

Officials are undertaking further work to determine timeframes and costs to fully implement the changes.

Limiting kick-start to under 18 year olds

Under the KiwiSaver Act, all enrolments for under 18 year olds should be through a provider; therefore age data is collected via providers on enrolment. However, system changes would be required in relation to how IR stores and uses this information to enable a robust kick-start entitlement decision to be applied.

IR has a low confidence in implementing a robust solution, for either a Budget day or 1 July 2015 implementation, which could validate and process age data received from providers to enable payment of the kick-start to under 18 year olds.

An implementation date of 1 July 2016 is likely possible, but further analysis is required to confirm this.

The impacts for "Transitional criteria", "Managing customers", and "Other issues" identified above for the complete removal of the kick-start payment also apply to limiting the kick-start payment to under 18 year olds. However a later implementation date would allow time for a smoother implementation and lessen the impacts on customers and providers.

If Ministers want to progress with this option Inland Revenue would need to complete detailed analysis to fully understand the full impacts, costs, timeline, and trade-offs for implementing these changes.