7 March 2008 SH-13-3-0

To: Office of the Minister of Finance

From: Tax Strategy, Treasury

AIDE MEMOIRE: PHASED SCENARIOS OF 5 MARCH

Treasury has costed two further phased scenarios. Each scenario implements a tax free zone to $10 000 through gradual reductions to the bottom rate. The second scenario is phased over four budgets and extends thresholds for the 33% and 39% rates further than scenario one.

Scenario one

On April 1 2009

- Abolish the Low Income Rebate and introduce a 10% rate up to $10 000
- 21% on income between $10 000 to $40 000
- 33% on income between $40 000 to $70 000
- 39% on income in excess of $70 000

On April 1 2010

- 5% on income up to $10 000
- 21% on income between $10 000 to $41 000
- 33% on income between $41 000 to $70 000
- 39% on income in excess of $70 000

On April 1 2011

- 0% rate (tax free zone) up to $10 000
- 21% on income between $10 000 to $42 000
- 33% on income between $42 000 to $75 000
- 39% on income in excess of $75 000

Scenario two

On April 1 2009

- Abolish the Low Income Rebate and introduce a 10% rate up to $10 000
- 21% on income between $10 000 to $40 000
- 33% on income between $40 000 to $70 000
- 39% on income in excess of $70 000

On April 1 2010

- 6.5% on income up to $10 000
- 21% on income between $10 000 to $42 000
- 33% on income between $42 000 to $70 000
- 39% on income in excess of $70 000

On April 1 2011

- 3% rate on income up to $10 000
- 21% on income between $10 000 to $42 000

- 33% on income between $42 000 to $75 000
- 39% on income in excess of $75 000

On April 1 2012

- 0% rate (tax free zone) up to $10 000
- 21% on income between $10 000 to $44 000
- 33% on income between $44 000 to $80 000
- 39% on income in excess of $80 000

Assumptions used

Costs are provided for June fiscal years.

Contributions to the Superfund in 2008/09 and 2009/10 are based on the increase to the future cost of superannuation from the full phased scenario. As with previous costings, fund contributions are volatile. For each scenario we show two sets of costings, the first using actual fund contributions and second with contributions averaged across the five years presented.

The second scenario anticipates changes from 1 April 2012. The first full year impact would be in 2012/13 which is beyond our current forecast period. We have made a number of assumptions regarding macro indicators for 2012/13, so costing precision could be reduced somewhat. Now that we have created a 2012/13 year in our costing model we present costs for this year for both scenarios.

COSTS FOR PHASED SCENARIO ONE

Table 1 shows the five year cost of phased scenario one.

Table 1: phased scenario one

	2008/09	2009/10	2010/11	2011/12	2012/13
Change to disposable income	-481	-2,289	-3,789	-5,012	-5,083
Change to residual cash	**-900**	**-2,053**	**-2,994**	**-3,791**	**-3,946**

As noted above, Superfund contributions are volatile in early years (in particular the $183 million reduction from the status quo in 2011/12). Table 2 shows the cost of the phased scenario where contributions are averaged across the five years; this provides a more accurate picture of the future cost of the tax changes.

Table 2: phased scenario one with averaged superfund contributions

	2008/09	2009/10	2010/11	2011/12	2012/13
Change to disposable income	-481	-2,289	-3,789	-5,012	-5,083
Change to residual cash	**-481**	**-1,884**	**-3,062**	**-4,077**	**-4,181**

COSTS FOR PHASED SCENARIO TWO

Table 3 shows the four year cost of phased scenario two.

Table 3: phased scenario two

	2008/09	2009/10	2010/11	2011/12	2012/13
Change to disposable income	-481	-2,224	-3,396	-4,468	-5,290
Change to residual cash	**-927**	**-2,054**	**-2,832**	**-3,592**	**-4,360**

Superfund contributions are not as volatile in scenario two, but nevertheless we have still produced in table 4 the cost for scenario two where contributions are averaged across the five years.

Table 4: phased scenario two with averaged superfund contributions

	2008/09	2009/10	2010/11	2011/12	2012/13
Change to disposable income	-481	-2,224	-3,396	-4,468	-5,290
Change to residual cash	**-624**	**-1,975**	**-2,893**	**-3,786**	**-4,488**

1 OCTOBER START DATE

We have also calculated the cost of a 1 October 2008 start date. An early start date primarily affects the cost in the 2008/09 year; although slight movements in fund contributions mean that the change to the residual cash position in future years can deviate by up to $20 million from the costs presented above. Tables 5 and 6 compare the cost in 2008/09 for a 1 October 2008 and 1 April 2009 start date under each option. Note that the additional cost from a 1 October 2008 start date is the same under each option.

Table 5: Costs in 2008/09 with alternate start dates for scenario one

	1-Oct-08	1-Apr-09	DIFFERENCE
Change to disposable income	-1,395	-481	-915
Change to residual cash	**-1,518**	**-900**	**-618**

Table 6: Costs in 2008/09 with alternate start dates for scenario two

	1-Oct-08	1-Apr-09	DIFFERENCE
Change to disposable income	-1,395	-481	-915
Change to residual cash	**-1,545**	**-927**	**-618**