THE TREASURY
Kaitohutohu Kaupapa Rawa

Treasury Report: Finalising the Budget 2008 Personal Tax Package

Date:	2 May 2008	**Report No:**	T2008/772

Action Sought

	Action Sought	Deadline
Prime Minister (Rt Hon Helen Clark)	**Indicate** your preferences in respect of finalising the Budget 2008 Personal Tax Package	Friday 2 May
Minister of Finance (Hon Dr Michael Cullen)	**Indicate** your preferences in respect of finalising the Budget 2008 Personal Tax Package	Friday 2 May
Associate Minister of Finance (Hon Trevor Mallard)	**Indicate** your preferences in respect of finalising the Budget 2008 Personal Tax Package	Friday 2 May

Contact for Telephone Discussion (if required)

Name	Position	Telephone		1st Contact
Mark Blackmore	Manager, Macro Policy	471 5247 (wk)	[deleted - privacy]	✓
Bill Moran	Manager, Tax Strategy	917 6947 (wk)	[deleted - privacy]	

Minister of Finance's Office Actions (if required)

None.

Enclosure: **No**

2 May 2008

Treasury Report: Finalising the Budget 2008 Personal Tax Package

Executive Summary

On 14 April 2008 Cabinet considered two possible tax packages for Budget 2008 - a **scenario A** package and an alternative **scenario B** package that would be considered if the Treasury's final forecasts were lower than the preliminary forecasts. Since then, delegated Ministers asked Treasury to provide information on an alternative **scenario C**. Scenario C is a close variation on scenario B.

Cabinet delegated authority to the Prime Minister, the Minister of Finance and the Associate Minister of Finance (Hon Mallard) to take final decisions on the tax package and its implementation date once Treasury had finalised its economic and fiscal forecasts (CAB Min (08) 14/9 refers).

The final fiscal forecasts have been revised down since the preliminary forecasts due to a combination of final macroeconomic forecasts, final budget decisions and updated SOE/CE forecasts. This has a material impact on the affordability of scenario A given the Government's long term fiscal objectives.

We are now projecting that scenario A (irrespective of the implementation date) will see debt rise to around 27% of GDP over the projection period and, as a consequence, would be inconsistent with the Government's long term fiscal objective of maintaining debt at around 20% of GDP. Alternatively, under scenarios B and C, debt is projected to peak at 21-22% of GDP, which would be broadly consistent with the long term debt objective.

In terms of the operating balance, scenario A results in the OBEGAL, excluding returns from the New Zealand Super Fund, going into and staying in deficit, which we would advise against. Scenario B sees the OBEGAL fall to just above zero in 2011/12 and stay there for the first two years of the projection period. Scenario C is slightly more expensive than scenario B but the OBEGAL, excluding returns from the NZSF, remains in surplus.

We consider scenarios B and C to be near the boundary of what would be a prudent fiscal package. In both cases, we would recommend that you signal in the FSR how you would respond (in very broad terms) if there was a risk that the OBEGAL could move materially into deficit. The messages could indicate that the government would take corrective action to maintain the robustness of the fiscal position if the OBEGAL looked like it might be heading even lower. In addition, you could signal that you would let any positive fiscal surprises flow through to a higher operating balance in the first instance. You could also signal that if the outlook for the fiscal position were to significantly improve, the first priority for any additional policy initiatives would be to increase the size of the tax reductions in later years.

Of the two scenarios, we would recommend scenario C as it delivers marginally more benefits in terms of the government's equity, efficiency and growth objectives than scenario B.

Scenarios B and C also incorporate a reduction in Budget operating allowances from $1.8 billion to $1.75 billion per annum. Given current fiscal pressures on future Budgets, this level of operating allowance would crowd out flagship initiatives without increases in future revenue forecasts or significant reprioritisation of current public services. This strengthens the need for Government to continue its focus on value for money in the public sector and the need to find ongoing reprioritisation opportunities.

On 14 April, Cabinet considered a number of consequential issues for other areas of the tax system flowing from scenarios A and B, including the implications of a 1 October or 1 April start date, and agreed that any consequential issues would flow through to any package agreed by delegated Ministers unless the basis of the package was to fundamentally change. The consequential impacts that were agreed by Cabinet on 14 April are summarised in annex 3.

Treasury and Inland Revenue have provided separate advice on the implications of bringing forward the indexation of Working for Families (the Family Tax Credit rates and the abatement threshold) to 1 October 2008 rather than 1 April 2009, which is the current date that this is expected to occur. A decision is sought on this point.

Treasury and Inland Revenue have also provided separate advice on whether an additional rate of secondary tax (at 12.5%) should be introduced and, if so, at which phase of the package. Treasury and Inland Revenue recommend against introducing a new secondary tax code from 1 October 2008 should the tax cut package be implemented from this date. A decision is sought on this point.

Recommended Action

We recommend that you:

a **note** that on 14 April 2008 Cabinet considered two possible tax scenarios as set out below:

Scenario A

On 1 October 2008 or 1 April 2009	On 1 April 2010	On 1 April 2011
12.5% to $15,000 21% to $40,000 33% to $70,000 39% over $70,000	12.5% to $20,000 21% to $40,000 33% to $75,000 39% over $75,000	12.5% to $25,000 21% to $45,000 33% to $80,000 39% over $80,000

Scenario B

On 1 October 2008 or 1 April 2009	On 1 April 2010	On 1 April 2011
12.5% to $14,000 21% to $40,000 33% to $70,000 39% over $70,000	12.5% to $17,500 21% to $40,000 33% to $75,000 39% over $75,000	12.5% to $20,000 21% to $42,500 33% to $75,000 39% over $75,000

b **note** that delegated Ministers asked Treasury to provide the following scenario for consideration:

Scenario C

On 1 October 2008 or 1 April 2009	On 1 April 2010	On 1 April 2011
12.5% to $14,000 21% to $40,000 33% to $70,000 39% over $70,000	12.5% to $17,500 21% to $40,000 33% to $75,000 39% over $75,000	12.5% to $20,000 21% to $42,500 33% to $80,000 39% over $80,000

c **note** that Cabinet delegated authority to the Prime Minister, the Minister of Finance and the Associate Minister of Finance (Hon Mallard) to take final decisions on the tax package and its implementation date once Treasury finalises its economic and fiscal forecasts (CAB Min (08) 14/9 refers);

d **note** that Treasury has revised down its final forecasts and this has had a material impact on the affordability of scenario A given the Government's long term fiscal objectives;

e **note** that scenarios B and C are consistent with the long term debt objective of maintaining debt at around 20% of GDP;

f **note** that Treasury recommends scenario C although this is near the boundary of what we would consider to be a prudent fiscal package given the forecast decline in the OBEGAL and the associated risks that accompany this. As a result you may wish to consider including additional messages in the *Fiscal Strategy Report* (in very broad terms) signalling how the government would respond to any positive or negative surprises from this forecast track;

g **agree** to scenario C for inclusion in Budget 2008:

Agree / disagree *Agree / disagree* *Agree / disagree*

h **indicate** which implementation date should be adopted for the first phase of the package:

1 Oct 2008 / 1 Apr 2009 *1 Oct 2008 / 1 Apr 2009* *1 Oct 2008 / 1 Apr 2009*

Consequential impacts to other parts of the tax system

i **note** that on 14 April 2008 Cabinet considered a number of consequential impacts to other parts of the tax system as a result of the tax package and agreed that these consequential issues would flow through to any package agreed by delegated Ministers as long as the as the basis of the changes remain unchanged;

j **note** that we do not consider there to be any problems with flowing through the decisions from this paper into the consequential issues highlighted in the Cabinet paper;

Indexation of Working for Families

k **note** that Treasury and Inland Revenue have provided separate advice on the implications of bringing forward the indexation of Working for Families (the Family Tax Credit rates and the abatement threshold) to 1 October 2008 rather than 1 April 2009;

l **indicate** when the indexation of Working for Families should be implemented:

1 Oct 2008 / 1 Apr 2009 *1 Oct 2008 / 1 Apr 2009* *1 Oct 2008 / 1 Apr 2009*

m **note** that it is possible to prevent recovery of tax credits overpaid as a result of bringing indexation forward;

n **note** that because any recovery would not be sought until after 31 March 2009 a rule that prevents this recovery is not required for inclusion in urgent legislation;

o **note** that any administrative costs will be determined and, if need be, reported to Cabinet after Budget day;

Either:

p **agree** that officials will report back after budget day on how to prevent the recovery of overpayments due to the use of composite rates;

Agree / disagree *Agree / disagree* *Agree / disagree*

Or

q **agree** that urgent legislation should include a rule that overpayments under a certain amount, defined by formula, would not be recovered;

Agree / disagree *Agree / disagree* *Agree / disagree*

Introducing a new secondary tax code

Either:

r **agree** that Inland Revenue and Treasury report back after Budget day on introducing a new secondary tax code (at 12.5%), as a result of these tax changes;

Agree / disagree *Agree / disagree* *Agree / disagree*

Or:

s **agree** that a new secondary tax code (at 12.5%) should be introduced on the same date as the implementation date chosen in recommendation h, as a result of these tax changes;

Agree / disagree *Agree / disagree* *Agree / disagree*

Reporting back to Cabinet

t **direct** Treasury to prepare a note on final decisions for delegated Ministers to table at Cabinet on Monday 12 May as per the delegated authority from Cabinet.

Bill Moran
Manager, Tax Strategy
Economic Performance Group
for Secretary to the Treasury

Rt Hon Helen Clark	**Hon Dr Michael Cullen**	**Hon Trevor Mallard**
Prime Minister	Minister of Finance	Associate Minister of Finance

Treasury Report: Finalising the Budget 2008 Personal Tax Package

Purpose of Report

1. The purpose of this report is to provide the final economic and fiscal forecast information from Treasury so that the Prime Minister, the Minister of Finance and the Associate Minister of Finance (Hon Mallard) can take final decisions on the Budget 2008 Personal Tax Package under the delegated authority from Cabinet.

Analysis

Background

2. On 14 April 2008 Cabinet (CAB Min (08) 14/9 refers) agreed to remove the Low Income Rebate and introduce the following statutory rates and thresholds over the next three years (for the purpose of this report we refer to this as **scenario A**):

On 1 October 2008 or 1 April 2009	On 1 April 2010	On 1 April 2011
12.5% to $15,000 21% to $40,000 33% to $70,000 39% over $70,000	12.5% to $20,000 21% to $40,000 33% to $75,000 39% over $75,000	12.5% to $25,000 21% to $45,000 33% to $80,000 39% over $80,000

3. The paper to Cabinet also noted that this scenario will be less affordable if the final economic and fiscal forecasts come out lower than Treasury's preliminary forecasts. In anticipation that this may occur, Cabinet also considered the following alternative scenario (for the purpose of this report we refer to this as **scenario B**):

On 1 October 2008 or 1 April 2009	On 1 April 2010	On 1 April 2011
12.5% to $14,000 21% to $40,000 33% to $70,000 39% over $70,000	12.5% to $17,500 21% to $40,000 33% to $75,000 39% over $75,000	12.5% to $20,000 21% to $42,500 33% to $75,000 39% over $75,000

4. Delegated Ministers have also asked Treasury to provide the following scenario for consideration (for the purpose of this report we refer to this as **scenario C**):

On 1 October 2008 or 1 April 2009	On 1 April 2010	On 1 April 2011
12.5% to $14,000 21% to $40,000 33% to $70,000 39% over $70,000	12.5% to $17,500 21% to $40,000 33% to $75,000 39% over $75,000	12.5% to $20,000 21% to $42,500 33% to $80,000 39% over $80,000

5. Final decisions were delegated from Cabinet as set out below:

> ***noted*** *that Treasury will finalise their economic and fiscal forecasts in late April and that it would be prudent to wait until these are finalised before taking a final decision on the design of the tax package and its implementation date;*
>
> ***delegated*** *authority to the Prime Minister, the Minister of Finance and the Associate Minister of Finance (Hon Mallard) to take final decisions on the design*

of the tax package and its implementation date once Treasury has finalised their economic and fiscal forecasts in late April;

***invited** the Prime Minister, the Minister of Finance and the Associate Minister of Finance (Hon Mallard) to report back to Cabinet before Budget day on final decisions;*

6. Information on the fiscal cost, tax savings, equity and effective marginal tax rate analysis on scenarios A, B and C is provided for your consideration separate to this report. Scenarios B and C are less expensive than scenario A by $1.3 billion and $1.2 billion respectively once fully implemented and therefore deliver less tax savings across the income distribution. In terms of meeting your equity, efficiency and growth objectives, all scenarios are very similar, with scenario C marginally better than scenario B.

Indexation of Working for Families

7. Treasury and Inland Revenue has provided separate advice on the implications of bringing forward the indexation of Working for Families (the Family Tax Credit rates and the abatement threshold) to 1 October 2008 rather than 1 April 2009, which is the current date that this is expected to occur. A decision on this point is sought in this paper. However, for the purpose of providing fiscal forecasts and projections, it is assumed that this will be brought forward to 1 October 2008.

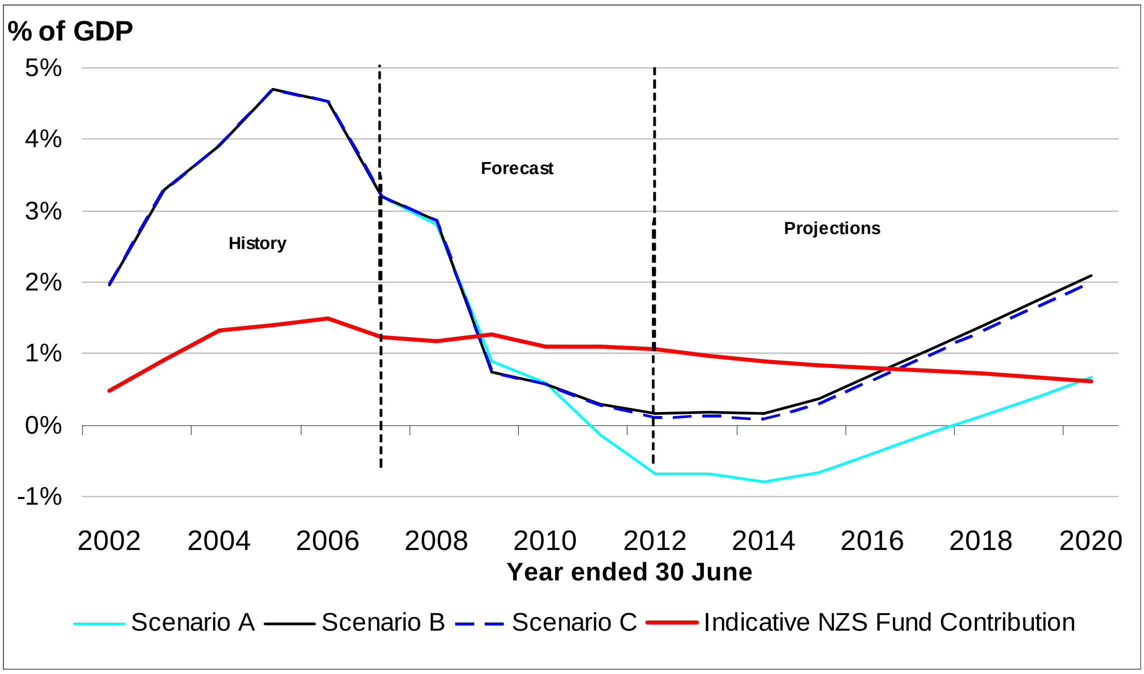
8. If indexation were brought forward delegated Ministers have indicated that overpayment of tax credits from the use of composite rates should not be recovered. Inland Revenue and Treasury consider that a rule that overpayments under a certain minimum, determined by formula, should not be pursued would achieve this. But since any overpayment would not be recovered until after 31 March 2009 such a rule would not need to be included in urgent legislation and could be considered along side other consequential issues after budget day. We would also advise that any rule should not apply where Inland Revenue had information indicating dishonesty by the applicant.

Final Treasury forecasts

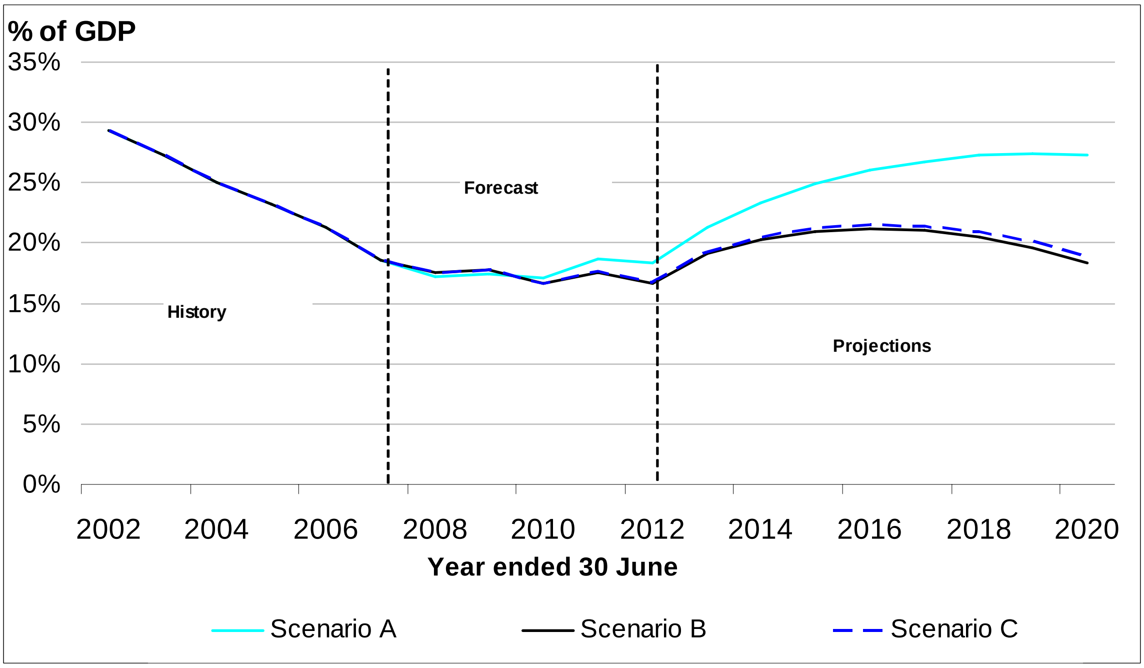
9. Annexes 1 and 2 provide details on the final macroeconomic and fiscal forecasts respectively.

10. The graphs below show updated fiscal projections for scenarios A, B and C. While a decision is sought on the implementation date for the package, the fiscal scenarios all assume a 1 October 2008 start date. Scenarios B and C also incorporate a two-year delay in the introduction of the fossil fuels into the Emissions Trading Scheme (ETS).

OBEGAL ex NZS Fund net returns (OBERAC until 2007/08)



Gross Sovereign Issued Debt ex Settlement Cash



11. Under Scenario A, GSID-to-GDP increases to over 27% in 2017/18. The OBEGAL, excluding NZ Fund returns, is in deficit from 2010/11 – 2015/16 and remains below the required contribution to the New Zealand Superannuation Fund over the period for which the 10-year fiscal objectives apply. We do not consider that this option is consistent with the Government's long term fiscal objective of maintaining GSID-to-GDP at around 20% of GDP.

12. Scenarios B and C (smaller tax packages coupled with an operating allowance of $1.75 billion), see GSID-to-GDP rising to around 21% in 2017/18 before trending lower and through 20% in subsequent years. The OBEGAL, excluding NZS Fund returns, sits a little above zero for a number of years and below the required contribution to the New Zealand Superannuation Fund from 2008/9 to 2016/17.

13. Scenarios B and C are consistent with the long term debt objective. They are also consistent with your operating balance objective, notwithstanding the period when the OBEGAL, excluding NZS Fund returns, is below the NZS Fund contribution rate. This is because over the build-up phase of the Fund (broadly 2001 to 2027) the OBEGAL is well in excess of contributions. Draft text is included in the Fiscal Strategy Report (FSR) to this effect. Of the two scenarios we recommend that you proceed with scenario C as from an equity, efficiency and growth objective, scenario C is marginally better than B.

14. Notwithstanding consistency with the Government's long term fiscal objectives and overall fiscal strategy, we think scenario C is near the boundary of what we would consider a prudent fiscal package. As was noted in BR2008/9, in general Treasury would advise that governments should avoid running persistent structural operating deficits for the following reasons:

    - Countries that go into structural deficit often take some time to move back to balance or into surplus, finding it difficult to make the necessary spending and tax changes.

    - The forecasts and projections build-in operating and capital spending allowances significantly lower than recorded over recent years. Meeting these allowances will require firm expenditure control and prioritisation between existing and new policy initiatives. The bigger the forecast decline in the structural balance, the more it will need to be rebuilt in order to achieve the Government's fiscal strategy of strengthening the fiscal position in advance of population ageing.

    - Rating agencies cite a very strong fiscal position and outlook as critical to New Zealand's sovereign credit rating, offsetting relative weakness in a number of other economic indicators.

    - Forecasts and projections of operating deficits, even if only for a short period, will make communication of the fiscal strategy more complex even if they are still consistent with fiscal objectives – as evidenced by the current need to explain consistency with the Government's operating balance objective.

15. Scenario C results in an increase in the government bond programme to around $3.4 billion per annum from about $2.5 billion of recent years. Given recent tender results, issuance in 2007/08 is likely to be about $2 billion. Discussions with market participants indicate such an increase is manageable, although with the current financial market turmoil, along with diversification away from holding government bonds by many domestic intermediaries, there is higher level of uncertainty about market reaction.

16. Monetary policy is currently facing some difficult trade-offs, having to weigh up the prospect of a marked slowdown in growth this year against still high domestic price inflation and inflation expectations, a global food and energy price shock and the introduction of the Emissions Trading Scheme. Budget 2008 adds to the challenges facing monetary policy, notwithstanding the fact that it is likely to occur at a time when others forces are acting as more of a drag on growth.

17. Each of Budget 2008 and the ETS on their own is likely to have allowed room for inflation pressures to ease back over the next few years. However the combination of the two could keep forecasts of annual CPI inflation in 2009 and 2010 above or at least close to 3%, given current judgements about other economic developments. This raised the possibility the Reserve Bank will not be able to meet the requirements of the Policy Targets Agreement of seeing CPI inflation comfortably inside the 1%-3% target range in the second half of its policy horizon on current policy settings. Applying the tax reductions from 1 October rather than 1 April marginally adds to these pressures.

Given the decision to delay the introduction of the fossil fuels into the ETS this risk is reduced.

18. Given the extra level of uncertainty as to how the economy will evolve over the next few years, and how tax revenue will track in the event of economic growth experiencing lower growth, there is a risk that Government runs an OBEGAL deficit that is larger or more sustained than shown in Scenario C. As is illustrated by Scenario A, such an outcome would stretch consistency with the fiscal strategy. It may also create economic risks, including putting greater pressure on New Zealand's sovereign credit rating and reducing policy flexibility in the event of future economic shocks.

19. Given these concerns/risks we think there is merit in signalling clearly, including in the FSR, how you might respond (in very broad terms) if the operating balance were to look like it might move more materially into deficit. This may be important for some audiences like rating agencies. For example, you could signal that the forecast/projection of the operating balance/OBEGAL is at the lower end of your comfort zone, that if the operating balance/OBEGAL looked like it was heading even lower, the government would take corrective action to maintain the robustness of the fiscal position, and in the event of positive revenue surprises you would let these flow through to a higher operating balance in the first instance.

20. You may also wish to signal that if over the longer term there are significant positive fiscal surprises you may look to expand on the tax package in scenario C back towards that included in scenario A.

Lower operating allowances

21. Scenarios B and C include ongoing Budget allowances of $1.75 billion. Budgets 2006 to 2008 had an average increase in Government expenditure of $1.9 billion if major flagship projects such as tax changes, KiwiSaver and Working for Families are excluded.

22. A Budget 2009 allowance of $1.75 billion could mean theme allocations (excluding pre-commitments) similar to those in Budget 2007, but less than in Budget 2008. Analysis of upcoming pressures indicates that there would be less room for discretionary spending than in Budget 2007 ($250 million p.a compared to $400 million p.a.) once likely pressures such as the Schools Operations Grant, School Plus and Effective Interventions are taken into account.

23. This indicates that future budget allowances of around $1.75 billion are tight but plausible; however, further flagship projects would require either an increase in future revenue forecasts or a significant reprioritisation of current public services. Any negative revenue surprises or forecast changes at March Baseline Update and October Baseline Update would need to be met from the $1.75 billion allowance, or they would decrease the operating balance. Any such pressure could also be eased by the use of reprioritisation to allow additional programmes to be funded.

Consequential impacts to other areas of the tax system

24. Cabinet on 14 April 2008 considered a number of consequential impacts to other areas of the tax system (e.g. Resident Withholding Tax, Fringe Benefit Tax, Maori Authority Tax rate etc.). To determine the final impacts on these issues Cabinet:

> ***agreed*** *that if the final tax cut package differs from that described in this paper and these differences do not affect the basis on which decisions on recommendations 6 - 23 in this paper have been made, the decisions taken on recommendations 6 - 23 in this paper apply to the amended tax cut package.*

25. The applicable recommendations are attached in Annex 3 so that delegated Ministers are aware of the impact of final decisions upon these consequential issues.

Secondary tax rates

26. Subsequent to consideration of the Tax Cabinet paper, the Minister of Finance instructed officials to consider the extent to which the secondary tax rates should be amended in light of the Personal Tax Package.

27. Treasury and Inland Revenue have provided separate advice on whether an additional rate of secondary tax (at 12.5%) should be introduced and, if so, at which phase of the package. Treasury and Inland Revenue recommend against introducing a new secondary tax code from 1 October 2008 should the tax cut package be implemented from this date. A decision is sought on this point.

Annex 1 – Final macroeconomic forecasts

Treasury forecasts (which incorporate tax scenario C and a two-year delay to the introduction of fossil fuels into the ETS) show economic growth slowing to around 1.5% in the year to March 2009, down from current rates of around 3%. This reflects the impact of drought on agricultural production, financial market volatility from abroad, and slowing domestic demand, particularly in consumption and residential investment as rising food and energy costs and high interest rates impact on households.

Relative to earlier preliminary forecasts, weaker world growth is predicted to have a more prolonged impact on the New Zealand economy, although growth is still predicted to increase to 2.3% in the March 2010 year as agricultural production levels recover from drought and household disposable incomes are boosted due to income tax changes. Beyond 2010 growth returns to around trend levels with export volume growth supported by an easing exchange rate while private consumption and consequently import growth remain muted due to high debt levels.

Annex 2

The table below provides a reconciliation between the preliminary fiscal forecasts:

Change in the OBEGAL excluding net NZS Fund revenue since preliminary forecasts

OBEGAL excluding net NZS Fund revenue	2008 Forecast $b	2009 Forecast $b	2010 Forecast $b	2011 Forecast $b	2012 Forecast $b
Preliminary forecasts	**6.1**	**3.2**	**1.9**	**0.8**	**0.4**
Tax forecasts	(0.1)	(0.2)	(0.1)	(0.3)	(0.4)
Benefit forecasts (including Kiwisaver)	(0.1)	(0.2)	(0.3)	(0.2)	(0.3)
SOE/CE results	(0.6)	(0.1)	(0.1)	(0.2)	(0.4)
Tax package allowance	-	(0.1)	(0.3)	(0.4)	(0.7)
Operating spending allowance reduction	-	-	0.2	0.4	0.6
Budget 2008 under/(overspends)	(0.1)	-	(0.1)	(0.1)	(0.1)
Tax policy decisions	-	-	(0.1)	(0.1)	(0.2)
Other minor items	(0.3)	0.2	0.2	(0.1)	(0.3)
Total	(1.1)	(0.5)	(0.6)	(0.9)	(1.7)
Near final forecasts - Scenario A	**5.0**	**2.7**	**1.3**	**(0.2)**	**(1.3)**
Scenario B adjustments	0.2	(1.4)	(0.3)	0.7	1.6
Near final forecasts - Scenario B	**5.2**	**1.3**	**1.0**	**0.5**	**0.3**
Threshold change	-	-	-	-	(0.1)
Near final forecasts - Scenario C	**5.2**	**1.3**	**1.0**	**0.5**	**0.2**

The change in the cash position since the preliminary forecasts is not as significant as the OBEGAL excluding the net NZS Fund revenue and the lower SOE/CE's return do not form part of core Crown residual cash calculation.

Change in residual cash since preliminary forecasts

Residual cash	2008 Forecast $b	2009 Forecast $b	2010 Forecast $b	2011 Forecast $b	2012 Forecast $b
Preliminary forecasts	**0.8**	**(2.9)**	**(3.0)**	**(3.8)**	**(3.8)**
Change since prelimary forecasts	0.7	0.2	(0.5)	(0.5)	(1.0)
Near final forecasts - Scenario A	**1.5**	**(2.7)**	**(3.5)**	**(4.3)**	**(4.8)**
Scenario B adjustments	(0.6)	(0.8)	0.4	0.9	1.5
Near final forecasts - Scenario B	**0.9**	**(3.5)**	**(3.1)**	**(3.4)**	**(3.3)**
Threshold change in last year	-	-	-	-	(0.1)
Near final forecasts - Scenario C	**0.9**	**(3.5)**	**(3.1)**	**(3.4)**	**(3.4)**

Annex 3

Recommendations from CAB Min (08) 14/9 that relate to consequential impacts to other areas of the tax system

Composite Rates

agreed that if a 1 October 2008 start date is chosen, composite income tax rates are adopted for the 2008-09 income year which would reflect a blended average of the 2007-08 income year rates and the 2009-10 income year rates which would be:

Income Range	Tax Rate
$0 - $9,500	13.75%
$9,501 - $15,000	16.75%
$15,001 - $38,000	21%
$38,001 - $40,000	27%
$40,001 - $60,000	33%
$60,001 - $70,000	36%
$70,001 and above	39%

PAYE rates

agreed that PAYE withholding rates are adjusted downwards from the date the tax cuts begin (including from 1 October 2008 if that is the intended start date for the tax rate reductions);

Fringe benefit tax (FBT)

agreed that the rates and thresholds that apply for the FBT square-up calculation be adjusted to reflect the tax cut package;

agreed that if a 1 October 2008 start date is chosen composite FBT rates be used for the transitional year which correspond to the personal tax rates under the composite rates table;

Resident Withholding Tax (RWT) and Portfolio Investment Entity (PIE) Tax Rates

agreed that the current PIE tax rates and RWT rates apply pending consultation between officials and managed funds and banks following announcement of the tax rate changes.

Provisional tax

agreed that from the 2009-10 income year:

- the standard uplift that would otherwise apply to calculate provisional tax instalments should be reduced as if the tax cut had applied to the whole of the previous tax year;
- a similar approach would be used for taxpayers using the GST ratio method to pay provisional tax; and
- a similar approach would also apply to the 2010-11 and 2011-12 income years;

agreed that if a 1 October 2008 start date is chosen, the figure on which provisional tax instalments are based should be reduced by the dollar amount of the maximum tax cut that a person earning $70,000 would receive as if the 2008-09 blended tax rate scale applied to the prior income year on which the uplift amount is determined;

ACC attendant care

agreed to change the amount of tax withheld by ACC on attendant care payments to 12.5% to reflect the new bottom income tax rate from the start date of the tax rate cuts;

Maori Authority

noted the Maori Authority tax rate will continue to be 19.5% and officials will report to me and the Minister of Revenue on implications for the Maori Authority tax rate from the personal tax rate changes later this year;

Minimum Family Tax Credit

noted the Minimum Family Tax Credit will be reviewed later this year and implications from the change in the personal tax rates will be considered in that review;

Other consequential changes

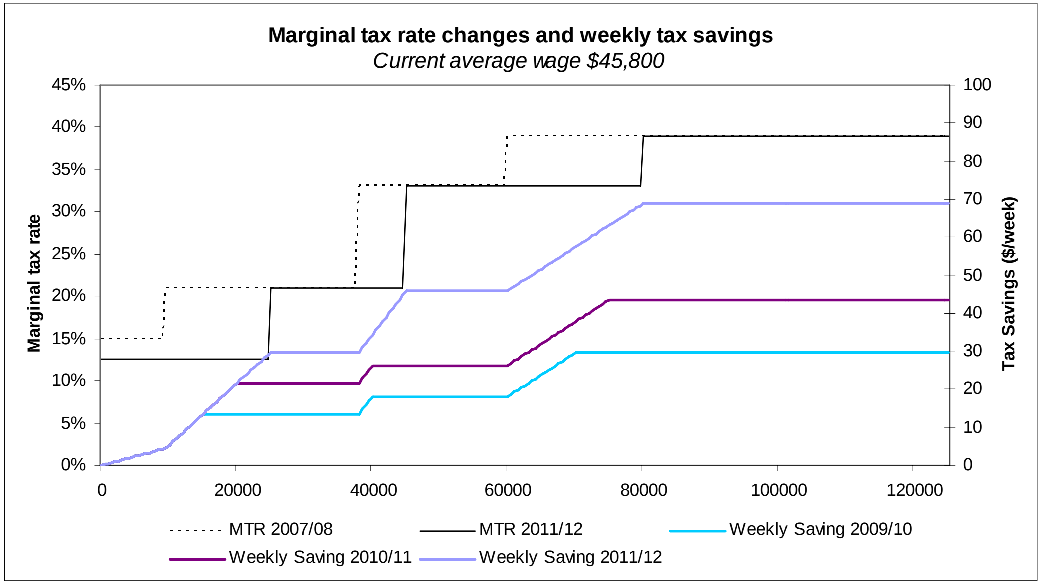
agreed to amend Income Tax Act provisions relating to secondary tax codes, specified superannuation contribution withholding tax (SSCWT), extra pay amounts, fund withdrawal tax, retirement scheme contribution tax and the child rebate to reflect the new personal tax rate structure;

agreed to other amendments to the Income Tax Act of a mechanical nature that are necessary to reflect the new personal tax rate structure;

Scenario A

Design		
On 1 April 2009	**On 1 April 2010**	**On 1 April 2011**
12.5% to $15k	12.5% to $20k	12.5% to $25k
21% to $40k	21% to $40k	21% to $45k
33% to $70k	33% to $75k	33% to $80k
39% over $70k	39% over $75k	39% over $80k

Fiscal Cost ($ million)	2011/12
Chg to disposable income	-4985
less clawback (17.1%)	852
	-4133



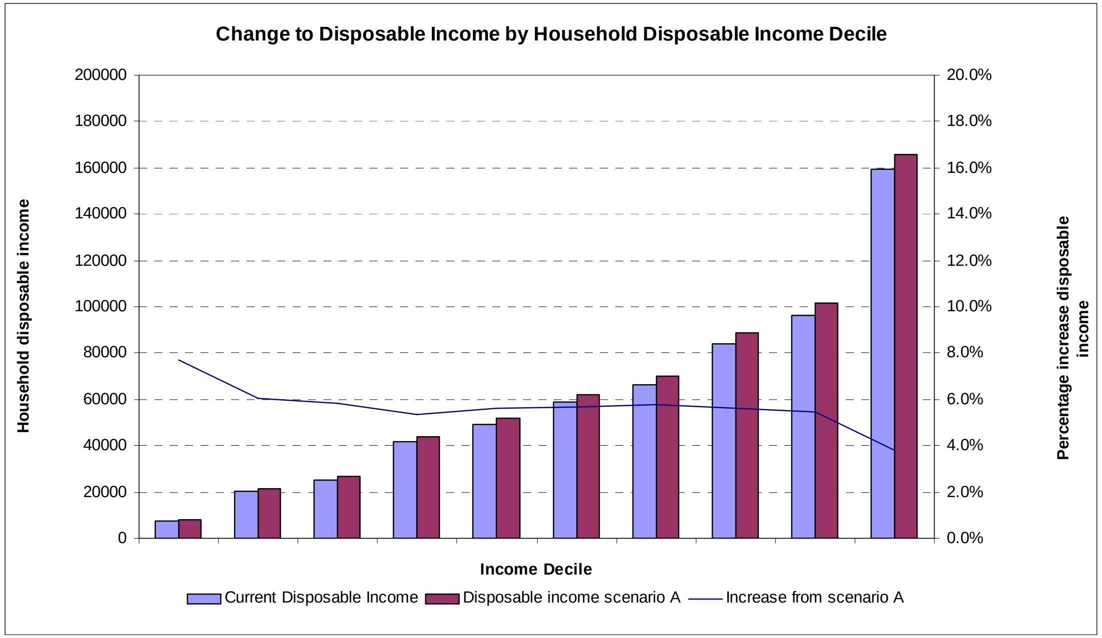
Incomes	Change in EMTR by 2011[1]				
	Increase	**No change**	**0 - 5% fall**	**5 - 10% fall**	**> 10% fall**
$0k - $10k	0	33,553	584,673	38,827	4,766
$10k - $20k	0	SOME	29,398	767,114	SOME
$20k - $30k	SOME[2]	161,622	14,640	228,534	SOME
$30k - $40k	SOME[2]	217,843	SOME	SOME	62,601
$40k - $50k	0	142,649	0	SOME	150,840
$50k - $60k	0	272,881	SOME	0	0
$60k - $70k	0	0	0	169,324	0
$70k - $80k	0	0	0	123,536	0
$80k - $90k	0	108,930	0	0	0
$90k - $100k	0	53,549	0	0	0
$100k+	0	181,208	0	0	0
Total[3]	**0**	**1,172,234**	**628,711**	**1,327,335**	**218,207**

Equality measures	
Status Quo Gini coefficient	0.353
New Gini coefficient (2011)	0.352
Status quo 80/20 ratio	2.942
New 80/20 ratio (2011)	2.941

1. These have been estimated using Treasury's Taxmod model which is based on Statistics NZ's Household Economic Survey dataset. In some cases there are too few observations in the sample to report groups separately.

2. There are some individuals who only have investment income and therefore do not qualify for the LIR. They will move from the 19.5% rate to the 21% rate.

3. The totals do not include those in the "some" categories.



Scenario B

Design		
On 1 April 2009	**On 1 April 2010**	**On 1 April 2011**
12.5% to $14k	12.5% to $17.5k	12.5% to $20k
21% to $40k	21% to $40k	21% to $42.5k
33% to $70k	33% to $75k	33% to $75k
39% over $70k	39% over $75k	39% over $75k

Fiscal Cost ($ million)	2011/12
Chg to disposable income	-3646
less clawback (17.1%)	623
	-3023

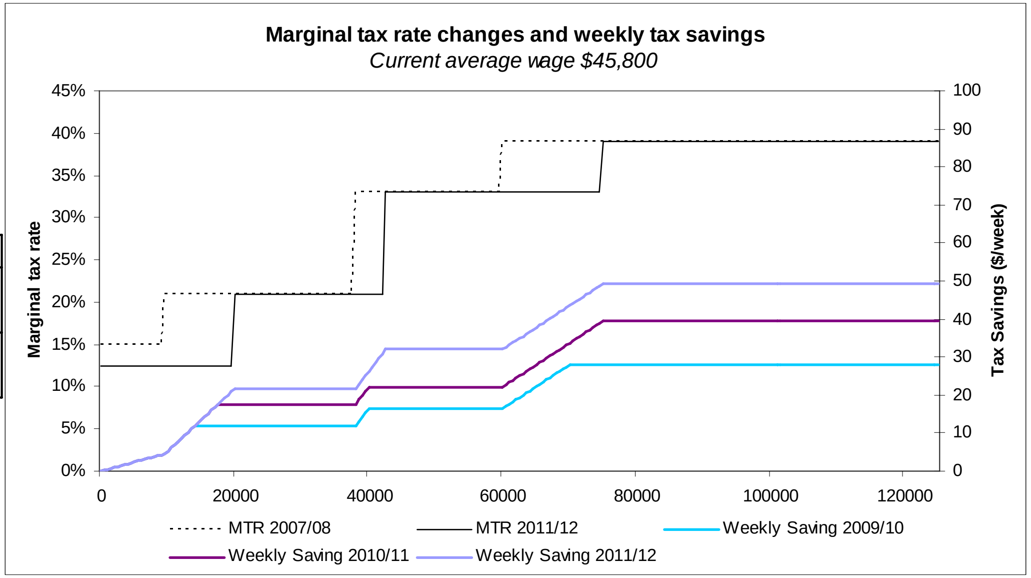
Incomes	Change in EMTR by 2011[1]				
	Increase	**No change**	**0 - 5% fall**	**5 - 10% fall**	**> 10% fall**
$0k - $10k	0	33,553	584,187	39,375	5,252
$10k - $20k	0	SOME	27,307	789,019	SOME
$20k - $30k	SOME[2]	352,082	21,572	4,910	SOME
$30k - $40k	SOME[2]	217,601	SOME	SOME	62,601
$40k - $50k	0	213,340	SOME	SOME	80,523
$50k - $60k	0	272,473	0	0	0
$60k - $70k	0	0	0	169,324	0
$70k - $80k	0	48,530	0	75,006	0
$80k - $90k	0	108,930	0	0	0
$90k - $100k	0	53,549	0	0	0
$100k+	0	181,208	0	0	0
Total[3]	**0**	**1,481,266**	**633,066**	**1,077,634**	**148,376**

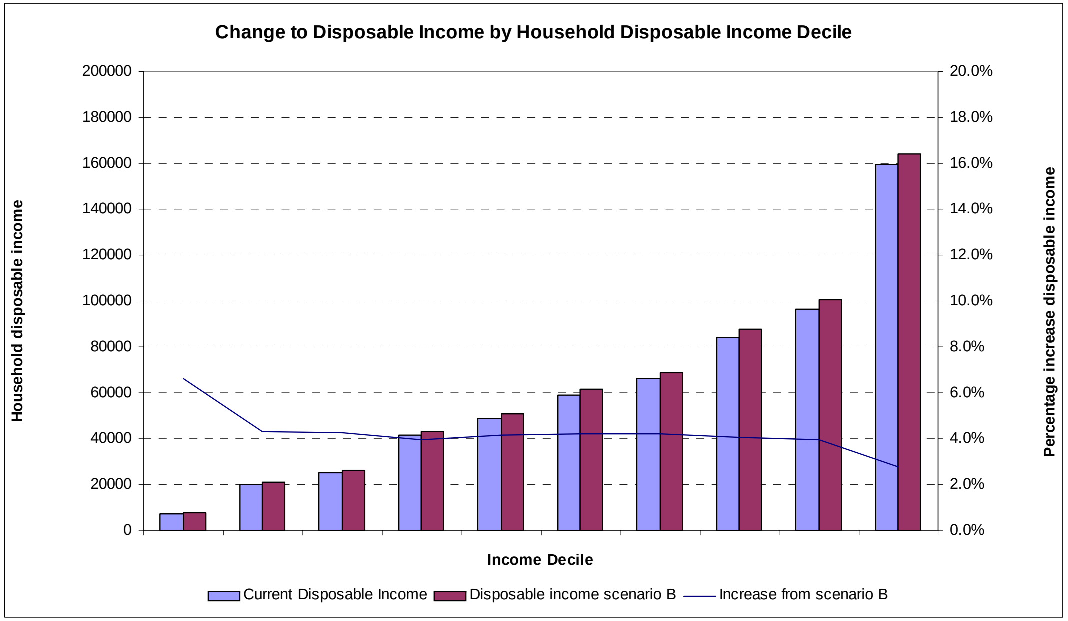
Equality measures	
Status Quo Gini coefficient	0.353
New Gini coefficient (2011)	0.352
Status quo 80/20 ratio	2.942
New 80/20 ratio (2011)	2.941

1. These have been estimated using Treasury's Taxmod model which is based on Statistics NZ's Household Economic Survey dataset. In some cases there are too few observations in the sample to report groups separately.

2. There are some individuals who only have investment income and therefore do not qualify for the LIR. They will move from the 19.5% rate to the 21% rate.

3. The totals do not include those in the "some" categories.

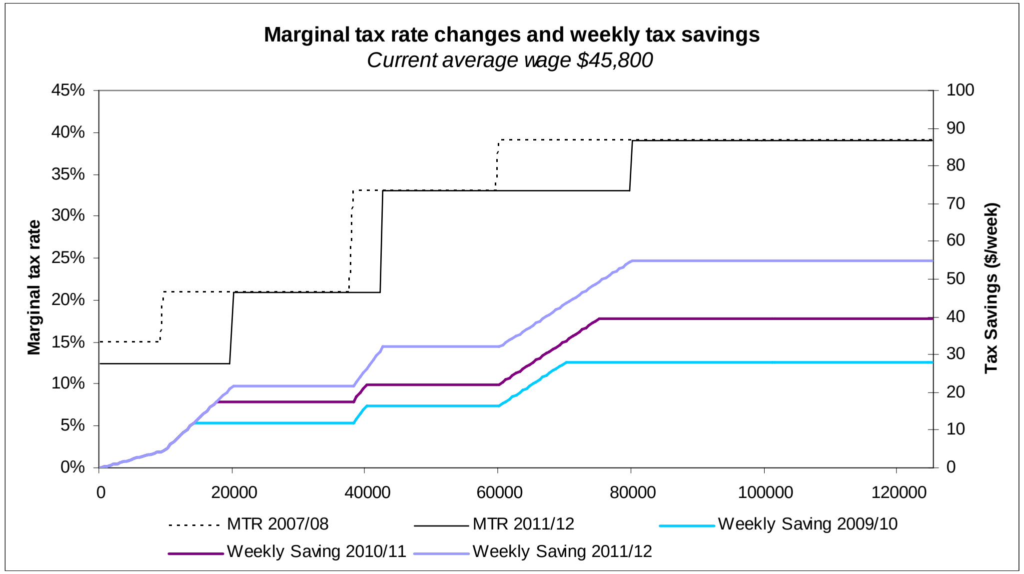




Scenario C

Design		
On 1 April 2009	**On 1 April 2010**	**On 1 April 2011**
12.5% to $14k	12.5% to $17.5k	12.5% to $20k
21% to $40k	21% to $40k	21% to $42.5k
33% to $70k	33% to $75k	33% to $80k
39% over $70k	39% over $75k	39% over $80k

Fiscal Cost ($ million)	2011/12
Chg to disposable income	-3759
less clawback (17.1%)	643
	-3116



Incomes	Change in EMTR by 2011[1] Increase	No change	0 - 5% fall	5 - 10% fall	> 10% fall
$0k - $10k	0	33,553	584,187	39,375	5,252
$10k - $20k	0	SOME	27,307	789,019	SOME
$20k - $30k	SOME	352,082	21,572	4,910	SOME
$30k - $40k	SOME	217,601	SOME	SOME	62,601
$40k - $50k	0	213,340	SOME	SOME	80,523
$50k - $60k	0	272,473	SOME	0	0
$60k - $70k	0	0	0	169,324	0
$70k - $80k	0	0	0	123,536	0
$80k - $90k	0	108,930	0	0	0
$90k - $100k	0	53,549	0	0	0
$100k+	0	181,208	SOME	0	0
Total[3]	**0**	**1,432,736**	**633,066**	**1,126,164**	**148,376**

Equality measures	
Status Quo Gini coefficient	0.353
New Gini coefficient (2011)	0.352
Status quo 80/20 ratio	2.934
New 80/20 ratio (2011)	2.934

1. These have been estimated using Treasury's Taxmod model which is based on Statistics NZ's Household Economic Survey dataset. In some cases there are too few observations in the sample to report groups separately.

2. There are some individuals who only have investment income and therefore do not qualify for the LIR. They will move from the 19.5% rate to the 21% rate.

3. The totals do not include those in the "some" categories.