

The Treasury

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August 2021

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- [36] 9(2)(h) - to maintain legal professional privilege
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- [38] 9(2)(j) - to enable the Crown to negotiate without disadvantage or prejudice
- [39] 9(2)(k) - to prevent the disclosure of official information for improper gain or improper advantage
- [40] Not in scope
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Tax Policy Report: Draft revenue strategy and high-level tax policy work programme for comment progress update

Date:	4 March 2021	Report No:	T2021/314 IR2021/080
		File Number:	SH-13-9

Action Sought

	Action Sought	Deadline
Minister of Finance (Hon Grant Robertson)	<p>Provide feedback to officials on the draft revenue strategy.</p> <p>Note officials will seek your agreement on updating the Government's short-term intentions and long-term objectives for revenue when reporting on the Fiscal Strategy report.</p> <p>Agree with the proposed timelines to obtain Cabinet's approval of the revenue strategy as part of the Budget Cabinet paper.</p> <p>Note officials have commenced work on a draft TPWP and will report to you with its contents once key decisions impacting the scope of the TPWP have been made.</p>	11 March 2021
Minister of Revenue (Hon David Parker)	<p>Provide feedback to officials on the draft revenue strategy.</p> <p>Agree with the proposed timelines to obtain Cabinet's approval of the revenue strategy as part of the Budget Cabinet paper.</p> <p>Note officials have commenced work on a draft TPWP and will report to you with its contents once key decisions impacting the scope of the TPWP have been made.</p>	11 March 2021

Contact for Telephone Discussion (if required)

Name	Position	Telephone	1st Contact
Jessica Rowe	Acting Manager, Tax Strategy, The Treasury	[39]	[35] ✓
Emma Grigg	Policy Director, Inland Revenue, Policy and Strategy	[23]	

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

Return the signed report to Treasury and Inland Revenue with feedback from Joint Ministers on the draft revenue strategy and high-level tax policy work programme.

Note any
feedback on
the quality of
the report

Enclosure: No/Yes (attached) OR Yes (iManage links)

Tax Policy Report: Draft revenue strategy and high-level tax policy work programme for comment progress update

Purpose of Report

1. You met with officials on 11 February 2021 to provide direction on the Government's revenue strategy and the setting of the Tax Policy Work Programme (TPWP). Prior to the meeting, officials provided advice on four key issues and content that could be included in the revenue strategy (refer T2021/85; IR 2021/052).
2. This report responds to the direction provided during that meeting and attaches a draft revenue strategy for your review and comment at Appendix 1. This report also provides an update on the progress of the proposed TPWP.

Key priorities included in the revenue strategy

3. We understand you were broadly comfortable with our earlier advice, our outline of key issues and the content we recommended be included in the revenue strategy (refer T2021/85; IR 2021/052). You asked officials to prepare a draft revenue strategy that includes references to matters of particular relevance to the Government. We have incorporated those references in the following ways:

Economic strategy

4. You asked that the revenue strategy outline the Government's overarching policy goals for the next three years as stated in the recently published Budget Policy Statement. We have included these goals directly in the draft revenue strategy, with examples showing how revenue policy can contribute to the Government's goals, including environmental goals, as discussed during the meeting.

Revenue objectives

5. You asked that the revenue strategy expand on the Government's objective of fairness in the tax system. The draft revenue strategy includes the objective of reducing wealth inequality, which is intended to reflect this discussion.

Fiscal strategy

6. In response to officials' advice that the revenue strategy needs to be consistent with the Government's overall fiscal strategy, the draft revenue strategy describes the fiscal pressures facing New Zealand and notes that the sustainability of the revenue base is critical to managing fiscal pressures over the long term.

Framework

7. We have responded to your request that the revenue strategy provide context on how the principles of a broad base-low rate framework and neutrality are reflected in the New Zealand tax system. We have also reflected your request that the revenue strategy indicates a focus on developing a tax system that is progressive, reduces income inequality and that is fit for purpose in a changing world. The draft revenue strategy expressly refers to ongoing work on international taxation and the digital economy.

8. A draft revenue strategy is attached for your review at Appendix 1, and we seek your comments so the revenue strategy can be finalised.

Should the Government's short-term intentions and long-term objectives also be amended?

9. The update of the revenue strategy also provides an opportunity to update the Government's short-term intentions and long-term objectives for Government revenue.
10. The Public Finance Act 1989 (sections 26J and 26K) requires the Fiscal Strategy Report (FSR) to state the Government's short-term intentions and long-term objectives for government revenue (as well as other fiscal variables: operating balance, expenses, debt and net worth). The short-term intentions relate to a period of at least two years. The long-term objectives must relate to a period of at least 10 years.
11. The intentions and objectives in the 2020 FSR, carried through to the 2021 Budget Policy Statement (BPS) (as described below as Option 1), could be maintained in the 2021 FSR.
12. We will shortly provide advice on the FSR including whether to amend the Government's short-term intentions and long-term objectives for Government revenue
13. Officials recommend that the short-term intentions remain unchanged but that the long-term revenue objective be amended with language more consistent with the updated revenue strategy (Option 2). The proposed wording starts with the level of revenue; this is intended to more closely align with the purpose of the requirement (in the Public Finance Act) that the FSR includes a long-term fiscal objective. The proposed wording then notes the Government's objectives for the tax system relate to fairness, efficiency and progressivity.

	Short term intention (3 years)	Long-term objective (10 years)
Option 1: Maintain the same wording as in 2020 FSR and 2021 BPS.	Our intention is to ensure revenue is consistent with the operating balance objective.	The Government will ensure a progressive taxation system that is fair, balanced and promotes the long-term sustainability and productivity of the economy, consistent with the debt and operating balance objectives.
Option 2: New wording to be consistent with updated revenue strategy.	[no change] Our intention is to ensure revenue is consistent with the operating balance objective.	The Government will ensure a sustainable level of revenue that is consistent with the debt and operating balance objectives. Revenue will be raised in a fair and efficient manner with a progressive tax system.

14. Whilst officials' recommend amending the long-term objective for Government revenue, you may want to consider the merits of making this change in the broader context of whether other changes are required in the FSR, and this will also be outlined in later FSR advice to the Minister of Finance.

Tax policy work programme update

15. We have commenced work on outlining a TPWP to reflect the core priorities in the draft revenue strategy. These priorities will be reflected in workstreams that are key priorities of the Government, such as housing, integrity measures to support the new top individual tax rate, along with environmental and international tax considerations.
16. In December 2020 Inland Revenue officials reported to the Minister of Revenue with a high-level overview of the current TPWP priorities for early 2021 (IR2020/517 refers). That report included an appended A3 (attached as Appendix 2) with a high-level overview of current workstreams. We consider that many of these workstreams still reflect Government priorities and should be carried over to the revised TPWP.
17. However, there is a prioritisation exercise that will have to be completed. From a resource allocation perspective, there are a number of key decisions that will have a large impact on the shape of the TPWP. These include:
 - 17.1 [33]
 - 17.2
 - 17.3
 - 17.4
18. We will report to Ministers with a recommended draft TPWP once the impact of these measures is known. To the extent these measures are progressed and require policy resources that are not supported by additional funding, decisions will need to be made on whether other items are either slowed down or stopped to accommodate them.
19. Another key consideration is that the TPWP has traditionally included Inland Revenue's social policy work programme. Although this sits outside of the revenue strategy, this work occupies a considerable percentage of Inland Revenue's policy and operational capacity.
20. As with previous work programmes, in formulating this draft, we will also consult with stakeholders regarding their key considerations for tax policy.

Next steps

21. Officials' propose meeting with you to discuss the content of the TPWP and the draft revenue strategy before reporting with a final revenue strategy for Cabinet approval.
22. This later report will also seek direction on how you would like the revenue strategy and TPWP to be communicated publically. In prior years, options have included inserting extracts of the revenue strategy in the FSR whilst publishing the complete revenue strategy on the Treasury's website and the TPWP on Inland Revenue's website.
23. The timeline below has been proposed to obtain Cabinet approval to the revenue strategy and to coordinate with the drafting of the FSR. To reduce the number of Cabinet papers being considered, we recommend finalising the revenue strategy with you and then appending it to the Budget Cabinet paper, to be approved with that paper. The alternative option is to have a separate revenue strategy Cabinet paper to be considered along a similar timeline.

	Milestone	Date
1	Joint Ministers meeting on the TPWP and revenue strategy if required	11 March
2	Officials provide a final revenue strategy	25 March
3	Cabinet confirms the revenue strategy as an appendix to the Budget Cabinet paper.	Early April
4	Publishing of the Fiscal Strategy Report (FSR) (which includes the revenue strategy)	May

24. As outlined in paragraph 15-20, the TPWP will not be able to be finalised until decisions have been made around key government priorities. Officials plan to report to you in late March or early April with a draft TPWP and Cabinet paper for noting by Cabinet. Precise timelines regarding proposed Cabinet dates and a timeline for publishing the TPWP will be canvassed in this later TPWP report.

Recommended Action

We recommend that you:

Revenue strategy

- a **review** and provide feedback to officials on the draft revenue strategy (refer to Appendix 1);
- b **note** officials will seek your agreement on whether to update the Government's short-term intentions and long-term objectives for revenue when reporting on the FSR;
- c **agree** to the following timeline for finalising the revenue strategy, as amended from earlier advice (refer T2021/85; IR 2021/052) with the revenue strategy being considered as part of the Budget Cabinet paper;

Agree/disagree

	Milestone	Date
1	Joint Ministers meeting on the TPWP and revenue strategy if required	11 March
2	Officials provide a final revenue strategy	25 March
3	Cabinet confirms the revenue strategy as an appendix to the Budget Cabinet paper.	Early April
4	Publishing of the Fiscal Strategy Report (FSR) (which includes the revenue strategy)	May

Tax Policy Work Programme

- d **note** the current TPWP priorities contained in Appendix 2; and
- e **note** officials are commencing work on a draft TPWP and will report to you with its contents once key decisions impacting the scope of the TPWP have been made.

Jessica Rowe
Manager (Acting)

Emma Grigg
Policy Director, Inland Revenue, Policy and Strategy

Hon Grant Robertson
Minister of Finance

Hon David Parker
Minister of Revenue

APPENDIX 2: DRAFT – NOT GOVERNMENT POLICY

Draft Revenue Strategy 2021 – for comment

Economic and fiscal strategy

The public finances, including government revenue, are important for wellbeing. Public policy supports New Zealanders' wellbeing when the social benefits of government expenditure outweigh the social costs of raising revenue.

The Government's overarching policy goals for the next three years are:

- Continuing to keep New Zealand safe from COVID-19;
- Accelerating the recovery and rebuild from the impacts of COVID-19; and
- Laying the foundations for the future, including addressing key issues such as our climate change response, housing affordability and child poverty.

Government revenue underpins many of these outcomes by funding the social expenditure needed to meet these challenges. In some cases, revenue policy has a more direct role in contributing to these goals. This includes policies that support the economic recovery, promote housing affordability and mitigate climate change.

Government revenue needs to be sufficient to ensure a sustainable fiscal outlook. The level of revenue will be maintained to be consistent with reducing operating deficits and stabilising net core Crown debt as a percentage of GDP by the mid-2020s and then reducing it as conditions permit (subject to any significant shocks).

A sustainable revenue base is critical for managing fiscal pressures over the long term. These pressures relate to the ageing population, health care costs, infrastructure demand and the need for resilience to climate change and other shocks. There is also rising global concern with inequality and many countries, including New Zealand, face the challenge of fostering inclusive growth.

Revenue objectives

The Government's revenue policy objective is to raise sufficient revenue in a fair and efficient manner. This will assist in fostering inclusive growth.

The Government's fairness objectives for the tax system are:

- *Progressivity*: Individuals with a higher income, and therefore ability to pay, should pay a greater proportion of their income in tax.
- *Reducing inequality*: the tax system should help in limiting excessive wealth inequality over the longer term.
- *Horizontal equity*: The principle that people that are in the same position should pay the same amount of tax.

The efficiency objective is to minimise the economic costs of raising revenue, subject to the Government's revenue and fairness objectives.

Continued public trust and confidence in the tax system and its administration is important. This supports voluntary compliance and broader social capital.

Framework

The Government has a strong focus on the fairness of the tax system. This means that the income tax system should be progressive and, in combination with transfers, reduces income inequality. The Government has increased the progressivity of the personal income tax system with a new top tax rate.

The tax framework is based on the principles of broad base-low rate and neutrality. Income and consumption tax bases are broad in the sense that there are few specific concessions for particular economic activities, goods or services. This enables tax rates to be set lower than otherwise. Neutrality in the tax treatment of different investments promotes economic efficiency and productivity. However, in another sense, New Zealand's revenue base is narrow, due to the inconsistent taxation of capital income.

In some cases, revenue policy will be used to influence behaviour. This is appropriate only where there is clear evidence of net social benefits, tax policy is the most appropriate instrument and fiscal risks can be managed. As an example, the research and development tax incentive promotes business innovation.

People and businesses must pay their fair share of tax, including multinational companies. The international tax framework needs to adapt to shifts in the global economy, including increased cross-border activity and digitalisation. New Zealand is continuing to work with the OECD to find a multilateral solution to the challenges that the digital economy poses for international taxation.

Tax settings will continue to be broadly stable and predictable. This supports efficiency and macroeconomic stability.

The Government expects Inland Revenue to maintain public confidence by administering the tax system in a fair and efficient manner. The tax system has been modernised and simplified through Inland Revenue's Business Transformation programme.

The tax system must remain fit for purpose in a changing world. Ongoing work will focus on implementing Government policy, maintaining the integrity of existing revenue bases and monitoring the sustainability and fairness of the tax system. The Generic Tax Policy Process shall be used to develop and consult on tax policy where practicable.

