The Treasury

Budget 2024 Information Release

September 2024

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Some parts of this information release would not be appropriate to release and, if requested, would be withheld under the Official Information Act 1982 (the Act).

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Where information has been withheld, no public interest has been identified that would outweigh the reasons for withholding it.

Key to sections of the Act under which information has been withheld:

[1] 6(a) - to avoid prejudice to the security or defence of New Zealand or the international relations of the government

[23] 9(2)(a) - to protect the privacy of natural persons, including deceased people

[25] 9(2)(b)(ii) - to protect the commercial position of the person who supplied the information or who is the subject of the information

[27] 9(2)(ba)(ii) - to protect information which is subject to an obligation of confidence or which any person has been or could be compelled to provide under the authority of any enactment, where the making available of the information would be likely otherwise to damage the public interest

[31] 9(2)(f)(ii) - to maintain the current constitutional conventions protecting collective and individual ministerial responsibility

[33] 9(2)(f)(iv) - to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials

[34] 9(2)(g)(i) - to maintain the effective conduct of public affairs through the free and frank expression of opinions

[35] 9(2)(g)(ii) - to maintain the effective conduct of public affairs through protecting ministers, members of government organisations, officers and employees from improper pressure or harassment;

[36] 9(2)(h) - to maintain legal professional privilege

[37] 9(2)(i) - to enable the Crown to carry out commercial activities without disadvantage or prejudice

[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] 18(c)(i) - that the making available of the information requested would be contrary to the provisions of a specified enactment

Where information has been withheld, a numbered reference to the applicable section of the Act has been made, as listed above. For example, a [23] appearing where information has been withheld in a release document refers to section 9(2)(a).

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TE TAI ŌHANGA
THE TREASURY

Reference: T2024/646

Date: 12 March 2024

To: Minister of Finance
(Hon Nicola Willis)

Deadline: None
(if any)

Aide Memoire: Further information on TR2024/598 (Personal Income Tax – initial distributional analysis of wider Package)

On 8 March 2024 you received TR2024/598 – "Personal Income Tax – initial distributional analysis of wider package". This note seeks to answer further questions you have asked about the content of this report, specifically:

1. **Why does the modelling approach show losers from the Working for Families (WFF) changes?**
    - They are referred to as "losers" as they would have less income in tax year 2027 under the reform than under the status quo in tax year 2027.
2. **Does the modelling estimate labour supply changes as a result of changes in individual's marginal tax rates?**
    - Labour supply changes are not factored into the results, but we can provide modelling on changes to financial incentives to work.
3. **Can individuals with children receive IETC?**
    - Yes, if they are not eligible for Working for Families.
4. **How will recipients of NZS be affected by PIT changes?**
    - They will receive tax relief based on their total taxable income.

More details are provided below.

Overview of Treasury's modelling

Treasury uses the TAWA (Tax and Welfare Analysis) microsimulation model as part of the budget process to estimate the costs and distributional impacts of potential personal tax and welfare policies. TAWA is also used to estimate future child poverty rates for the Child Poverty Report.

Why does the modelling approach show losers from the WFF tax changes?

TAWA estimates household incomes in a future tax year under current policy settings and then estimates the impact of a policy reform on those future household incomes. The model shows how much they would gain or lose compared to their future incomes under the status quo. The "gain" and "loss" is therefore not an increase/decrease in income between two years and is instead a comparison of alternative future incomes at the same point in time.

In TR2024/598, the "losing" households have less income in tax year 2027 under the reform than they would have had under the status quo in tax year 2027.[33] ,

They would fall into the "losers" category regardless of their income in previous years.

Does the modelling estimate labour supply changes as a result of changes in marginal tax rates?

TAWA does not estimate changes in labour supply as a direct result of changes in marginal tax rates. The model operates as a static or non-behavioural microsimulation model. This essentially means that it does not factor in the potential behavioural responses of individuals, such as changes in their labour supply.

Labour supply responses are one source of uncertainty in microsimulation modelling – others include data quality issues, take up, and economic forecast uncertainty. Recent Treasury analysis has demonstrated that the impact on model results from labour supply effects tends to be less significant than other forms of uncertainty, particularly changes in economic forecasts. Treasury has thus prioritised improving how the TAWA model can account for changes in economic forecasts and take-up and improving the input data using the IDI[1].

While behavioural microsimulation models exist and are capable of incorporating labour supply responses to tax changes, these models are often criticised for their lack of transparency. Other, more transparent methods can be used to consider potential effects of a reform on labour supply.

TAWA can be used to assess the outcomes of reforms on the distribution of effective marginal tax rates (EMTRs). We can provide information on the number of families that would experience a change in their effective marginal tax rates, which provides a picture of changes in their incentives to work. So, while TAWA does not directly model labour supply changes, it can be used as a tool to assess and communicate the consequences of policy reforms on work incentives and household incomes.

[1] Stats NZ's Integrated Data Infrastructure.

Can individuals with children receive IETC?

WFF tax credits include the [33]

Individuals with children whose family is not in receipt of any WFF tax credits are eligible to receive IETC (subject to meeting the income test).

This could, for example, be the case where a family's combined earnings are high enough such that they are ineligible for any WFF credits, but an individual within that family earns an amount that qualifies for IETC.

Further explanation of the interaction between IETC and WFF, including further worked examples, can be found in the Inland Revenue Briefing Note 2024/091 - "Interaction between the Independent Earner Tax Credit and Working for Families tax credits".

How will recipients of NZS be affected by PIT changes?

Recipients of New Zealand Superannuation (NZS) will gain from this package due to NZS being set as a gross amount. This means tax is recalculated under the new settings, so recipients will directly receive tax relief based on their taxable income, which includes the total amount they receive of NZS and any other taxable income.

Personal income tax relief policies will also impact indexation. NZS rates are indexed using a either CPI or the net average after-tax wage (depending on which results in a larger payment). As the average after-tax wage increases due to New Zealanders paying less tax on the same income, NZS payments will increase (depending on CPI).[2]

Meghan Stephens, Principal Advisor, Analytics and Insights, [39]
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[2] The formula for indexing NZS rates is complex. NZS rates are indexed to the maximum growth in CPI or 66% of the net average after-tax wage (i.e., referred to as the wage floor). In the near term, the CPI indexation results in rates above the wage floor, but this will change over time.