CHAPMAN TRIPP

brief counsel TAX

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An every cent counts budget

Budget 2012 has its hands down the sides of the couch searching for loose change to bring the books back into balance by 2014/15.

Although the budget has quite a busy programme of tax changes, they are projected to bring in only $1.7 billion over the next four years. But without that package, and a bit of finessing on KiwiSaver, the fragile surplus of $197 million projected for 2014/15 could not have been included in the budget forecasts.

Whether it will actually be achieved will depend on a lot of factors, most of which are beyond the government's control and many of which are now being decided in the capitals of Europe.

This Brief Counsel provides an overview to the budget.

Budget forecasts in overview

Economic data					
March years (%)	2012	2013	2014	2015	2016
Real GDP growth	1.6	2.6	3.4	3.1	2.9
Inflation	1.6	2.6	2.5	2.4	2.4
Unemployment	6.3	5.7	5.2	5.0	4.7
Fiscal data					
Operating balance	-4.1	-3.6	-0.9	0.1	0.8
Net Crown debt (%GDP)	25.0	28.1	28.7	28.6	27.7
Net Crown debt ($b)	51.9	61.3	66.5	69.8	70.7

Economic forecasts

As always, the budget forecasts will live or die according to the accuracy of the growth track. Treasury's growth forecasts in the last three budgets have not been achieved and there is at least a prospect that this may happen again. Certainly, Treasury's growth picks in the 2014, 2015 and 2016 years are above market expectations and most of the developments out of Europe since the forecasts would have been finalised have been bad.

Assumptions behind the growth forecasts are:

- a strong stimulus from the Canterbury rebuild (expected to contribute a full percentage point to annual growth each year from 2012 to 2016)
- continued "historically low" interest rates
- a return to net migration inflows within two years, and
- ongoing solid demand for New Zealand's primary sector exports.

Fiscal forecasts

The forecasts show a government that is prepared to bear the brunt of the Global Financial Crisis and the Canterbury earthquakes on its own accounts by way of increasing net debt (to $70 billion by 2015 from $10 billion in 2008). The government will hold Crown expenditure as best it can (as opposed to significant cost slashing in other, more hard-hit economies) and with only minor changes in the tax system.

Core Crown expenses will continue to increase in nominal terms over the forecast period (rising by $6.8 billion), but are projected to fall as a proportion of GDP from 35.2% currently to 30.2% by 2016.

This reflects two years of near zero budgets and continuing small budgets for the foreseeable future. How realistic this is politically will depend on how long the electorate maintains its appetite for austerity.

Tax package

The budget tax changes are relatively minor and were well-telegraphed in advance.

- IRD is to be given an extra $78 million towards auditing and compliance, which is expected to raise an extra $384 million in taxes over the next four years.
- Both the changes proposed to farmers' ability to change valuation methods under the livestock scheme and the changes to the treatment of "mixed use assets" were foreshadowed in a discussion document in August.
- Owners of "mixed use assets", such as holiday homes and boats, that are partly used for income producing purposes and partly for private purposes, will find their ability to claim deductions tightened. Costs will be deductible in the same proportion that actual use for producing income bears to actual private use. For example, if a holiday home is rented out for 30 days a year and used privately for 30 days a year, the owner will be able to claim a tax deduction for only 50% of the costs of ownership. Currently owners claim deductions based on the proportion of the year that the asset is available for hire.

There are also some changes that will impact on families. The under $9,800 tax credit and the childcare and housekeeper credits are to be repealed – this will mean a change in PAYE tax codes for some employees. The tax credit for children is to be replaced with a limited tax exemption.

The government expects the mixed use asset, livestock and tax credit changes to save approximately $410 m over the next four years.

Also of note, in the area of taxes generally, are increases in tobacco excise, fuel excise and road user charges.

All up the tax and excise measures are predicted to raise an additional $1.7 billion over the next four years. This is in the context of a predicted 30% increase in the total annual tax take over that period – from $54.3 billion to $70.2 billion a year. This healthy increase, during a time when real GDP is predicted to increase by around 3% annually, is put down to the expiration of tax losses and increased activity including, in particular, the Canterbury rebuild.

The KiwiSaver finesse

The proposed auto-enrolment of all employees not already in KiwiSaver has been deferred from 2014/15 until the budget is in sufficient surplus for the government to pay the up to $514 million four-year added cost which the Crown would incur in its employer capacity. Without this deferral, the projected return to surplus would not be possible.

The other KiwiSaver changes are disclosures and operations-focussed and are no surprise:

- a requirement for retail schemes to report returns, fees, costs and other key information on their websites in a standard format (allowing investors to make direct scheme comparisons) was already pending and consulted on last year, and
- a review of the KiwiSaver default provider arrangements (their number, structure and investment mandate) will no doubt be influenced by aspects of last year's Savings Working Group report.

The new disclosure rules will take effect on 1 April 2013. The government will release a discussion paper on the default provider review later in the year and make decisions by year's end (for implementing before the current default providers' seven-year term expires on 30 June 2014).

Significantly, there are no new changes this year to KiwiSaver contributions or incentives. The increase to minimum 3% contributions (announced last year) will still take effect on 1 April 2013 as announced in last year's budget.

The budget growth package

The government has sought to address those critics who say that it is not doing enough to stimulate economic growth or to increase the productivity of the economy.

Research, science and innovation gets another $385 million (not large enough to be transformative, perhaps, but significant in terms of this budget). Specific items are:

- $166 million to redevelop an Advanced Technology Institute to assist high-tech firms
- $60 million for a series of National Science Challenges
- a $100 million increase for the Performance-Based Research Fund, and
- $59 million in extra funding for science and engineering courses.

Kiwibank

The budget lists as a new unquantified risk the possibility that Kiwibank will require a capital injection from the public purse over the next three years to enable it to meet the new Basel III regulatory requirements and because New Zealand Post is "reaching constraints" in its ability to support Kiwibank.

This funding will come from the Future Investment Fund which will receive the proceeds from the Mixed Ownership Model policy. Although this fund will be dry until the first share offer is completed, the budget allocates the first $559 million as follows: $250 million toward KiwiRail's Turnaround Plan; $88 million for hospital developments; $76 million for the capital costs of the new Advanced Technology Institute, and $34 million for new schools.

Other candidates for funding identified in the budget include: other Crown capital spending, earthquake strengthening of government buildings and the irrigation investment fund.

CHAPMAN TRIPP

DAVID PATTERSON – CONSULTANT
T: +64 4 498 6330
M: +64 27 610 2031
E: david.patterson@chapmantripp.com

CASEY PLUNKET – PARTNER
T: +64 9 357 9027
M: +64 27 561 0013
E: casey.plunket@chapmantripp.com

MIKE WOODBURY – PARTNER
T: +64 4 498 6324
M: +64 27 459 9014
E: mike.woodbury@chapmantripp.com

AUCKLAND
23 Albert Street
PO Box 2206, Auckland 1140
New Zealand
T: +64 9 357 9000
F: +64 9 357 9099

WELLINGTON
10 Customhouse Quay
PO Box 993, Wellington 6140
New Zealand
T: +64 4 499 5999
F: +64 4 472 7111

CHRISTCHURCH
245 Blenheim Road
PO Box 2510, Christchurch 8140
New Zealand
T: +64 3 353 4130
F: +64 3 365 4587

www.chapmantripp.com

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