In Confidence

Office of the Minister of Revenue

Chair, Cabinet Legislation Committee

INCOME TAX (FRINGE BENEFIT TAX, INTEREST ON LOANS) AMENDMENT REGULATIONS 2022 (NO 2)

Proposal

1 This paper seeks the Cabinet Legislation Committee's agreement to submit an Order in Council amending the Income Tax (Fringe Benefit Tax, Interest on Loans) Amendment Regulations 2022 (No 2) to the Executive Council. The proposal is to increase the FBT prescribed interest rate for low-interest, employment-related loans from 4.78% to 6.71%, in line with an increase in market interest rates.

2 Changes to the prescribed interest rate are a routine matter and do not involve a change of policy. The methodology used for setting the rate has been applied consistently since the early 1990s.

Policy

3 The fringe benefit tax (FBT) rules tax non-cash benefits provided to employees. Included in the definition of 'fringe benefit' is any employment-related loan on which the employer is charging a rate of interest that is below the market rate. The interest differential is taxable. A prescribed rate set by regulations is used as a proxy for the market rate of interest to save employers the compliance costs associated with determining the market rate relevant to loans that they have provided to their employees.

4 The Income Tax Act 2007 ('the Act') allows regulations to be made to set the prescribed rate. Once a rate is set, it remains the prescribed rate of interest until changed by a subsequent Order in Council. The current FBT prescribed rate, which has applied since 1 July 2022, is 4.78%.

5 The prescribed rate of interest is based on a Reserve Bank survey of first mortgage housing interest rates on the last day of each month ('floating first mortgage new customer housing rate'). This is calculated as the weighted average interest rate for the surveyed institutions, the weightings being based on each institution's share of total lending for housing purposes. This Reserve Bank series is selected as the benchmark for setting the FBT prescribed rate because it is seen as a good indication of market interest rates.

Timing

6 The Act provides that when regulations to change the prescribed rate of interest are made, they apply to quarters starting at least one month following the date the regulations were made by the Governor General by Order in Council. Regulations that reduce the rate may apply for the current quarter if made at least one month before the end of the quarter.

7 In accordance with the Act, I recommend that the regulations to raise the rate have effect from 1 January 2023 – the beginning of the next quarter. No waiver of the 28-day rule is required.

Compliance

8 The regulations comply with each of the following, where applicable:

8.1	the principles of the Treaty of Waitangi	Not applicable
8.2	the New Zealand Bill of Rights Act 1990	Not applicable
8.3	the Human Rights Act 1993	Not applicable
8.4	the principles and guidelines set out in the Privacy Act 1993	Not applicable
8.5	relevant international standards and obligations	Not applicable
8.6	the Legislation Guidelines (2018 edition) which are maintained by the Legislation Design and Advisory	Committee Complies

Regulations Review Committee

9 Officials consider that there are no grounds for the Regulations Review Committee to draw the Order in Council to the attention of the House under Standing Order 319.

Certification by Parliamentary Counsel

10 The regulations have been certified by Parliamentary Counsel as being in order for submission to Cabinet.

Impact Analysis

11 The proposal is of a minor and mechanical nature and does not substantially alter existing arrangements. Therefore, a regulatory impact assessment is not required.

12 The proposal will not increase compliance costs as it is simply a change in the prescribed interest rate.

Publicity

13 Inland Revenue will publish an article about these changes in its *Tax Information Bulletin*.

Proactive Release

14 I propose to proactively release this Cabinet paper, associated minutes, and key advice papers in whole within 30 working days of Cabinet making final decisions.

Consultation

15 The Treasury has been consulted in the preparation of this paper.

Revenue implications

16 Raising the prescribed interest rate to 6.71% will increase the amount of FBT that will be collected by approximately $1.83 million over the 2022/23 year and $3.66 million per year over the remaining forecast period.

Recommendations

17 I recommend that the Cabinet Legislation Committee:

a. **note** that the regulations set the prescribed rate of interest for calculating the taxable benefit of low-interest, employment-related loans;

b. **agree** that, consistent with the results of the Reserve Bank's survey for August 2022, the FBT prescribed rate of interest should be raised from 4.78% to 6.71% from the quarter commencing on 1 January 2023**;**

c. **note** the following changes as a result of the decision in recommendation 2, with a corresponding impact on the operating balance:

			$millions increase/(decrease)		
Vote Revenue	**2022/23**	**2023/24**	**2024/25**	**2025/26**	**2026/27 & out years**
FBT revenue	**2.54**	**5.08**	**5.08**	**5.08**	**5.08**
Company tax	**(0.71)**	**(1.42)**	**(1.42)**	**(1.42)**	**(1.42)**
Net Revenue	**1.83**	**3.66**	**3.66**	**3.66**	**3.66**
Impact on Operating balance	**1.83**	**3.66**	**3.66**	**3.66**	**3.66**

d. **note** that the changes are forecast changes and do not have appropriation implications;

e. **authorise** the submission to the Executive Council of the Income Tax (Fringe Benefit Tax, Interest on Loans) Amendment Regulations 2022 (No 2).

Authorised for lodgement

Hon David Parker

Minister of Revenue